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"The significant point is that people unfit for freedom—who cannot do much with it—are hungry for power. The desire for freedom is an attribute of a 'have' type of self. It says: leave me alone and I shall grow, learn and realize my capacities. The desire for power is basically an attribute of a 'have-not' type of self. If Hitler had had the talents and the temperament of an artist, if Stalin had had the capacity to become a first-rate theoretician, if Napoleon had had the makings of a great poet or philosopher they would hardly have developed the all-consuming lust for absolute power."

— Eric Hoffer, The True Believer

Tax and Financial Strategies

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Wealth Creation Strategies

The Joys of Purging Old Records

You've missed reading this Letter, and I've missed writing it. Expecting new tax law last year, I waited…and waited. In the interim, with some time on my hands, I purged!

It's not that I haven't periodically shredded old records, but this time I went about it more methodically and carefully than ever. I shrank my own financial history (the back-up for old tax returns—never dispose of those!) by about half, freeing up much-needed space.

And yet…I've already come across—or rather, haven't come across—two missing personal items, helpful if not crucial for my own current and future planning. Perhaps these records are misplaced (a home improvement and an old pension document); perhaps they're gone. But I haven't found them yet. Which goes to show how carefully one must purge. I don't "think" I tossed them, but who knows. To get a good idea of what you can and can't safely discard, see page 7 of issue # 47 of *Wealth Creation Strategies* at www.DougThorburn.com.

After shrinking my own records, I still had time on my hands (the rest of summer and all of fall 2017). I looked at the morass of old client records, which took up way too much space, and asked whether I really need these? As a tax pro, I'm not required to keep anything after four years, but I've learned from long experience that certain old records can come in handy for clients. And, I want to be sure that someone has these if the need comes up. A good example of the types of items I looked for in old files were sales of homes under the now-ancient rules under which sellers "rolled" gains from one home into another, as well as closing settlement statements on homes and rentals.

Also included were Federal and California returns from 1982 through 1986 reporting IRA contributions, when federal rules generally allowed up to a $2,000 deduction, while California allowed a maximum of $1,500 and often less. Because the contribution was already taxed by California, it shouldn't be taxed again when withdrawn. I tried to ensure this "basis" would be captured on future withdrawals by giving clients a chart detailing California basis in their IRAs and keeping a copy in their files. Unfortunately, clients *never* remembered this, and we didn't have as perfect a "carry forward" system in those days as we have now, in which items that may prove useful in future years (such as this basis history) are kept in current tax files.

It's not that I hadn't previously purged. Over the years, I had disposed of at least 200 banker's boxes of ancient tax returns and supporting documents, particularly from years for which I have computer back-up. But I'd never done so as carefully, with a desire to free up as much space as possible, without removing items that might be useful for a client's future (especially where it might save taxes).

And, too, there is history. The Rosetta Stone, which held the key to deciphering Egyptian hieroglyphics, was a tax document detailing the tax-exempt status of temples; the stones (there were actually many such stones) served as a warning to tax collectors to not step foot inside the temples. Tax documents and records intended to track income for purposes of the pharaoh's taxes helped us to understand the history of ancient civilizations. Similarly, clients' histories help to confirm many hypotheses I have long held about wealth creation and preservation.

Combing through old tax records, I was reminded of stories of both rags to riches and riches to rags. There were many just starting out who found great success; others, who I thought had great potential (especially some actors), weren't heard from after a few years (and yes, I looked for a few on Facebook and can't find them). I found divorces and marriages and wonderful people and…well, we won't go there, but those who know me might imagine what else I saw. Let's just say, times were more interesting before weeding them out. If you are reading this, you are not among them, which makes my work less interesting but more satisfying and meaningful.

Old audits were particularly interesting. I rarely tossed the key papers from those. In the ancient days, especially the 1980s, there were many more full-on sit-down face-to-face IRS audits than today (and there were few if any correspondence audits, which now make up the vast majority). Many started out with authorities demanding $2,500 or $25,000 and ending with a request for $250 or nothing at all. Those were scary times; it's amazing to see what clients and I went through and survived.

