Taxation of Individual Income

ELEVENTH EDITION

SPRING 2018 SUPPLEMENT

Addressing changes resulting from the 2017 tax legislation

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Chapter 1

INTRODUCTION

On December 22, 2017, President Donald Trump signed into law major tax legislation commonly referred to as the "Tax Cuts and Jobs Act of 2017." In broad overview, the legislation affects the topics covered in Chapter 1 in the following ways*:

temporarily reduces the individual income tax rates under § 1;

temporarily increases the standard deduction provided by § 63;

temporarily eliminates the personal exemption of § 151;

temporarily disallows miscellaneous itemized deductions under § 67; and

temporarily suspends § 68.

** We note § 199A provides a deduction of 20% for "qualified business income." Although having limited applicability to the Chapter 1 Problem, we recommend that discussion of this complex "pass-through deduction" be deferred until Chapter 12 which will address issues. including "qualified business income," "qualified trade or business," "specified service trade or business," and the exception for "specified service businesses based on a taxpayer's income."*

Page 5, last paragraph:

There is a reference to alimony as having tax consequences. Note the 2017 tax legislation eliminates both the inclusion and deduction provisions related to alimony for any divorce or separation instrument executed after December 31, 2018.

Page 9, first paragraph:

Pursuant to the 2017 tax legislation, the top individual income tax rate will be 37% through December 31, 2025. § 1(j)(2). Maximum rates on net capital gains and qualified dividends remain unchanged.

Page 9, second paragraph:

For taxable years beginning after December 31, 2017, and before January 1, 2026, the personal exemption of § 151 is suspended. Thus, during the suspension period, for individuals who do not itemize their deductions, "taxable income" means adjusted gross income minus the standard deduction and the so-called "pass-through deduction" of § 199A . For all other individuals, "taxable income" means adjusted gross income minus the deductions allowed by Chapter 1 (including the "pass-through deduction") other than the standard deduction.

Page 9, third paragraph:

The paragraph notes a list of 15 items constituting gross income. As of 2019, that list will be reduced as a result of the elimination of § 61(a)(8) regarding alimony.

Page 10, last full paragraph:

The paragraph notes a top tax rate of 39.6%; that rate as of January 1, 2018 will be 37% through 2025.

Page 11, last paragraph:

The last paragraph notes that approximately 2/3 of filers have taken advantage of the standard deduction. That fraction will undoubtedly increase given the increased standard deduction provided by the new tax legislation.

Page 12:

In footnote 1, delete the reference to the basic standard deduction for 2015. For 2018, the basic standard deduction will be $24,000 for married individuals filing jointly; $18,000 for heads of household; and $12,000 for unmarried individuals.

Page 13, last full paragraph:

Delete the last sentence of the last full paragraph. The management fee is a miscellaneous itemized deduction and, as such, is disallowed under § 67(g) as added by the 2017 legislation. See update for page 16.

Page 14, third full paragraph:

This paragraph indicates there is an above-the-line deduction for interest expense incurred in a trade or business. The tax legislation limits the business interest deduction, a topic addressed in Chapter 12.

Page 14–15:

These paragraphs discuss a range of state and local taxes and note that Caroline is put to an election regarding the deduction of state income tax or the sales tax. While, under the 2017 tax legislation, Caroline will be subject to the same election, she is limited to a $10,000 deduction in the aggregate for real property taxes and state income (or sales) taxes. Although Caroline's real property taxes and state income tax (in lieu of the sales taxes) total $19,000, her deduction will be limited to $10,000.

Page 15, carryover paragraph:

Delete footnote 2.

Page 15, first full paragraph:

Note the increase to 60% in the § 170(b)(1)(A) limit for cash contributions to charities. § 170(b)(1)(G).

Page 15, calculation of adjusted gross income:

The calculation of Caroline's gross income of $320,000 and her adjusted gross income of $230,000 remains unchanged. However, Caroline's below-the-line deductions are reduced to $37,000 (as a result of the $10,000 limitation on the total of the real property taxes and state income tax and the disallowance of the management fee).

Page 16, carryover paragraph at the top of page:

Under the new tax legislation, Caroline's standard deduction as an unmarried individual is $12,000. Given her itemized deduction of $37,000, Caroline will obviously opt to itemize.

Page 16:

Add the following sentence to the end of the § 67 paragraph:

> Because the bank management fee is a miscellaneous itemized deduction, it is disallowed for taxable years beginning after December 31, 2017, and before January 1, 2026, regardless of whether the miscellaneous itemized deduction exceeds 2% of adjusted gross income.

Delete the § 68 paragraph as this Code sections have been suspended for taxable years beginning after December 31, 2017, and before January 1, 2026. Also, delete footnote 3.

Page 17:

Delete the three paragraphs addressing the personal exemption and footnotes 4 and 5.

Delete the calculation of taxable income and insert the following in its place:

Adjusted Gross Income ----------------------------------$230,000
less: Itemized Deductions ------------------------------$ 37,000
Taxable Income ---$193,000*

* As noted in the preface to this update, we are not addressing the detail of the pass-through deduction of § 199A. We therefore have not calculated the amount of that deduction for purposes of this hypothetical. The pass-through deduction will be developed in detail in Chapter 12.

