Tax Cuts and Jobs Act of 2017—Individual Tax Provisions

By Robert E. Ward*

Robert E. Ward summarizes the individual tax provisions of the recently enacted Tax Cuts and Jobs Act of 2018.

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A. Reduction and Simplification of Rates

Act Section 11001: Modification of Rates

The Act temporarily replaces the existing individual income taxable rate structure with a rate structure as follows:

The Act repeals the "Kiddie Tax" and, instead, computes the tax on a child's unearned passive income above $2,100 by applying the ordinary income and capital gains tax rates for estate and trusts (*see* Chart 1), rather than the marginal tax rate of the child's parent.

Effective Date: Taxable years beginning after December 31, 2017.

Code Sections Affected: Code Secs. 1 and 1250 amended.

Sunset Date: Taxable years beginning after December 31, 2025.

Act Section 11002: Inflation Adjustments Based on Chained CPI

The Act changes the computation of inflation adjustments. The Department of Labor is required to use the Chained Consumer Price Index for All Urban Consumers ("C-CPI-U"), instead of the Consumer Price Index for All Urban Consumers.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 1 by adding subsection 1(j).

Sunset Date: None.

Act Section 11021: Increase in Standard Deduction

The Act temporarily increases the basic standard deduction for individuals across all filing categories. The new provision increases the basic standard deduction from $6,350 to $12,000 for single individuals and married individuals filing separate returns, from $12,700 to $24,000 for married individuals filing jointly and certain surviving spouses, and from $9,350 to $18,000 for head of household filers. The amounts will be subject to inflation adjustments starting in 2019.

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CHART 1

IF TAXABLE INCOME IS:	THEN INCOME TAX EQUALS:
Single Individuals	
Not over $9,525	10% of the taxable income
Over $9,525 but not over $38,700	$952.50 plus 12% of the excess over $9,525
Over $38,700 but not over $82,500	$4,453.50 plus 22% of the excess over $38,700
Over $82,500 but not over $157,500	$14,089.50 plus 24% of the excess over $82,500
Over $157,500 but not over $200,000	$32,089.50 plus 32% of the excess over $157,500
Over $200,000 but not over $500,000	$45,689.50 plus 35% of the excess over $200,000
Over $500,000	$150,689.50 plus 37% of the excess over $500,000
Heads of Households	
Not over $13,600	10% of the taxable income
Over $13,600 but not over $51,800	$1,360 plus 12% of the excess over $13,600
Over $51,800 but not over $82,500	$5,944 plus 22% of the excess over $51,800
Over $82,500 but not over $157,500	$12,698 plus 24% of the excess over $82,500
Over $157,500 but not over $200,000	$30,698 plus 32% of the excess over $157,500
Over $200,000 but not over $500,000	$44,298 plus 35% of the excess over $200,000
Over $500,000	$149,298 plus 37% of the excess over $500,000
Married Individuals Filing Joint Returns and Surviving Spouses	
Not over $19,050	10% of the taxable income
Over $19,050 but not over $77,400	$1,905 plus 12% of the excess over $19,050
Over $77,400 but not over $165,000	$8,907 plus 22% of the excess over $77,400
Over $165,000 but not over $315,000	$28,179 plus 24% of the excess over $165,000
Over $315,000 but not over $400,000	$64,179 plus 32% of the excess over $315,000
Over $400,000 but not over $600,000	$91,379 plus 35% of the excess over $400,000
Over $600,000	$161,379 plus 37% of the excess over $600,000
Married Individuals Filing Separate Returns	
Not over $9,525	10% of the taxable income
Over $9,525 but not over $38,700	$952.50 plus 12% of the excess over $9,525
Over $38,700 but not over $82,500	$4,453.50 plus 22% of the excess over $38,700
Over $82,500 but not over $157,500	$14,089.50 plus 24% of the excess over $82,500
Over $157,500 but not over $200,000	$32,089.50 plus 32% of the excess over $157,500
Over $200,000 but not over $300,000	$45,689.50 plus 35% of the excess over $200,000
Over $300,000	$80,689.50 plus 37% of the excess over $300,000
Estates and Trusts	
Not over $2,550	10% of the taxable income
Over $2,550 but not over $9,150	$255 plus 24% of the excess over $2,550
Over $9,150 but not over $12,500	$1,839 plus 35% of the excess over $9,150
Over $12,500	$3,011.50 plus 37% of the excess over $12,500

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The additional deduction for taxpayers who are over age 65 or blind under Code Sec. 63(f) has been retained.

Planning Implications: For many taxpayers it may be possible to finesse the use of the standard deduction by bunching charitable contributions (and perhaps other deductible expenses) in alternate years. For example, instead of making significant charitable contributions at the end of 2018, those contributions might be deferred until January 2019. The strategy of combining charitable contributions made each year into January and December of every other year allows organizations to still benefit from the support of their donors while enabling the donors to maximize the tax benefit of contributions. This strategy can be further facilitated through the use of donor advised funds or private foundations. These organizations enable a donor to "prepay" charitable contributions by making the contribution in one year which is then released to charities important to the donor in subsequent years through the donor advised fund or private foundation.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected:

Code Sec. 63 amended by adding subsection 63(c)(7).

Sunset Date: Taxable years beginning after December 31, 2025.

