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# 2017 Tax Reform

A review and analysis of key highlights from the  
Advanced Consulting Group of Nationwide®

These are the highlights and provisions of the Tax Cuts and Jobs Act.<sup>1</sup>

## Changes for individuals

### Individual tax brackets

| 2018 under previous tax law |                       |                        | 2018 under the new law |                       |                        |
|-----------------------------|-----------------------|------------------------|------------------------|-----------------------|------------------------|
| Tax Rate                    | Taxable Income        |                        | Tax Rate               | Taxable Income        |                        |
|                             | Individual            | Married Filing Jointly |                        | Individual            | Married Filing Jointly |
| 10%                         | \$0 - \$9,525         | \$0 - \$19,050         | 10%                    | \$0 - \$9,525         | \$0 - \$19,050         |
| 15%                         | \$9,526 - \$38,700    | \$19,051 - \$77,400    | 12%                    | \$9,526 - \$38,700    | \$19,051 - \$77,400    |
| 25%                         | \$38,701 - \$93,700   | \$77,401 - \$156,150   | 22%                    | \$38,701 - \$82,500   | \$77,401 - \$165,000   |
| 28%                         | \$93,701 - \$195,450  | \$156,151 - \$237,950  | 24%                    | \$82,501 - \$157,500  | \$165,001 - \$315,000  |
| 33%                         | \$195,451 - \$424,950 | \$237,951 - \$424,950  | 32%                    | \$157,501 - \$200,000 | \$315,001 - \$400,000  |
| 35%                         | \$424,951 - \$426,700 | \$424,951 - \$480,050  | 35%                    | \$200,001 - \$500,000 | \$400,001 - \$600,000  |
| 39.6%                       | \$426,701 +           | \$480,051 +            | 37%                    | \$500,001 +           | \$600,001 +            |

Effective: 1/1/2018

Revert to 2017 law: 1/1/2026

Code sec. 1

Bill sec. 11001

These tax brackets will be adjusted for inflation using new factors.

## Standard deductions

| 2018 Filing Status     | Deduction Amount |
|------------------------|------------------|
| Single                 | \$12,000         |
| Married Filing Jointly | \$24,000         |
| Head of Household      | \$18,000         |
|                        |                  |
| Personal Exemption     | \$0              |

The withholding rules for 2018 will remain the same as the 2017 rules and change for 2019.

Generally, taxpayers may take the standard deduction or itemize deductions and receive a personal exemption for each family member. The Act increases the standard deduction amount, reduces or eliminates numerous itemized deductions (as will be discussed in more detail below) and eliminates the personal exemption. The result of these changes is that millions more Americans are likely to take the standard deduction rather than itemize.

If working for a company, individuals should review the amount their employers are withholding in light of the lower tax rates, the higher child tax credit (discussed below), loss of the personal exemption and the higher standard deduction.

*Effective: 1/1/2018*

*Reverts back to 2017 law: 1/1/2026*

*Code secs. 63 and 151*

*Bill sec. 11041 (personal exemption) and 11021 (standard deduction)*

*Deduction amounts will be adjusted each year by new inflation factor.*

## Adjustments to capital gains taxation

Rates for long-term capital gains and qualified dividends will continue to use the prior income thresholds. This means that capital gains and qualified dividend rates will no longer line up with the ordinary income tax brackets.

| Capital Gains Rate/Filing Status | Single Filer (income amount) | Married Filing Jointly (income amounts) |
|----------------------------------|------------------------------|---|
| 0%                               | \$0 - \$38,600               | \$0 - \$77,200                          |
| 15%                              | \$38,601 - \$425,800         | \$77,201 - \$479,000                    |
| 20%                              | \$425,801 +                  | \$479,001 +                             |

*Effective: 1/1/2018*

*Code sec. 1(h)*

*Bill sec. 11001*

## Child tax credit

The child tax credit is increased from \$1,000 to \$2,000. Begins to phase out for taxpayers whose AGI is over \$400,000 (joint filers) and \$200,000 in all other cases (these thresholds are not indexed for inflation). Provides a new nonrefundable credit of \$500 for each dependent who is not a qualifying child.

The refundable portion of the credit cannot exceed \$1,400 for a qualifying child (adjusted for inflation after 2018).

