December 6, 2018

Dear Client:

As we move into the holiday season, we wanted to thank you for your business and wish you a happy, healthy and prosperous year.

As a reminder, The Tax Cuts and Jobs Act of 2017 (TCJA) is arguably one of the most significant pieces of tax legislation since 1986 when the passive activity rules were implemented. The TCJA eliminated or modified numerous tax provisions starting in 2018.

## Individual Tax Changes

**Personal Exemptions**
Personal exemptions are **eliminated** for tax years 2018 through 2025.

**Standard Deductions**
The standard deduction for married couples filing a **joint return in 2018 is $24,000**. For **singles and married individuals filing separately, it is $12,000**, and for **heads of household, the deduction is $18,000**.

The additional standard deduction for blind people and senior citizens in 2018 is $1,300 for married individuals and $1,600 for singles and heads of household.

**Income Tax Rates**
In 2018 the top tax rate of 37 percent affects individuals whose income exceeds $500,000 ($600,000 for married taxpayers filing a joint return). Marginal tax rates for 2018 are as follows: 10%, 12%, 22%, 24%, 32%, 35%, and 37%. While the tax rate structure remains similar to prior years (i.e., with seven tax brackets), the tax-bracket thresholds increased significantly for each filing status under tax reform.

**Estate and Gift Taxes**
In 2018 there is an exemption of **$11.18 million** per individual for estate, gift, and generation-skipping taxes, with a top tax rate of 40 percent. **The annual exclusion for gifts is $15,000**.

**Alternative Minimum Tax (AMT)**
For 2018, exemption amounts increased to $70,300 for single and head of household filers, $109,400 for married people filing jointly and for qualifying widows or widowers, and $54,700 for married taxpayers filing separately.

**Pease and PEP (Personal Exemption Phaseout)**
Both Pease (limitations on itemized deductions) and PEP (personal exemption phase-out) have been eliminated under TCJA.

**Flexible Spending Account (FSA)**
A Flexible Spending Account (FSA) is limited to $2,650 per year in 2018 (up from $2,600 in 2017) and applies only to salary reduction contributions under a health FSA. The term "taxable year" as it applies to FSAs refers to the plan year of the cafeteria plan, which is typically the period during which salary reduction elections are made.

**Long-Term Capital Gains**
In 2018 tax rates on capital gains and dividends **remain the same as 2017** rates (0%, 15%, and a top rate of 20%); however, threshold amounts are different in that they don't correspond to the tax bracket structure as they did in the past. For example, taxpayers whose income is below $38,600 for single filers and $77,200 for married filing jointly pay 0% capital gains tax. For individuals whose income is at or above $425,800 ($479,000 married filing jointly), the rate for both capital gains and dividends is capped at 20 percent.

**Miscellaneous Deductions**
Miscellaneous deductions exceeding 2% of AGI (adjusted gross income) are eliminated for tax years 2018 through 2025. As such, you can no longer deduct on Schedule A expenses related to tax preparation, moving (except for members of the Armed Forces on active duty who move because of a military order), job hunting, or unreimbursed employee expenses such as tools, supplies, required uniforms, travel, and mileage. Business owners are not affected and can still deduct business-related expenses on Schedule C.

## Tax Credits

**Adoption Credit**
In 2018 a nonrefundable (i.e., only those with tax liability will benefit) credit of up to $13,810 is available for qualified adoption expenses for each eligible child.

**Child and Dependent Care Credit**
The Child and Dependent Care Tax Credit was permanently extended for taxable years starting in 2013 and remained under tax reform. As such, if you pay someone to take care of your dependent (defined as being under the age of 13 at the end of the tax year or incapable of self-care) in order to work or look for work, you may qualify for a credit of **up to $1,050 or 35 percent of $3,000 of eligible expenses**.

For two or more qualifying dependents, you can claim up to 35 percent of $6,000 (or $2,100) of eligible expenses. For higher income earners the credit percentage is reduced, but not below 20 percent, regardless of the amount of adjusted gross income.

**Child Tax Credit and Credit for Other Dependents**
For tax years 2018 through 2025, the **Child Tax Credit increases to $2,000 per child**, up from $1,000 in 2017, thanks to the passage of the TCJA. The refundable portion of the credit increases from $1,000 to $1,400 - 15 percent of earned income above $2,500, up to a maximum of $1,400 - so that even if taxpayers do not owe any tax, they can still claim the credit. Please note, however, that the refundable portion of the credit (also known as the additional child tax credit) applies only when the taxpayer isn't able to fully use the $2,000 nonrefundable credit to offset their tax liability. Under TCJA, a new tax credit - Credit for Other Dependents - is also available for dependents who do not qualify for the Child Tax Credit. The $500 credit is nonrefundable and covers children older than age 17 as well as parents or other qualifying relatives supported by a taxpayer.

**Earned Income Tax Credit (EITC)**
For tax year 2018, the maximum earned income tax credit (EITC) for low and moderate-income workers and working families increased to $6,431 (up from $6,318 in 2017). The maximum income limit for the EITC increased to $54,884 (up from $53,930 in 2017) for married filing jointly. The credit varies by family size, filing status, and other factors, with the maximum credit going to joint filers with three or more qualifying children.
Individuals - Education Expenses

**Coverdell Education Savings Account**
You can contribute up to $2,000 a year to Coverdell savings accounts in 2018. These accounts can be used to **offset the cost of elementary and secondary education**, as well as post-secondary education.

**American Opportunity Tax Credit**
For 2018, the maximum American Opportunity Tax Credit that can be used to offset certain higher education expenses is $2,500 per student, although it is phased out beginning at $160,000 adjusted gross income for joint filers and $80,000 for other filers.

