The RFB CPA Group, PLLC

Certified Public Accountants & Consultants

December 15, 2018

Dear Clients:

2018 has been a year of tremendous change in the taxation of all types of entities due to the massive new tax legislation enacted late last year. This Letter is devoted to this new tax legislation.

The changes to the tax law relating to both individual tax provisions and estate tax provisions are temporary and expire after 2025 unless made permanent by Congress. The tax provisions will revert automatically to the rules that were in effect for 2017. The changes to the corporate tax provisions however are permanent.

The tax legislation is hundreds of pages, and we will give you the highlights. We work entirely for you, our clients. We trust you will find our summary of the new law helpful. Please don't hesitate to call or send us an e-mail if you have questions.

Very truly yours,

The RFB CPA Group, PLLC

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PERSONAL TAXES

Standard deductions have almost doubled to $24,00 for couples, $12,000 for singles and $18,000 for heads of households. Seniors age 65 and up and blind people get $1,300 more per person ($1,600 if unmarried). Based on these increases, far fewer people will itemize.

The new law reduces or eliminates many deductions claimed by individuals:

Personal exemptions for individual filers and their dependents are repealed.

Home mortgage interest deductions have been reduced. Interest can be deducted on up to $750,000 of new acquisition debt on a primary and second residence; down form $1 million. The new limit generally applies to mortgage debt incurred after December 14, 2017. Older loans and refinancing's up to the old loan amount; get the $1 million cap. No write-off is allowed after 2017 for interest on existing or new home equity loans from which the proceeds are used to buy a car, pay down credit card debt and other similar items.

State and local tax deductions have been limited. You can deduct any combination of residential property taxes and income or sales taxes up to a $10,000 cap. Property taxes remain fully deductible for taxpayers in a business or for-profit activity, so taxes paid on rental realty can be taken in full on Schedule E.

Several other write-offs have been eliminated as follows:

- Deductions for job related moves except for the military;
- All miscellaneous write-offs subject to the 2% of AGI threshold, including employee business expenses, tax return preparation costs, hobby expenses, and brokerage and IRA fees.
- Theft losses;
- Alimony for post 2018 divorce instruments (recipients won't be taxed on such alimony they receive);
- Personal casualty losses except for casualty losses that are incurred in presidentially declared disaster areas.

Charitable contribution write-off is preserved, with some changes. The AGI limitation on cash donations to qualified charities is increased from 50% to 60%, However, gifts to colleges in exchange for choice seating rights at athletic events are eliminated.

Medical expense deduction has been increased. The AGI threshold for deducting 2017 and 2018 medical expenses on Schedule A has been lowered from 10% to 7.5%.

The write-off for personal gambling losses to the extent of winnings is unchanged.

The phaseout of itemized deductions has been eliminated.

Obamacare's individual mandate has been repealed for post 2018 years. It continues to apply for 2018.

Tax Brackets – the new law keeps seven tax brackets, but with different rates and break points. For example, the top individual rate is lowered from 39.6% to 37%, but that rate kicks in at a higher income level. Whatever new bracket you fall into, more of your taxable income will be hit with lower rates than before.

Inflation indexing of income tax brackets and various tax breaks is altered. Tax brackets, standard deductions and many other items are now adjusted annually using a chained consumer price index, resulting in lower inflation adjustments and thus small annual increases than with the pre-2018 index. Unless changed, this could result in higher taxes in the future. Call us for a further discussion of the new tax brackets and how they will affect you.

Tax rates on long-term capital gains and qualified dividends do not change. However, before 2018, the capital gain and dividend rate depended on your tax bracket. With the new bracket changes, Congress decided to set income thresholds instead.

- 0% rate – applied to taxable income up to $38,600 on single-filed returns and $77,200 on joint filers;
- 15% - applied to taxable incomes between $38,600 - $428,800 on single-filed returns, and $77,200 - $479,000 for joint filers;
- 20% - applied to taxable income over $428,800 on single-filed returns, and $479,000 for joint filers;
- The 3.8% surtax on net investment income remains and applies to single filers with modified AGI over $200,000; $250,000 for joint filers.

Minimum tax – the individual alternative minimum tax remains but higher exemptions; $109,400 for joint return filers and $70,300 for singles and head of households. Additionally, the exemption phaseout starts at much higher income levels which are above $1 million for couples and $500,000 for singe filers and head of households.

Tax credits

- The child tax credit is doubled to $2,000 for each dependent under age 17, with up to $1,400 of the credit refundable to lower income taxpayers. The income phaseout thresholds are much higher; AGI over $400,000 for joint filers, and $200,000 for all other filers. Each child must have a social security number.
- There is a new $500 credit for each dependent who is not a qualifying child including for example an elderly parent you take care of or a disabled adult child. It's nonrefundable and phases out under the same thresholds as the child credit.

Kiddie tax – has been modified so that unearned income of children under 18 is taxed at the ordinary income and capital gains rates applicable to trusts and estates, and not at their parents' marginal tax rate.