Finally, I found that file folder labels last only about 25 years and rubber bands, which held some files together, about 20 years.

Still, despite the dust and no new *Wealth Creation Strategies* for the longest period since its inception, it was a fascinating year. And I cleared out so much that when we remodeled our 60-year-old kitchen in the late fall (30+ years overdue), I decided it was the perfect time to extend the remodeling through the copy room and hallway into my own office. I suspected that, having eliminated so much paper, I had created enough space in the rest of the office to move all my office stuff there for a few weeks. While that was true, it was barely so. Worse, by late fall I expected tax reform to fail—so it was crazy when it was passed on December 21st with the coinciding remodeling, regular year-end planning and "other" issues. With the largest tax overhaul since 1986 and "other" trials and tribulations, this was the most challenging Season since our first in-house tax software failed in late February 1989. (I worked 90 hour weeks to catch up—I was younger then!) This year wasn't quite as grueling (even if one could argue, age-adjusted, it was). The office looks great. And we're clearly more streamlined after The Great Purge of 2017.

As for why you're reading this only now, so late in the year: the intersection of old and new tax law in 2018 created massive complexities, as well as planning opportunities, keeping us much busier with clients in the off-season than usual. In addition, understanding new law well enough to write about took months—we started this in June, so you can only imagine the difficulties in trying to write so that you will understand it. We hope this and the next few issues accomplishes this goal.

The Best of the Tax Cuts and Jobs Act (TCJA)

In any law re-arranging theft, there are winners and losers and, by necessity, aspects of the law that are good and bad, great and ugly. The **Tax Cuts and Jobs Act** (**TCJA**, or "**the Act**") is no different from any other. We'll discuss the good, bad and ugly in the next newsletter, but we'll start with the best parts here.

Lower tax rates improve incentives to produce, save and invest

Tax rates were reduced across the board, although not as dramatically as in the Tax Reform Act of 1986, the granddaddy of all tax reforms of the last three generations. That Act lowered the maximum advertised individual tax rate from 50% to 28% (and maximum corporate rate from 50% to 35%). The TCJA, not nearly as much. It may not be "great," but it needs to go first so you can follow the rest of the discussion. At the least, it's "good."

Old and New Advertised Tax Rates

Tax Rates* for Single Filers on "Chunks" of Taxable Income**			
Old Rates		New Rates	
Taxable Income	Tax Year 2017	Taxable Income	Tax Year 2018
Not over $9,325	10%	Not over $9,525	10%
$9,325-$37,950	15%	$9,526-$38,700	12%
$37,951-$91,900	25%	$38,701-$82,500	22%
$91,901-$191,650	28%***	$82,501-$157,500	24%
$191,651-$416,700	33%***	$157,501-$200,000	32%***
$416,701-$418,400	35%***	$200,001-$500,000	35%***
$418,401 & up	39.6%	$500,001 & up	37%

Tax Rates* for Married Joint Filers on "Chunks" of Taxable Income**			
Old Rates		New Rates	
Taxable Income	Tax Year 2017	Taxable Income	Tax Year 2018
Not over $18,325	10%	Not over $19,050	10%
$18,651-$75,900	15%	$19,051-$77,400	12%
$75,901-$153-100	25%	$77,401-$165,000	22%
$153,101-$233,350	28%	$165,001-$315,000	24%
$233,351-$416,700	33%***	$315,001-$400,000	32%
$416,701-$470,700	35%	$400,001-$600,000	35%***
$470,701 & up	39.6%	$600,001 & up	37%