Act Section 11041: Suspension of Deduction for Personal Exemptions

The Act eliminates the ability of a taxpayer to take a personal exemption for each taxpayer and dependent claimed on the taxpayer's return. Prior law allowed each taxpayer to deduct $4,050 per person claimed on the taxpayer's return. Further, the Act modifies the filing requirements for income tax returns through an increase in the standard deduction. The following individuals are required to file income tax returns: (i) individuals with gross income for the taxable year in excess of $12,000; (ii) individuals (including certain surviving spouses) entitled to file a joint income tax return with gross income in excess of $24,000; and (iii) individuals filing as heads of household with a gross income in excess of $18,000.

Effective Date: Taxable years beginning after December 31, 2017.

Code Sections Affected:

Code Secs. 151(d), 642(b)(2)(C), 3402(a)(2), 6012, and 6334(d) amended.

Sunset Date: Taxable years beginning after December 31, 2025.

B. Treatment of Business Income

Act Section 11011: Deduction for Qualified Business Income

Overview

The Act creates new Code Sec. 199A, titled *Qualified Business Income* (QBI), which provides qualifying taxpayers with a 20% deduction against the QBI of passthrough entities owned by the taxpayer (the "199A Deduction").

What types of businesses are eligible for the 199A Deduction? The 20% deduction under Code Sec. 199A is available to owners of any business other than one conducted through a C corporation, including sole proprietorships. Only one type of business activity will not qualify for the 199A Deduction: the business of performing services as an employee is barred from qualification by Code Sec. 199A(b)(d)(1)(B). Any other business activity will qualify including performance of professional services. However, service businesses falling within the definition of "specified service trades or businesses" (SSTBs) are subject to severe limitations which may deny eligibility for the relief provided by Code Sec. 199A.

What income is eligible for the 20% deduction? Only income satisfying the definition of QBI is eligible for the 20% deduction under Code Sec. 199A. QBI includes "qualified REIT dividends" as defined in Code Sec. 199A(e)(3) and "qualified publicly traded partnership income" as defined in Code Sec. 199A(e)(5). However, the most commonly encountered type of income subject to relief will be the net amount of items of income, gain, deduction, and loss effectively connected with the conduct of a U.S. trade or business within the meaning of Code Sec. 864(c). Expressly excluded from QBI are:

- Short- and long-term capital gains and losses,
- Dividends and dividend equivalents,
- Interest income other than interest income properly allocable to a trade or business,
- Income from commodities, transactions, and foreign currency gains described in Code Sec. 954(c)(1)(C) and (D),
- Income from notional principal contracts taken into account under Code Sec. 954(c)(1)(F), subject to certain modifications,
- Annuity income, and
- Items of deduction or loss properly allocable to the preceding items.

What restrictions exist on the 199A Deduction? Taxpayers who own any type of business entity other than C corporations, including sole proprietorships ("passthrough entities") are eligible for the 20% deduction under Code Sec. 199A. There are two filters which restrict the deduction. The first is the taxable income of the taxpayer. The second is the W-2 wage income of the passthrough entity. The second filter only applies to taxpayers caught by the first filter. The filters are applied to each passthrough entity generating QBI.

The first filter looks at the taxable income of the owner of the passthrough entity. Taxable income for this purpose appears to be the amount shown on 43 of Form 1040. The taxable income limitation is comprised of three tiers.

Tier One. Taxpayers whose taxable income does not exceed $315,000 in the case of married taxpayers filing jointly and $157,500 in the case of all other taxpayers (the "Tier One Amounts") can deduct 20% of the QBI properly allocable to the taxpayer.

Tier Two. For taxpayers whose taxable income exceeds Tier One Amounts but is less than $415,000 in the case of married taxpayers filing jointly and $207,500 in the case of all other taxpayers (the "Tier Two Amounts"), the 199A Deduction is subject to limitations based on capital investments and W-2 wages paid by the passthrough entity generating the QBI (the "W-2 Wage Limitation").

The W-2 Wage Limitation is based on two alternative measurements. The first looks solely to the W-2 wages paid by the passthrough entity in the year in which the deduction arises. If the amount of the deduction (20% of the passthrough entity's QBI) is less than 50% of the W-2 wages paid by that passthrough entity, the owners are entitled to the full deduction. Alternatively, if the potential 199A Deduction exceeds 50% of W-2 wages, a second measurement is available. The amount of W-2 wages taken into account is reduced from 50% to 25% but the amount derived is increased by an amount equal to 2.5% of the unadjusted cost basis of all tangible property used in the trade or business conducted by the passthrough entity which is subject to depreciation under Code Sec. 167. If the amount of the

199A Deduction is less than the combination of 25% of W-2 wages and 2.5% of the passthrough entity's capital investment, the entire 20% deduction is available to the owners of the passthrough entity. If the potential 199A Deduction exceeds both alternative measurements of the W-2 Wage Limitation, the owners of the passthrough entity are allowed a deduction equal to the measurement yielding the largest amount. The excess 199A Deduction is subject to reduction, but is not entirely lost.

In the case of taxpayers whose taxable income is between the Tier One and Tier Two Amounts and whose potential 199A Deduction exceeds the W-2 Wage Limitation, the amount in excess of W-2 Wage Limitation is subject to reduction. The amount of the reduction is determined by the amount by which the taxpayer's taxable income exceeds the Tier One threshold.

