MONEY TALKS

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# Trump Tax Plan

**EDITORIAL**

This entire newsletter is devoted to the "Tax Cuts and Jobs Act," also known as the "Trump Tax Plan," that provides the biggest change in the tax code in 40 years. I will discuss the key tax changes and their impact on individuals and businesses.

Many individual taxpayers will pay less in federal income taxes in 2018 compared to 2017. Many taxpayers will have at least an additional $1,000 in their bank accounts in 2018 as a result of the reduction in tax rates and the increase in the standard deduction.

*Some individuals might not have any changes in the income tax they pay, or they might pay more as a result of the elimination of the deductions for State and local taxes, miscellaneous deductions and casualty losses.*

Virtually all *business owners* will benefit from this tax plan.

For the first time in 20 years corporate multinational public companies based in the USA will start paying income taxes in the USA. It is about time. In years past many small businesses paid more income taxes on a percentage basis than USA-based multinationals did. The Trump Tax Plan provides incentives to pay corporate income in the USA as a result of three key provisions that become effective in 2018:

- Reduction in the top corporate rate from 35 percent to a 21 percent flat rate.
- Repatriation of overseas assets that will be taxed at 15.5 % -- down from 35 %.
- Expensing of new and used fixed asset purchases (such as equipment, furniture, vehicles, and computers) at a full 100 percent against taxable income (compared to a rate of 50 percent in 2017).

These incentives will reduce the federal debt by increasing income to the federal treasury. Businesses now can invest more money in increasing their revenue and profits. Higher revenue and profits mean that they will be paying more taxes in dollar terms while the percentage of taxes they pay will decrease. In other words, the pie is getting bigger; the US treasury may be getting a smaller *percentage* of corporate revenue, but it will be getting that percentage from a bigger base.

<u>Some experts disagree with the new corporate tax rates; they think they are too low. These experts do not seem to understand that a company that never paid income taxes in the USA before will now be paying income taxes. This definitely means more revenue for the US treasury.</u>

***The Trump Tax Plan is complicated and there are no golden rules to apply, but overall this tax plan gets an A+ from me. The complexities of the tax law may produce technical corrections later that may produce nega-***

# Individual Taxpayers and the Tax Cuts and Jobs Act

## Tax Rates

There is an overall reduction in tax rates of about three percent for each tax bracket. See page 4 for the new tax rates for 2018. The long-term capital gains rate is retained at 15 percent and 20 percent (the 20 percent rate starts at taxable income levels of $425,800 to $479,000 depending on filing status).

*Other Deductions from Adjusted Gross Income (AGI)*

Health Savings Accounts (HSAs). This deduction has been retained.

Alimony. Payments to spouses no longer are deductible; payments received by spouses no longer are included as income. This is generally effective for divorces after 12/31/18.

Moving Expenses. These are no longer deductible except by members of the Armed Forces.

Individual Retirement Accounts (IRAs). IRA deductions are allowed, but there is a major trap in the new law regarding IRA to Roth IRA conversions (recharacterization).

Educators' Classroom Expenses. These have been retained.

*Itemized Deductions, Standard Deduction, and Personal Exemptions*

The following changes in *Itemized deductions* take effect in 2018:

Medical Expenses. This deduction has been retained; it is available to all taxpayers. Deductions are allowed for all medical expenses in excess of 7.5 percent of income; the prior excess percentage was 10 percent.

Taxes. This is limited to $10,000 for State and local income taxes, sales tax, and property taxes. Note: The limit on the deduction for taxes may have a negative effect on some taxpayers, especially those that live in high tax states. It is possible that these taxpayers may pay more federal income taxes for 2018 than they did for 2017

Mortgage Interest. This has been retained for the most part. However, the maximum mortgage amount that is deductible is limited to $750,000 for 2018, down from $1,000,000. Interest paid on home equity loans no longer is deductible in 2018.

Charitable Contributions. This deduction has been retained.

Casualty Losses. This deduction now is available only for losses resulting from a "qualified disaster," which is an incident that the President of the United States has declared as a disaster.

Miscellaneous Deductions. These deductions (which include employees' business expenses, investment fees, tax preparation fees, and union dues) no longer are available.

Gambling Losses. This deduction has been retained; the deductible amount is limited to the amount of gambling winnings.

The *standard deduction* has been increased – it has virtually doubled to $24,000 for married taxpayers and $12,000 for individuals.

*Personal exemptions* are no longer allowed, but see below for some good news.

*Child Tax Credit, Estate and Gift, and AMT*

The $2,000 Child Tax Credit. This has been expanded. This credit is expanded to a modified Adjusted Gross Income of $400,000 or less for married taxpayers and $200,000 or less for single taxpayers. This is an increase from $110,000 for married taxpayers and $75,000 for single taxpayers. The maximum refundable amount is $1,400.

The Estate and Gift Taxes. The exemption has been increased from $5,000,000 to $10,000,000 in 2018.

Alternative Minimum Tax (AMT). The Act offers some relief. The AMT exemption is increased in 2018 to $109,400 for married taxpayers and $70,300 for single taxpayers.

# Business Taxes and the Tax Cuts and Jobs Act

## Introduction

The Trump Tax Plan makes great changes that will reduce business income taxes and increase a business's cash flow. Key changes driving the lower taxes include the ability to expense fixed asset purchases, the deductions for business pass-through entities, and preserving the cash method of accounting.