Page 18, first paragraph:

Note the seven new brackets in § 1(j) of the tax legislation. For the taxable years 2018 through 2025, the brackets are: 10%, 12%, 22%, 24%, 32%, 35% and 37%.

Delete the calculation of Caroline's tax for 2015. Insert in its place the following calculation:

Under the tax rate table of § 1(j)(2)(C) for 2018, the tax on a return with taxable income of $193,000 is $32,089.50 on the first $157,500 plus $32% of the excess over $157,500 or $11,360. Thus computed, Caroline's *preliminary* § 1(j)(2)(C) tax liability is $43,449.50. This liability is preliminary because it can be affected by maximum capital gain provisions of § 1(h). As noted in the second paragraph on page 18, Caroline's net capital gain remains unchanged at $16,000 and will be taxed at a 15% rate. Accordingly, Caroline's tax liability is limited to the sum of two amounts:

(1) the regular § 1(j)(2)(C) tax on $ 177,000 which is $38,329.50 (The $177,000 figure represents the previously determined taxable income of $193,000 less the net capital gain $16,000 - which would otherwise be taxed at 32%); plus

(2) the special § 1(h) tax rate of 15% on the $16,000 net capital gain, which equals $2,400. But for § 1(h), this $16,000 would be taxed at the higher rate of § 1(j).

Applying § 1(h), the § 1 tax liability is thus $40,729.50.

Page 18, last sentence of last paragraph:

Note that, in view of the above calculations, Caroline will owe the U.S. Treasury $729.50 ($40,729.50 minus $40,000).

Delete footnote 6.

CHAPTER 2

GROSS INCOME: CONCEPTS AND LIMITATIONS

Page 24, last full paragraph:

The paragraph notes alimony as an example of gross income. Under the new tax legislation, alimony and separate maintenance payments do not constitute gross income under a divorce or separation instrument entered into after 2018.

Page 30. end of the only full paragraph on the page:

As will be discussed in later chapters, the 2017 tax legislation imposes new limitations on both the deduction of home mortgage interest and real property taxes.

CHAPTER 5

GIFTS, BEQUESTS AND INHERITANCE

Page 95, footnote 1:

Section 274(j), as amended by the 2017 tax legislation, further limits the definition of employee achievement awards. See Chapter 7 update *infra*.

CHAPTER 7

SCHOLARSHIPS AND PRIZES

Page 135, last full paragraph:

The paragraph notes the transfer-to-charity rule of § 74(b)(3) may be useful where itemized deductions are less than the standard deduction, a circumstance likely to occur more frequently given the 2017 legislation. In the update to Chapter 1, note the doubling of the standard deduction under the new legislation.

Page 135–136, carry-over paragraph:

The last sentence on page 135 notes that a qualifying "employee achievement award" (excludable from the employee's income and deductible by the employer) must consist of "tangible personal property." The 2017 legislation amends § 274(j)(3) to exclude a variety of items, such as cash, most gift cards, meals, lodging, securities and "similar items" from the definition of "tangible personal property."

CHAPTER 8

LIFE INSURANCE AND ANNUITIES

Page 153, second full paragraph:

The paragraph notes the transfer-for-value rule of § 101(a)(2) limiting the exclusion under § 101(a)(1). The 2017 tax legislation adds § 101(a)(3) pursuant to which the second sentence of § 101(a)(2) shall not apply to commercial transfers designated as "reportable policy sales."

Page 162, second full paragraph:

The 2017 legislation repealed the rule permitting contributions to a non-Roth IRA to be recharacterized as contributions to a Roth IRA. § 408A(d)(6)(B)(iii).

CHAPTER 9

DISCHARGE OF INDEBTEDNESS

Page 167, Code assignment and throughout the Chapter:

Section 61(a)(12) is temporarily renumbered § 61(a)(11). (See previous comments on the elimination of alimony as an item of gross income.)

Page 176, second full paragraph:

The 2017 tax legislation amended § 108(f) (excluding from gross income the discharge of certain student loans) to extend the exclusion, for discharges after December 31, 2017, and before January 1, 2026, to discharges on account of the death or total and permanent disability of the student. § 108(f)(5).

Page 177, second full paragraph:

Note the 2017 tax legislation did not extend the exclusion provided by § 108(a)(1)(E), which was scheduled to expire as of December 31, 2016.

CHAPTER 11

FRINGE BENEFITS

Page 219, last paragraph:

The paragraph notes § 119 excluding from gross income meals furnished to an employee (or an employee's spouse or dependent) for the convenience of the employer. The new tax legislation does not repeal this exclusion, but provides the employer may not deduct amounts paid for such meals after 2025! § 274(o) (as amended).

Page 222, first full paragraph and footnote 2:

The paragraph and footnote refer to qualified moving expense reimbursement (also addressed in Chapter 19) as an excludable fringe benefit under § 132(a)(6). The 2017 tax legislation suspends that exclusion in taxable years beginning after December 31, 2017, and before January 1, 2026 except for active-duty members of the U.S. Armed Forces. § 132(g)(2) (as amended).

Page 228, last paragraph regarding *de minimis* fringe benefits:

This paragraph references a regulation provision addressing the exclusion of the value of meals at an employer operated eating facility as a *de minimis* fringe benefit. That regulation is supported by § 132(e)(2). Effective for amounts incurred or paid after December 31, 2025, however, there will be no employer deduction for the operation of such a facility or for the expense of food or beverage associated with such a facility. § 274(o)(1)(as amended).