Tax Rates* for Head of Household Filers on "Chunks" of Taxable Income **			
Old Rates		New Rates	
Taxable Income	Tax Year 2017	Taxable Income	Tax Year 2018
Not over $13,350	10%	Not over $13,600	10%
$13,351-$50,800	15%	$13,601-$51,800	12%
$50,801-$131,200	25%	$51,801-$82,500	22%
		$82,501-$157,500	24%
$131,201-$212,500	28%***	$157,501-$200,000	32%***
$212,501-$416,700	33%***	$200,001-$500,000	35%***
$416,701-$444,550	35%	$500,001 & up	37%
$444,551 & up	39.6%		

* There were and still are innumerable hidden tax rates buried in the law, including an additional 5% tax rate as the Child Tax Credit (and a new "Family" Tax Credit, discussed later) is phased out. Another common hidden rate includes the additional (reduced under new law) 10.2% and 18.7% add-on rates to which Social Security recipients are subjected as "benefits" are added to the taxable base for those in the new 12% and 22% brackets, respectively. For example, this creates real (but hidden) marginal rates for Social Security recipients of (12% + 10.2% =) 22.2% for those in the advertised 12% bracket and (22% + 18.7% =) 40.7% for those in the advertised 22% bracket.

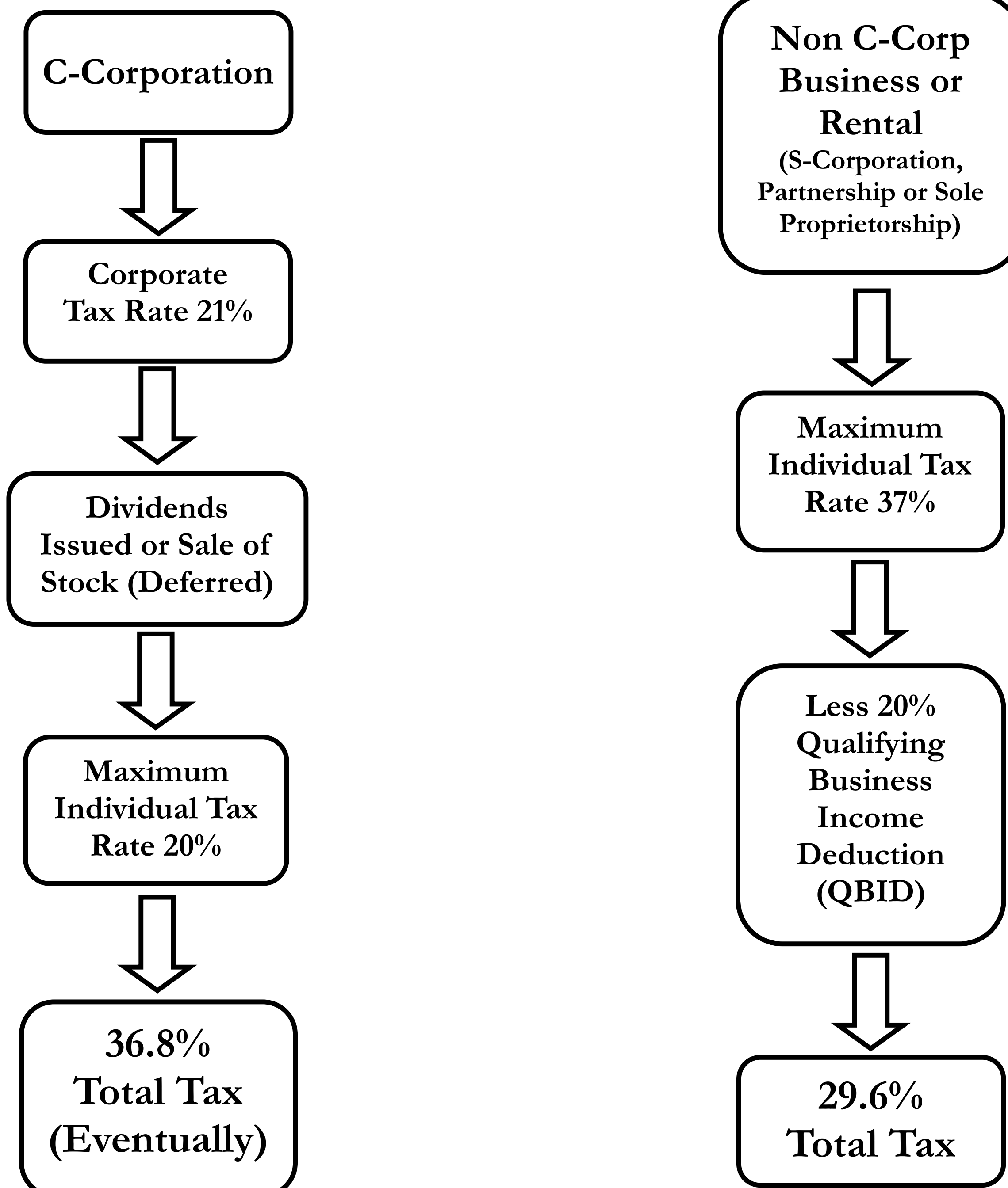
** Taxable income is Adjusted Gross Income (wages, net self-employment and rental income, investment income and the like, minus pension contributions, etc.) less either the "standard" or itemized deductions, plus exemptions (allowed in 2017 but not in 2018). For 2018-on, all taxpayers except dependents with non-work-related income (i.e., investment, IRA, scholarship and other so-called "unearned" income) get a minimum $12,000 standard deduction, which more than replaces the old standard deduction plus personal exemptions, except for large families.

