Tax Tidbits

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Overview of the Tax Cut and Jobs Act of 2017

On December 22, 2017, President Trump signed into law the Tax Cuts and Jobs Act of 2017. The new law overhauls the Internal Revenue Code by lowering tax rates and altering a number of tax provisions. Many supporters claim that it will help the economy and create jobs. Opponents claim that according to the House and Senate Conference Committee report the new law will add $1.5 trillion to the federal deficit during the years 2018 through 2027. Those supporters for the Administration will claim that the deficit will be offset by future economic growth, which will result from potential new tax revenue growth.

The House and Senate Conference Committee report indicates that a typical family of four earning a median family income of $73,000 will receive a tax cut of $2,059. During the 2017 tax year, our software illustrated to tax clients the 2017 numbers affected by the 2018 tax law. In many cases, the 2018 tax summary showed people benefiting by their taxes decreasing from 2017 to 2018. It also showed that many of our clients may not be itemizing due to the new tax law significantly increasing the standard deduction.

For instance, the standard deduction for Single filers was $6,350 in 2017 and is now $12,000 in 2018 and Married filing jointly was $12,700 and is now $24,000 in 2018. Our clients are finding themselves in a quandary. They have been gathering tax documents and records to itemize their deductions for years and now they are not sure if they should even do that anymore. My advice to our clients is to continue gathering documents for one more year, then we can make a determination of whether they should stop gathering their documents. Going forward, the probability of how they will file will level off.

Another major change in the itemized deduction area is the capping of the state and local tax deduction at $10,000. This has the potential of hitting clients hard. However, some of the people that this applies to were getting hit with alternative minimum tax (AMT), thus negating the benefit of a deduction for state and local taxes. Some states like New York have put into place countermeasures to circumvent the new Federal law.

Another group that is very concerned about the effects of the tax law change are charities and churches. I have spoken to a number of clergy and directors of charities and their feeling is that the perceived "loss of a deduction" for donating to a charity may cause some people to give less or stop giving at all. This will remain to be seen. Donating appreciated assets, such as capital stock with a fair market value in excess of the original cost, can help both the giver with tax savings and the charity with increased cash flow.

To wrap up the personal tax highlights, you will find that if you have been subject to AMT in the past, you will probably not be starting in 2018. The new law raises the exemption amounts for married taxpayers to $109,400 and $70,300 for all others. The exemption phase out begins at $1 million for married taxpayers and $500,000 for all other taxpayers.

Finally, the business tax reform contains some interesting developments. At the top of the charts, the corporate tax rate was reduced to 21% for C-corporations. This is driving the question whether S-corporations should be converted back to C-corporations. Additionally, there is a new section in the tax code called the Qualified Business Income Deduction (QBID). This deduction is available to shareholders, owners of flow-through entities and sole proprietors. The QBID is basically a 20% deduction based on the flow-through income of the entity owned by the taxpayer subject to limitations.

2018 will be interesting for a lot of reasons; however, we would advise people not to wait to find out what the full effects of the new tax law will be on their taxes come April 2019. We recommend you contacting our office for tax planning or with any questions that you have.

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Schedule A Changes in 2018

The new Tax Cuts and Jobs Act begs the question, "Can or should I itemize in 2018?" The first substantial change is that the standard deduction will almost double for each filing status in 2018. This will sometimes make it a very easy question. For example, if you filed your 2017 tax return as single and had itemized deductions totaling $9,000, in 2018 your standard deduction will be $12,000, which will give you less taxable income for the year. You will also not have to keep records for the standard deduction; this is the amount the IRS gives you to deduct from your income with no questions asked.

If you are still planning to itemize your deductions in 2018, there are a few things you should know:

1. Your medical expenses are still deductible to the extent that the expenses exceed 7.5% of your adjusted gross income (AGI) for 2018 and will increase to 10% in 2019 but, will expire after 2025.
2. The home mortgage interest deduction is still allowed with the acquisition debt limit reduced to $750,000 from the prior $1,000,000 limit.
3. The home equity debt is no longer deductible if you use the funds for something other than work completed on your home. In other words, if you take out a home equity loan to purchase a new car or to go on a vacation, it would not be deductible.
4. The taxes paid portion of the Schedule A has now been limited to $10,000 ($5,000 MFS). This includes real estate taxes paid and state and local income taxes or state and local sales tax. This provision expires after 2025.

The biggest change is the removal of the miscellaneous itemized deductions subject to the 2% of AGI limitation. This means that investment management expenses, tax preparation fees, unreimbursed employee business expenses, repayment of income that is $3,000 or less and repayment of Social Security benefits are no longer deductible. This provision expires after 2025 as well.

The new Tax Cuts and Jobs Act is the most significant change to the tax laws since 1986. Before deciding what option is best for your tax situation, we encourage you to call us to speak to a tax preparer.

Amy M. Chacho
Business Services/Tax Specialist

Borrowing Vehicles...Am I Covered?