Page 228–29:

The 2017 tax legislation eliminates the employer deduction for any "qualified transportation fringe" benefit for amounts paid or incurred after December 31, 2017. § 274(a)(4). In addition, the exclusion under § 132(a)(5) for qualified bicycle commuting reimbursement is suspended for taxable years beginning after December 31, 2017, and before January 1, 2026. § 132(f)(8) (as amended). The 2017 legislation also provides that "no deduction is allowed ... for any expense incurred for providing any transportation, or any payment or reimbursement, to an employee of the taxpayer in connection with travel between the employee's residence and place of employment, except as necessary for ensuring the safety of the employee."

Chapter 12

BUSINESS AND PROFIT SEEKING EXPENSES

Page 251, following first full paragraph:

Deduction for Qualified Business Income of Pass-Thru Entities. The 2017 tax legislation added a major new business deduction (the so-called "pass-through deduction"[1]) allowable to individuals in their capacities as sole proprietors, as partners in a partnership, or as shareholders in an S corporation.[2] More specifically, § 199A provides individuals with a 20-percent deduction which will generally equal the **lesser** of

(a) the taxpayer's "combined qualified business income" or

(b) 20% of the excess of the taxpayer's taxable income over net capital gains (as defined in § 1(h)).[3]

In no event, however, will the deduction exceed the taxable income reduced by the taxpayer's net capital gain for the taxable year.

Unless the taxpayer's taxable income for the taxable year exceeds a threshold amount ($157,000 or $315,000 in the case of joint returns) adjusted for inflation, the "combined qualified business income" is generally 20% of the taxpayer's "qualified business income" with respect to a "qualified trade or business."[4] (If the taxpayer's taxable income exceeds the threshold amount, the "combined qualified business income" is reduced pursuant to § 199A(b)(3)(B).)

Qualified business income" is defined in § 199A(c)(1) as generally equaling "the net amount of qualified items of income, gain, deduction, and loss with respect to any qualified trade or business of the taxpayer." The term "qualified items of income, gain, deduction, and loss" includes only those items "effectively connected with the conduct of a trade or business within the United States" and must be "included in determining taxable income for the taxable year." The term does not include, among other items, capital gains and losses, dividends, interest income (other than interest income allocable to a trade or business), or reasonable compensation

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[1] Income earned by a partnership or S corporation is not taxed to the partnership or S corporation, but is instead "passed through" and taxed directly to the partner or S corporation shareholder; hence the label "pass-through deduction."

[2] The deduction" is not allowable to corporations taxed under Subchapter C of the Code.

[3] § 199A(a)(1). This assumes the taxpayer has no "cooperative dividends - a topic which is beyond the scope of this casebook.

[4] This assumes the taxpayer has no qualified REIT dividends or qualified publicly traded partnership income for the taxable year. REIT dividends and qualified publicly traded partnership income are not topics addressed in this casebook.

paid to the taxpayer by a qualified trade or business for services rendered to the business. § 199A(c)(3)(A), (B) and (c)(4)(A).

The term "qualified trade or business" does not include the trade or business of performing services as an employee. §199A(d)(1)(B). It also does not include a "specified service trade or business." § 199(A(1)(A). A "specified service trade or business" includes "the performance of services in the fields of 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." §§ 199A(d)(2)(A); 1202(e)(3)(A).[5] An exception is made whereby a specified service business will be treated as a qualified trade or business if a taxpayer's taxable income does not exceed a certain amount. In that circumstance, however, the deduction is capped. § 199A(d)(3).

The "pass-through deduction" is not allowed in computing adjusted gross income. § 62(a), as amended. It is allowed to nonitemizers (§ 63(b), as amended); and it is allowed to itemizers without limits on itemized deductions. § 63(d), as amended. The deduction is not applicable to taxable years beginning after December 31, 2025. § 199A(i).

New limitation on business deductions. The 2017 tax legislation created a new limitation on business deductions, a limitation on the "excess business losses" of noncorporate taxpayers. See § 461(l), and the Chapter 27 update, *infra*.

Limitation on business interest deduction. The 2017 tax legislation added a limitation on the deduction for business interest. Under § 163(j), as amended , the deduction for business interest is limited, for most taxpayers covered by the provision, to the sum of the taxpayer's business interest income plus 30 percent of the taxpayer's taxable income, as adjusted. The disallowed business interest is carried over to the following year. The limitation does not apply to businesses that meet the gross receipts test of § 448(c)(3), that is, taxpayers with gross receipts that do not exceed $25,000,000.

Pages 260–61, footnote 2:

Section 162(m) was amended by the 2017 tax legislation. The amendment repeals the "performance-based" and "commission" exceptions to the deduction limitation; modifies the definition of "covered employees;" and expands the definition of "applicable employer." The amendment is effective generally for taxable years beginning after December 31, 2017.

[5] Engineering and architecture, however, are excluded from the definition of "specified service trade or business." § 199A(d)(2)(A).