*Effective: 1/1/2018*

*Reverts back to 2017 law: 1/1/2026*

*Code sec. 24*

*Bill sec. 11022*

## Temporary reduction in medical expense deduction floor

For tax years 2017 and 2018 medical expenses that exceed 7.5% of AGI will be deductible for all taxpayers. The percentage will go back to 10% in 2019.

*Code sec. 213*

*Bill sec. 11027*

## 529 account funding for elementary and secondary education

529 plan distributions can be used for elementary or secondary public, private or religious school expenses, up to \$10,000 per year per student. So, even though a student may be the beneficiary of multiple accounts, only \$10,000 per year can be distributed tax-free for that student.<sup>2</sup>

*Effective: 1/1/2018*

*Code sec. 529*

*Bill sec. 11032*

## Limitation on deduction for state and local taxes

The aggregate amount of all state and local property, income and sales taxes that are deductible will be \$10,000 (\$5,000 if married filing separately) per year. EXCEPT, if any of those taxes are paid in carrying on a trade or business then the cap does not apply. Also, unless paid or accrued in carrying on a trade or business, a taxpayer can no longer deduct foreign real property taxes.

If a state/local tax is paid before 1/1/2018 for a tax imposed for a taxable year beginning after 12/31/2017, the tax will be treated as paid on the last day of the taxable year for which such tax is imposed.

The Joint Committee on Taxation analysis of the Act makes it clear that an individual may not claim an itemized deduction in 2017 on pre-payment of income tax for a future taxable year in order to avoid the \$10,000 cap.

*Effective: 1/1/2018*

*Reverts back to 2017 law: 1/1/2026*

*Code sec. 164*

*Bill sec. 11042*

## Limit on deduction for qualified residence interest

Interest paid on home equity indebtedness is not deductible.

Interest on a qualified residence is limited to \$750,000 (\$375,000 married filing separately) of indebtedness. This is lowered from \$1 million (\$500,000 married filing separately).

This provision applies only to indebtedness incurred after 12/15/2017.

*Effective: 1/1/2018*

*Reverts back to 2017 law: 1/1/2026*

*Code sec. 163(h)*

*Bill sec. 11043*

## Suspension of miscellaneous itemized deductions

No miscellaneous itemized deductions are allowed. (Taxpayers have been able to deduct miscellaneous items that exceed 2% of AGI up to certain threshold amounts.)

*Effective: 1/1/2018*

*Reverts back to 2017 law: 1/1/2026*

*Code sec. 67*

*Bill sec. 11045*

Code sec. 68 currently has an overall limit on all itemized deductions. Bill sec. 11046 removes this limit for tax years 2018 through 2025.

For tax years 2018 through 2025, qualified moving expense reimbursement will be included in the taxpayer's income.

*Code sec. 132*

*Bill sec. 11048*

For tax years 2018 through 2025, there will be no deduction for moving expenses except for members of the Armed Forces.

*Code sec. 217*

*Bill sec. 11049*

Taxpayers will no longer be able to take a deduction for alimony payments, and alimony recipients will no longer include the payment in income. This applies to alimony payments made pursuant to a divorce or separation instrument executed after 12/31/2018 and to one executed before that date that is modified after that date if it is done so to have this statutory change apply to the modification.

*Code secs. 215 and 61(a)(8)*

*Bill sec. 11051*

## Suspension of personal casualty loss deduction

Personal casualty loss deductions will be allowed only for a Federally-declared disaster.

*Effective: 1/1/2018*

*Reverts back to 2017 law: 1/1/2026*

*Code sec. 165*

*Bill sec. 11044*

## Repeal of individual mandate

Repeals the penalty tax on individuals who do not have health insurance.

*Effective: 1/1/2019*

*Code sec. 5000A*

*Bill sec. 11081*



**The legislative history indicates that an individual may not claim an itemized deduction in 2017 on pre-payment of income tax for a future taxable year in order to avoid the \$10,000 cap.**

## Estate/gift tax

For estates of decedents who die or for gifts made after 12/31/2017 and before 1/1/2026, the basic exclusion amount is \$10 million (indexed for inflation occurring after 2011). The annual gift exclusion amount is \$15,000. Basis step-up rules remain unchanged.

For decedents dying in 2018, the estate tax exemption amount is \$11.2 million. Life insurance planning for these taxes may see an even greater decrease.