*** The fact that old rates were lower than new rates on this huge swath of income for these classes of filers would seem out of character for the Act, except for the fact that most filers in these income ranges were hit with an Alternative Minimum Tax that subjected those with taxable incomes in the range of upper $100,000s through low $400,000s to an effective 35% tax rate. Still, Head of Household and Single filers probably get the least benefit of all filers once they hit $157,500.

Entrepreneurs and workers of the world, rejoice, the QBID is here!

Along with the tax rate changes, Congress did something fascinating, even if horribly confusing and complex (which may have been due to the necessity to make law via "budget reconciliation," due to Republicans holding less than 60 Senate seats): while reducing C-Corporation (regular, usually publicly-held corporations, which pay tax at the corporate level) tax rates from generally 35% to a flat 21%, Congress felt the need to decrease tax rates on non-corporate (sole proprietorships and rental properties) and flow-through business entities (S-Corporations and Partnerships) to try to match the corporate tax cuts and disincentivize non C-Corporate entities from incorporating (as C-Corporations).

Congress reasoned that regular corporations ("C"-Corporations) are taxed once at the corporate level and again at the personal level when cash is paid to investors in the form of dividends and capital gains. With a flat federal corporate tax rate of 21%, the 79% left over will be taxed ultimately at the shareholder level, whose federal income tax at the highest rates on "qualifying" dividends and long-term capital gains is 20%. This results in a combined 36.8% marginal tax rate [79% x 80% = 63.2%; 100% – 63.2% = 36.8%]. Since the new highest individual marginal tax rate is 37%, you'd think that would make things even, but because corporations can defer paying dividends for extended periods (there's enormous value in retaining earnings for capital investment), there'd be an incentive (due to the time value of money) for non-corporate entities and S-Corporations to incorporate as C-Corporations.



Pre-2018 law taxed individuals at roughly 20% less than the corporate tax plus dividends/capital gains tax. (Corporate tax rates were 35%; 100% – 35% = 65%; qualifying dividends and long-term capital gains were taxed at 20%; 65% times the inverse of the tax rate of 80% = 52%; the highest individual rate was 39.6%, or a bit more than 20% less than the top combined corporate-individual rate.) To equalize tax rates across business types under the Act, Congress opted to give non C-Corporate businesses a 20% of net income deduction, reducing the effective tax rate from a maximum 37% to (37% x 80% =) 29.6%, close to the 20% reduction from combined corporate/individual tax rates of (36.8% x 80% =) 29.44%. This new non-cash flow deduction is called the **Qualified Business Income Deduction** (**QBID**).