Example 1: The taxpayer is a sole proprietor or sole owner of an S corporation with $1 million of QBI. The taxpayer is entitled to a 199A Deduction of $200,000 unless the taxpayer's taxable income exceeds the Tier One Amounts. Assume the taxpayer's taxable income is $167,500 and the taxpayer does not file a joint return. The taxpayer's taxable income exceeds the Tier One Amount by $10,000. Assume further that the passthrough entity paid $300,000 of W-2 wages during the taxable year in which the deduction arises and has very little depreciable property. The W-2 Wage Limitation is $150,000. The amount by which the taxpayer's potential 199A Deduction exceeds the W-2 Wage Limitation is $50,000. This excess amount is subject to reduction by an amount which corresponds to the ratio of (a) the amount by which taxable income of the taxpayer exceeds Tier One Amount to (b) $50,000. The ratio of $10,000 to $50,000 is one-fifth. Consequently, the taxpayer's 199A Deduction is reduced by $10,000 (one-fifth times $50,000) to $190,000.

Tier Three. Tier Three applies to taxpayers whose taxable income is in excess of the Tier Two Amounts. For these taxpayers, the 199A Deduction is limited to the amount of the W-2 Wage Limitation (that is, the greater of the two measurements calculated as described above).

What limitations apply to taxpayers engaged in service trades or businesses? Taxpayers engaged in SSTBs are subject to more stringent limitations on the 199A Deduction.

What is a specified service trade or business?

Code Sec. 199A(d)(2)(A) references Code Sec. 1202(e)(3)(A) to define the business activities within the scope of *SSTBs*. SSTBs are service businesses in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, investing or investment management, business trading or dealing in securities, partnership interests or commodities as defined in Code Sec. 475(e)(2) and any other "trade or business in which the principal asset of the trade or business is the reputation or skill of one or more of its employees." Expressly excluded from the definition of an SSTB are service businesses in the fields of engineering and architecture.

What limitations are imposed on the 199A Deduction for QBI of an SSTB? As with non-service businesses, owners of passthrough entities engaged in an SSTB whose income does not exceed the Tier One Amounts are entitled to the full section 199A Deduction. Taxpayers whose taxable income exceeds the Tier One Amounts but not the Tier Two Amounts are subject to reduction in the deduction based upon the same ratio computed as described above and illustrated by the example. However, the ratio is applied to the entire amount of the 199A Deduction instead of just the excess of the deduction over the W-2 Wage Limitation.

Example 2: The facts are the same as Example 1 except that the business in which the passthrough entity is engaged is an SSTB. The ratio of the amount by which the taxpayer's taxable income exceeds the Tier One amount ($10,000) to $50,000 is applied to the entire potential 199A Deduction resulting in a diminished deduction of $160,000 ($200,000 – 1/5 × $200,000).

What if the taxpayer is not the only owner of the passthrough entity? In the case of taxpayers who are co-owners of a passthrough entity, items of income, gain, deduction, and loss are apportioned among the owners based on their allocable shares of each item of income, gain, deduction, and loss. The W-2 wages of the passthrough entity which are taken into account by the owners are their allocable shares of the passthrough entity's wage expenses. In contrast, the owners' allocable shares of the basis of the passthrough entity's tangible depreciable property correspond to their allocable shares of depreciation.

Planning Opportunity. The first filter for the 20% deduction under Code Sec. 199A looks to the taxable income of the owner of the passthrough entity. Consequently, traditional strategies utilized to reduce taxable income may reduce taxable income from Tier Two and Tier Three levels to not exceed the Tier One Amounts: deferring income, increasing deductions taken to arrive at taxable income, and use of an increased gift and generation-skipping transfer tax ("GSTT") exemption to transfer assets which produce

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income to other family members. Similarly, for taxpayers whose taxable income exceeds the Tier One Amounts, reduction (and perhaps elimination in the case of owners of SSTBs) of the 199A Deduction can be avoided by hiring additional personnel or increasing the pass-through's investments in tangible depreciable property in order to increase the amount of the W-2 Wage Limitation. In the case of passthrough entities taxable as partnerships, the amount of W-2 wages may be increased by converting the partnership to an S corporation. The guaranteed payments made to the partners are not W-2 wages. Conversion to an S corporation paying amounts equivalent to the guaranteed payments as W-2 wages increases the W-2 Wage Limitation, thereby reducing reduction of the 199A Deduction in the case of taxpayers whose taxable income exceeds Tier One and Tier Two Amounts.

The more stringent limitations imposed on SSTBs may require reorganization of those entities into service and non-service businesses. Spinning off non-service business activities into separate passthrough entities enables the non-service activity to qualify for a portion of the 199A Deduction even if the taxable income of the owners reaches Tier Three levels. In the case of a purely service SSTB, bifurcation of the SSTB into two separate entities may enable the creation of a non-service business.

> **Example 3:** The taxable income of each physician who is a partner in a medical services partnership exceeds the Tier Three Amounts. *In lieu* of forfeiting the 199A Deduction, the physicians set up an S corporation which employs the non-professional staff of the medical services partnership. The Receptionist and other personnel engaged in IT support, secretarial services, marketing, document management (including secure file storage), and other services in support of the medical SSTB are employed by NewCo. The medical services partnership pays an arm's-length amount to NewCo for the services provided by NewCo's personnel. Only that portion of the 199A Deduction realized from NewCo which exceeds the W-2 Wage Limitation will be subject to reduction in the case of those owners of NewCo whose taxable income exceeds the Tier One (but not Tier Two) Amounts. For those owners whose taxable income exceeds the Tier Two Amounts, the entire 199A Deduction is reduced, but not eliminated.