Page 265, last paragraph beginning on this page:

The § 162(f) disallowance of deductions for fines or similar penalties paid to a government for the violation of any law was broadened in the 2017 tax legislation to include any amount paid or incurred "to or at the direction of a government or governmental entity in relation to the violation of any law or the investigation or inquiry by such government or entity into the potential violation of any law." Certain exceptions are provided.

Page 267, footnote 7:

The 2017 tax legislation repealed the exception for local lobbying expenses contained in the disallowance of deductions for lobbying expenses in § 162(e).

Page 265, last paragraph beginning on this page:

The 2017 tax legislation added amended § 162(q) providing that no deduction is allowed for settlements or payments or attorney's fees related to sexual harassment or sexual abuse if the settlement or payment is subject to a nondisclosure agreement.

Page 270, first full paragraph:

The last sentence refers to deductible employee expenses and § 67. As miscellaneous deductions under § 67, employee business expenses are nondeductible for taxable years beginning after December 31, 2017, and before January 1, 2026. See Chapter 1 update, *supra.*

Page 272, footnote 8:

See page 270 update, *infra*, relating to employee business expenses.

Chapter 14

DEPRECIATION

Pages 333–34, last paragraph:

The 2017 tax legislation amended § 168(k) in two particularly significant ways. First, § 168(k) now provides 100-percent expensing for qualifying property placed in service for taxable years beginning after December 31, 2017, and before January 1, 2023; 80-percent expensing before January 1, 2024; 60-percent expensing before January 1, 2025; 40-percent expensing before January 1, 2026; and 20-percent expensing before January 1, 2027. § 168(k)(1)(A), (6)(A), as amended. Second, § 168(k) is extended to *used property* by broadening the definition of qualifying property to encompass not only property the "original use" of which begins with the taxpayer, but also property "that was not used by the taxpayer at any time prior to [the taxpayer's] acquisition," provided the taxpayer acquires the property by purchase. § 168(k)(2)(A)(ii), (E)(ii), as amended.

Page 335–37:

The 2017 tax legislation amended § 179 to increase the dollar limits for expensing under that provision. First, the dollar limit of § 179(b)(1) is increased from $500,000 to $1,000,000. Second, the dollar amount (in § 179(b)(2)) at which phase-out of § 179(b)(1) limit begins is increased from $2,000,000 to $2,500,000. § 179(b), as amended. The role of § 179 appears greatly diminished for years in which 100-percent expensing under § 168(k) is available. See the preceding note.

Chapter 15

LOSSES AND BAD DEBTS

Page 367, second full paragraph:

See the note *infra* regarding Chapter 24 and personal casualty losses.

Page 372, last full paragraph:

See the note *infra* in Chapter 27 for the disallowance of excess business losses for noncorporate taxpayers under § 461(l), as amended by the 2017 tax legislation.

Chapter 16

TRAVEL EXPENSES

Page 402, last paragraph:

The 2017 tax legislation prohibits any deduction to an employer for the expense of providing transportation, payment or reimbursement to an employee for travel between the employee's residence and place of employment, except as necessary for the safety of the employee. § 274(l), as amended.

Page 404, first full paragraph:

Most § 212 expenses, other than those attributable to rent and royalties, are miscellaneous itemized deductions and, as such, are nondeductible for taxable years beginning after December 31, 2017, and before January 1, 2026. See the Chapter 1 update, *supra.*

Page 404, last paragraph of Overview:

As noted in the update to Chapter 17, *infra*, entertainment expenses are nondeductible under the 2017 tax legislation.

Chapter 17

ENTERTAINMENT AND BUSINESS MEALS

Pages 425–31:

The 2017 tax legislation has eliminated any deduction for entertainment expenses. Section 274(a), as amended, now prohibits a deduction for any activity generally considered to constitute entertainment, amusement or recreation. The prior exception, allowing a deduction (albeit limited to 50 percent of the otherwise allowable expense by § 274(n)) for expenses directly related to, or associated with, the active conduct of a trade or business has been eliminated. The prohibition on deductions for facilities used in connection with the entertainment activity is retained. The special rule in § 274(a)(2)(C) allowing the deduction of certain club dues has also been eliminated. § 274(a), as amended. Conforming amendments have been made to § 274(d) and (n).

Page 427, first full paragraph:

As noted above, the deduction for entertainment expenses has been eliminated. The deduction for business meals, equal to 50 percent of the otherwise allowable amount, has been retained.

Page 431–432:

Because the deduction for the expenses of entertainment activities has been eliminated, the related substantiation requirements for such expenses under § 274(d)(2) have been repealed.

Page 432:

Note the update to page 427 to the effect that the deduction for business meals equal to 50 percent of the otherwise allowable amount has been retained.

Chapter 18

EDUCATION EXPENSES

Page 477:

The 2017 tax legislation extended § 529 to cover expenses for tuition, not in excess of $10,000, at an elementary public, private or religious school. § 529(c)(7), (e)(3)(A), as amended.

Chapter 19

MOVING EXPENSES, CHILD CARE, LEGAL EXPENSES

Pages 479–83:

The 2017 tax legislation suspended the § 217 deduction for moving expenses for taxable years beginning after December 31, 2017, and before January 1. 2026.

