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FINANCIAL MANAGEMENT, INC.

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Tax Reform, DBFM Happenings and Bitcoin

Key Provisions of Tax Reform

The Tax Cuts and Jobs Act of 2017 (TCJA) will pave the way for sweeping changes in the tax code beginning in 2018. The bill calls for new personal income tax rates, new corporate tax rates, and modifications to many deductions. Individuals should consult with a tax professional to understand how changes to the tax code may impact their strategies for deductions, estate planning, education funding, and small-business-income.

For Businesses

- C - Corporations and some personal service corporations will now pay a flat rate of 21%. The Corporate Alternative Minimum tax has been eliminated.

For Individuals

- The new tax code will reduce several of the marginal income tax rates (**see chart below**). The new tax brackets and the other changes to the individual tax code are temporary - Congress would need to act or the rules would revert to current law after December 31, 2025.
- The new bill will combine the personal exemption and standard deduction **into a single higher standard deduction \$12,000 if single/\$24,000 married filing jointly**, which will be indexed for inflation. As a result a filer's itemized deductions for 2018 will need to be greater than the new standard deduction amounts for the filer to benefit from listing deductions separately. The additional standard deduction of \$1,300 per person if married, \$1,600 if single for filers age 65 and older or blind will remain.
- Higher standard deductions mean fewer people will itemize deductions—so charitable giving, medical expenses, home mortgage interest, and other itemized deductions, will all face a higher threshold before they become useful. In addition, the proposal directly changes or limits a large number of deductions and credits. As an example:
 - **Mortgage Interest:** Beginning in 2018, mortgage interest is limited to \$750,000 of mortgage debt for a first and second home. The changes also suspend deductions for



- interest on home equity debt unless the proceeds of the loan are used for the acquisition or substantial improvement of the home.
- **State, Sales and Property taxes:** The deduction for the combination of all (3) taxes is capped at \$10,000.
 - **The Child Tax Credit** doubles the amount of the credit from \$1,000 to \$2,000 per qualifying children 17 years old or under at the end of the year. So if you have one child, you'll be able to claim a \$2,000 credit. For two children, your credit is \$4,000. A credit reduces your tax bill dollar for dollar. The tax law further raises the phase out so more filers will be eligible. Phase outs, which are not indexed for inflation, will begin with AGI of more than \$400,000 for married filers and more than \$200,000 for all other taxpayers.
 - In addition the credit is now refundable up to \$1,400, subject to phase outs. In other words, even if a taxpayer has no tax liability, the taxpayer can get back up to \$1,400 for each qualifying child beginning in 2018. However, the refundable portion of the credit is capped at 15% of your earned income in excess of \$4,500.

The tax reform bill also includes a non-refundable \$500 family credit for other dependents. Examples include an aging parent who depends on you for care or a child whose support you provide, but is 17 years old or older.

- Changes **to the personal Alternative Minimum Tax (AMT)** will limit the impact of the tax. The AMT was designed to prevent high-income individuals from avoiding income tax by piling up deductions.
- **Retirement savings incentives** are unaffected. The new rules do not call for changes to existing retirement savings incentives, preserving the favorable tax treatment and contribution limits for 401(k)s, IRAs, and other retirement savings accounts. The proposals also left the rules for health savings accounts intact. However, the proposal does call for ending the Roth IRA re-characterization option starting in 2018. Re-characterization allowed taxpayers to undo a Roth IRA conversion for a limited time, and was often useful if the value of the converted investments fell in value. The IRS has confirmed that people have until October 15th, 2018, to undo 2017 Roth IRA conversions.
- The **Federal Estate tax exemption** increases dramatically. The legislation will roughly double the federal estate tax exemption to \$11 million per person (\$22 million per couple). That limit would be indexed for inflation, but would expire and revert back to current law after 2025. Beneficiaries will also still get a step up in basis, meaning there will be no capital gains tax due



on inherited assets at the time of the transfer, and the cost basis—the value used to compute tax liability—would be reset to the price at that date.

- Under the law **College 529 Plan accounts** become more flexible. Beginning in 2018 account owners may take tax-free withdrawals up to \$10,000 per year per student for tuition expenses at public, private, or religious schools K-12. **Please note: this provision now also applies to elementary, middle, and high schools.** Payments for K-12 tuition expenses cannot exceed a combined total of \$10,000 per beneficiary from all qualified tuition programs.
- Under the new legislation, 529 account owners can also roll over their savings to an Achieving A Better Life Experience (ABLE) account owned by the same beneficiary or member of the beneficiary’s family. ABLE Accounts are tax-advantaged savings accounts for individuals with disabilities and their families. A rollover will count toward the annual ABLE account contribution limit, which increased to \$15,000 on January 1, 2018.

IRA and H.S.A. Contribution Deadlines for 2017

The deadline for IRA **contributions** is April 17, 2018. The 2017 contribution limit is \$5,500. If you were age 50 by 12/31/17 you can contribute an additional \$1,000. The limits for 2018 remain the same.

The deadline for H.S.A. **contributions** is also April 17, 2018. The 2017 contribution limit is \$3,400 for a single person or \$6,750 for a family. If you were age 55 or older by 12/31/17, you can contribute an additional \$1,000.

The H.S.A. limits for 2018 are \$3,450 for a single person and \$6,900 for a family. The catch up for those over age 55 remains at \$1,000.

