INDIVIDUAL YEAR END NEWSLETTER DEC 2018

LUONGO & ASSOCIATES, PC (301) 952-9437 WWW.LUONGOCPA.COM

Unlike recent years, in which the tax rules have been fairly stable, 2018 brings extensive changes not seen in over 30 years. As a result of a large tax overhaul that passed Congress last December (Tax Cuts and Jobs Act – H.R.1), these changes will affect how your 2018 taxes will be calculated. In preparing for this upcoming tax season, we have spent countless hours in continuing education classes making sure that we are ready to help each and every one of our clients take full advantage of all the tax law changes. As a result of the new law change, we will have a minimum fee increase of 20% as compared to your 2017 fee.

Taxable Income Brackets for 2018 Returns

Rate	Joint Return	Single Return	Rate	Joint Return	Single Return
10%	$0 - $19,050	$0 - $9,525	**32%**	$315,000 - $400,000	$157,500 - $200,000
12%	$19,050 - $77,400	$9,525 - $38,700	**35%**	$400,000 - $600,000	$200,000 - $500,000
22%	$77,400 - $165,000	$38,700 - $82,500	**37%**	Over $600,000	Over $500,000
24%	$165,000 - $315,000	$82,500 - $157,500			

For 2018 individual tax returns, two of the most significant changes are the **repeal of the personal exemption** deductions and the **increase in the standard deduction amounts**. The standard deduction amounts are almost twice what they were in 2017: $24,000 for joint filers and surviving spouses, $18,000 for heads of household, and $12,000 for single individuals and those who are married but filing separately. Additional amounts for the elderly and blind are also available. Because the standard deduction is generally claimed only when it exceeds available itemized deductions, the increase in the standard deduction will not benefit you if you itemize deductions. The repeal of the personal exemption deductions, by contrast, will affect you whether you itemize or not.

To compensate for the repealed exemptions for dependents, the new law increased the child tax credit from the 2017 amount of $1,000 (which was fully refundable) to $2,000 ($1,400 of which is refundable). The maximum age for a child eligible for the credit remains 16 (at the end of the tax year). In addition, a $500 nonrefundable tax credit for dependent children over age 16 and all other dependents is also available beginning in 2018.

Other significant changes as a result of the new tax law, as discussed below, include the elimination of many expenses that were previously deductible and new limitations on other expenses, particularly the $10,000 limitation on the deduction of state and local income and property taxes (SALT). While you may have itemized your deductions in prior years, we need to review whether that still makes sense in light of the increased standard deduction and the changes in the deductibility of other expenses, as well as state tax return impacts.

For instance, in the state of Maryland, you can only take itemized deductions if you itemize on your federal return. The Maryland Maximum Standard deduction for a married filing joint return is $4,500 compared to $24,000 on the federal return and Maryland is still recognizing the personal exemptions. All of this means that we will still have to add up your itemized deductions and probably do comparison returns, both with and without itemized deductions to see which way saves you the most money when doing both your federal and state returns. These changes and comparisons will add to the complexity of your tax returns this year.

ITEMIZED DEDUCTIONS CHANGES

State and Local Income and Property Taxes

New for 2018, there is a $10,000 limit on the deduction for state and local income and property taxes. No deduction is allowed for foreign property taxes.

Mortgage Interest

The mortgage interest deduction on acquisition indebtedness (e.g., mortgages) of more than $750,000 obtained after December 14, 2017, is limited to the portion of the interest allocable to $750,000 ($375,000 in the case of married taxpayers filing separately). In the case of acquisition indebtedness incurred before December 15, 2017, the limitation is the same as it was under prior law: $1,000,000 ($500,000 in the case of married taxpayers filing separately). Additionally, no deduction is allowed for interest paid on home equity indebtedness used for purposes other than buying or improving your home.

Medical, Dental, and Vision Expenses

For 2018, you can deduct medical, dental, and vision expenses to the extent they exceed 7.5% of your adjusted gross income (AGI). In order to take this deduction in future years, such expenses must exceed 10 percent of your AGI. Thus, to the extent you are planning any elective medical, dental, or vision procedures, the expenses of which you can accelerate into 2018, the bunching up of those expenses in 2018 may help reduce your taxable income if you will be itemizing deductions. Such expenses must be primarily to alleviate or prevent a physical or mental defect or illness. They do not include expenses that are merely beneficial to general health, such as vitamins, or the costs of cosmetic surgery.

Charitable Contributions

Whether it makes sense to take an itemized deduction for your charitable contributions depends on whether your total itemized deductions exceed your standard deduction. It's also worth noting that a new change in the law increases the maximum contribution percentage limit from 50% of your contribution base to 60% for cash contributions to public charities.