Congress introduced the QBID to create a positive economic benefit across society by keeping more capital in the hands of entrepreneurs. Why is this important? Capital is the primary key to wealth creation. Consider the difference between a truck driver and a Chinese coolie. One carries goods to other producers and consumers using a truck; the other, his back. One moves goods measured in tonnage; the other in pounds. Who produces more? Consequentially, who earns more? An American truck driver is no smarter or stronger or moral than the Chinese coolie of yore, but he out-earned (because he out-produced) the coolie by an order of magnitude. The difference, which made all the difference in the world, was the truck, which can be manufactured and made useful only with billions of dollars invested in factories and transportation systems.

Entrepreneurs, who make "capital allocation" decisions, are the secondary key to wealth creation. They decide whether to buy more trucks and computers or build more factories that build trucks and computers. For capital to be rationally allocated, there must be a feedback mechanism, which tells entrepreneurs whether they are making good or bad decisions in terms of both what and how much to produce. That mechanism, the profit and loss system, is tough and blunt. Err in a big way and the entrepreneur goes out of business (another way of saying, he is "nudged" into doing something for which both he and society will derive greater benefit). Do well in a big way by pleasing Consumer Kings and become wealthy.

Contrast entrepreneurs with governments, which are terrible capital allocators. They can't go out of business for doing a rotten job, and if something doesn't work well (and it usually doesn't for the price expended), they either siphon more money from producers or ration whatever they are supplying. When taxes are increased, government has more money to spend unwisely, without the benefit of the feedback provided by the profit and loss system. When taxes are reduced, more wealth is retained by entrepreneurs, who are able to invest more. With greater investment, living standards improve. When living standards improve overall, wages in the aggregate increase. With this new deduction, Congress explicitly recognized the value of capital allocators in increasing overall living standards.

But they didn't give the QBID to every business. Because it will be taken on one's personal tax return (even for "flow-through" entities like Partnerships and S-Corporations; hence, "flow-through"), personal taxable income must be under certain thresholds to reap the benefits of the deduction without undue complications. Regardless of income level, it's also limited to the lesser of 20% of (1) net business income or (2) taxable income minus other tax-favored income (for geeks: the excess of net long-term capital gains over net short-term capital losses plus qualifying dividends).

Who Gets the Qualified Business Income Deduction (QBID) Without a Phase-Out?

	Taxable Income up to:	Deduction is:	Limited to:
Single filers*	**$157,500**	**20% of net business income**	**Lesser of 20% of Taxable Income** or 20% of combined net business and renal income**
Married filers	**$315,000**	**20% of net business income**	

* Includes unmarried Heads of Household and married filing separate filers

** Taxable income without regard to the QBID, minus the excess of net long-term capital gains over net short-term capital losses, plus qualifying dividends (generally, dividends from publicly traded C-Corporations). We believe "depreciation recapture" (depreciation previously taken) from the sale of rental real estate is considered "business income" for this purpose, but the balance of any capital gain is not.

Let's say a married couple has $315,000 of net business income and no other income or deductions. You would think they will get a huge ($315,000 x 20% =) $63,000 deduction (with a tax savings of $15,120 at the new 24% marginal rate on that level of taxable income), but you'd be wrong. The QBID is the ***lesser*** of 20% of net business income or 20% of taxable income. Their taxable income is $315,000 less their new $24,000 (joint filer, both under age 65) standard deduction, or $291,000. $291,000 x 20% = a $58,200 QBID, which reaps a nice ($58,200 x 24% =) $13,968 in tax savings. Not as large, but still not bad!

The definition of QBI depends on the entity type. Different entities have different definitions.

What is Qualifying Business Income (QBI)?