Chapter 20

HOBBY LOSSES

Pages 491–508:

The 2017 legislation effectively temporarily renders § 183 surplusage by disallowing miscellaneous itemized deductions for taxable years beginning after December 31, 2017, and before January 1, 2026. (See the Chapter 1 update, *supra*.) The effect of the temporary disallowance is to bar for the years in question any deduction for activities not engaged in for profit—i.e., for hobby losses—other than the deductions available whether or not an activity is engaged in for profit.

Page 497, first full paragraph:

Delete paragraphs two and three under the heading "Deductions Allowable Under Section 183." In lieu of those paragraphs, add the following paragraph:

> There are certain deductions, e.g., the home mortgage interest deduction and the deduction for real property taxes, which are allowed to a taxpayer whether or not an activity is engaged in for profit. Pursuant to § 183, other deductions attributable to an activity not engaged in for profit are allowable only to the extent the gross income from the activity exceeds these always-allowable deductions. The deductions § 183 makes allowable are miscellaneous itemized deductions under § 67(b). Prior to the 2017 tax legislation, miscellaneous itemized deductions were deductible to the extent they exceeded the § 67(a) 2% floor. As noted elsewhere in this Supplement, § 67(g), added by the 2017 tax legislation, disallows temporarily a deduction for all miscellaneous itemized deductions. In effect, at least for the next several years, the authorization under § 183 to deduct expenses to the extent of income from the activity, subject to the § 67 2-percent floor, is overridden by the § 67(g) disallowance of miscellaneous itemized deductions.

Chapter 21:

HOME OFFICES, VACATION HOMES, AND OTHER DUAL USE PROPERTY

Pages 520–21:

Computers or peripheral equipment have been removed from the list of "listed property" by the 2017 tax legislation. § 280F(d)(4), as amended.

Pages 521–22:

The § 280F(a)(1)(A) limits on depreciation for "luxury automobiles" have been increased by the 2017 tax legislation. The new limits for 2018 and succeeding years are: 1st taxable year - $10,000; 2nd taxable year - $16,000; 3rd taxable year - $9,600; and each succeeding taxable year - $5,760. § 280F(a)(1)(A), as amended.

Chapter 22

THE INTEREST DEDUCTION

Page 533, first full paragraph after indented quote:

The 2017 tax legislation imposes a limitation on the deductibility of business interest. See § 163(j) and the Chapter 12 update, *supra*.

Pages 534–37:

For taxable years beginning after December 31, 2017, and before January 1, 2026, the 2017 tax legislation has (1) disallowed the deduction for interest on home equity indebtedness by excluding such interest from the definition of "qualified residence interest"; and (2) lowered the $1,000,000 limitation on acquisition indebtedness to $750,000 ($375,000 for a married individual filing a separate return). Special rules apply to indebtedness incurred before December 15, 2017 and to binding contracts entered into before December 15, 2017. The elimination of the interest deduction on home equity indebtedness affects Examples 3 and 4 on page 536 and other references to home equity indebtedness on these pages. References to the $1,000,000 acquisition indebtedness limitation should now be understood to refer to a $750,000 limitation.

Chapter 23

THE DEDUCTION FOR TAXES

Page 559, footnote 1:

Note the § 164(b)(5) election to deduct state and local general sales taxes, in lieu of state and local income taxes, was made permanent in 2015.

Page 560, at the end of the carryover paragraph at the top of the page:

For years beginning after December 31, 2017, and before January 1, 2026, the 2017 tax legislation limits to $10,000 for any taxable year ($5,000 for a married individual filing a separate return) the aggregate amount taken into account for (1) state and local real property taxes; (2) state and local personal property taxes; and (3) pursuant to the § 164(b)(5) election, state and local income taxes or state and local sales taxes. Foreign real property taxes may not be taken into account at all. The $10,000 aggregate amount limitation does not apply to taxes in connection with carrying on a trade or business or an activity described in § 212, or to foreign income taxes. § 164(b)(6).

Chapter 24

CASUALTY LOSSES

Page 572, first paragraph:

The 2017 tax legislation significantly reduced the scope of the § 165(c)(3) casualty deduction. For taxable years beginning after December 31, 2017, and before January 1, 2026, a personal casualty loss (with an exception noted below) is deductible only to the extent it is attributable to a Federally declared disaster, as defined in § 165(i)(5). Thus, to the extent cases and rulings prior to 2018 discuss personal casualty losses not attributable to a Federally declared disaster, such losses would be nondeductible under current law even to the extent they exceed the 10-percent-of-adjusted-gross-income floor of § 165(h)(2)(A). The new legislation provides an exception where a taxpayer has a personal casualty gain. To the extent of the personal casualty gain, a loss that is not attributable to a Federally declared disaster may be deducted (subject to the § 165(h) limitations). If a taxpayer with a personal casualty gain also has a casualty loss attributable to a Federally declared disaster, the amount of the gain must be reduced by the amount of such loss before the taxpayer applies the exception permitting losses not attributable to a Federally declared disaster to be deducted to the extent of personal casualty gain. § 165(h)(5)(B).

The new legislation also provided what was essentially a retroactive suspension of the § 165(h) rule making a net casualty loss deductible only to the extent it exceeds 10 percent of the taxpayer's adjusted gross income. For 2016 and 2017 only, a taxpayer's "net disaster loss," attributable to a Presidentially declared 2016 major disaster, is deductible without regard to the 10-percent floor, but is subject to a $500 (not $100) reduction under § 165(h)(1).

