Smart Bear Educational White Paper
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The Tax Cuts and Jobs Act (TCJA) was enacted in 2017 and will expire in 2025. This means your tax obligation will likely increase between 19% and 27%, even with increased deductions starting in 2026!

How much more will *you* owe? What moves should you consider to make now to optimize taxes in advance of this increase?

Let's look at the TCJA, what it means, and what you can do to prepare strategies to minimize your liabilities and/or avoid unexpected financial obligations.

Overview of TCJA
Many provisions of the TCJA will expire unless Congress and the President extend or change them. The expected expiration will present challenges for most taxpayers and investors, who may want to consider strategies for minimizing tax liabilities, optimizing long-term income and savings, or maximizing the values of charitable giving or estates.

If TCJA is allowed to expire, key impacts include:

- Income tax rates increase
- Estate and Gift tax lifetime exemptions decrease
- Standard exemption decrease - SALT cap removed, but PEASE phase-outs return
- Personal exemptions return - Personal Exemption Phase-outs (PEP) also return
- The threshold for owing Alternative Minimum Tax (AMT) reduced

The remainder of this document will provide details about the changes and examples of their expected impact. We also suggest several strategies for successfully navigating these changes to minimize their effect on your taxes, financial planning, and well-being, as well as your charitable contributions and estate plans.

<u>Changes</u>:

Tax rates are increasing in most brackets.

Income tax rate changes	
2023	**2026 (expected)**
10%	**10%**
12%	**15%**
22%	**25%**
24%	**28%**
32%	**33%**
35%	**35%**
37%	**39.6%**

The Lifetime estate and gift tax exemption is reduced by more than half.

Estate Tax changes			
	Before 2018	**2024**	**2026 (expected)**
Lifetime estate and gift tax exemption (single/married couple)	**$5M / $10M**	**$13.6M/ $27.2M**	**~$5M / ~$10M + Inflation adjustment**
Annual Gift tax exclusion	**$15k**	**$18k**	**?**

Standard deductions are returning to the 2018 baseline, and State and Local Tax (SALT) deduction limitations are disappearing.

Standard Deduction			
	2018	**2023**	**2026 (expected)**
Single	**$6,350**	**$13,850**	**$6350 + inflation adjustment**
Married filing jointly	**$12,700**	**$27,700**	**$12,700 + inflation adjustment**
● **State and Local Tax (SALT) deduction cap of $10k lifted** ● **Mortgage Interest deduction cap reverts to $1M (from $750k)** ● **Home equity loans deductible up to $100k - not limited to home repair and improvements** ● **Itemized deduction phase-out returns (aka PEASE[1]) - 3% reduction above AGI of $266,700 single and $320,000 married filing jointly up to 80% reduction of deductions.**			

Alternative Minimum Tax (AMT) will apply to millions more taxpayers (again).

Other
● **The threshold for owing AMT is reduced as the AMT exception amount will be reduced - more people will be hit with AMT** ● **Long Term Capital Gains (LTCG) brackets re-attached to ordinary income tax brackets** ○ **0% LTCG tax rate for those in the 10% and 15% ordinary income tax bracket** ○ **15% LTCG tax rate for those in the 25%, 28%, 33%, and 35% ordinary income tax bracket** ○ **20% LTCG tax rate for those in the 39.6% ordinary income tax bracket** ● **199a (Qualified Business Deduction) eliminated** ● **Personal exemptions return, PEP also returns**

[1] This provision, named after the late Congressman Donald **Pease**, reduces the value of itemized deductions for high income taxpayers.

Tax calculation examples:

Married Filing Jointly			
	Federal Taxes paid in 2023	Federal Taxes paid in 2026	Tax increase
Annual Income: $100,000	$8,236	$10,453	26.9%
Annual Income: $150,000	$17,521	$21,722	24.0%
Annual Income: $250,000	$40,152	$48,127	19.9%

Source: Smarter Bear calculations using Holistiplan and “apples to apples” assumptions about deductions, capital gains, personal exemptions

Strategies to consider before TCJA provisions sunset:

- Consider accelerating income, if possible, to fill up brackets before 2026 at existing lower rates.
- Consider whether a Roth conversion strategy makes sense given the totality of your circumstances and the current lower income tax rates.
- Consider deferring expenses such as Charitable donations and timing of tax payments that could be more valuable as itemized deductions post-TCJA
- Depending on circumstances - consider recognizing capital gains if rates are currently lower and buying back positions. This is called “capital gains harvesting” - no wash sale on gains.
- Consider actions now to minimize the impact of AMT preference items such as incentive stock options, private activity bond interest, foreign tax credits, passive income, and net operating loss deductions when higher exemptions and exemption phaseouts sunset. ISO exercises and holds are very complex topics, and scenarios should be run for specific circumstances.
- For high-net-worth families, consider gifting strategies utilizing currently higher lifetime gifts and estate tax exemptions. Gifting appreciated assets to family members in lower capital gains tax brackets can result in significant tax savings.

- One potential strategy would wait until after the TCJA sunset. Depending on other circumstances, it may make sense to delay Donor Advised Fund (DAF) funding, donation bundling, or other substantial charitable donations until after sunset, when the deductions could be more valuable.

Overall, this is a complex and dynamic topic, and the impact and opportunities will vary depending on each individual/family's specific circumstances.

Smarter Bear is always available for a no-cost initial consultation to answer questions and discuss whether our services can help address your needs. We also offer no-cost second opinions for professionals, retirees, or investors who are experienced and comfortable directing their own investments and strategies or who are working with another investment or financial advisor.