

# Professional Notes

SPRING 2018

TAX & ESTATE PLANNING

## Summary of the Tax Cuts and Jobs Act

### Introduction

In the final weeks of 2017, the House and Senate wrangled and horse-traded their way into a new tax law known as the Tax Cuts and Jobs Act, and the President signed it into law on December 22. One surprising result was that many items slated for elimination somehow survived the political process. For example, despite the broad ambitions of the original House bill, tax-exempt bonds were not eliminated, nor was the so-called Johnson Amendment. That 1954 amendment bans political campaign activity by charities. It was stricken from the proposed legislation by the Senate because it violated the Byrd Rule.<sup>1</sup>

Still, the changes that made it into the tax code were significant, especially in the income and estate tax areas, and long-term reverberations are likely in the charitable sector.

This edition of *Professional Notes* provides a chart summarizing the major changes affecting individuals and trusts and estates, as well as some of the significant changes affecting charities, corporations, and pass-through entities. Future columns will consider the impact of these changes on individuals and charities, and explain how The New York Community Trust can help those considering charitable gifts under the new law.

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<sup>1</sup> The effect of the so-called “Byrd Rule,” named for Senator Robert Byrd of West Virginia, has been to prevent the use of the reconciliation process for provisions that would increase the deficit beyond 10 years after the reconciliation measure or are otherwise “extraneous,” by permitting senators to block such measures. (2 U.S.C. § 644) The removal of such provisions has been described as a “Byrd Bath”; who says the Senate doesn’t have a sense of humor?

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# Professional

	DESCRIPTION	FORMER PROVISION	NEW LAW
INDIVIDUAL	Individual tax rates	Top rate of 39.6% applicable to income over \$470,700 for married filing jointly (MFJ); \$418,400 single	Top rate of 37% applicable to income over \$600,000 MFJ; \$500,000 single
	Personal exemption	\$4,050, subject to phase out	Eliminated
	Standard deduction	\$12,700 MFJ; \$6,350 single	\$24,000 MFJ; \$12,000 single
	"Pease" phase out	Phases out most individual deductions; up to 80% of most deductions lost if AGI exceeded \$313,800 MFJ; \$261,500 single	Eliminated
	Deduction for state and local taxes	Fully deductible; subject to Pease phase out	\$10,000 cap on deduction for state and local income taxes, sales tax, and real property taxes for MFJ or single taxpayers. No phase out
	Mortgage interest deduction	Mortgage interest limited to interest on \$1 million mortgages to acquire property plus \$100,000 home equity loan; subject to Pease phase out	Mortgage interest deduction limited to \$750,000 acquisition indebtedness (old mortgages grandfathered); may include home equity loan only if used to buy or substantially improve qualified residence. No phase out
	Charitable contributions	Deduction limited to 50% of AGI for gifts of cash to public charities	Increases deduction to 60% of AGI
	Miscellaneous itemized deductions	Deductible to extent exceeded 2% of AGI	No deduction
	Dependent tax credits	\$1,000 per qualifying child subject to phase out beginning at \$110,000 MFJ and \$75,000 single	\$2,000 per qualifying child (\$500 per non-child dependent); only \$1,400 refundable; phase out beginning at \$400,000 MFJ, \$200,000 single
	AMT (alternative minimum tax)	28% max rate; exemption of \$84,500 (MFJ) phases out beginning at \$160,900	28% max rate, exemption \$109,400 (MFJ); \$70,300 single; phase out begins at \$1,000,000 (MFJ), \$500,000 single
	Capital gains rate	15/20% (plus 3.7% surtax)	No change
	Carried interests	Treated as capital assets subject to capital gains rate	3-year holding period for long-term capital gains treatment
	529 saving plans	Limited to higher education expenses	Up to \$10,000 per year also may be used for qualified expenses at elementary and secondary schools
TRUSTS & ESTATES	Estate & gift tax exemption/rate	\$5,490,000 exemption (indexed for inflation); 40% maximum rate	Approximately \$11,200,000 exemption (indexed for inflation) through 2025; 40% maximum rate
	Basis	Step up (or down) in basis to fair market value at death	No change
	Annual gift tax exclusion amount	\$15,000 per person for each donee (indexed)	No change
	Trust tax rates	Top income tax rate of 39.6%	Top income tax rate of 37% (beginning at \$12,500)

# Notes

	DESCRIPTION	FORMER PROVISION	NEW LAW
<b>CORPORATE</b>	Tax rates	35% max rate	Flat rate of 21%, including personal service corporations
	AMT	20% max rate	Eliminated
	Interest expense	Unlimited deduction	Limited to interest income earned plus 30% of EBITDA; no limit for small businesses (≤\$25 million gross receipts)
	Dividend received deduction	80% deduction for dividends received by 20% corporate shareholder; 70% if owns less than 20% (100% deduction if affiliated group)	80% reduced to 65%; 70% reduced to 50% (no change for 100% dividend received deduction)
	Foreign source income	Taxed on worldwide income; deferrals	100% of foreign source dividends are exempt to 10% corporate shareholder
	Deemed repatriation tax	None	U.S. shareholders owning 10% interest taxed on accumulated foreign earnings (15.5% rate to extent held in cash equivalents, 8% on balance)
	Sexual harrassment lawsuits	None	No deduction for settlement payment if subject to nondisclosure provision
<b>PASS-THRU ENTITIES</b>	Tax rates	Taxed to partners or shareholders at rates up to 39.6%	Individual taxpayer or trust or estate may deduct 20% of domestic qualified business income from partnership, S corporation or sole proprietorship. Limited to greater of 50% of wages paid or 25% of wages plus 2.5% of qualified property used in production of the income. Further limitation if pass-through service business
<b>CHARITY</b>	UBIT (unrelated business income tax)	No specific provision	UBIT must be separately calculated for each trade or business activity
	Excise tax on executive compensation	None	21% excise tax on charity for individual compensation in excess of \$1 million
	Tax on college endowments	None	1.4% excise tax on net investment income of colleges with at least \$500,000 investment assets per full time student and more than 500 such students

## Conclusion

Many of these changes upend long-standing policies, such as the reduction in the amount of mortgage indebtedness qualifying for the mortgage interest deduction, which for decades promoted home ownership. Another change is the limit on state and local tax deductions, which particularly affects residents of high tax states including New York, New Jersey, and Connecticut.

Almost all the changes to individual income tax provisions are temporary (most expire in 2025) while most of the corporate provisions are permanent. This will undoubtedly create tax complexity and political difficulties in the years ahead.

Our upcoming issues of *Professional Notes* will examine some of these changes in greater detail and offer ways The New York Community Trust might be helpful.

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Are your clients doing estate planning?

Are they making charitable decisions now?

Selling a business? Managing an inheritance?

## The Trust helps you help clients.

For more than 90 years, we've worked with nonprofits, donors, and attorneys in New York. Our grants bolster the arts, protect the environment, feed the hungry, educate children, and more. Because The New York Community Trust is a public charity, donors are ensured the maximum deduction allowed by law.

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