Page 576:

In determining the amount of the casualty loss, see the page 572 update, *supra.*

Chapter 25

MEDICAL EXPENSES

Page 591, footnote 1:

The 2017 tax legislation extended the nondeductible 7.5 percent floor to all taxpayers (regardless of age) for the years 2017 and 2018. Unless further extended, the floor will be raised to 10 percent for all taxpayers for 2019 and later years. The 2017 tax legislation further provided that, for minimum tax purposes, the nondeductible floor is also 7.5 percent for 2017 and 2018.

Chapter 26

CHARITABLE DEDUCTIONS

Page 602, first full paragraph:

The top tax bracket under the 2017 tax legislation is 37 percent, not 39.6 percent. The dollar amount of $604 and $396 would become $630 and $370, respectively, in the 37-percent bracket.

Page 606, second full paragraph:

The 2017 tax legislation amended § 170(l) to bar any deduction for amounts paid in exchange for the right to purchase tickets at college athletic events.

Page 607, third full paragraph:

For cash contributions in taxable years beginning after December 31, 2017, and before January 1, 2026, the limitation on the taxpayer's deductible contributions is increased to 60 percent of the taxpayer's contribution base. § 170(b)(1)(G).

Page 614, second full paragraph:

The 2017 tax legislation repealed the exception to the § 170(f)(8) substantiation requirements for contributions reported to the Internal Revenue Service by the donee organization. § 170(f)(1)(D), prior to repeal.

Chapter 27

LIMITATIONS ON DEDUCTIONS

Page 661, at end of last paragraph:

Add new Part E as follows:

E. Limitation on Losses for Taxpayers Other Than Corporations

The 2017 tax legislation added new § 461(l), entitled "Limitation on Excess Business Losses of Noncorporate Taxpayers." The provision applies to taxable years of noncorporate taxpayers beginning after December 31, 2017, and before January 1, 2026. The "excess business loss" of such a taxpayer is nondeductible. An "excess business loss" is the excess of the taxpayer's deductions for the year attributable to trades or businesses of the taxpayer over the sum of (1) the aggregate gross income or gain for the year attributable to such trades or businesses plus (2) $250,000 ($500,000 on a joint return). See § 461(l)(3). The dollar amounts are adjusted for inflation. The disallowed loss is treated as a net operating loss carryover to the following year under § 172.

Chapter 28

CASH METHOD ACCOUNTING

Page 680, second full paragraph:

Section 451(h) is redesignated § 451(j) by the 2017 tax legislation.

Chapter 29

ACCRUAL METHOD ACCOUNTING

Pages 707–10:

The 2017 tax legislation has essentially codified Revenue Procedure 2004-34, discussed in these pages and included in the Chapter 29 Materials. Section 451(b), as amended by the new legislation, requires an accrual method taxpayer to treat the all events test as having been met, and thus to include an item in income, no later than the time the item is included under an "applicable financial statement," as defined in the statute, or such other financial statement as may be specified by the Secretary. § 451(b). Section 451(c), as amended by the new legislation, requires that accrual method taxpayers include "advance payments," as defined by the statute, in income upon receipt, subject to an election to defer inclusion until the following taxable year, except for any portion of the advance payment required, under amended § 451(b), to be included in the year of receipt. The statutory definition of "advance payment" generally applies the definition in Rev. Proc. 2004-34.

Page 717, last paragraph beginning on this page:

Section 448(a)(1) generally prohibits use of cash method accounting by C corporations and certain partnerships. An exception in § 448(b)(3) permits these entities to use the cash method if they satisfy a $5,000,000 "gross receipts test." The 2017 tax legislation increased that dollar limit permitting use of the cash method to $25,000,000. § 448(c), as amended.

Chapter 30

ANNUAL ACCOUNTING

Page 749, carryover paragraph:

The example assumes a standard deduction of $5,000 to illustrate the application of the tax benefit rule to a state income tax refund. Under the 2017 tax legislation, the standard deduction for an unmarried taxpayer in 2018 is $12,000.

Page 749, carryover paragraph and footnote 2:

Section 68 is suspended for taxable years beginning after December 31, 2017, and before January 1, 2026. See the Chapter 1 update, *supra.*

Page 751, carryover paragraph:

Section 172 has been amended by the 2017 tax legislation. For most taxpayers, the 2-year carryback period is eliminated and the carryover period is unlimited. § 172(b)(1), as amended. The amendment applies to net operating losses arising in taxable years beginning after December 31, 2017.

In addition, the 2017 tax legislation amended § 172(a) to provide that the net operating loss deduction for any year is the lesser of two amounts: (1) the aggregate of the net operating loss carryover and carryback to such year, or (2) 80 percent of the taxpayer's taxable income, computed without regard to the § 172 deduction. § 172(a), as amended. The amendment is effective for losses arising in taxable years beginning after December 31, 2017.

In computing a net operating loss, the deduction under § 199A is not allowed. § 172(d)(8).

