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Dear Friends,

The following is our annual "Tax Update" letter. Our very first letter was written in 1984. So we have been doing this for a while. Still, this year is a little different.

Section 1 of this Tax Update summarizes the Families First Coronavirus Response Act (FFCRA) enacted on March 18, 2020. FFCRA provides benefits to employee's if they are unable to work because of the Coronavirus. It also provides a mechanism to help their employer's pay for the cost.


The Coronavirus Aid, Relief, and Economic Security (CARES) Act was enacted nine days later, on March 27, 2020. Section 2 provides a brief overview of the centerpiece of that Act, the Paycheck Protection Program; while section 3 summarizes the other parts of the CARES Act.

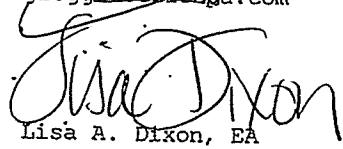
Then we cover more normal topics in Sections 4 - Individuals, 5 - Business, 6 - Passive Activities & Rentals, 7 - Farmers, 8 - Partnerships "Stuff," and close with Section 9 - Miscellaneous Tax Facts.


We expect a new Stimulus Package to become law in the next week or so; but wanted to get this to you now. We will send a follow-up when they finally agree on a new Act.

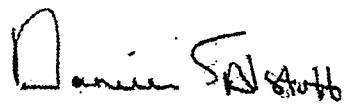
If you get a chance to read this letter, please let us know if you have any questions.

Sincerely,

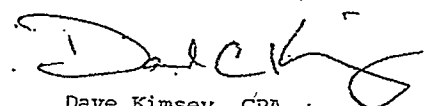

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2020 ANNUAL TAX UPDATE

| | Page |
|--|-------|
| ----- | |
| SECTION 1. THE FAMILIES FIRST CORONAVIRUS RESPONSE ACT | |
| ----- | |
| A. PAID LEAVE | 1 |
| B. PAID LEAVE CREDITS | 1 |
| C. SELF-EMPLOYED LEAVE CREDITS | 1 |
| ----- | |
| SECTION 2. THE PAYCHECK PROTECTION PROGRAM | |
| ----- | |
| A. THE CARES ACT | 2 |
| B. PPP FLEXIBILITY ACT | 2 |
| C. PPP LOAN FORGIVENESS | 2 |
| ----- | |
| SECTION 3. THE REST OF THE CARES ACT | |
| ----- | |
| A. RECOVERY REBATES | 3 |
| B. EMPLOYEE RETENTION CREDIT | 3 |
| C. CHARITABLE CONTRIBUTIONS | 4 |
| D. PAYROLL TAX DEFERRAL | 4 |
| E. NET OPERATING LOSS | 4 |
| F. EXCESS BUSINESS LOSS | 4 |
| G. INTEREST EXPENSE LIMITATION | 4 |
| H. QUALIFIED IMPROVEMENT PROPERTY | 4 - 5 |
| I. STUDENT LOAN PAYMENTS | 5 |
| J. NO REQUIRED MINIMUM DISTRIBUTION (RMD) | 5 |
| K. RETIREMENT DISTRIBUTIONS | 5 |
| ----- | |
| SECTION 4. INDIVIDUALS | |
| ----- | |
| A. KIDDIE TAX | 6 |
| B. REQUIRED MINIMUM DISTRIBUTIONS | 6 |
| C. PELL GRANT INCOME | 6 |
| D. CANCELED STUDENT LOANS | 7 |
| E. IRS AUDIT & AMENDMENT WINDOW | 7 |
| ----- | |
| SECTION 5. BUSINESS | |
| ----- | |
| A. MINIMUM WAGE | 8 |
| B. NEW FORM 1099-NEC | 8 |
| C. ENTERTAINMENT EXPENSES | 8 |
| D. MEALS & DRINKS | 8 |
| E. AUTO EXPENSES | 9 |
| F. TRAVEL ON COMPANY PLANE | 9 |
| G. QUALIFIED BUSINESS INCOME DEDUCTION | 9 |
| H. WAYFAIR NEXUS EFFECT | 9 |
| I. 100% BONUS DEPRECIATION | 9 |
| ----- | |
| SECTION 6. PASSIVE ACTIVITIES & RENTALS | |
| ----- | |
| A. MATERIAL PARTICIPATION | 10 |
| B. LATE ELECTION TO TREAT RENTALS AS SINGLE ACTIVITY | 10 |
| ----- | |
| SECTION 7. FARMERS | |
| ----- | |
| A. CORONAVIRUS FOOD ASSISTANCE PROGRAM | 10 |
| B. FARMERS CAN REVOKE UNICAP ELECTION | 10 |
| ----- | |
| SECTION 8. PARTNERSHIP STUFF | |
| ----- | |
| A. AMENDED-RETURNS | 11 |
| B. PRIORITY PROFITS | 11 |
| C. TAX BASIS REPORTING | 11 |
| D. 704(c) GAIN/LOSS | 11 |
| E. AT-RISK REPORTING | 11 |
| ----- | |
| SECTION 9. MISCELLANEOUS TAX FACTS | 12 |
| ----- | |