**Lifetime Learning Credit**
A credit of up to $2,000 is available for an unlimited number of years for certain costs of post-secondary or graduate courses or courses to acquire or improve your job skills. For 2018, the modified adjusted gross income threshold at which the Lifetime Learning Credit begins to phase out is $112,000 for joint filers and $56,000 for singles and heads of household.

**Employer-Provided Educational Assistance**
As an employee in 2018, you can exclude up to $5,250 of qualifying postsecondary and graduate education expenses that are reimbursed by your employer.

**Student Loan Interest**
In 2018 you can deduct up to $2,500 in student-loan interest as long as your modified adjusted gross income is less than $65,000 (single) or $135,000 (married filing jointly). The deduction is phased out at higher income levels.
Individuals - Retirement

**Retirement Contribution Limits**

For 2018, the elective deferral (contribution) limit for employees who participate in 401(k), 403(b), most 457 plans, and the federal government's Thrift Savings Plan is $18,500 ($18,000 in 2017). For persons age 50 or older in 2018, the limit is $24,500 ($6,000 catch-up contribution).

**Retirement Savings Contributions Credit (Saver's Credit)**

In 2018, the adjusted gross income limit for the saver's credit for low and moderate-income workers is $63,000 for married couples filing jointly, $47,250 for heads of household, and $31,500 for married individuals filing separately and for singles. The maximum credit amount is $2,000 ($4,000 if married filing jointly). Also of note is that starting in 2018, the Saver's Credit can be taken for your contributions to an ABLE (Achieving a Better Life Experience) account if you're the designated beneficiary. However, keep in mind that your eligible contributions may be reduced by any recent distributions you received from your ABLE account.

## Business Taxes

**Tax Rates**

The final tax bill lowers the maximum corporate tax rate from 35 percent to 21 percent, the lowest since 1939. The United States has one of the highest corporate tax rates in the world. But most corporations don't pay more than 15 percent.

**New 20% deduction for pass-through businesses.**

This is possibly the most complex and contentious aspect of the bill and will require more time and attention to thoroughly sort out for each impacted taxpayer. See our accompanying endnote for further insight on these new rules[i]. The deductions are limited once the income reaches $157,500 for singles and $315,000 for joint. Pass-through businesses include sole proprietorships, partnerships, limited liability companies, and S corporations. They also include real estate companies, hedge funds, and private equity funds, but limitations exist for taxpayers providing primarily professional services.

**Section 179 Expensing and Bonus Depreciation Rules.**

The TJTA allows **businesses to deduct higher levels of depreciable assets** acquired in one year instead of amortizing them over several years. It does not apply to structures with certain exceptions. To qualify, the equipment must be purchased after September 27, 2017, and before January 1, 2023. Up to $1 million in qualified equipment can be written off in a year under section 179. The write off phases-out when purchases exceed $2.5 million in a year.

**Method of Accounting**

The new law generally liberalizes the use of the **cash method of accounting** for businesses with average annual gross receipts under $25 million.

**Net Operating losses (NOLs) may no longer be carried back** by businesses other than farmers. NOL carryforwards are limited to 80% of taxable income.

**Alternative Minimum Tax (AMT)**

The TCJA **eliminates the corporate AMT.** The corporate AMT had a 20 percent tax rate that kicked in if tax credits pushed a firm's effective tax rate below that level. Companies could no longer deduct research and development spending or investments in low-income neighborhood. Elimination of the corporate AMT adds $40 billion to the deficit.

If you have any questions about these and other tax provisions that could affect your tax situation, don't hesitate to call.

Sincerely,

SEIGNEUR GUSTAFSON LLP

Certified Public Accountants and Consultants

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[i] **Pass-through income deduction**

For tax years after 2017 and before 2026, individuals would be allowed to deduct 20% of "qualified business income" from a partnership, S corporation, or sole proprietorship, as well as 20% of qualified real estate investment trust (REIT) dividends, qualified cooperative dividends, and qualified publicly traded partnership income. (Special rules would apply to specified agricultural or horticultural cooperatives.)

A limitation on the deduction would be phased in based on W-2 wages above a threshold amount of taxable income. The deduction would also be disallowed for specified service trades or businesses with income above a threshold.

For these purposes, "qualified business income" would mean the net amount of qualified items of income, gain, deduction, and loss with respect to the qualified trade or business of the taxpayer. These items must be effectively connected with the conduct of a trade or business within the United States. They do not include specified investment-related income, deductions, or losses.

"Qualified business income" would not include an S corporation shareholder's reasonable compensation, guaranteed payments, or—to the extent provided in regulations—payments to a partner who is acting in a capacity other than his or her capacity as a partner.

"Specified service trades or businesses" include any trade or business in the fields of accounting, health, law, consulting, athletics, financial services, brokerage services, or any business where the principal asset of the business is the reputation or skill of one or more of its employees.

The exclusion from the definition of a qualified business for specified service trades or businesses phases in for a taxpayer with taxable income in excess of $157,500 or $315,000 in the case of a joint return.

For each qualified trade or business, the taxpayer is allowed to deduct 20% of the qualified business income with respect to such trade or business. Generally, the deduction is limited to 50% of the W-2 wages paid with respect to the business. Alternatively, capital-intensive businesses may yield a higher benefit under a rule that takes into consideration 25% of wages paid plus a portion of the business's basis in its tangible assets. However, if the taxpayer's income is below the threshold amount, the deductible amount for each qualified trade or business is equal to 20% of the qualified business income with respect to each respective trade or business.