Charitable Contributions for age 70 ½ or older clients

Taxpayers 70 1/2 years old and older who own an IRA are required to take minimum distributions from that account each year and include those amounts in taxable income. If you are in this category, a special rule allows you to make a charitable contribution directly from your IRA to a charity. This has several benefits. First, since charitable contributions deductions are usually only available to individuals who itemize, individuals who take the standard deduction instead can benefit from this rule. Second, making the contribution directly to a charity counts towards your required minimum distribution but that amount is not included in income and thus reduces your taxable income and adjusted gross income. A lower AGI is advantageous because it increases your ability to take medical expense deductions that you might not otherwise be able to take. In addition, as AGI increases, more of your social security income is subject to tax.

Miscellaneous Itemized Expenses

If you deducted miscellaneous itemized expenses, such as job related expenses or investment advisor fees, in prior years, such deductions are no longer available for 2018. The miscellaneous itemized expense deduction has been eliminated for tax years 2018 through 2025.

OTHER ITEMS

Individual Healthcare Penalty

While the tax penalty on individuals who fail to carry health insurance, which was enacted as part of the Affordable Care Act, has been eliminated for tax years after 2018, **the penalty still applies for 2018 unless a taxpayer is exempt from the penalty because the taxpayer's income falls beneath a certain level.**

Child and Dependent Care Expenses

If you paid someone to take care of your child or a dependent so you can work or look for work, you may be entitled to a tax credit for up to 35% of the expenses paid. Various qualifications must be met in order to be eligible for the credit, but if you incurred such expenses, you may qualify.

Education-Related Expenses

If you have any student loans outstanding, the interest you paid on those loans may be deductible. A deduction of up to $2,500 of interest paid on a qualified student loan is deductible in computing adjusted gross income. The deduction is phased out if your modified adjusted gross income is between $65,000 and $80,000 ($130,000 and $160,000 if filing a joint return). If you are an educator and spend your own money on school supplies, up to $250 may be deductible from gross income. You must maintain the receipts for these expenses.

Moving Expense Reimbursement

If you received a reimbursement from your employer for moving expenses incurred in 2018, the reimbursement is now taxable income. However, if you receive a reimbursement in 2018 for 2017 moving expenses, that is not taxable income. While taxpayers could previously deduct employment-relating moving expenses, this deduction is no longer available for moves taking place in years 2018-2025, unless the taxpayer is a member of the U.S. Armed Forces on active duty who moves pursuant to a military order to a permanent change of station.

Alternative Minimum Tax

If you were subject to the alternative minimum tax in prior years, you may get a break this year as the result of increases in the alternative minimum tax (AMT) exemption amounts as well as the increases in the income level at which the exemption is phased out.

Distributions from a 529 Plan

New for 2018, if you have a 529 Plan, you can use up to $10,000 in aggregate 529 distributions per year for elementary and secondary school tuition. Previously, 529 distributions could only be used for higher education expenses.

Qualified Business Income

Another change in the law, effective for 2018, allows a 20 percent deduction for qualified business income from sole proprietorships, S corporations, partnerships, and LLCs taxed as partnerships. If you qualify for the deduction, which is available to both itemizers and nonitemizers, it is taken on your individual tax returns as a reduction to taxable income. The new tax break is subject to some very complicated restrictions and limitations, but the rules that apply to individuals with taxable income at or below $157,500 ($315,000 for joint filers) are simpler and more permissive than the ones that apply above those thresholds.

2019 Retirement Plan Limits

IRA	Traditional & Roth IRA Limit Over age 49 catch up	$ 6,000 $ 1,000
SEP	Maximum Contribution Over age 49 catch up	$ 56,000 $ 0
SIMPLE	Maximum deferral Over age 49 catch up	$ 13,000 $ 3,000
401-K, 403-B, and 457	Maximum deferral Over age 49 catch up Maximum contribution all sources	$ 19,000 $ 6,000 $ 56,000 plus catch up
2019 Defined Benefit Plan Limit		$225,000

Retirement Plans Considerations

Fully funding your company 401(k) with pre-tax dollars will reduce your current year taxes, as well as increase your retirement nest egg. For 2018, the maximum 401(k) contribution you can make with pre-tax earnings is $18,500. For taxpayers 50 or older, that amount increases to $24,500.

If you have a SIMPLE 401(k), the maximum pre-tax contribution for 2018 is $12,500. That amount increases to $15,500 for taxpayers age 50 or older.

If certain requirements are met, contributions to an individual retirement account (IRA) may be deductible. For taxpayers under 50, the maximum contribution amount for 2018 is $5,500. For taxpayers 50 or older but less than age 70 1/2, the maximum contribution amount is $6,500. Contributions exceeding the maximum amount are subject to a 6 percent excise tax. Even if you are not eligible to deduct contributions, contributing after-tax money to an IRA may be advantageous because it will allow you to later convert that traditional IRA to a Roth IRA. Qualified withdrawals from a Roth IRA, including earnings, are free of tax, while earnings on a traditional IRA are taxable when withdrawn.