SECTION 1. THE FAMILIES FIRST CORONAVIRUS RESPONSE ACT

A. PAID LEAVE - Employers with fewer than 500 employees are generally required to provide paid leave. However, employers with fewer than 50 employees are exempt if doing so would jeopardize the entity's ability to continue as a going concern. Paid leave includes:

(a) paid "sick" leave to employees who are unable to work because:

1. you were subject to a Federal, state or local quarantine or isolation order related to COVID-19,
2. you were advised by a health care provider to self-quarantine due to concerns related to COVID-19, or
3. you have experienced symptoms of COVID-19 and are seeking a medical diagnosis.

(b) paid "care" leave to employees who are unable to work because of a need to care for someone with COVID-19, or to care for a child because their school or place of care is closed due to COVID-19.

B. PAID LEAVE CREDITS - Employers are compensated for the required paid leave by claiming credits against their payroll taxes (FICA but not Medicare) as follows:

1. The credit for paid "sick" leave is limited to the employee's regular rate of pay, up to \$511 per day and \$5,110 in total, for a total of 10 days.
2. The credit for paid "care" leave is limited to two-thirds employee's regular rate of pay, up to \$200 per day and \$2,000 in total, for up to 10 days.

C. SELF-EMPLOYED LEAVE CREDIT - Self-employed taxpayers will also be able to claim credits as follows:

1. If you qualify for paid "sick" leave based on the rules noted in (A) above, the credit for paid "sick" leave is equal to the number of days you were unable to perform services in your trade or business, multiplied by the average daily self-employment income for the taxable year, up to \$511 per day & \$5,110 in total, for up to 10 days.
2. If you qualify for paid "care" leave based on the rules noted in (A) above, the credit for paid "care" leave is equal to the number of days you were unable to perform services in your trade or business, multiplied by the average daily self-employment income for the taxable year, up to \$200 per day & \$2,000 in total, for up to 10 days.

SECTION 2. THE PAYCHECK PROTECTION PROGRAM

A. THE CARES ACT - The Paycheck Protection Program (PPP) was a \$669-billion business loan program enacted on March 27, 2020, as a centerpiece of the CARES Act. The initial provisions included:

1. Forgiveness - Loans were to be fully forgiven when used to pay up to 8-weeks of payroll costs, interest on mortgages, rent, and utilities. However, at least 75% of the loan must be used for payroll.
2. Employees - Forgiveness based on the employer maintaining or quickly rehiring employees and maintaining salary levels. Forgiveness would be reduced if full-time headcount declined, or if salaries or wages decreased.
3. Eligible - Small businesses with 500 or fewer employees eligible.
4. Applying - Application began April 3, 2020, and were required to be submitted by June 30, 2020. However, the Small Business Administration suggested "to apply as quickly as you can because there is a funding cap and lenders need time to process your loan."
5. Payroll - Qualified payroll including salary, wages, commissions and tips were capped at \$100,0000 on an annualized basis for each employee.