New Tax Brackets

Single Filing Status

| <u>Prior Law</u> | | <u>Tax Cuts and Job Act</u> | |
|-------------------------|--------------------|------------------------------------|-----------------------|
| <u>Bracket</u> | <u>Rate</u> | <u>Rate</u> | <u>Bracket</u> |
| \$0 - \$9,525 | 10% | 10% | \$0 - \$9,525 |
| \$9,526 - \$38,700 | 15% | 12% | \$9,526 - \$38,700 |
| \$38,701 - \$93,700 | 25% | 22% | \$38,701 - \$82,500 |
| \$93,701 - \$195,450 | 28% | 24% | \$82,501 - \$157,500 |
| \$195,451 - \$424,950 | 33% | 32% | \$157,501 - \$200,000 |
| \$424,951 - \$426,700 | 35% | 35% | \$200,001 - \$500,000 |
| \$426,700 + | 39.6% | 37% | \$500,001 + |



Married Filing Jointly Status

| <u>Prior Law</u> | | <u>Tax Cuts and Job Act</u> | |
|-----------------------|-------------|-----------------------------|-----------------------|
| <u>Bracket</u> | <u>Rate</u> | <u>Rate</u> | <u>Bracket</u> |
| \$0 - \$19,050 | 10% | 10% | \$0 - \$19,050 |
| \$19,051 - \$77,400 | 15% | 12% | \$19,051 - \$77,400 |
| \$77,401 - \$156,150 | 25% | 22% | \$77,401 - \$165,000 |
| \$156,151 - \$237,950 | 28% | 24% | \$165,001 - \$315,000 |
| \$237,951 - \$424,950 | 33% | 32% | \$315,001 - \$400,000 |
| \$424,951 - \$480,050 | 35% | 35% | \$400,001 - \$600,000 |
| \$480,051 + | 39.6% | 37% | \$600,001 + |

DBFM Happenings

We are very pleased to formally introduce Max Dickmeyer as a new member of our team. Many of you already know Max. He has worked for us during the summers since he was a senior in high school and he worked for us part time in 2017 after graduating from Purdue University with a degree in Mechanical Engineering. Separately, during the last year, Max introduced a new product – Digital Composites through his company Remember U, LLC. He will continue to work on developing a market for his new business. But, Max has committed most of his efforts to supporting DBFM and its clients. His primary responsibilities will continue to be investment research but in addition he will cultivate relationships with new prospective clients, engage existing clients with timely writing pieces of pertinent information (see the Bitcoin piece below) and support the asset management and technology needs of our operation.

Max began learning our stock research process six years ago. Over the past several years he has improved our process and added automation, thereby enabling us to analyze triple the number of stocks we had previously been able to evaluate.

Max’s title is Investment Advisor Representative. He will be involved in portfolio management, but he will play many roles at DBFM as Max has a technology background as well as an eye for process improvement. So, beyond his roles in portfolio management and stock research, he will provide technical support in improving our business processes. We are pleased to have him on board. Please join us in welcoming Max Dickmeyer.

Bitcoin

Over the course of the last year we’ve received a few questions about Bitcoin. What is it? Should I invest in it? Is it a good investment? We thought a little education about Bitcoin would be appropriate.

It is important for everyone to know that Bitcoin is not a company. Bitcoin is one of hundreds of digital currencies also referred to as cryptocurrencies. In order to own Bitcoin you would need to create an



online account and purchase Bitcoin with dollars. That account is called a digital wallet, and your transaction is a kin to a currency exchange with a bank. Bitcoins can also be electronically mined. This approach is not discussed here.

Bitcoin was originally intended to be a currency separate from governments and financial institutions. By eliminating government backing and regulation, the currency value is independent of any single country's economic conditions. By eliminating financial institutions, i.e. banks and credit card companies, the currency is transacted without cost.

A person would buy Bitcoin as a convenient way to pay for goods and services, not as an investment. An investment in a business or real estate has tangible value. Additionally, debt or equity investment in a corporation is supported by the corporation's earnings and their ability to produce. In contrast, currency traders must speculate the future differences in currency value to generate profit. Buying Bitcoin, not for use as medium of exchange, is not an investment, it is speculation.

In addition to not qualifying as an investment, Bitcoin is also not a good choice of currency. A currency must fulfill two requirements. It must act as a medium of exchange, and a store of value. Bitcoin fails as a medium of exchange because it is not widely accepted and cannot be spent in stores or with online retailers. Bitcoin also fails as a store of value, because its value changes rapidly.

A counter argument to these issues with Bitcoin would be that it is a disruptive technology and the appropriate system for assigning value to Bitcoin is not understood. However, Bitcoin is not a technology to be applied. Bitcoin is an application of blockchain technology. Blockchain as it relates to Bitcoin is used to securely and efficiently verify Bitcoin transactions. It does nothing to secure your digital holdings only the transactions. Blockchain technology is currently being explored for new applications and could become a revolutionary technology. Any future success of applied blockchain technology will not affect the value of Bitcoin.

In conclusion, buying Bitcoin is not an investment, it is speculation. Bitcoin is a currency that fails to perform as a currency. Bitcoin is innovative but its value is independent of other uses of blockchain technology.

Please let us know if you have any questions about any of the information enclosed in this note. We look forward to serving you again in 2018.

Sincerely,

A handwritten signature in black ink that reads "Ian D. Boyce".

Ian Boyce, CFP®
Certified Financial Planner™
Principal Owner

A handwritten signature in black ink that reads "Dave Dickmeyer".

Dave Dickmeyer, M.B.A.
Wealth Advisor
Principal Owner