*C Corporations*
A change that affects C-Corporations (C-Corps) is the reduction of the top corporate income tax rate from 35 percent to 21 percent. A C-Corp pays its own income taxes and does not pass through income or loss to the owners to be included on their personal returns. This appears to be an option that some pass-through entities (such as partnerships, LLCs, S-Corps) might consider. However, changing from a pass-through entity to a Corp is risky and will reduce your cash flow in the short run and the long run.

Some business owners might look at this 21 percent rate and compare that to their federal personal income tax rate of 34 percent thinking that they could save money. The key item that they miss is that it is necessary to pay a reasonable salary to the business owner to get this 21 percent rate, Therefore, after paying themselves a reasonable salary at the 22 percent personal tax rate, the combined tax rate is 43 percent which is 9 percentage points higher than their original 34 percent rate. There also is the double taxation on the sale of the business as a C-Corp. Becoming a C-Corp may be a profitable option for only approximately 5 percent of all small businesses.

*Depreciation*
Bonus Depreciation. This is increased from 50 percent to 100 percent effective September 27, 2017. This depreciation applies to new and used property; all leasehold improvements are eligible. There is no limit in the amount of bonus depreciation you can take. However, it is important to remember that bonus depreciation may create a loss in a pass-through business, and you can only take that loss if you have basis.

Section 179 Depreciation. This has been expanded. The immediate expensing of fixed assets is increased from $500,000 to $1 million. Non-residential improvements such as roofs, HVAC systems, and alarm systems are included now.

***New Business Pass-Through Entities Income Deduction.***
**The Act allows business owners of pass-through entities such as S-Corporations, Partnerships, Sole Proprietors, and LLCs to deduct 20 percent of qualified business income from the income on their individual income tax returns. The deduction for *nonprofessional* service businesses with taxable income of less than $315,000 for married couples filing jointly and $157,500 for single taxpayers. Taxpayers whose taxable income exceeds these amounts are limited to a percentage of W-2 wages above the $315,000 amount. Professional service businesses (health, legal, financial, accounting, and consulting businesses) may deduct 20 percent of the business's income up to $315,000 for married filers and $157,500 for single filers with a further amount limited up to $415,000.**

*Accounting Methods*
Cash Method. This has been expanded. Taxpayers may use the cash method of accounting if their sales do not exceed $25 million. The previous limit was $1 million.

Inventories and Capitalization Rules. This has been expanded to allow taxpayers the option of expensing inventories if their sales are under $25 million. The capitalization rules of allocating some overhead costs to inventory will not apply to businesses with sales under $25 million.

*Other Items*
Net Operating Losses. This has been diminished. Net operating losses no longer may be carried back to prior years to get tax refunds. Net operating losses may be carried forward indefinitely.

Domestic Production Activities. This has been eliminated effective for the 2018 tax year.

Business Losses. This will be limited beginning in 2018 when business losses from pass- through entities will be limited to a total of $500,000 for married taxpayers and $250,000 for single taxpayers. Business losses in excess of these amounts may be carried forward to future years to offset income.

## 2018 TAX BRACKETS

### MARRIEDS

| Taxable Income Is | The Tax Is |
|---|---|
| No More Than $19,050 | 10% of taxable income |
| Over $19,050 but not more than $77,400 | $1,905 + 12% of excess over $19,050 |
| Over $77,400 but not more than $165,000 | $8,907 + 22% of excess over $77,400 |
| Over $165,000 but not more than $315,000 | $28,179 + 24% of excess over $165,000 |
| Over $315,000 but not more than $400,000 | $64,179 + 32% of excess over $315,000 |
| Over $400,000 but not more than $600,000 | $91,379 + 35% of excess over $400,000 |
| Over $600,000 | $161,379 + 37% of excess over $600,000 |

### SINGLES

| Taxable Income Is | The Tax Is |
|---|---|
| No More Than $9,525 | 10% of taxable income |
| Over $9,525 but not more than $38,700 | $953 + 12% of excess over $9,525 |
| Over $38,700 but not more than $82,500 | $4,454 + 22% of excess over $38,700 |
| Over $82,500 but not more than $157,500 | $14,090 + 24% of excess over $82,500 |
| Over $157,500 but not more than $200,000 | $32,090 + 32% of excess over $157,500 |
| Over $200,000 but not more than $500,000 | $45,690 + 35% of excess over $200,000 |
| Over $500,000 | $150,690 + 37% of excess over $500,000 |

### HEAD OF HOUSEHOLDS

| Taxable Income Is | The Tax Is |
|---|---|
| No More Than $13,600 | 10% of taxable income |
| Over $13,600 but not more than $51,800 | $1,360 + 12% of excess over $13,600 |
| Over $51,800 but not more than $82,500 | $5,944 + 22% of excess over $51,800 |
| Over $82,500 but not more than $157,500 | $12,698 + 24% of excess over $82,500 |
| Over $157,500 but not more than $200,00 | $30,698 + 32% of excess over $157,500 |
| Over $200,000 but not more than $500,000 | $44,298 + 35% of excess over $200,000 |
| Over $500,000 | $149,298 + 37% of excess over $500,000 |



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