	Sole Proprietorship (Schedule C)	Partner in a Partnership	Shareholder in an S-Corporation	Rental Property Owner
QBI is:	**Net business income**	**Net partner income after any "guaranteed payments"**	**Net income after all business expenses including any owner wages plus pension contributions**	**Net rental income after all expenses including interest and depreciation deductions**

There are some neat tax arbitrage and planning opportunities created by the new QBID. If the deduction is 20% of net business income, such income is (obviously) subject to a 20% lower tax rate than other, non-Qualifying Business Income. These new phantom tax brackets are lower than the advertised ones.

Good Phantom Tax Brackets, For a Change

"Advertised" tax bracket	QBID	Possible "phantom" tax bracket for QBI
10%	20% of 10% = 2%	8%
12%	20% of 12% = 2.4%	9.6%
22%	20% of 22% = 4.4%	17.6%
24%	20% of 24% = 4.8%	19.2%
32%	20% of 32% = 6.4%	25.6%
35%	20% of 35% = 7%	28%
37%	20% of 37% = 7.4%	29.6%

Because the deduction is 20% of the ***lesser*** of QBI or taxable income, when taxable income creates a lower deduction than non-qualified income (e.g., retirement income, wages, interest income and other "ordinary" income), you can get the benefit of the phantom QBID tax rates. Conversely, itemized or other deductions would save at this lower rate as well. The fact that non-QBI can get the benefit of these lower rates is best seen by example.

Assume Jack and Jill are married, and Jill's sole proprietor's net business income is $75,000. If this is their only income and they take the standard deduction of $24,000, taxable income is $51,000. The QBID is the *lesser* of 20% of $75,000 (= $15,000) or 20% of $51,000 (= $10,200). Taxable income *after* the QBID is, then, ($51,000 - $10,200 =) $40,800.

But assume now that Jack has $30,000 of other ordinary income, such as wages, a penalty-free IRA withdrawal or a Roth conversion. Looking at the tax tables, you'd think their marginal tax bracket is 12%, right? Wrong! Never believe the advertised tax brackets! The QBID increases by 20% of the increase in taxable income until the QBID equals 20% of net business income, or $15,000. The real marginal tax rate, then, on the additional $30,000 of non-QBI is [12% - (20% of 12%) =] 9.6%. (Proof: $75,000 net business income plus $30,000 other income less $24,000 standard deduction = $81,000 taxable income x 20% = $15,000 QBID). In fact, because taxable income after the QBID is ($81,000 - $15,000 QBID =) $66,000 and the tax rate is 12% on taxable income up to $77,400, they can earn an additional $11,400 at the still low 12% rate. Nice.

The key takeaway here is that with net self-employment and/or rental income, individuals may be able to take advantage of a 9.6% (or other lower-than-advertised) marginal federal income tax bracket for

purposes of taking additional income of *any* kind.

Conversely, itemized or other deductions may *save* at *only* a 9.6% rate, changing the math for the decision to create more deductions, including whether to invest in pre-tax retirement accounts. When additional reductions in taxable income serve to further reduce their QBID, the real marginal rate for a retirement plan contribution would be 9.6%/17.6%/19.2%, not the advertised 12%/22%/24%. I've long counseled that retirement savings for those in the old 15% bracket should generally be invested in after-tax accounts, especially Roth IRAs. For a discussion of *why* those in lower brackets *generally* should strive to create more income and/or minimize deductions, please see issue # 53 (pgs. 5-6) and issue # 27 (pgs. 4-5) of *WCS*.

Another couple has $101,400 net business income. If this is their only income, after a $24,000 standard deduction, taxable income is $77,400, which you might think (looking at the table on page 6) puts the couple at the nub of the 22% advertised marginal tax rate. Nope! The QBID is the lesser of 20% of QBI, or ($101,400 x 20% =) $20,280, OR 20% of taxable income, or ($77,400 x 20% =) $15,200. The QBID further reduces taxable income by the $15,200, creating an effective 9.6% tax rate for up to $15,200 in additional ordinary income, such as spouse's wages, Roth conversions and the like. Only when *taxable* income (after the $24,000 standard deduction), including the deduction for QBI, reaches $101,400 will this couple reach the nominal 22% bracket; at that point their real marginal tax rate is (80% of 22% =) 17.6% on any additional net business or rental income.