Most people have an idea of what's covered and not covered under their various insurance policies, but at Valicenti Insurance Services Inc., we get a lot of questions about borrowing or loaning a car.

Now that summer is here and you might be looking to borrow your neighbor's truck for a home-improvement project or a trip to the local landfill, we thought it was a great time to provide a little more information.

Generally, insurance coverage follows the vehicle rather than the driver. So, in most instances, as long as the owner of the car has insurance, it's covered even if someone other than the owner is driving it — as long as they have the owner's permission. The borrower's insurance is considered secondary, meaning that in the event of an accident, it could apply if the owner's insurance is insufficient to fully cover the damage.

It's important to note that there are some exceptions to what is called "permissive use" coverage. For example, permission must be given by the owner, unless the borrower has a reasonable belief that they are allowed to use the car. The borrower cannot give permission to someone else. So if your teenager allows one of his or her friends to drive your car to the mall, your coverage likely won't apply.

Coverage might also be denied if the borrower operates the vehicle in a negligent or criminal manner. If the borrower is using your car for business purposes, your personal auto policy likely won't cover that either.

If you have a regular long-term arrangement to either borrow or to lend a car, the borrower should probably be added to the owner's personal auto policy. Those who don't own a car, but often borrow one, might also consider "named non-owner coverage," an endorsement that provides bodily injury and property damage liability, uninsured motorist coverage and more.

Ultimately, it's usually safe to loan your friend your car for occasional errands or projects. The same goes for borrowing a car. Just make sure it's for "normal" use. You'll want to confirm that the car has coverage and that your insurance, whether you're the owner or the borrower, will apply.

If you have any questions, feel free to give us a call — after all, you don't want to wait until after an accident to get answers!

Suzanne M. Valicenti
President/CEO

Cost Basis of Bond Amortization

Over the past decade, you've seen interest rates go lower and lower. Savings accounts yield close to nothing, CDs get maybe 1% and your bond portfolio yields somewhere around 3%. In this low rate environment, you can still buy bonds with higher coupon payments, maybe 4 or 5% a year, but you'll have to pay a premium to get access to them. However, unlike a bond not trading at a premium, you'll receive less than what you paid at maturity, excluding interest payments. So, how does that work from a tax perspective?

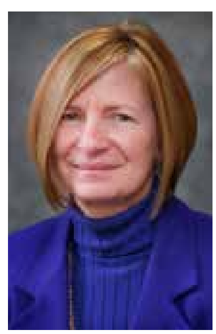
Knowing how much tax you'll pay on a stock is fairly straightforward. You buy it at "x" sell it for "y" and "harvest" the difference based on your tax bracket and the time held. A bond acts much differently. When you buy a bond, it's either at par ($1,000), a discount (<$1,000) or a premium (>$1,000). With a stock, you don't know what that future selling price will be but, with a bond, the price pulls to par. That means regardless of how much you paid for it, when the bond matures, you should receive par per bond. For example, if you paid $10,500 for $10,000 worth of bonds that will mature in five years, you'll slowly lose $500 over that time period (not including the interest payments). The IRS realizes this as well and has allowed investors to amortize this movement (done automatically at brokers since 2014).

Amortization means distributing expenses over the useful life of an asset, which is maturity in the case of a bond. In the example above, you could realize that $500 loss at maturity but, since you're receiving periodic payments, you should match income with expenses. Therefore, every year that you hold the bond, you'll realize a slight loss, based on an amortization table to help offset your taxes. The opposite holds true for a discount bond as well. Since you paid $9,500 for $10,000 worth of bonds, you'll owe taxes on $500 over time, as the price pulls to par.

No one enjoys paying extra for things, but a premium bond may help you meet your goals. Knowing about bond amortization could help you in dealing with the tax man each year!

Matthew L. Melott
Security Analyst/Trader

KISS Method for Taxes (Keep It Simple Sweetie)



Doing your taxes can be complicated, so any chance you can get to keep things simple is usually much appreciated. Suspending the personal exemptions of $4,050 and almost doubling the standard deduction are just a couple of instances in which the IRS gives you a break. Tax reform made dramatic changes to the standard deduction and the personal exemption deduction. Let's look more closely at what the amounts for the standard deduction will be and the changes from last year.

How much the standard deduction amounts for 2018 increased

During most years, standard deductions increase by small amounts to reflect inflation, however, thanks to tax reform, the increases in the standard deductions for 2018 were really big.

Filing Status	Standard Deduction for 2018 Tax Year	Standard Deduction for 2017 Tax Year
Single or MFS	$12,000	$6,350
Married filing jointly	$24,000	$12,700
Head of household	$18,000	$9,350

SOURCE: IRS

In addition, some taxpayers get even larger standard deductions. If you're 65 or older, then you can add $1,600 to your standard deduction if you're single or $1,300

See **Method** *on Page 4*

Changes to Meal and Entertainment Expenses

Starting in 2018, the Tax Cut and Jobs Act of 2017 imposed additional limitations on the deductibility of certain business meals and entertainment. If you are an employee, these expenses are no longer deductible. If you are a business owner or independent contractor, the changes may effect what you are able to deduct. No deductions are allowed for entertainment, amusement or recreation. Examples of deductions that are no longer deductible are golf outings, show tickets, spa visits, sports tickets or outdoor sports outings.