*Effective: 1/1/2018*

*Reverts back to 2017 law: 1/1/2026*

*Code sec. 2010(c)*

*Bill sec. 11061*

## Changes for businesses

### Pass-through entities

The Act adds a new Code sec. 199A

— Qualified Business Income, which is intended to allow pass-through entities to deduct the first 20% of their business income up to a threshold amount of \$157,500 (\$315,000 if joint return), adjusted for inflation after 2018. This is meant to allow a lower effective tax rate for taxpayers' business enterprise income, but to still subject a portion of their earnings to the individual tax rates.

Because the deduction is meant to assist businesses and not wage earners, the deduction cannot be taken by those in specified personal service professions whose income is above the threshold amount plus \$50,000 (\$100,000 if filing a joint return). These include health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business *where the principal asset of such trade or business is the reputation or skill of 1 or more of its employees* (new provision) and the performance of services that consist of investing and investment management, trading or dealing in securities, partnership interests or commodities. The Act specifically excludes engineering and architecture from the list of service providers who cannot take advantage of the deduction.

These new rules are complex and it will likely take time some time for privately-held companies to determine when or if it makes sense to convert to a C corporation, or for a C corporation to convert to a pass-through entity.

*Effective: 1/1/2018*

*Reverts back to 2017 law: 1/1/2026*

*Code sec. 199A (new)*

*Bill sec. 11011*

### Corporate tax rate

The corporate rate is changed from a graduated rate ranging from 15% to 35% to a flat tax rate of 21%.

*Effective: 1/1/2018*

*Code sec. 11*

*Bill sec. 13001*

### Alternative minimum tax

This tax is repealed for corporations.

*Effective: 1/1/2018*

*Code sec. 55(a)*

*Bill sec. 12001*

The repeal of the alternative minimum tax (AMT) will be a win for companies that own corporate-owned life insurance (COLI) or bank-owned life insurance (BOLI) policies because cash values and death benefits are a preference item under the AMT.

The AMT remains in place for noncorporate taxpayers; however, the exemption amount increases to \$109,400 for joint return/surviving spouse (up from \$86,200) and \$70,300 all others (up from \$55,400 for single filers and \$43,100 for married filing separate returns [except estates and trusts]). The phase out thresholds are increased to \$1 million for joint filers (up from \$164,100 for joint filers and surviving spouses) and \$500,000 for all other taxpayers (up from \$123,100 for single filers and \$82,020 for married filing separately [except estates and trusts]). These amounts are indexed for inflation.

*Effective: 1/1/2018*

*Reverts back to 2017 law: 1/1/2026*

*Code sec. 55(d)*

*Bill sec. 12003*



**Estates of decedents dying in 2018 will have an exemption of \$11.2 million. The need for life insurance to pay estate taxes may be reduced.**

## Expensing depreciable business assets

The annual cost that can be taken into account is increased from \$520,000 (in 2018) to \$1 million. This limit is reduced by the amount by which the cost of section 179 property placed in service during the year exceeds \$2.5 million (increased from \$2,070,000 in 2018). It also expands the definition of section 179 property.

*Effective for property placed in service after 12/31/2017*

The \$1 million and \$2.5 million are indexed for inflation beginning 1/1/2019.

*Code sec. 179*

*Bill sec. 13101*

## Temporary 100% expensing for certain business assets

New depreciation schedule for “qualified property” depending on when it is first placed in service (“qualified property” means property that has a recovery period of 20 years or less; computer software, etc.)

| Placed in Service After | Before   | Rate |
|-------------------------|----------|------|
| 9/27/2017               | 1/1/2023 | 100% |
| 12/31/2017              | 1/1/2024 | 80%  |
| 12/31/2023              | 1/1/2025 | 60%  |
| 12/31/2024              | 1/1/2026 | 40%  |
| 12/31/2025              | 1/1/2027 | 20%  |
| 12/31/2026              | 1/1/2028 | 0%   |

The current rate is 50% which would have expired 12/31/2019 under current law.

For certain other property, including transportation property, certain aircraft and property with a recovery period of at least 10 years, the rates are the same but the date that the property must be placed in service “before,” is one year later than in the chart above.

The table above also applies to plants bearing fruits and nuts for plants planted or grafted before/after those dates.