Coordination with AMT

For alternative minimum tax purposes, QBI is determined without regard to any adjustments, items of tax preference, the disallowance of certain losses, or certain calculation provisions found in Code Sec. 59.

Applicability of Accuracy-Related Penalty

The Act amends Code Sec. 6662(d)(1) by adding a new sub-paragraph (C) which lowers the threshold for application of accuracy-related penalty for substantial understatements from 10% of the tax required to be shown on the return to 5%.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 199A added.

Sunset Date: Taxable years beginning after December 31, 2025.

C. Simplification and Reform of Family and Individual Tax Credits

Act Section 11012: Limitation on Losses for Taxpayers Other Than Corporations

The Act adds new Code Sec. 461(l) (although currently there is no Code Sec. 461(k)) to disallow losses in excess of $250,000 ($500,000 for married taxpayers filing jointly) in any taxable year incurred by non-corporate taxpayers operating trades or businesses. The new Code section replaces the provisions of Code Sec. 461(j) relating to excess farm losses of taxpayers other than C corporations. For partnerships and S corporations, the new rules are applied at the partner or shareholder level for losses from those business interests.

The $250,000-limitation on losses is applied by aggregating the income and expenses of all the taxpayer's active businesses. The $250,000 amount is indexed for inflation. The limitation is applied only after passive losses are taken into account under Code Sec. 469.

Any disallowed losses are carried forward as a net operating loss (NOL) to the following taxable year under the NOL rules of Code Sec. 172, as modified by the Act. NOLs will be deductible against only 80% of the taxpayer's income (*see*

Code Sec. 172(a) as amended by Act section 13302).

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 461 amended by adding subsection 461(l).

Sunset Date: Taxable years beginning after December 31, 2025.

Act Section 11022: Increase in and Modification of Child Tax Credit

The Act adds new Code Sec. 24(h) and increases the child tax credit per qualifying child from $1,000 to $2,000, subject to phase-outs. Further, new Code Sec. 24(h)(5) provides that the child tax credit is refundable up to $1,400, as adjusted for inflation.

The Act also provides a $500 nonrefundable credit for each dependent (who is not a qualifying child). For example, if the taxpayer's child is not a citizen of the United States, the child will not be considered a qualifying child but will be considered a dependent and thus eligible for the $500 nonrefundable credit.

Under prior law, the child tax credit was reduced by $50 for every $1,000 of the taxpayer's adjusted gross income over certain thresholds. The Act increases the thresholds to $400,000 for jointly filed returns and $200,000 for all others returns.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 24 amended by adding subsection 24(h).

Sunset Date: Taxable years beginning after December 31, 2025.

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Act Section 11025: Rollovers to ABLE Programs from 529 Programs

The Act amends prior law to allow rollovers from qualified 529 tuition plans to Achieving a Better Life Experience ("ABLE") accounts. Any amount rolled over from a 529 plan to an ABLE account counts toward the maximum allowable contribution limits applicable to ABLE accounts.

Effective Date: For distributions from 529 Plan after the date of enactment.

Code Section Affected: Code Sec. 529(c)(3)(C) amended.

Sunset Date: Rollovers after December 31, 2025.

Act Section 11031: Treatment of Student Loans Discharged on Account of Death of Disability

The Act modifies the treatment of student loan debt discharges with respect to inclusion in gross income. Under this provision, discharges of student loan debt upon the death or disability of the debtor will be excluded from gross income. Loans eligible for the exclusion include loans made by any organization described in Code Sec. 108(f)(2) (generally, state and federal governments, certain tax-exempt public benefit corporations, and tax-exempt educational institutions) and private education loans from private financial institutions for postsecondary education.

Effective Date: Discharges of student loan debt after December 31, 2017.

Code Section Affected: Code Sec. 108(f) is amended by adding Code Sec. 108(f)(5).

Sunset Date: Discharges after December 31, 2025.

Act Section 11032: 529 Account Funding for Elementary and Secondary Education

This Act expands prior law to provide "qualified higher education expenses" permitted to be funded from 529 Plans include expenses for tuition in connection with enrollment or attendance at an elementary or secondary public, private, or religious school. Distributions for the expanded purposes are limited to $10,000 per year.

Effective Date: Distributions after December 31, 2017.

Code Sections Affected: Code Sec. 529(c) is amended by adding subsection 529(c)(7) and 529(e)(3)(A).

Sunset Date: None.

Act Section 11046: Suspension of Overall Limitation on Itemized Deductions

The Act suspends the overall limitation on itemized deductions. Under prior law, Code Sec. 68 inhibited taxpayers with annual gross income over certain thresholds from taking the full amount of their itemized deductions and imposed either a 3% decrease in itemized deductions or an 80% allowable deduction, whichever is less. Taxpayers (without regard to income) will be entitled to deduct the full amount of their itemized deductions.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 68 temporarily repealed.

Sunset Date: Taxable years beginning after December 31, 2025.

