

# Financial Advisor

## Here's Where All The Deductions Have Gone

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Under the tax reform legislation passed by Congress late last year, several familiar itemized tax deductions have ceased for 2018, such as those for unreimbursed employee business expenses, tax-preparation costs and investment-management fees, personal casualty losses, interest on some home-equity debt and moving expenses, to name a few.

Common itemized deductions for high-net-worth taxpayers have included those for mortgage interest, property and state income taxes, investment fees and charitable donations. "All except charitable contributions can generate alternative minimum tax," said John Mezzanotte, managing partner at Marcum in Greenwich, Conn. "With the impact of AMT greatly reduced and the increased joint standard deduction ... taxpayers are confused on how to minimize taxes."

"The biggest confusion is that there's not really a one-size-fits-all when it comes to losing itemized deductions," added Brian Stoner, a CPA in Burbank, Calif. For instance, the mortgage interest deduction can be limited to interest on \$750,000 in loan balances if your high-net-worth client just purchased a residence, he said.

And "taxpayers can still deduct interest on a home equity loan, home equity line of credit or second mortgage ... as long as the borrowed funds were used to buy, build or substantially improve the taxpayer's home that secures the loan," added James McGrory, CPA with Drucker & Scaccetti in Philadelphia and a member of the Pennsylvania Institute of Certified Public Accountants.

McGrory also noted that he has several wealthy clients who own land or vacation homes in Canada and Mexico. "In the [reform] confusion related to the overall \$10,000 limitation on state and local income taxes and property taxes," he said, "a little-known provision that slipped by is that foreign real property taxes, other than those incurred in a trade or business, are no longer deductible."

What can high-net-worth clients still deduct in 2018? A real win for taxpayers has been the suspension of the Pease limitations, McGrory said, which capped or phased out some itemized deductions once a client's adjusted gross income hit certain thresholds. High-net-worth clients "will actually see some benefit from this new provision," he added.

The tax reform legislation also retains the itemized deduction for medical and dental expenses, which this year needs to exceed 7.5 percent of AGI (the threshold reverts to 10 percent in 2019). Another still-solid deduction: "Charity, gifting and giving current and future interests in wealth," said Daniel Morris, CPA and senior partner with Morris + D'Angelo, headquartered in San Jose, Calif. "Thresholds on some charitable giving aspects have risen from 50 percent to 60 percent of annual AGI."

One often-discussed strategy is bunching several years' worth of charitable deductions into 2018 by making a multiyear contribution to a donor-advised fund. This can help taxpayers accumulate enough itemized deductions for the total to exceed the standard deduction (\$12,000 for single taxpayers and \$24,000 for married couples filing jointly) for one year and then claim the standard deduction in the years when the donor-advised fund makes actual grants to public charities.

Effective bunching for some high earners, however, requires careful math: Assuming that high-net-worth taxpayers who are married and filing jointly deduct the maximum of \$10,000 in property and state income taxes each year, they still face a gap of \$14,000 to hit the new standard deduction. Even bunching two years of \$7,000 annual donations into one year produces no advantage, Mezzanotte said.

"Bunching results is the biggest tax benefit for [high-net-worth] taxpayers who don't have a mortgage and who donate significantly more than \$7,000 per year," according to Mezzanotte.

Given the loss of deductions for investment fees, it's important to look at how fees are calculated, Morris says. "I might look at [advisors] changing their compensation model. Ultimately, an advisor is helpful to minimize risks of poor decisions and to create objective decision-making," he said.

"Fee deductibility should only be one consideration" when a client has a relationship with an investment manager, Stoner added.

Wealthy clients should also examine local tax breaks. One Pennsylvania credit, for instance, allows state residents to contribute to eligible scholarship and educational improvement organizations and receive a federal charitable contribution deduction and a credit against state taxes, according to McGrory.