Overall, the QBID incentivizes entrepreneurial activities by letting entrepreneurs keep more of what they earn. Indirectly, it may also incentivize other income-producing activities by reducing the effective real marginal tax rate on those activities. It may also disincentivize saving in pre-tax retirement plans. But one needn't save for retirement only in pre-tax retirement accounts.

The same phantom tax brackets apply to net rental income. The QBID for a married couple with $150,000 of wages and $10,000 of net rental income ("net" is income after depreciation, mortgage interest and all other deductions) is 20% of $10,000, or $2,000. The advertised marginal rate on their wages (assuming the standard deduction) is 22%, while the phantom-but-real marginal rate on the net rental income is 80% of 22%, or 17.6%.

A big offset to the QBID

Unfortunately, business and rental losses offset business and rental net income for purposes of calculating the QBID. Worse, combined net losses among all business and rental activities carry forward into subsequent years, offsetting future business income for purposes of the QBID (but losses incurred prior to 2018 don't count for this!). With this nasty feature, the government is telling you to not lose money. In so doing, they made the interest deduction on rental or business loans worth less, because you save less. If your "advertised" tax rate is 24% and your net income is reduced by interest paid, your real marginal tax rate becomes (80% of 24% =) 19.2%. If your advertised tax rate is 22%, your phantom-but-real marginal rate would be (80% of 22%=) 17.6%. Of course, the "loss" in tax savings is true for all business deductions (so long as your taxable income is less than the above thresholds), but interest paid can be controlled more easily than can other expenses by paying down the loan, effectively decreasing the tax savings from business expenses (including interest paid), while increasing the return on an "investment" of loan repayments.

While the QBID is very entrepreneurial, it adds complexity if we wish to avoid wasting low tax brackets. The QBID reduces the tax savings from the use of leverage, which may have been Congress's intent, and it may reduce the tax savings from retirement plan contributions, which was *not* likely intended.

Entrepreneurs and consumers of the world, rejoice!

The TCJA immediately doubles the estate tax exemption from nearly $5.5 million ($11 million for married couples) to nearly $11 million ($22 million for married couples). It "eventually" (in 2024) eliminates the federal estate tax altogether.

This is especially good for family businesses, which will less frequently be sold to pay estate taxes. Because this allows the family and other heirs, rather than government bureaucrats, to invest more of the decedent's funds, savings and capital formation will increase across the country. Because the rational allocation of capital maximizes wealth, median aggregate household incomes will increase, benefiting everyone.

The elimination of the estate tax is also great for marketplace competitiveness because more family businesses will continue operating. I've long hypothesized that the reason Germany does as well as it does economically (despite the stifling degree of government intervention in its economy) is because there is no estate tax (a tax on the estate regardless of heir) and a relatively low inheritance tax (a tax on inheritances that varies by heir) for close family members, especially for those who take over the family business and continue to operate it. When businesses remain private for generations, there are more such businesses competing against publicly-held big businesses (in some cases a close 2nd to government in their wastefulness); the business founders and families care more about the goods and services they provide. The more businesses owned and operated by individuals and their families, the more everyone benefits from increased competition, garnering consumers lower prices and better quality goods and services. I think this best explains the extraordinary efficiency of German businesses.