Chapter 31

CAPITAL GAINS AND LOSSES

Page 774, bottom of the page:

Correct the heading to read: **Adjusted Net Capital Gain: 20-Percent, 15-Percent and 0-Percent Rates.** The 2017 tax legislation retains the 20-percent, 15-percent, and 0-percent rates for adjusted net capital gain. However, it uses new terminology to describe the 15-percent and 0-percent brackets. Section 1(h)(1)(B)(I) is amended to describe the 0-percent bracket, not in terms of taxable income "taxed at a rate below 25 percent," but in terms of taxable income "below the maximum zero rate amount." The maximum zero rate amount is $77,200 for a joint return or a surviving spouse; $51,700 for a head of household; and $38,600 for other individuals. The dollar amounts are adjusted for inflation. Section 1(h)(1)(C)(ii)(I) is amended to describe the 15-percent bracket, not in terms of taxable income "taxed at a rate below [the-then maximum rate of] 39.6 percent, but in terms of taxable income "below the maximum 15-percent rate amount." The maximum 15-percent rate amount is $479,000 for a joint return or surviving spouse; $239,500 for a married individual filing a separate return; $452,400 for a head of household; and $425,800 for other individuals. The dollar amounts are adjusted for inflation.

Page 786, second full paragraph:

Section 1221(a)(3) is amended by the 2017 tax legislation to apply to, and thus potentially exclude from capital asset status pursuant to that provision, "a patent, invention, model or design (whether or not patented), a secret formula or process." (A conforming amendment is made to § 1231(b)(1)(C), dealing with property excluded from the definition of "property used in the trade or business," and thus ineligible for capital gain or loss treatment under § 1231.)

Chapter 33

RECAPTURE OF DEPRECIATION

Page 829, first full paragraph:

The example in this paragraph ignores any depreciation conventions and any depreciation under § 168(k).

Page 832, first full paragraph:

The example in this paragraph ignores any depreciation conventions.

Page 833, last full paragraph under Example:

This paragraph refers to an income tax bracket of 39.6 percent. Under the 2017 tax legislation, the top tax rate is 37 percent.

Chapter 34

ASSIGNMENT OF INCOME

Page 845, second full paragraph:

The kiddie tax referred to in this paragraph was significantly changed by the 2017 tax legislation and is discussed in the update for Chapter 35, *infra*.

Page 846, last full paragraph:

This paragraph refers to § 704(e) as directed at "family partnerships." While § 704(e) was previously so-entitled, it is now entitled "Partnership Interests Created by Gift."

Chapter 35

THE KIDDIE TAX

Page 863, third paragraph:

The 2017 tax legislation fundamentally changed the § 1(g) kiddie tax for taxable years beginning after December 31, 2017, and before January 1, 2026. For those years the net unearned income of a covered child is not taxed at the top marginal rate of his or her parents. Instead, the net unearned income is taxed at the rates and brackets applicable to estates and trusts as set forth in § 1(j)(2)(E) under the 2017 tax legislation. § 1(j)(4). Taxable income attributable to earned income for the year is taxed at the rates and brackets applicable to unmarried individuals. But to the extent taxable income is attributable to net unearned income, both ordinary income and capital gains are taxed under the schedule for estates and trusts. Thus, for the years to which these changes apply, neither the parents' marginal rate nor the allocable parental tax (discussed on page 865) is relevant.

Page 864, first paragraph:

For taxable years beginning after December 31, 2017, and before January 1, 2026, delete the last sentence with its reference to taxing net unearned income at the parental rate.

Page 864, second paragraph:

For taxable years beginning after December 31, 2017, and before January 1, 2026, delete the references to the personal exemption. See the Chapter 1 update, *supra*.

Page 864, third paragraph:

Delete the paragraph. For taxable years beginning after December 31, 2017, and before January 1, 2026, the kiddie tax is determined not under § 1(g)(1), but under § 1(j)(4).

Page 865, first full paragraph:

Delete the paragraph. The "allocable parental tax" does not apply to taxable years beginning after December 31, 2017, and before January 1, 2026.

Chapter 36

INTEREST-FREE OR BELOW-MARKET LOANS

Page 875, footnote 2:

Under 2017 tax legislation, the dollar amount under § 7872(g)(2), pursuant to which certain loans to continuing care facilities are not subject to § 7872, is adjusted for inflation based upon the Chained Consumer Price Index for all Urban Consumers (C-CPI-U) published by the Bureau of Labor, rather than the Consumer Price Index (CPI). § 7872(g)(5), as amended.

Chapter 37

TAX CONSEQUENCES OF DIVORCE

Page 885, first paragraph:

The 2017 tax legislation reverses the long-standing tax treatment of alimony. Sections 71 and 215 are repealed and, accordingly, alimony received is not included in income and alimony paid is not deductible. This reversal of prior law is effective with divorce or separation instruments executed after December 31, 2018 (or modification of divorce or separation instruments executed before December 31, 2018, where the modification expressly provides the new tax treatment shall apply).

Page 885, first paragraph:

Note the reference to the deduction for personal exemptions. As noted in the Chapter 1 update, *supra*, the deduction for personal exemptions is suspended for taxable years beginning after December 31, 2017, and before January 1, 2026.

Pages 885–89:

These pages discuss the definition of alimony under § 71. As noted above, § 71 is repealed for divorce or separation instruments executed after December 31, 2018.

Pages 889–90:

These pages discuss the provisions of § 71(c) under which reductions in payments denominated alimony, and thus includable by the recipient and deductible by the payor, might be deemed nonincludable and nondeductible. As noted above, § 71 has been repealed, effective for divorce or separation instruments executed after December 31, 2018.