B. PPP FLEXIBILITY ACT - The Act, signed into law June 5, 2020, includes:

1. Extended the PPP loan forgiveness period, from 8 weeks after the date of loan disbursement, to 24 weeks after the date of loan disbursement.
2. Reduced the 75% payroll requirement to 60%,
3. Eliminated the 2-year loan repayment restrictions. Increased the maturity date of PPP loans that are approved by the SBA or after June 5, 2020, to 5-years.
4. Allows payroll tax deferment for PPP recipients,
5. Extended the June 30 rehiring deadline to December 31, 2020.
6. Provided for documenting a former employee's refusal to return to work as an acceptable reason for lower headcounts or pay.

C. PPP LOAN FORGIVENESS - The Loan Forgiveness Application is due 10 months after the end of the covered period. So, if your loan was disbursed on April 10, 2020, the 24-week period would end on September 24, 2020, and your Loan Forgiveness Application would be due July 24, 2021.

Otherwise, principal and interest loan payments would begin the next month.

The IRS has notified lenders not to file any Form 1099-C - Cancellation of Debt for PPP loan forgiveness purposes.

SECTION 3. THE REST OF THE CARES ACT

A. RECOVERY REBATES - The Stimulus payments you received are called Recovery Rebates.

Individuals are eligible for a \$1,200 credit (\$2,400 on a joint return) plus \$500 for each qualified dependent. The credit is reduced "by \$5 for every \$100 that the taxpayer's Adjusted Gross Income exceeds \$150,000 on joint returns, \$112,000 on Head of Household returns, and \$75,000 on single returns.

These payments are actually an advance of amounts to be reported on 2020 tax returns when you will reduce your eligible credit by any advance payments received.

If the taxpayer receives a rebate but their 2020 income makes them ineligible, no repayment is required.

If the taxpayer was not eligible based on 2018 or 2019 income; but are eligible based on their 2020 income, they can claim the rebate on their 2020 tax return.

Also, you may be able to increase the overall amount of recovery rebates if you claimed a dependent in 2018 or 2019, but don't claim them in 2020

If an individual died before receiving the rebate, the payment is ineligible and must be returned. This rule would also apply if payment was made to a surviving spouse or the parents of a deceased qualifying child.

B. EMPLOYEE RETENTION CREDIT - Certain employers can claim a credit for 50% of qualified wages, up to \$10,000 per employee (a \$5,000 credit), paid between March 13, 2020 and December 31, 2020.

However, if the employer receives a covered Paycheck Protection Program (PPP) loan, they are not eligible to claim the employee retention credit.

Qualified employers include tax-exempt organizations, employers with suspended operations due to a government order, and those who experienced a significant decline in gross receipts.

Qualified wages must be paid during a calendar quarter in which the employer experiences an economic hardship.

Qualified wages include the cost of employer-provided health insurance, but not Paid Leave required by the Families First Coronavirus Response Act.

Qualified wages vary depending on the number of full-time employees (FTE) during 2019. If the employer had:

- 100 or fewer FTE, the credit is based on wages paid to all employees, regardless if they worked,
- more than 100 FTE, the credit is allowed only for wages paid to employees for time they did not work.

To claim the credit, employers must report the qualified wages and health insurance costs for each quarter on their quarterly payroll tax returns (Form 941).