D. Simplification and Reform of Deductions and Exclusions

Act Section 11023: Increased Limitation for Certain Charitable Contributions

The Act increases the amount an individual taxpayer can deduct for charitable contributions in any calendar year from 50% of the taxpayer's charitable contribution base (generally, adjusted gross income) to 60% of the taxpayer's charitable contribution base for gifts to charities described in Code Sec. 170(b)(1)(A) (that is, public charities, private foundations other than nonoperating private foundations, and certain governmental units).

Effective Date: Contributions made in taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 170(b)(1) by adding subsection 170(b)(1)(C).

Sunset Date: Contributions made in taxable years beginning after December 31, 2025.

Act Section 11028: Relief for 2016 Disaster Areas and Distributions from Eligible Retirement Plans

The Act permits the early withdrawal of funds from a qualified individual retirement plan without the payment of 10% early withdrawal tax imposed by Code Sec. 72(t) if the withdrawal is for $100,000 or less and qualifies as a "2016 disaster distribution." This disaster distribution allowance is only permitted for those whose domicile in 2016 was within a Federally declared disaster area and who sustained an economic loss related to such disaster (a "Qualified Disaster-Related Personal Casualty Loss"). Further, the provision allows disaster withdrawals from retirement plans to be repaid within three years of the distribution.

The Act also allows for an increased casualty loss deduction, in addition to the standard deduction, for those in a Federally declared disaster area. This deduction is equal to (a) the taxpayer's net disaster loss plus (b) an amount equal to the difference between (i) 10% of the taxpayer's AGI and (ii) the amount by which the personal casualty losses of the taxpayer exceed personal casualty gains. The term "net disaster loss" is defined as the excess of the Qualified Disaster-Related Personal Casualty Losses of the taxpayer over personal casualty gains as defined in Code Sec. 165(h)(3)(A).

The Act does not change the requirement that a casualty loss must exceed $500 per casualty in order to be deductible.

Effective Date: Taxable years beginning on or after January 1, 2016, and before January 1, 2018.

Code Section Affected: None. Implemented entirely through the Act.

Sunset Date: Taxable years beginning after December 31, 2017.

Act Section 11042: Limitation on Deduction for State and Local Taxes

Under prior law, taxpayers could claim an itemized deduction for all state, local, and foreign real property taxes, state and local personal property taxes, and state, local, and foreign income taxes paid.

The Act imposes a $10,000 ($5,000 in the case of a married individual filing a separate return) cap on the deduction available to individual taxpayers for state and local real property taxes, state and local personal property taxes, and state and local income taxes paid by the taxpayer. Further, the Act prohibits any deduction for foreign real property taxes but does not limit deductions for foreign income taxes (or subject such taxes to the $10,000 cap).

The Act does not limit deductions for state, local, and foreign real or personal property taxes paid or accrued in carrying on a trade or business.

The Act expressly provides that state and local income taxes paid in 2017 for the 2018 tax year will be treated as if paid in 2018.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 164(b) amended by adding subsection 164(b)(6).

Sunset Date: Taxable years beginning after December 31, 2025.

Act Section 11043: Limitation on Deduction for Qualified Residence Interest

Under prior law, taxpayers could deduct qualifying mortgage interest for acquisition indebtedness up to $1 million and interest on home equity debt up to $100,000.

The Act amends the mortgage interest deduction by reducing the acquisition indebtedness threshold from $1 million to $750,000 (or from $500,000 to $375,000 in the case of married taxpayers filing separately). This reduction applies to acquisition indebtedness acquired on or after December 15, 2017. Acquisition indebtedness incurred before December 15, 2017, is grand-fathered.

Home equity indebtedness will no longer be deductible regardless of when incurred.

Effective Date: Taxable years beginning after December 31, 2017. However, mortgage obligations incurred before December 15, 2017, are grand-fathered. Indebtedness incurred before December 15, 2017, will reduce the amount of any subsequent indebtedness eligible for interest deduction under the statue. In order to qualify, the contract must have been executed before December 15, 2017, to close on purchase of a principal residence before January 1, 2018, with actual purchase occurring before April 1, 2018. In the case of refinancing, the refinanced obligation will be treated as being incurred on the date of the original mortgage debt as long as the refinancing proceeds do not exceed the amount of the debt remaining unpaid on the prior mortgage. Generally, the term of the refinancing cannot exceed the term of the initial indebtedness.

Code Section Affected: Code Sec. 163(h)(3) amended by adding subsection 163(h)(3)(F).

Sunset Date: Interest paid in taxable years beginning after December 31, 2025.

Act Section 11044: Modification of Deduction for Personal Casualty Losses

The Act modifies the deduction for personal casualty and theft losses. The Act allows individual taxpayers to deduct casualty or theft losses sustained during the taxable year that are not compensated by insurance only when the loss was attributable to a disaster declared by the President under section 401 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act of 2016 (a "Federally declared disaster area").

Effective Date: Losses incurred in taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 165(h) amended by adding subsection 165(h)(5).

Sunset Date: Losses incurred in taxable years beginning after December 31, 2025.

Act Section 11045: Suspension of Miscellaneous Itemized Deductions

Under prior law, Code Sec. 67 allowed individual taxpayers to claim miscellaneous itemized deductions for any taxable year only to the extent that the aggregate amount of such deductions exceeds 2% of the taxpayer's adjusted gross income for that year.