Pages 890–92:

These pages discuss the excess front-loading rules of § 71(f), repealed along with all of § 71, for divorce or separation instruments executed after December 31, 2018.

Page 892:

Section 692 was repealed by the 2017 tax legislation, effective for divorce or separation instruments executed after December 31, 2018.

Pages 892–94:

These pages deal with the dependency exemption for children of divorced or separated parents. Deductions for personal exemptions, as noted in the Chapter 1 update, *supra,* are suspended for taxable years beginning after December 31, 2017, and before January 1, 2026.

Page 894:

The filing status of divorced or separated parents was unchanged by the 2017 tax legislation.

Pages 894–98:

The discussion of property transfers is unchanged by the 2017 tax legislation.

Pages 898–99:

The special rules regarding personal residences under § 121 are unchanged by the 2017 tax legislation (except for a conforming amendment to § 121(d)(3) related to the repeal of § 71).

Page 899, first full paragraph:

As noted in the Chapter 1 update, *supra*, the deductibility of miscellaneous itemized deductions is suspended for taxable years beginning after December 31, 2017, and before January 1, 2026.

Chapter 39

LIKE KIND EXCHANGES

Page 949, first paragraph:

The 2017 tax legislation made a major change to the scope of § 1031. Effective for exchanges completed after December 31, 2017, § 1031 exchanges are limited to exchanges of real property, excluding any real property "held primarily for sale." See § 1031(a)(1), (2), as amended. Exchanges of personal property no longer qualify under § 1031. In reading the remainder of this Overview, the new limitation on the scope of § 1031 should be kept in mind.

Page 952–53:

Delete the references on these pages to exchanges of personal property, which, as noted above, do not fall within the scope of § 1031 after December 31, 2017.

Chapter 41

INSTALLMENT SALES

Page 1031, first full paragraph:

See the Chapter 39 update, *infra*, describing the change made to the scope of § 1031 by the 2017 tax legislation.

Chapter 42

SALE OF BUSINESS AND SALE-LEASEBACKS

Page 1049, second full paragraph and succeeding paragraphs:

See the Chapter 39 update, *infra*, describing the change made to § 1031 by the 2017 tax legislation.

Chapter 43

ORIGINAL ISSUE DISCOUNT

Page 1091, last paragraph:

Under the 2017 tax legislation, inflation adjustments to the $2,000,000 statutory limit applicable to the cash method election of § 1274A(c) will be based on the Chained Consumer Price Index for all Urban Consumers (C-CPI-U) published by the Bureau of Labor, rather than the Consumer Price Index (CPI). § 1274A(d)(2), as amended.

Page 1092, second full paragraph:

Under the 2017 tax legislation, inflation adjustments to the $2,800,000 statutory limit on the discount rate applicable to qualified debt instruments, as defined in § 1274A(b), will be based on the Chained Consumer Price Index for all Urban Consumers (C-CPI-U) published by the Bureau of Labor, rather than the Consumer Price Index (CPI). § 1274A(d)(2), as amended.

Chapter 44

LIMITATIONS ON TAX SHELTERS - SECTIONS 465 AND 469

Page 1107, first full paragraph:

The passive activity loss limitations are applied after the § 465 at risk limitations. Reg. § 1.465-2T(d)(6). The limitation on excess business losses of noncorporate taxpayers, enacted as part of the 2017 tax legislation, is applied after the application of § 469. See § 461(l)(6).

Page 1107, first full paragraph and footnote 12:

With regard to the reference to § 183, note the update to Chapter 20, *supra*, describing the impact of the 2017 tax legislation on hobby losses.

Chapter 45

THE ALTERNATIVE MINIMUM TAX

Page 1120, carryover paragraph at top of page:

The 2017 tax legislation increased the exemption amount for taxable years beginning after December 31, 2017, and before January 1, 2026. The increased amounts are $109,400 for joint returns and surviving spouses; $70,300 for individuals not married and not a surviving spouse; and $54,700 for married individuals filing separately. § 55(d)(4), as amended. The dollar amounts are adjusted for inflation after 2025.

Page 1120, first full paragraph:

The 2017 tax legislation increased the beginning of the phase-out range to $1,000,000 for joint returns and surviving spouses and to $500,000 for individuals not married and not a surviving spouse and for married individuals filing separately. § 55(d)(4), as amended.

Page 1120, second full paragraph:

Miscellaneous itemized deductions are nondeductible under the 2017 tax legislation for taxable years beginning after December 31, 2017, and before January 1, 2026. See the Chapter 1 update, *supra*. The § 68 overall limitation on itemized deductions is suspended under the 2017 tax legislation for taxable years beginning after December 31, 2017, and before January 1, 2026. See the Chapter 1 update, *supra.*

Page 1120, last full paragraph:

The alternative minimum tax for corporations was repealed by the 2017 tax legislation.

Page 1121, second paragraph:

Miscellaneous itemized deductions are not allowed for regular tax purposes under the 2017 tax legislation for taxable years beginning after December 31, 2017, and before January 1, 2026.

Page 1122, first full paragraph:

Under the 2017 tax legislation, medical expenses for 2017 and 2018 are deductible for regular tax purposes to the extent they exceed 7.5 percent of adjusted gross income.