Businesses purchasing new or used vehicles get much faster depreciation allowances and deductions

Because Congress long ago decided to preclude business owners from taking large deductions for cars, they created a category, "luxury autos," which included, unrealistically, any auto costing more than roughly $19,000 and having a gross vehicle weight of less than 6,000 pounds. This capped depreciation on such business-use vehicles at roughly $3,160 in year one, $5,100 in year two, $3,050 in year three and $1,875 per year in years four-on. This was woefully inadequate for most cars costing anything north of $30,000. The resulting 30+-year depreciation period for vehicles in the $60,000+ range was absurd. "Bonus" (extra first-year) depreciation was only allowed for new cars and capped at $8,000; the maximum first year depreciation deduction was, therefore, ($8,000 + $3,160 =) $11,160, with the paltry numbers listed above for subsequent years. The TCJA increases annual depreciation and allows bonus depreciation in year one for both new *and*, surprisingly, used cars. New maximum deductions are as much as $18,000 in year one (including $8,000 bonus depreciation), $16,000 year two, $9,600 year three and $5,760 year four and subsequent years; these figures are lower for vehicles costing less than $68,000. Now, your $60,000 business-use vehicle can be depreciated in just about eight years, a welcome and massive improvement. Nevertheless, many business owners, especially Uber and others driving many miles yearly, save much more in tax in the long run by deducting the optional mileage allowance which, in 2018, is 54.5 cents per mile, in lieu of actual expenses plus depreciation. The greatest benefit of the new depreciation allowances will accrue to those who use their cars mostly for business but drive relatively few miles yearly (less than 10,000 miles or so might be a good rule of thumb).

All rental property owners — "bonus" depreciation expanded and massively increased

Rental property owners with net income benefit not only from the QBID already described, but also from monumentally enhanced depreciation deductions due to new "bonus" depreciation rules that can now be applied to both new and, in an extraordinary liberal change, used property. Bonus depreciation allows a 100% deduction for any property with a "class life" of 20 years or less, making such purchases instantly deductible. This makes "cost segregation studies," in which property is divvied up between the main structures (27.5 year for residential income property and 39 years for commercial property), land improvements such as driveways, fencing and landscaping (15 years) and certain floor coverings, appliances and furnishings (5 years and 7 years), profitable for all but the smallest purchases.

The fly in the ointment is that prices have again been driven to unsustainable levels and, therefore, what you save in tax could be easily lost by overpaying for property. On the other hand, "look-back" cost segregation studies can be done on properties you already own, which can save a bundle by "catching up" depreciation that could have been taken, but which wasn't. This will be worth doing only for those who have profits, or with losses not limited by the passive loss rules (which limit the deductibility of losses, especially for those with incomes over $150,000), and who are in at least the new 22% marginal federal tax bracket and who do not mind missing out on the new 20% QBID to the extent net profits are reduced. (Do you see there are a lot of moving parts to sound tax return decision-making?)

Commercial (non-residential) rental owners can immediately deduct a slew of big-ticket items

A slew of items previously depreciated over 39 years can now be expensed in the year of purchase under a new application of Section 179 rules, which previously applied only to businesses. Newly 100% deductible items include roofs (which often could be expensed under other rules, but this increases the number of qualifying fully deductible roof replacements), heating systems, ventilation systems, air conditioning, fire protection and alarm systems, security systems, and other "qualified improvement property" (pending a technical change to tax law) that Congress has made a mess of. (Internal Revenue Code § 168(e)(6) describes these as any improvement to the interior of nonresidential property placed in service after the date the building was first placed in service, so long as it doesn't involve enlargement of the building, internal structural framework of the building, or elevators and escalators). We hope Congress extends these rules to residential rental property.

Those in low tax brackets who should take advantage of Roth conversions

Most of you know we're huge proponents of generally paying all the tax you can at lower rates (up to the old 15% tax rate) to avoid paying higher rates in retirement, when the funds are withdrawn. The main vehicle we use for this purpose is Roth conversions.

Now, with the new 12% bracket (which may not last forever), I suggest that nearly everyone taxed at low brackets do Roth conversions, starting now! While there is no "one size fits all" approach, you can rarely do better. We'll discuss Roth conversions under the new law in greater detail in an upcoming issue of *Wealth Creation Strategies*, but please start to plan for this now.

Dear Reader: We hope you've enjoyed this issue of *WCS* — much more on the TCJA will be coming in future issues of *WCS*, out in the coming weeks!