If you already have a traditional IRA, we should evaluate whether it is appropriate to convert it to a Roth IRA this year. You'll have to pay tax on the amount converted as ordinary income, but subsequent earnings will be free of tax and the decrease in tax rates that are effective this year makes such a conversion less costly than it would have been in previous years. Of course, this option only makes sense if the tax rates when the money is withdrawn from the Roth IRA are anticipated to be higher than the tax rates when the traditional IRA is converted. And if you have a traditional 401(k), 403(b), or 457 plan that includes after-tax contributions, you can generally rollover these after-tax amounts to a Roth IRA with no tax consequences. A rollover of a SIMPLE 401(k) into a Roth IRA may also be available. As with all tax rules, there are qualifications that apply to these rollovers that we should discuss before any actions are taken.

Capital Gains: New Law

Rate	Filing Status	Breakpoint (Income)
0%	Individual & Married Filing Separately Head of Household Married Filing Joint	Up to $38,600 Up to $51,700 Up to $77,200
15%	Individual & Married Filing Separately Head of Household Married Filing Joint	$38,600 - $425,800 $51,700 - $452,400 $77,200 - $479,000
20%	Individual & Married Filing Separately Head of Household Married Filing Joint	$425,800 + $452,400 + $479,000 +

Capital Gains and Losses

If your stock portfolio includes stocks that have lost value since you originally invested and you've decided you want to divest yourself of them, we should evaluate whether you might benefit from selling off appreciated stocks, particularly those that would generate a short-term capital gain, and using the resulting gain to limit your exposure to a long-term capital loss, the deduction of which is limited. And any net capital gain you may reap, will be taxed at the substantially reduced capital gain tax rate.

The tax rate for net capital gain is generally no higher than 15 percent for most taxpayers. Some or all of your net capital gain may be taxed at 0 percent if your income is not above $38,600 (single), $77,200 (joint), or $51,700 (head of household). However, a 20 percent tax rate on net capital gain does apply to the extent that your ordinary taxable income is over $425,800 (single), over $479,000 (joint), $239,500 (married filing separately), or over $452,400 (head of household). There are a few other exceptions where capital gains may be taxed at rates greater than 15 percent: (1) the taxable part of a gain from selling certain qualified small business stock is taxed at a maximum 28 percent rate; (2) net capital gains from selling collectibles (such as coins or art) are taxed at a maximum 28 percent rate; and (3) the portion of certain unrecaptured gain from selling real property is taxed at a maximum 25 percent rate. If you have been involved in any such transactions during the year, we should review your options for reducing the tax on those transactions.

Foreign Bank Account Reporting

If you have an interest in a foreign bank account, it must be disclosed; failure to do so carries stiff penalties. You must file a Report of Foreign Bank and Financial Accounts (FBAR) if: (1) you are a U.S. resident or a person doing business in the United States; (2) you had one or more financial accounts that exceeded $10,000 during the calendar year; (3) the financial account was in a foreign country; and (4) you had a financial interest in the account or signatory or other authority over the foreign financial account. If you are unclear about the requirements or think they could possibly apply to you, please let me know.

COMPARISON OF TAX CUTS AND JOBS ACT AND PRIOR LAW

	Prior Law (2017)	H.R. 1 (2018)
Child Tax Credit	$1,000 All refundable	$2,000 Refundable to $1,400
Standard Deduction	S: $6,350 MFJ: $12,700 HH: $9,350	S: $12,000 MFJ: $24,000 HH: $18,000
Individual Rates	10%, 15%, 25%, 28%, 33%, 35%, 39.6%	10%, 12%, 22%, 24% 32%, 35%, 37%
Personal Exemptions	$4,050	Repealed
State & Local Taxes	Deductible if itemized	Maximum of $10,000 deduction
Mortgage Interest Deduction New acquisitions incurred before 12/15/17 is grandfathered in at $1 million	Mortgage of $1 million limit	Mortgage of $750,000 limit
Alternative Minimum Tax	Individual: 26%, 28% Corporate: 20%	Individual: exemption increased Corporate: Repealed
Home Equity Interest	Deductible is used for home repairs	Repealed
Individual Insurance Mandate	Penalty Varies	Repealed
Moving Expenses	Partially Deductible	Repealed
Recharacterization of IRA to Roth Conversion	Allowed	Repealed
Alimony	Payment deductible Receipt taxable	Repealed for divorce or Separation after 12/31/18
Medical Expense Deduction	Expenses that exceed 10% of AGI	Expenses that exceed 7.5% of AGI
Tuitions & Fees Deduction	Allowed	Repealed
Casualty Losses	Allowed	Repealed except in disaster area
529 Plan	Tax free withdraw for College only	Also allows $10,000 tax free withdraw grades K-12 expenses for public, private & homeschooling
Miscellaneous Itemized deductions subject to 2% AGI	Allowed	Repealed
Federal Estate Tax	5.49 Million Federal Only	10.98 Million Federal Only
Annual Gift Tax Limit	$14,000 per year/ per individual	$15,000 per year/ per individual