Tax Cuts and Jobs Act

By Bruce A. Rawls November 2017

Yesterday, the Ways and Means Committee Chair, Kevin Brady (R-Tex), released the text of a bill titled "Tax Cuts and Jobs Act" that would make many changes in the Internal Revenue Code.

In terms of items that affect **individuals**, here are some of the major proposed changes:

- There are 4 tax brackets: 12%, 25%, 35% and 39.6%. For married individuals filing jointly, there would effectively be a 0% rate on the first $24,000; from $24,000 - 90,000 would be subject to the 12% rate; from $90,001 - 260,000 would be subject to the 25% rate, above $260,000 - $1,000,000 would be subject to 35% rate, and above $1,000,000 would be subject to the 39.6% rate. If a married couple had wages of $260,000 and no deductions, that translates into an overall tax rate of 19.392% of their *gross* income or 22.585% of their *taxable* income ($260,000 of gross income minus $24,000 standard deduction equals $236,000 of taxable income). For "high income" taxpayers there is a mechanism that is designed to phase out the benefit of the 12% tax bracket by, essentially taxing the amount that would be subject to the 12% rate at the 39.65% rate instead. There is still preferential taxation of net long-term capital gains.

- There is what appears to be a convoluted mechanism that is designed to tax at no more than 25% that portion of the income of "pass-through" entities (partnerships, LLCs, S corporations) which is "business income." So much for tax simplification. Pass-through entities in personal service businesses (doctors, lawyers, accountants, engineers, etc.) are restricted, if not precluded, from the benefits of this provision.

- The standard deduction for a married couple filing jointly is increased to $24,000 (for 2017 the standard deduction for marrieds filing jointly is $12,700) and would be indexed for inflation.

- There are no personal exemptions.

- The following itemized deductions are eliminated - medical expenses, fees for the preparation of tax returns, casualty loss deduction, and the deduction of trade or business expense if the trade or business is that of performing services as an employee.

- A couple of "above the line" deductions are eliminated - the deduction for alimony payments and moving expenses.

- Other itemized deductions are retained. Home mortgage interest is still deductible but is limited to "acquisition" indebtedness on one's principal residence (goodbye home equity lines of credit) and the present $1 million cap is reduced to $500,000 (existing mortgages in excess of the $500,000 cap are grandfathered). Charitable gifts remain deductible and largely unchanged, although a special rule which presently allows a deduction of 80% of the amount paid for the right to buy college football tickets would be repealed.

- In the sensitive area involving state/local property tax and income taxes, the bill does away with the deduction of state/local income taxes, but it allows a deduction for state/local real property taxes, but that deduction is capped at $10,000.

- The present exclusion for up to $500,000 (married filing jointly) of gain from the sale of a principal residence is tightened. To qualify the home must be owned and used as a principal residence for at least 5 years in the 8-year period preceding the sale (currently, it has to be owned and used for 2 years in the 5-year period before the sale). The bill would phase out the $500,000 exclusion ($250,000 for single filers) by the amount the taxpayer's adjusted gross income exceeds $500,000 (or $250,000, as the case may be).

- The estate, gift and generation skipping taxes are scheduled to terminate after the year 2023. In the meantime, as of January 1, 2018, these taxes would basically not apply to married couples transferring less than $20 million (which would be indexed for inflation). Beginning in 2018, the top gift tax rate drops from 40% to 35%. The bill preserves the current rules that re-set the basis of a decedent's assets to fair market value, *i.e*, the "stepped-up basis" rules.

These are some of the major provisions affecting individuals, but these are certainly not the only things. As we work our way through the proposed legislation -- which is sure to change as it proceeds (if it proceeds) -- we will have more to offer.

To discuss this further, please contact:

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