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Tax, Benefits, and Private Client

JANUARY 2018 • NO. 2

2017 New Tax Law: Tax Planning—Accelerate Deductible Expenses before Year End

*This client alert is part of a special series on the Tax Cuts and Jobs Act and related changes to the tax code, where Blank Rome's lawyers share their analysis of different provisions in the Act and how they may affect you and your business, along with specific action items. To see the full list of client alerts in this series, please click **here**.*

On December 20, 2017, Congress passed its comprehensive tax reform bill, the Tax Cuts and Jobs Act ("the Act" or "the Bill"), which is expected to be signed into law by President Trump in early January 2018. The Bill represents one of the most extensive modifications to the U.S. tax code in recent history, significantly modifying U.S. taxation for individuals and businesses. Most provisions in the bill take effect on January 1, 2018.

2017 TAX PLANNING: ACCELERATE DEDUCTIBLE EXPENSES BEFORE YEAR END

Actionable Advice: As a result of the increase in the standard deduction and the elimination of many itemized deductions and limitations on remaining itemized deductions, individual taxpayers should consider accelerating certain deductible expenses into 2017.

Background

Individual taxpayers can deduct the greater of the standard deduction or eligible itemized deductions. Effective January 1, 2018, the standard deduction is increased from $6,350 for individuals and $12,700 for married couples filing jointly to $12,000 for individuals, and $24,000 for married couples filing jointly.

Under the Act, the only allowable itemized deductions are:

1. **Home mortgage interest.** Through 2025, a taxpayer may deduct interest on up to $750,000 of the aggregate indebtedness used to acquire, construct, or substantially improve the taxpayer's principal and/or secondary residence ("acquisition indebtedness") or $375,000 in the case of married taxpayers filing separately. In the case of acquisition indebtedness incurred before December 15, 2017, the aggregate limitation is $1,000,000, or $500,000 in the case of married taxpayers filing separately. Further, interest on a home equity loan is not deductible.

2. **State and local taxes.** Through 2025, an individual may claim an itemized deduction of up to $10,000 ($5,000 for married taxpayer filing a separate return) for the aggregate of (i) state and local property taxes not paid or accrued in carrying on a trade or business, or an activity described in section 212, and (ii) state and local income, war profits, and excess profits taxes (or sales taxes in lieu of income, etc. taxes) paid or accrued in the taxable year. Further, an individual may not claim an itemized deduction in 2017 on a pre-payment of income tax for a future taxable year in order to avoid the dollar

limitation applicable for taxable years beginning after 2017. Notably, this limitation does not apply to the pre-payment of property taxes.

3. **Charitable contributions.** With limited exception, deductions for charitable contributions are still permitted, with an increase in the percentage limit for charitable contributions of cash to public charities to 60 percent of adjusted gross income ("AGI") (from 50 percent of AGI). However, the Act eliminates a charitable deduction for payments made in exchange for college athletic event seating rights.

4. **Medical expenses.** Through 2025, the Act increases the floor for the deduction of medical expenses. For 2017 and 2018 these expenses can be claimed as itemized deductions to the extent they exceed 7.5 percent of AGI. Under current law, the floor was 10 percent of AGI, except that for 2017 it was 7.5 percent of AGI for age-65-or-older taxpayers.

The reduction of and limitation on allowable itemized deductions combined with the increase in the standard deduction will mean that many individual taxpayers will not be able to itemize their deductions and therefore will not receive a benefit from a portion of mortgage interest on their primary or a second home or on home equity loans and will not receive a benefit from the payment of state and local taxes in excess of $10,000 per year. Further, since total allowable itemized deductions must exceed the standard deduction, many individuals will not receive a benefit from their charitable contributions. For example, a married couple who does not have a mortgage and is capped at $10,000 of state and local taxes, will receive no benefit from their charitable contributions unless their charitable giving exceeds $14,000 per year.

Specific Action Items to Consider: Taxpayers who may be affected by the changes described above should consider the following before December 31, 2017:

1. **Accelerate charitable giving.** Consider making additional charitable gifts this year. Charitable giving for future years can be prefunded, resulting in a current deduction, through the use of a Donor Advised Fund or Private Foundation. Make sure that your check is dated and mailed in 2017 or pay online using your credit card before the end of this year.

2. **Prepay property taxes.** Taxpayers may be able to prepay their property taxes this year. Again, make sure that your check is dated and mailed in 2017 or pay online using your credit card before the end of this year. However, check with your local taxing authority as certain jurisdictions will not accept property tax pre-payments.

3. **Prepay 2017 income taxes.** Consider paying all or a portion of your 2017 state and local tax liability by December 31. Please note that this prepayment applies to your fourth quarter 2017 estimate only since you are not permitted to receive a deduction for prepaying your 2018 state tax liability.

4. **Prepay medical expenses.** To the extent possible with only a few days remaining in the year, consider accelerating "discretionary" medical expenses into this year. For example, before the end of the year, get new glasses or contacts, or see if you can squeeze in other medical expenses if you will be able to deduct them this year.

Caution: Individuals are urged to check with their tax return preparer to make certain that they will be able to take advantage of any accelerated deductions on their 2017 income tax return. For example, any benefit may be reduced or eliminated for taxpayers who are subject to the Alternative Minimum Tax, charitable deductions are subject to complex AGI limits, and all existing itemized deductions are subject to an overall limitation for certain high income taxpayers.

Clients who would like more information about their specific circumstances should contact a member of Blank Rome's Tax, Benefits, and Private Client practice group.

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