

# 2018 Tax Reform - Understanding the New Rules

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## 2018 “Somewhat” Reduced Individual Income Tax Rates

Rate	For Single Filers, Taxable Income Over	For Married Individuals Filing Joint Returns, Taxable Income Over	For Heads of Households, Taxable Income Over
10%	\$0	\$0	\$0
12%	\$9,525	\$19,050	\$13,600
22%	\$38,700	\$77,400	\$51,800
24%	\$82,500	\$165,000	\$82,500
32%	\$157,500	\$315,000	\$157,500
35%	\$200,000	\$400,000	\$200,000
37%	\$500,000	\$600,000	\$500,000

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## 2018 Long Term Capital Gain & Qualified Dividend Tax Rates

Rate	For Single Filers, Adjusted Gross Income Less Than	For Married Individuals Filing Joint Returns, Adjusted Gross Income Less Than	For Heads of Households, Adjusted Gross Income Less Than
0%	\$38,600	\$77,200	\$51,700
15%	\$425,800	\$479,000	\$452,400
20%	More than \$425,799	More than \$478,999	More than \$452,399

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## 2018 Higher Standard Deduction But Personal Exemptions Repealed

### 2018 Standard Deduction

Year	Single	Married Filing Jointly	Heads of Household
2018	<b>\$12,000</b>	<b>\$24,000</b>	\$18,000

The standard deduction is increased for individuals over age 65 or blind by **\$1,300** each for joint returns and **\$1,600** for others.

### Compare to 2017 Standard Deduction + Personal Exemptions

	<u>Single</u>	<u>MFJ</u>
2017	\$6,350 standard deduction + \$4,050 personal exemption = <b>\$10,400</b>	\$12,700 standard deduction + (\$4,050 * 2) personal exemptions = <b>\$20,800</b>

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## 2018 Itemized Deductions Trimmed

- Itemized deduction for taxes capped at \$10,000
  - Virginia income taxes
  - Local real estate and personal property taxes
  - Same cap whether single or married filing jointly
- Miscellaneous itemized deductions eliminated
  - Unreimbursed employee business expenses
  - Tax preparation fees
  - Investment management fees

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## Negative Impact on Charitable Contributions?

### 2017 Married Filing Joint:

- Itemized deductions \$24,000 (\$8,000 mortgage interest, \$3,000 Virginia income tax, \$3,000 real estate tax, \$10,000 charitable contributions)
- Itemizing more beneficial than \$12,700 standard deduction
- \$10,000 charitable contribution saved \$3,000+ in income taxes

### 2018 Married Filing Joint:

- \$24,000 standard deduction available whether or not \$10,000 charitable contribution made
- **NO tax savings** from \$10,000 charitable contribution

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## Contribution Strategies

- **To optimize tax deductions:** “bunch” contributions in “giving years” (to exceed standard deduction) and take standard deduction in other years
  - Example: Desired gift is \$10,000/year, give \$30,000 in one year and skip the next 2 years
- **Donor Advised Fund** can be used to *smooth out* the cash flow to the charity

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## New 2018 “Postcard” 1040

- IRS has released drafts of new 2018 “postcard” tax return
- Just a reorganization not simplification
  - Short cover form
  - Attachments/schedules as needed for particular circumstances

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# Senior Help in 2019

## New Form 1040SR for Seniors (65+)

- Similar to Form 1040EZ
- Can use even if income includes:
  - Social Security
  - Distributions from Retirement Plans
  - Capital Gains
- Maybe Large Print?

## 2018 Estate Tax Exemption Doubled

	2017	2018
Basic Exclusion Amount	\$5.49M	\$11.18M (\$22.36M couple)
Top Estate Tax Rate	40%	40%
Annual Gift Exclusion	\$14,000	\$15,000

## Estate Planning in 2018

Family Net Worth	Primary Planning Considerations
< \$11.2 Million	No Specific Estate <u>Tax</u> Planning Needed Capital Gains Tax Family Dynamics Probate Avoidance
Between \$11.2 and \$22.4 Million	How to Handle Possible Sunset in 2026 Capital Gains Tax Family Dynamics Probate Avoidance
> \$22.4 Million	Traditional Estate Tax Avoidance Techniques How to Handle Possible Sunset in 2026 Capital Gains Tax Family Dynamics Probate Avoidance

## Big News for Retirement Plans: Cutbacks NOT Enacted

- Proposals to severely limit 401(k) contributions and overall total contributions NOT enacted
- Familiar plan designs still alive and well
  - 2018 401(k) \$18,500 + \$6,000 catch up (>age 49)
  - 2018 DC combined contributions \$55,000/\$61,000
  - Add Cash Balance plan additional \$150,000+
  - ESOP still available as a strategic solution

## QCD from IRA More Valuable

- Increase in standard deduction will reduce or eliminate the tax benefit from charitable contributions
- ALL taxpayers age 70½ should make all charitable contributions via Qualified Charitable Distributions
  - Distribution from IRA directly to charity
  - \$100,000/year max per taxpayer
  - No reporting on individual tax return
  - Credited against minimum distribution requirements
  - Reduces AGI for Social Security taxation
  - Reduces AGI for Medicare B & D premiums

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## Roth IRA Recharacterizations Gone

- Prior law: conversion of traditional IRA to Roth IRA could be unwound (recharacterized) until October 15<sup>th</sup> of following year
  - unique tax loophole of getting a free do-over of an otherwise completed taxable transaction
- Effective for conversions January 1, 2018 or later recharacterization option is repealed
- Note: conversion of traditional pre-tax retirement & IRAs (deductible & non-deductible) to Roth is still OK

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## Tax Breaks for All Businesses

C-corporations: Federal tax rate for 1.6M C-corps permanently reduced 40% (from 35% to 21%)

- 10 year “cost” to U.S.Treasury \$1.4T

All other businesses: Temporary (2018-2025) 20% tax deduction for 35.3M owners of profitable “pass-through” entities (§199A)

- Sole Proprietors (1040 Schedule C)
- Partners (1065 K-1)
- S-Corp shareholders (1120S K-1)
- Owners of LLCs taxed as any of these 3
- 10 year “cost” to U.S.Treasury \$415B

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## §199A Deduction

### **New Internal Revenue Code §199A creates:**

- an income tax deduction
- taken on the personal tax return (Form 1040\*)
- of an **owner** of a pass-through entity
- equal to 20% of the Qualified Business Income (QBI) passing through

### **Deduction is taken:**

- After all other items of income and deduction
- After standard or itemized deductions
- Last adjustment before applying tax rate tables

\* Form 1041 in the case of an Estate or Trust

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## 3 Limitations on the 20% Deduction

1. Can't exceed 20% of taxable income
2. If taxable income "too high" will be subject to a wage & property limitation on the deduction
3. If taxable income "too high" AND in a "specified service trade or business" §199A deduction is lost entirely

"Too High" > \$315,000 MFJ, \$157,500 Others

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## Questions?

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# §199A 20% QBI Deduction for Small Business Owners

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