The Act eliminates all miscellaneous itemized deductions. These include expenses for the production or collection of income, tax preparation fees, unreimbursed job expenses, home office expenses, moving expenses, professional dues, work-related education expenses, professional liability insurance premiums, and tools and supplies purchased for employment.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 67 temporarily repealed.

Sunset Date: Taxable years beginning after December 31, 2025.

Act Section 11047: Suspension of Exclusion for Qualified Bicycle Commuting Reimbursement

The Act temporarily repeals the exclusion for employer paid qualified bicycle commuting reimbursements. Under prior law employees could exclude employer reimbursement for bicycle commuting expenses from both gross income for income tax purposes and wages for employment tax purposes. As a result of the repeal, employer reimbursement for bicycle commuting expenses will be taxable to employees for both income tax and employment tax purposes.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 132(f) amended by adding subsection 132(f)(8).

Sunset Date: Taxable year beginning after December 31, 2025.

Act Section 11048: Suspension of Exclusion for Qualified Moving Expense Reimbursement

The Act temporarily repeals the exclusion available for qualified moving expense reimbursements (that is, amounts deductible under Code Sec. 217 for expenses incurred by a taxpayer to move to a new principal place of work). The only taxpayers who are permitted to exclude moving expense reimbursements are those actively serving in the U.S. armed forces, and who move in connection with a permanent change of station pursuant to a military order.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 132(g) amended.

Sunset Date: Taxable years beginning after December 31, 2025.

Act Section 11049: Suspension of Deduction for Moving Expenses

In addition to temporarily repealing the exclusion for reimbursement of qualified moving expenses, the Act also repeals the deduction by employees or self-employed individuals for moving expenses incurred to move to a new principal place of work. Such expenses will still be deductible by military personnel described above.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 217 amended by adding subsection 217(k).

Sunset Date: Taxable years beginning after December 31, 2025.

Act Section 11050: Expansion of Expenses Deductible Against Gambling Income

The Act clarifies that under Code Sec. 165(d) "losses from wagering transactions" include expenses incurred in connection with the wagering activities (such as travel, room and board, and sustenance). These losses are still subject

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to the Code Sec. 165(d) restriction which permits the deduction of losses only to the extent of the gains from the wagering activities.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 165(d) amended.

Sunset Date: Taxable years beginning after December 31, 2025.

Act Section 11051: Repeal of Deduction for Alimony Payments

The Act repeals the deduction for alimony and separate maintenance payments made by the payor spouse and provides that payments for alimony and separate maintenance are no longer included in the payee spouse's gross income. The Act does not change the Code provisions pertaining to child support.

Effective Date: Effective for any divorce or settlement agreement entered into after December 31, 2018, and any divorce or settlement agreement entered into prior to December 31, 2018, but modified after December 31, 2018.

Code Sections Affected: Code Secs. 61, 71, and 215.

Sunset Date: None.

Act Section 13704: Repeal of Deduction for Amounts Paid in Exchange for College Athletic Event Seating Rights

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The Act repeals the deduction previously available for 80% of certain contributions made by a taxpayer to a college which gave the taxpayer the right to purchase tickets to college sporting events.

Effective Date: Contributions made in taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 170(l) amended.

Sunset Date: None.

E. Savings, Pensions, and Retirement Accounts

Act Section 11024: Increased Contributions to ABLE Accounts

This Act temporarily increases the limitation for contributions to ABLE accounts in the case of certain individuals. The general overall limitation on contributions, the per-donnee annual gift tax exclusion of $10,000 as adjusted for inflation ($14,000 in 2017; $15,000 in 2018), will remain the same. However, once this limitation is reached, an ABLE account's designated beneficiary may contribute an additional amount: up to the lesser of (a) the Federal poverty line for a one-person household or (b) the individual's compensation (as defined in Code Sec. 219(f)(1)) for the taxable year. In order to be eligible for the increased contribution limit, the designated beneficiary cannot be an individual with respect to whom contributions were made to a Code Sec. 414(i) defined contribution plan, a Code Sec. 403(b) annuity, or a Code Sec. 403(b) deferred compensation plan.

The Act also allows a designated beneficiary of an ABLE account to claim the Saver's Credit for contributions made to an ABLE account. Thus, a designated beneficiary of an ABLE account can claim a nonrefundable tax credit, usually reserved for qualified retirement savings account contributions, for up to $2,000 in annual contributions made to an ABLE account. As provided in the Saver's Credit tables, the credit will depend upon the adjusted gross income of the beneficiary. The Saver's Credit is in addition to any deduction or exclusion that would otherwise apply with respect to the contribution.

Effective Date: Taxable years beginning after date of enactment.

Code Section Affected: Text of Code Sec. 529A(b)(2)(B) amended. Subsection 529A(b)(7) added. Code Sec. 25B(d)(1) amended by adding subsection 25B(d)(1)(D).

Sunset Date: Contributions made after December 31, 2025.

Act Section 13611: Repeal of Special Rule Permitting Recharacterization of Roth Conversions

Under prior law, a taxpayer making a contribution to an individual retirement arrangement (either a traditional IRA or Roth IRA) could recharacterize the contribution as one made to the other type of IRA before the due date for the individual's income tax return for that year.

The Act revises the conversion rule so that a taxpayer may no longer reverse a rollover or conversion to a Roth IRA and treat the contribution as made to a traditional IRA. However, recharacterization is still permitted with respect to other contributions. For example, a taxpayer may still make a contribution to a traditional IRA and convert the traditional IRA to a Roth IRA before the due date for the individual's income tax return for that year.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 408A(d)(6)(B) amended by adding subsection 408(d)(6)(B)(iii).