IRA's and other savings plans – generally the tax benefits have not been curtailed, however, the new law bars IRA owners who convert their traditional IRAs into Roth IRAs from later undoing the conversion and recovering the income tax paid on the switch.

529 college savings plans have been improved to allow annual distributions of up to $10,000 per student to pay tuition for elementary and secondary education. Make sure to check with your specific state to see if they follow the federal law on this change.

Write-off of business losses – this write-off has been capped at $500,000 for joint filers and $250,000 for other filers, with any excess losses carried forward. This limitation applies after application of the current passive activity loss rules.

ESTATES & TRUSTS

Estates - Congress has doubled the lifetime estate and gift tax exemption to $11,180,000. The rate remains at 40%. The annual gift tax exclusion for 2018 is $15,000 per donee. There's no change in the asset basis step-up for heirs of estates of any size.

Estates & Trusts - The income tax rates and brackets for trusts and estates have been revised.

If income of an estate or trust is:

- Not over $2,550 the tax is 10% of taxable income;
- Over $2,550 but less than $9,150 the tax is $255 plus 24% of excess over $2,550;
- Over $9,150 but less than $12,500 the tax is $1,839 plus 35% of excess over $9,150;
- Over $12,500 the tax is $3,012 plus 37% of excess over $12,500.

EXEMPT GROUPS

Exempt organizations are now required to include in unrelated business taxable income the value of employer-provided employee transportation and parking benefits.

BUSINESS TAXES

The new law has dramatically changed the taxation of businesses of all sizes.

C-corporations

- The tax rate is now a flat 21% down from the previous top rate of 35%. This lower rate began in 2018 and is permanent;
- The Corporate AMT was eliminated.

Pass-through's

- Many individual owners of pass-through firms get a new 20% deduction of qualified business income. The rules cover sole proprietors and owners of S corporations, partnerships and LLCs, REIT shareholders and partners in publicly traded partnerships.
- There are numerous limits and restrictions on this new deduction. These provisions are among some of the most complex in the new law. For example, two limits apply to individuals with higher taxable

incomes in excess of $315,000 for joint returns and $157,500 for all other filers. First, the deduction phases out for thee high-income taxpayers in certain service fields. They include health, law, accounting, actuarial science, performing arts, consulting, athletics, financial, brokerage, investment management and securities trading. Second, there is now a W-2 wages-paid limitation for high income individuals that applies even if the person isn't engaged in a specified service business.

Enhanced write-offs for business asset purchases

- 100% bonus depreciation for many assets put into service after September 27, 2017, and is temporary through 2022 and then phasing out 20% annually thereafter;
- The section 179 deduction for expensing business assets doubled to $1,000,000;
- More property is eligible for bonus depreciation;
- Depreciation limitations on passenger automobiles are increased.

Interest deduction is capped at 30% of adjusted taxable income, with disallowed interest carried forward. Firms with $25 million or less of gross receipts, real estate companies and certain regulated public utilities are exempt from this rule.

Other business deductions are eliminated or scaled back

- Business entertainment;
- Country club dues;
- The 9% domestic production deduction;
- Net operating losses can offset only 80% of taxable income and NOL carrybacks are generally prohibited;
- Tax deferred like kind exchanges are limited to real property not held primarily for sale;
- Sexual harassment settlement payments are not deductible if accompanied by a nondisclosure agreement;
- Meals in on premises dining facilities are limited to 50% through 2025 after which the deduction is eliminated;
- The deduction for the cost of transportation related fringe benefits for workers is disallowed. Employees can still use pretax money for parking and transit passes, but not biking.

Paid family or medical leave – firms entitled to a new credit equal to 12.5% of the amount of wages paid during the period of leave for 2018 and 2019.

Section 965 repatriation tax – this is a new tax on multinational corporations and 10% or more US shareholders of controlled foreign corporations (CFC) which imposes a one-time tax on previously untaxed accumulated overseas earnings at December 31, 2017 regardless of whether any amount is distributed to the shareholder. The rate is 15.5% on foreign cash and liquid assets and 8% on other reinvested profits. Taxpayers may elect to pay this tax over an 8-year period, interest free. (CFC's include corporations and flowthrough entities).

S corporations, but not partnerships or sole proprietorships, (where the S corporation owns the 10% or more) can elect to defer the repatriation tax liability unless a specified triggering event occurs as described in the law.

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<u>GILTI Tax</u> – The new law requires that 10% or more US shareholders of CFC's include in currently taxable income "global intangible low-taxed income" (GILTI), effective with the CFC's first tax year beginning after December 31, 2017, regardless of whether any amount is distributed to the shareholder. GILTI applies to both corporations and flowthrough entities as CFC US shareholders. There are numerous rules and regulations that affect this computation that cannot be described in this highlight summary of the new law.

There are hundreds of pages of other provisions and changes contained in the new tax law – those noted above are highlights and have only just touched the surface. We trust that you have found this summary helpful.

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