*Code sec. 168(k)*

*Bill sec. 13201*

## Modification of net operating loss deduction

Limits the net operating loss (NOL) deduction to 80% of taxable income (determined without regard to the deduction), for losses arising in taxable years beginning after 12/31/2017. The limitation does not apply to a property and casualty insurance company.

Repeals the two-year carryback and the special carryback provisions, but provides a two-year carryback in the case of certain losses incurred in the trade or business of farming.

In addition, it provides a two-year carryback and 20-year carryforward for NOLs of a property and casualty insurance company.

The provision does not increase NOL carryovers.

*Effective: 1/1/2018*

*Code sec. 172*

*Bill sec. 13302*

## Employer deduction for fringe benefits

Eliminates deduction for entertainment, amusement or recreation activities.

No deduction is allowed for qualified transportation fringe benefits under Code sec. 132(f) (subsidized bus pass, parking, bicycle commuting reimbursement).

No deduction will be allowed for entertainment, amusement or recreation activities, membership dues for clubs organized for business, pleasure, recreation or other social purpose, or a facility used in connection with any of these activities.

Taxpayers may still generally deduct 50% of the food and beverage expenses associated with operating their trade or business (e.g., meals consumed by employees on work travel). For amounts incurred and paid after 12/31/2017 and until 12/31/2025, this 50% limitation is extended to expenses of the employer associated with providing food and beverages to employees through an eating facility that meets requirements for de minimis fringes and for the convenience of the employer. Such amounts incurred and paid after 12/31/2025 are not deductible.

*Effective: 1/1/2017 except for meals provided at convenience of employer becomes effective 1/1/2026*

*Code sec. 274*

*Bill sec. 13304*



## Denial of deduction for cash, gift cards and other non-tangible personal property as employee achievement awards

No deduction is allowed for the cost of an employee achievement award if it is cash, gift cards, vacations, meals, tickets to sporting events, etc.

*Effective: 1/1/2018*

*Code sec. 274(j)*

*Bill Sec. 13310*

## Transfer for value of a life insurance contract

Any person who acquires a life insurance contract or any interest in a life insurance contract in a “reportable policy sale” must report information about the purchase to the IRS and the insurance carrier. When the insurance company receives such information, it is then required to report the basis of the contract to the IRS and to the seller. When a “reportable death benefit” is paid under the contract, the insurance company is required to report information about the payment to the IRS and to the payee, including the gross amount of the payment and an estimate of the buyer’s basis in the contract.

A “reportable policy sale” means 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 life insurance contract). An indirect acquisition includes the acquisition of an interest in a partnership, trust, or other entity that holds an interest in the life insurance contract.” A “reportable death benefit” is a death benefit paid under a life insurance contract that was transferred in a reportable policy sale.

In addition, the exceptions to the transfer for value rules do not apply in the case of a transfer that is a reportable policy sale. This means that a reportable policy sale that occurs after 12/31/2017 and reportable death benefits paid after 12/31/2017 will be treated like a transfer for value and a portion of the death benefit will be taxable to the beneficiary. Note that this applies to policies already in-force that are transferred in a reportable policy sale after 12/31/2017.

*Code sec. 101*

*Bill sec. 13520*

## Basis of life insurance and annuity contracts

The Act reverses the IRS’s position in Revenue Ruling 2009-13 by providing that in determining the basis of a life insurance or annuity contract, no adjustment is made for mortality, expense or other reasonable charges incurred under the contract (the cost of insurance). In other words, the seller’s basis will no longer be reduced by the cost of insurance for transactions entered into after August 25, 2009.

*Bill sec. 13520*

## Retirement plans

### Repeal rule permitting recharacterizations of Roth conversions

The special rule that allows a contribution to one type of IRA to be recharacterized as a contribution to the other type of IRA does not apply to a conversion contribution to a Roth IRA. Thus, recharacterization cannot be used to unwind a Roth conversion.

However, recharacterization is still permitted with respect to other contributions. For example, an individual may make a contribution for a year to a Roth IRA and, before the due date for the individual’s income tax return for that year, recharacterize it as a contribution to a traditional IRA.

*Effective: 1/1/2018*

*Code sec. 402*

*Bill sec. 13611*

### Extended rollover period for the rollover of plan loan offset amounts in certain cases

Extends the deadline to avoid having a plan loan be treated as a taxable distribution as a result of an individuals’ separation from service (or in the event of plan termination) by permitting employees to roll over the loan balance to an IRA/plan by the due date for filing their tax return (including extensions).