Sunset Date: None.

Act Section 13612: Modification of Rules Applicable to Length of Service Award Plans

Code Sec. 457 governs the taxation of eligible deferred compensation plans of State and local government and private, tax-exempt employers. However, plans paying solely length of service awards to *bona fide* volunteers (or their beneficiaries) on account of qualified services performed by the volunteers are excluded from the rules found in Code Sec. 457(b). For purposes of Code Sec. 457, "qualified services" consist of firefighting and fire prevention services, emergency medical services, and ambulance services.

The Act increases the aggregate amount of length of service awards that may accrue for a *bona fide* volunteer with respect to any year of service from $3,000 to $6,000. The Act also provides for a cost-of-living adjustment to the limit (adjusted in $500 increments) after 2017. Further, the Act provides that if the plan is a defined benefit plan, the limit applies "to the actuarial present value of the aggregate amount of length of service awards accruing with respect to any year of service."

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 457(e) amended.

Sunset Date: None.

Act Section 13613: Extended Rollover Period for Loan Offset Amounts

Employer-sponsored retirement plans (that is, tax qualified retirement plans, Code Sec. 403(b) plans, or governmental Code Sec. 457(b) plans) may provide loans to employees. In certain circumstances, the obligation to repay the loan may be accelerated and the taxpayer's balance in the plan offset by the amount of the unpaid loan. The loan offset amount will be treated as a distribution from the plan at the time of the offset and taxed as though an actual distribution occurred unless the taxpayer rolls over the loan offset amount to another eligible retirement plan.

The Act provides that a "qualified plan loan offset amount" means a plan loan offset amount which is treated as distributed from a qualified employer plan to a participant or beneficiary solely by reason of (1) the termination of the qualified employer plan or (2) the failure to meet the repayment terms of the loan from such plan because of severance from employment by the participant.

The Act extends the period during which a qualified plan loan offset amount may be rolled over to another eligible retirement plan from 60 days from the offset to the due date (including extensions) for filing the Federal income tax return for the taxable year in which the plan loan offset occurs.

Effective Date: Effective for plan loan offset amounts treated as distributed in taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 402(c) amended by adding subsection 402(c)(3).

Sunset Date: None.

F. Modification of Estate, Gift, and Generation-Skipping Transfer Taxes

Act Section 11061: Increase in Estate, Gift, and Generation-Skipping Transfer Tax Exemptions

The Act revises Code Sec. 2010(c)(3) to increase the basic exclusion amount for estates and gifts from $5 million to $10 million. Thus, for 2018, the basic exclusion amount, as indexed for inflation, is increased from $5.6 million to almost $11.2 million. (Because of the change made by section 11002 of the Act in the method for computing inflation adjustments, the 2018 gift, estate, and GSTT exemption amount will be less than $11.2 million.) Because of the way in which the GSTT is computed, the GSTT exemption is also increased in the same amount.

In order to calculate a decedent's federal estate tax liability, post-1976 taxable gifts and the gift taxes paid on those gifts are taken into account. Under prior law, the amount of the gift tax was determined by the gift tax rate in effect for the year which the gift was made. The Act simplifies the computation of the gift tax paid by a decedent by allowing the rate schedule in Code Sec. 2001(c) in effect on the decedent's date of death to be used to calculate the gift tax for all gifts, regardless of when the gift was made.

Planning implications: Because of the temporary nature of the increase in the exclusion amount (or the risk of a reduction by future legislation before 2026), individuals contemplating significant gifts (whether for estate and generation-skipping transfer tax savings or for income shifting benefits) should act quickly.

Planning implications: The increase in the exclusion amount creates a significant opportunity to take advantage

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of the lower income tax rates of certain family members by making gifts of income-producing property.

Planning implications: An increased generation-skipping transfer tax exclusion allows GSTT exclusion to be allocated to trusts which are not fully or even partially exempt.

***Observation*:** Because of the language used in most wills and trusts to fund Bypass/Credit Shelter Trusts, the increase in the basic exclusion amount makes it imperative to review and perhaps amend those documents.

Effective Date: Gifts made and decedents dying after December 31, 2017.

Code Sections Affected: Code Sec. 2010(c)(3) amended by adding subsection 2010(c)(3)(C). Code Sec. 2001(g) amended.

Sunset Date: The increase in the basic exclusion amount reverts to $5 million (subject to inflation adjustments) for gifts made and decedents dying after December 31, 2025.

G. Alternative Minimum Tax

Act Section 12003: Increased Exemption for Individuals

The Act increases the exemption amount and the exemption amount phase-out thresholds for the individual alternative minimum tax for tax years beginning after December 31, 2017. The exemption amount is increased from $78,750 (as adjusted for inflation) to $109,400 for married taxpayers filing jointly (50% of this value for married individuals filing separately) and from $50,600 (as adjusted for inflation) to $70,300 for non-married individuals.

The Act increases the phase-out threshold from $150,000 (as adjusted for inflation) to $1,000,000 for married taxpayers filing jointly (50% of this value for married individuals filing separately). The Act increases the phase-out threshold for non-married taxpayers from $112,500 (as adjusted for inflation) to $500,000.

