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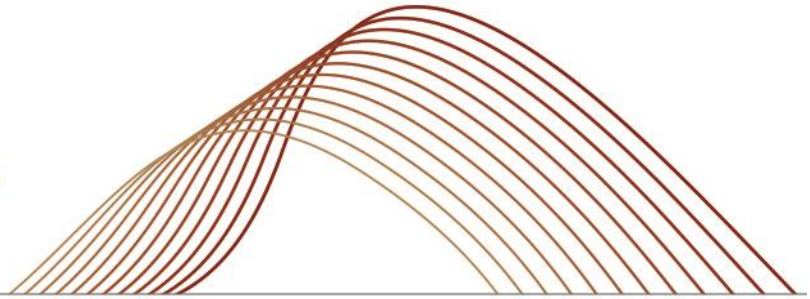

December 2017

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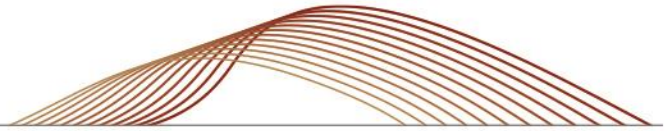
Tax Cuts and Jobs Act Significantly Impacts Individual Taxation Provisions

By Andrew Short, David Makso & Rob Wilson

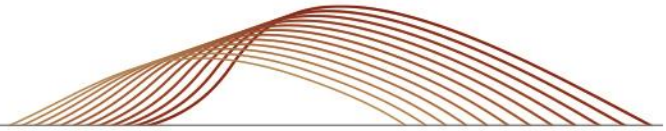
On December 22, 2017, President Trump signed into law tax reform legislation (the "Act") formerly known as the Tax Cuts and Jobs Act. With respect to individual taxation provisions, the Act represents a compromise between the House Bill passed November 16, 2017 and the Senate Bill passed December 2, 2017. The key individual taxation provisions of the Act include:

- *New Tax Brackets and Tax Rates*: Establishes a new top tax rate of 37% applicable to taxable income over $600,000 for married individuals filing joint returns and taxable income over $500,000 for individuals and heads of households and creates a new seven tier bracket structure.
  - Payroll agents begin to adjust withholding rates on wages paid in January 2018 with taxpayers experiencing the impact by February 2018. The IRS plans to issue guidance in this area in January 2018.
- *Standard Deduction*: Increases the standard deduction to $24,000 for married individuals, $18,000 for head-of-household filers and $12,000 for all other individuals.
- *Personal Exemption*: Suspends the personal exemption.
- *Limitation of $10,000 for SALT Deductions*: Limits an individual's itemized deduction for state and local income tax, property tax and sales tax paid to $10,000.
  - Pre-payments of 2018 state or local income tax are not deductible in 2017.
  - Depending on the jurisdiction, individuals may be able to deduct pre-payments of 2018 property tax.
- *Active Loss Limitation*: Limits an individual's deduction for active losses to active income.
  - Disallowed losses will be treated as a net operating loss carryover to the following year. The new active loss limitation provisions will apply to existing active business activities.
- *Inflation Adjustment*: Changes the CPI measure for adjusting thresholds and parameters of the tax system to chained consumer price index for all-urban consumers (C-CPI-U) which is generally a lower inflation rate than CPI.



  - This provision will slow inflation adjustments to the tax brackets, standard deduction, personal exemption and the alternative minimum tax.

- *Mortgage and Home Equity Interest Deduction*: Caps at $750,000 the principal amount of a mortgage for which an individual can deduct interest payments.
  - The $750,000 cap will apply to mortgages on secondary residences as well.
  - A $1,000,000 cap will continue to apply to mortgages incurred before December 15, 2017.
  - Interest payments on home equity indebtedness are no longer deductible.
- *Gain on Sale of Principal Residence*: Leaves unchanged all provisions relating to the rollover of gain on the sale of a principal residence.
- *Alternative Minimum Tax*: Increases the AMT exemption amount for each filer and increases phase-out thresholds.
- *Charitable Deduction*: Increases the income-based percentage limit for charitable deductions from 50% to 60% of an individual's adjusted gross income.
- *Affordable Care Act*: Eliminates the individual responsibility payment for individuals who are not covered by a minimum essential health care plan.
- *Limitation on Itemized Deductions*: Suspends all miscellaneous itemized deductions that are subject to the 2% floor under current law (e.g., unreimbursed business expenses).
- *Student Loan Interest*: Retains deductibility of student loan interest.
- *Child Tax Credit*: Doubles the child tax credit to $2,000 per child under the age of 17, refundable up to $1,400.
- *529 Education Plan*: Allows withdrawals of up to $10,000 annually for tuition at elementary and secondary public, private and religious schools.
- *Medical Expenses*: Lowers the floor for medical expense deductions to 7.5% of adjusted gross income for the 2017 and 2018 tax years.
- *Alimony Payments*: Repeals the deduction for alimony payments, effective for settlements after December 31, 2018.
  - Alimony recipient will no longer include alimony payments in income.
- *Tax Preparation Expenses*: Repeals the deduction for tax preparation expenses.
- *Moving Expenses*: Repeals the deduction for moving expenses in connection with the commencement of work by an individual, except for members of the Armed Forces.
- *Estate Tax Exemption*: Doubles the estate tax exemption (and not repealing it after 2024 as was proposed in the House Bill).



The Act should simplify tax computation because far fewer individuals will itemize their deductions as a result of these changes. The Joint Committee on Taxation estimates that the percentage of individuals that will itemize their deductions will drop from approximately 30% under current law to approximately 6% under the Act. The impact of these changes on individuals is dependent on each individual's unique circumstances. If you have any questions about this Client Alert, please contact any member of the Paul Hastings Tax Department.

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If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

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