Preparing for the Tax Cuts & Jobs Act Sunset

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The Tax Cuts and Jobs Act (TCJA) was signed into law back in 2017, bringing about a slew of changes to the U.S. tax code for both individuals and corporations. While some of the changes were permanent, many others are set to expire at the end of 2025. In this article, Senior Investment Advisor Matt Sampson, CFP®, CEPA®, outlines how the tax landscape may change and how to prepare for it.

What provisions will sunset?

If the past couple of years have taught us anything, it's that time truly does fly. December of 2025 will be here before we know it. Accordingly, we thought we'd take this opportunity to help readers understand how their tax planning situation may evolve. Before enacting any planning strategies, it is important to note there is the possibility of legislators successfully enacting laws extending these provisions, or perhaps bringing about further change. However, given our current political state of dysfunction and hyper partisanship, we would be inclined to bet that new laws are improbable.

To set the stage for this article, the below table outlines what changes were made permanent versus which are set to expire at the end of 2025.

Permanent Provisions
These took effect in 2018, and extend indefinitely.
No deductions for alimony payments required by divorce agreements dated after 2019.
No more recharacterizations of Roth IRA conversions
No penalty for failure to have health coverage
529 plans may distribute up to $10,000 tax-free annually to cover qualified K-12 expenses
Elimination of charitable write-off of payment to college if it entitles you to buy tickets to athletic events
For businesses:
Flat 21% corporate federal income tax rate
Elimination of the corporate alternative minimum tax (AMT)

Temporary Provisions
These took effect in 2018 and will expire as of the end of 2025.
Reduced federal income tax rates and condensed brackets
Increased federal gift & estate tax exemptions
$10,000 limitation on state and local tax deductibility (SALT)
Expanded standard deductions
Limitations on itemized deductions for home mortgage interest
60% adjusted-gross-income limit for itemizing deductions for cash donations to public charities
Increased child tax credit and higher income thresholds for the child credit phaseout
More favorable alternative minimum tax (AMT) rules
Deduction for up to 20% of qualified business income from pass-through entities for non-corporate owners
Elimination of itemized deductions for miscellaneous expenses

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Lifetime Estate Tax Exemption

We suspect that many investors are aware of the federal lifetime estate tax exemption, set to revert back to its previous lower threshold — approximately half of the current amount. If there is no further action out of DC, the exemption is projected to decrease to around $7M per individual, or $14M for a married couple (depending on inflation) at the end of 2025.

This change has been highly publicized, and the wealth management and estate planning community offer many compelling family and charitable gifting strategies to consider. If you have not yet utilized the entirety of your current larger estate tax exemption and are desirous of doing so, time is of the essence.

Income Tax Changes: Itemizing Deductions

While the estate tax exemption has garnered significant attention, changes on the income tax side also deserve a closer look. Remember when taxpayers in high income tax states were able to deduct the entirety of state and local taxes? The $10,000 limitation on “SALT” is set to sunset, which will present a material impact for many high-income taxpayers in high tax jurisdictions.

This provision was one of the key reasons many taxpayers stopped itemizing deductions, coupled with the increased standard deduction the TCJA introduced. (The increased standard deduction is another temporary provision that is set to expire.) For context on the massive impact this had on taxpayers, the Tax Foundation estimates the percentage of taxpayers itemizing deductions dropped from 31% pre-TCJA to 13% post-TCJA.

Given where mortgage interest rates have gone, we can foresee a tax planning landscape where the number of taxpayers itemizing their deductions climbs back toward the higher, pre-TCJA figure. Higher interest rates lead to higher mortgage interest deductions, a small silver lining for those purchasing homes in today’s interest rate environment. As a reminder, mortgage interest is deductible on up to $750,000 of acquisition indebtedness. Coincidentally, another temporary provision was reducing the amount of acquisition indebtedness from $1,000,000 to $750,000. With no further change, we could see the amount of deductible mortgage interest increase rather substantially.

Roth Conversions

How about individuals who are considering Roth conversions? The TCJA reduced income tax rates and collapsed income tax brackets rather substantially. If you are considering a Roth conversion today, it is critical to make an informed assumption on where you think tax rates are headed in the future.

In our opinion, one of the most important questions to answer when considering a Roth conversion is whether you think you’ll be in a lower tax bracket at the time of conversion, or when you begin taking withdrawals in retirement. This is only one aspect of the myriad considerations and nuances that go into Roth conversion planning, but it is a key data point to consider given the potential for higher income tax rates in the near future.

If this is of interest to you in your personal planning, please let your advisor know and our team will introduce the appropriate resources.

Start Planning Now

The rapid pace of change we have seen in the tax planning landscape seems unlikely to pause, especially if we see a reversion to previous law. Having a firm grasp of how each of these provisions impacts your personal financial planning presents an opportunity to optimize your long-term cash flow and retirement planning.

As always, please reach out to your advisory team to discuss any of this in further detail.