*Effective: 1/1/2018*

*Code sec. 408A*

*Bill sec. 13611*

## Relief for 2016 disaster areas

There will be no 10% additional tax on early distributions from qualified plans, 403(b) plans and IRAs if it's a qualified 2016 disaster distribution. The aggregate distribution for a taxable year cannot exceed the excess of (1) \$100,000 over (2) the aggregate amounts treated as qualified 2016 disaster distributions received by such individual for all prior taxable years. (Controlled group rules apply.) Special rules will allow the distribution to be repaid to the plan. The distribution will be included in income over a 3-year period, ratably.

*Applies to 2017 and 2018 tax years for casualty losses arising in 2016 and 2017*

*Code sec. 72(t)*

*Bill sec. 11028*

Note: Reducing the tax rate on pass-through entities below the owner's individual tax rate could have a negative impact on the adoption or maintenance of qualified retirement plans. The difference between the reduced marginal tax rate on pass-through entities as a result of the 20% deduction allowed to them and the 37% top individual rate on ordinary income (as well as the favorable tax rate on capital gains income at 20%) may mean the small business owner's retirement benefits could be taxed at 37% (or at 39.6% after 12/31/2025) when distributed, instead of the lower pass-through effective rate and the 20% capital gains rate on accumulated earnings. More than 90% of businesses are organized as pass-through entities, and more than 320,000 of these entities sponsor a retirement plan with an average of 75 participants, so the impact may be significant.

## Farm operations and farm cooperatives

### Repeal of deduction for income attributable to domestic production activities

Eliminates the deduction that is equal to 9% of the lesser of the taxpayer's qualified production activities income or taxable income produced or marketed through cooperatives.

*Effective: 1/1/2018*

*Code sec. 199 is eliminated (Income attributable to domestic production activities)*

*Bill sec. 13305*

### Modifications of treatment of certain farm property

The provision shortens the recovery period from 7 to 5 years for any machinery or equipment (other than any grain bin, cotton ginning asset, fence, or other land improvement) used in a farming business, the original use of which commences with the taxpayer and is placed in service after 12/31/2017.

The provision also repeals the required use of the 150% declining balance method for property used in a farming business (i.e., for 3, 5, 7, and 10-year property). The 150% declining balance method will continue to apply to any 15-year or 20-year property used in the farming business to which the straight-line method does not apply, or to property for which the taxpayer elects the use of the 150% declining balance method.

The term "farming business" means a trade or business involving the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity (e.g., the trade or business of operating a nursery or sod farm; the raising or harvesting of trees bearing fruit, nuts, or other crops; the raising of ornamental trees [other than evergreen trees that are more than six years old at the time they are severed from their roots]; and the raising, shearing, feeding, caring for, training, and management of animals). A farming business includes processing activities that are normally incidental to the growing, raising, or harvesting of agricultural or horticultural products. A farming business does not include contract harvesting of an agricultural or horticultural commodity grown or raised by another taxpayer, or merely buying and reselling plants or animals grown or raised by another taxpayer.

*Effective for property placed in service after 12/31/2017*

*Code sec. 168*

*Bill sec. 13203*

## Use of alternative depreciation system for electing farming businesses

The provision requires an electing farming business, i.e., a farming business electing out of the limitation on the deduction for interest, to use an alternative depreciation system to depreciate any property with a recovery period of 10 years or more (e.g., property such as single purpose agricultural or horticultural structures, trees or vines bearing fruit or nuts, farm buildings, and certain land improvements).

*Effective: 1/1/2018*

*Code sec. 168*

*Bill sec. 13205*

## Exchange of like-kind property (Code sec. 1031)

Code section 1031 is modified so that the nonrecognition of gain in a like-kind exchange is now limited to real property that is not held primarily for sale. Personal property such as equipment, trucks, livestock and artwork can no longer receive the favorable tax treatment under Code sec. 1031.

*Applies to exchanges completed after 12/31/2017*

*Code sec. 1031*

*Bill sec. 13303*



<sup>1</sup> The Senate Parliamentarian ruled late on December 18, 2017 that certain provisions of the Act violated the Byrd rule. Included among the changes is that the Act must be cited by its full, official name which is, An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018.

<sup>2</sup> A Senate amendment removed the language that would have allowed home schooled students to benefit from this provision.

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