Items Affecting 2018 Tax Returns

(updated 2/16/19)

The Tax Cut and Jobs Act (TCJA) generally took effect 1/1/18. TCJA made substantial changes to common deduction you may have taken in the past and will be in effect through 12/31/25. The IRS has yet to issue guidance in some areas, so it may be better to wait to file affected returns until they do so. Here are highlights of some of the issues affecting most returns and items for which we will require additional information to prepare your return:

Business & Rental

1. C-Corporations are taxed at a flat rate of 21%. There is still the penalty tax for personal holding companies.
2. All businesses and K-1s must now include additional information on the type of business, total assets and wages (including the wage portion of staff leases) in order for individuals to properly compute their personal Qualified Business Income Deduction (QBID). See QBID section below.
3. Rental real estate activities will generally <u>not</u> qualify for the QBID unless certain criteria are met. If these criteria are met, you will need to comply with the 1099 requirements. See QBID section below.
4. Entertainment costs are no longer deductible. Make sure they are separately categorized from meals.
5. Business meals are still 50% deductible. You must still keep a record of who was there and the business purpose of the meeting.
6. Meals for the convenience of the employer are now 50% deductible.
7. Reimbursements for moving expenses must be included in W-2 wages and taxed accordingly, except for certain members of the armed forces.
8. Partnership audit rules have changed significantly in that, unless an exception can be met, any increase in partnership taxable income for prior years under audit will be assessed tax at 35-37% tax rate to the PARTNERSHIP (rather than the individual partners) in the <u>current year</u>. Aside from the potential collection/reimbursement challenges, this creates additional issues where partner interests have changed over the years. <u>You may need to amend your LLC/partnership agreements</u>.
9. Like kind exchanges and the deferment of the gain has been limited to only real property. The exchange of any non-real property is treated as a sale and purchase.
10. For net operating losses (NOL) arising in 2018 and after, the NOL carryovers are limited to 80% of the taxable income of the year to which they are applied.

Individuals

1. The home mortgage interest deduction was changed, with some minor grandfather provisions. Residential mortgage interest is only deductible if the money was used to buy or improve the primary or secondary residence it is secured by and the total loan balances do not exceed $750,000 (the previous limit was $1 million). Home equity interest (on prior or new home equity loans) is no longer deductible, unless all the funds were used to buy or improve the residence.
2. Miscellaneous itemized deductions on Schedule A are no longer deductible.
3. The deduction on Schedule A for taxes paid (real estate, state income, sales taxes, personal property, etc.) is limited to a total of $10,000.
4. The overall limitation on Schedule A, itemized deductions, has been eliminated.
5. The deduction for personal exemptions is gone for now, but they increased the standard deduction to almost double what it was
6. Tax rates have been restructured and will generally be lower for most folks.
7. For new or revised alimony agreements, alimony is no longer deductible, nor does it have to be included in the recipient’s income.
8. Moving expenses are no longer deductible, except for certain members of the armed forces.
9. Personal casualty and theft losses are no longer deductible, except if in a federally declared disaster area.

10. The child tax credit has been increased, along the due diligence requirements (Form 8867) to verify the actual existence and residence of household members for tax credits and Head of Household status. In this regard, we may ask you for more information than we have in the past.
11. In order to compute the QBID, there will need to be more information disclosed on the K-1s you receive and for your schedule C business interest, including wages the business paid and depreciable assets. If the required information is not disclosed, you will have to obtain it in order for the deduction to be properly computed.
12. You can no longer undo IRA to ROTH conversions.

Qualified Business Income Deduction (QBID)

1. To provide parity for the reduced 21% corporation tax rate, a Qualified Business Income Deduction (QBID) is now available to <u>individual taxpayers</u>.
2. An individual taxpayer generally may deduct 20% of qualified business income from a partnership, S corporation, or sole proprietorship, as well as 20% of aggregate qualified REIT dividends, qualified cooperative dividends, and qualified publicly traded partnership income. The deduction is limited by individual taxable income.
3. In the case of a partnership or S corporation, the deduction applies at the individual partner or shareholder level.
4. For taxpayers with 2018 taxable income that exceeds $315,000 for a married couple filing a joint return, or $157,500 for all other taxpayers, the deduction is subject to limitations such as the type of trade or business, the taxpayer's taxable income, the amount of W-2 wages paid by the qualified trade or business and the unadjusted basis immediately after acquisition (UBIA) of qualified property held by the trade or business. Income earned through a C corporation or by providing services as an employee is not eligible for the deduction.
5. If taxable income is below the $315,000/$157,500 threshold, the deduction is available for all qualified business income, even that from a specified service trades or businesses (SSTB).
6. Special rules apply to specified agricultural or horticultural cooperatives.
7. Most of the information required to compute the deduction must be provided by the business entity to the individual investors. All businesses and K-1s must now include additional information on the type of business, total depreciable assets and wages in order for individuals to properly compute their QBID.
8. Recent Treasury Regulations have clarified that not *all* direct real estate investing will actually qualify for the QBID. Instead, investors must be able to demonstrate that they are operating a real estate "business" in order to qualify and show that either they personally, or other employees of the business, are spending a substantial amount of time actually engaged with the real estate (to differentiate a *business* from a mere real estate "investment" instead).
9. If you expect to take the QBID for your rental real estate as a qualified trade or business, you must issue 1099s to all persons you paid for services, aggregating $600 or more, during the year. 1099s must be issued by January 31.
10. There are special safe harbor rules for real estate that will allow the QBID to apply, even though the rental real estate is not a qualified trade or business. See IRS Notice 2019-07
11. Triple net lease activities do NOT qualify for the QBID.