Under the old 2017 rules, entertainment-related meals, sporting event tickets and club memberships were partially or fully deductible. Under the new tax law, no deductions are allowed. This means if your business meal is included in entertainment, neither is deductible. Meals included in charitable sports package were 100% deductible. Under the new law, they are 50% deductible.

Meals provided for the convenience of the employer or meals provided to employees occasionally and overtime meals were 100% deductible. Water, coffee and snacks provided at the office were also deductible 100%. Those expenses are only 50% deductible under the new rules and will be nondeductible after 2025.

Several expenses such as client business meals remain 50% deductible. Business must be conducted and the taxpayer needs to be present for the meal to be deductible. The meal cannot be lavish or extravagant. Meals during business travel remain 50% deductible. Meal expenses for business meetings of employees are 50% deductible. Office meetings and partner meetings are included in this category and are 50% deductible, as long as there is a business purpose. Meals at a convention or seminar are 50% deductible. If the cost of the meal is not separately stated from the

See **Changes** *on Page 4*

Qualified Business Income Deduction

Nothing gets a tax preparer more excited than a new Internal Revenue Code section. Well, this is it – Section 199A – Qualified Business Income Deduction (QBID). This deduction only applies to an entity that is not a C-corporation. Besides sole proprietorships, S-corporations and partnerships, trusts and estates also qualify as being eligible for this 20% deduction.

To qualify for QBID, the entity cannot be classified as a "specified service business" and the eligible income of the entity must be ordinary income (as opposed to capital gains income). A specified service business involves the performance of services in several different fields such as health, law, accounting, investing, performing arts, consulting and others. The key determinant is if the business performs services where the "principal asset" of such trade or business is the reputation or skill of one or more of its employees or owners.

The deduction is not a flat 20%. There is a somewhat complicated formula, which is determined by applying an "applicable percentage" to the taxpayer's share of qualified business income, the business W-2 wages and unadjusted basis of qualified business property. There is one more part of the calculation that determines the deduction based on income thresholds relating to marital filing status. Once these calculations have been made, the deduction is calculated as 20% or less.

This new code section will provide an interesting twist to the tax returns of owners of flow-through entities.

Paul E. Hornbuckle, CPA
Vice President of Tax and Business Services

Changes

(continued from Page 3)

convention or seminar, it must be calculated by the taxpayer.

Office holiday parties or company picnics remain 100% deductible. Food made available to the public for free, such as at a promotional campaign or seminar, is 100% deductible. If the meal expense is included as taxable compensation to the employee or independent contractor, then the expense can be deducted 100%.

Businesses will still need to keep documentation to substantiate the deduction. Documentation should include the amount, time, date and place of the expenditure. The attendees and purpose of the business discussion should be included as well. It is important to set up accounts such as 0% deductible, 50% deductible or 100% deductible to track each meal category separately.

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Method

(continued from Page 3)

if you're married. Those who are blind get the same boost to their standard deduction. The Child Tax Credit and New Family Credit are two more changes to the tax law which help to increase credits for families. The Child Tax Credit doubles per qualifying child under the age of 17 from $1,000 to $2,000 and allows parents to receive up to $1,400 as a refund, if the credit is larger than their federal income tax liability. The credit is available to far more households, thanks to a massive raise in the phase out thresholds. Also, the new non-refundable Family Credit of $500 is allowed for each person that is not a qualifying child, but is a qualifying dependent under the old dependency rules; therefore, a child over age 16 that no longer qualifies for the $2,000 credit may be allowed a $500 credit, assuming that the old dependency rules are met.

It's better, but you're losing a vital tax benefit at the same time

It's important to realize that while the Child Tax Credit is going up, taxpayers are losing the personal exemption that until now has been obtainable for every taxpayer and each of his/her dependents.

For 2018, before the new tax bill was passed, the personal exemption was set to rise to $4,150 per person. As a result, a married couple with two children would have been permitted to four of these.

The loss of the taxpayers' personal exemptions is more than offset by the big increase in the 2018 standard deduction. In the case of dependents, the new higher child tax credit helps make up the difference.

To clarify this, the $1,000 in additional credit for each child will be more than the benefit from the personal exemption that many taxpayers would have been entitled to, particularly for middle-income households in the lower tax brackets and people whose incomes were formerly too high to use the credit at all. It's not truly "doubled" when you factor in the personal exemption loss.

So is it really the KISS METHOD?

Evelyn L. Bristol
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Please note that our Tax and Business Services Department, our Insurance Division and our Investment Advisors are available to answer any questions that you may have regarding the articles in this publication. We look forward to hearing from you.