The Act provides that the exemption amounts and phase-out threshold amounts are to be adjusted for inflation in taxable years beginning after December 31, 2018.

Effective Date: Taxable years beginning after December 31, 2017.

Code Section Affected: Code Sec. 55(d) amended by adding subsection 55(d)(4).

Sunset Date: Taxable years beginning after December 31, 2025.

H. Insurance Reforms

Act Section 13520: Tax Reporting for Life Settlement Transactions

The Act adds new Code Sec. 6050Y which requires every person who acquires a life insurance contract or an interest in a life insurance contract to file an information return with the IRS, with a copy to any person identified in the information return. The information returns must provide information regarding the buyer, seller, terms of sale, and policy sold. In addition, the life insurance company that receives either a notice of a policy sale or a notice that a life insurance contract is being transferred to a foreign person must file an information return with the IRS identifying the seller of the life insurance policy, the policy number, and the seller's investment in the policy being sold.

The Act requires any person who pays reportable death benefits during any taxable year to file an information return with the IRS, with a copy to each person identified in the information return, describing the payor, payee, date the payment was made, and the payor's estimate of the life insurance contract owner's investment in the contract. The term "reportable death benefits" means amounts paid due to the death of the insured under a life insurance contract that has been transferred in a reportable policy sale. A "reportable policy sale" is defined by Code Sec. 101(a)(3)(B) (added by Act section 13522) as "the acquisition of an interest in a life insurance contract, directly or indirectly, if the acquirer has no substantial family, business, or financial relationship with the insured apart from the acquirer's interest in the contract." The term "indirectly" specifically refers to the acquisition of an interest in a partnership, trust, or other entity that holds an interest in a life insurance contract.

Notice 2018-4 describes proposed regulations Treasury and the IRS intend to issue implementing the requirements of new Code Sec. 6050Y. Proposed regulations will require purchasers to furnish written statements to issuers no later than 20 days after a reportable policy sale or five days after expiration of a state law rescission period, but not later than January 15 of the year after the year in which the reportable policy sale occurred. For reportable policy sales and reportable death benefit payments after December 31, 2017, but before publication of final regulations in the Federal Register, proposed regulations will allow additional time to file information returns and required written statements.

Effective Date: Applicable to reportable policy sales occurring and to reportable death benefits paid after December 31, 2017.

Code Section Affected: Code Sec. 6050Y added.

Sunset Date: None.

Act Section 13521: Clarification of Tax Basis of Life Insurance Contracts

In Rev. Rul. 2009-13, the IRS determined that an insured person selling a life insurance contract must reduce the insured's basis in that contract by the cost of insurance. The Act changes this result by providing no adjustment to basis occurs for costs of insurance incurred in life insurance contracts or annuities.

Effective Date: Transactions entered into after August 25, 2009 (the date of Rev. Rul. 2009-13).

***Observation*:** Taxpayers who computed gain on sale of a life insurance contract as required by Rev. Rul. 2009-13 should consider filing a claim for refund.

Code Section Affected: Code Sec. 1016(a)(1) amended.

Sunset Date: None.

Act Section 13522: Exception to Transfer for Valuable Consideration Rules

The Act provides that the exception to the transfer-for-value rules found in Code Sec. 101(a)(2) does not apply to the transfer of a life insurance contract or an interest therein which is a "reportable policy sale," as defined by Code Sec. 101(a)(3)(B) as added by section 13522 of the Act (discussed above).

Effective Date: Transfers occurring after December 31, 2017.

Code Section Affected: Code Sec. 101(a) amended by adding subsection 101(a)(3).

Sunset Date: None.

I. Elimination of Shared Responsibility Payment for Individuals Failing to Maintain Minimal Essential Coverage

Act Section 11081: Elimination of Shared Responsibility Payment for Individuals Failing to Maintain Minimal Essential Coverage

The Act eliminates the penalty for individuals failing to maintain minimum health insurance coverage. Suspension of the health insurance individual mandate will be postponed for one calendar year, thus taking effect for all months beginning after December 31, 2018.

Effective Date: Months beginning after December 31, 2018.

Code Section Affected: Code Sec. 5000A(c) amended.

J. Procedural Issues

Act Section 11071: Extension of Time Limit for Contesting IRS Levy

The Act extends the length of time a taxpayer has to bring a civil action in a district court of the United States seeking a determination the IRS has wrongfully levied the taxpayer's property from nine months to two years from the date of the levy.

Effective Date: For levies made after the date of enactment. The extension also applies to levies made on or before the date of enactment if the nine-month period under Code Sec. 6343(b) has not expired before the date of enactment.

Code Section Affected: Code Secs. 6343(b) and 6532(c) amended.

Sunset Date: None.[1]

ENDNOTES

* This article would not have been possible without the able assistance of other lawyers in the Bethesda office of WardChisholm, P.C.: Richard S. Chisholm, Alison Keller-Micheli, Bridget A. Alzheimer, and Alyson Hoffman.

1 H.R. 1, known as the "Tax Cuts and Jobs Act of 2017" (the "Act"), was passed by the House on December 20, 2017, and by the Senate on December 19, 2017. The Act was signed into law by President Trump on December 22, 2017. The Joint Explanatory Statement of the Committee of Conference released on December 15, 2017 (the "Explanation") explains the provisions of the Act, as well as the differences between the House bill, the Senate amendment, and the Act.

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