- C. CHARITABLE CONTRIBUTIONS - For 2020, taxpayers can claim an above-the-line deduction for up to \$300 in cash/check charitable contributions.
- D. PAYROLL TAX DEFERRAL - For payroll tax deposits due between March 27, 2020, and December 31, 2020, the Cares Act allows employers to delay paying the employer's share of social security tax (6.2% of wages) as follows:
- 50% must be paid by December 31, 2021, and
 - the other 50% must be paid by December 31, 2022.
- For self-employed taxpayers, 50% of the social security portion of their self-employment tax will also be eligible for the deferral using the same dates.
- E. NET OPERATING LOSS - The Act retroactively suspends the limitation that only 80% of taxable income can be sheltered by a Net Operating Loss (NOL) for 2018, 2019, and 2020.
- The Act also requires NOLs arising in 2018, 2019, or 2020, to be carried back to the five tax years preceding the year of the loss.
- If the taxpayers do not want to carryback NOLs created in 2018, 2019, or 2020, they must make an election to waive the carryback on their 2020 tax return.
- F. EXCESS BUSINESS LOSS - The Act eliminates the Excess Business Loss (EBL) rules for 2018, 2019, and 2020. Those rules disallowed net losses when they exceeded certain thresholds, originally set at \$250,000 in 2018 (\$500,000 if MFJ), indexed for inflation.
- G. INTEREST EXPENSE LIMITATION - The Act reduced the Interest Expense Limitation for large taxpayers (average \$25 Million of gross receipts) from 30% to 50% of adjusted taxable income.
- H. QUALIFIED IMPROVEMENT PROPERTY - Under the CARES act, a 15-year recovery period is retroactively assigned to Qualified Improvement Property (QIP).
- QIPs are internal improvements to nonresidential property placed in service after December 31, 2017. However, they do not include costs for elevators, escalators, or building enlargements.
- QIPs may be depreciated over 15 years. They also qualify for 100% bonus depreciation.
- Revenue Procedure 2020-25, released April 17, 2020, allows taxpayers who placed QIP property in service during 2018, 2019, or 2020, and now want to claim 15-year depreciation, or 100% bonus depreciation, the option to file an amended return, an Administrative Adjustment Request (AAR), or a Form 3115 - Application for Change of Accounting Method.

H. QUALIFIED IMPROVEMENT PROPERTY - Continued

Using Form 3115 allows taxpayers with \$50,000 or less of total changes to recognize those in the current year, while larger amounts would get deducted over 3-years.

I. STUDENT LOAN PAYMENTS - The Act allows up to \$5,250 of "student loan" payments, paid by an employer, to qualify as part of a Qualified Educational Assistance Program. To qualify:

1. there must be a written plan,
2. the plan must not discriminate in favor of highly compensated employees, and
3. No more than 5% of the annual expense of the plan may be provided to the business owners, their spouses, or their dependents.

J. NO REQUIRED MINIMUM DISTRIBUTION (RMD) - The CARES Act suspended RMDs for 2020.

K. RETIREMENT DISTRIBUTIONS - The CARES Act allows taxpayers to take up to \$100,000 in Coronavirus-related distributions from their retirement plans. These distributions are:

1. not subject to the 10% early distribution penalty, and
2. taxable ratably over a 3-year period beginning with the year of distribution.

However, taxpayers can elect to have the entire amount taxed in the year received.

Taxpayers also have the option to repay part or all of the distribution anytime during the 3-year period.

SECTION 4. INDIVIDUALS

A. KIDDIE TAX - The Old Kiddie Tax rules taxed children's "unearned" income, including interest, dividends, & capital gains, at their parent's marginal tax rates.

- 2018 & 2019 - Then, beginning with 2018 returns, the Tax Cuts & Jobs Act (TCJA) eliminated the connection to the parent's tax rates and, instead, taxed the unearned income of children using the "Trust & Estate" tax rates. This new regime was called the TCJA Kiddie Tax.

Next, the Further Consolidated Appropriations Act of 2020 (FCAA) eliminated the TCJA Kiddie Tax beginning in 2020. However, FCAA also gave taxpayers the option to use either method for 2018 and 2019. But, in order to take advantage of that new option, you may need to amend your child's 2018 or 2019 tax return.

And unfortunately, which scenario produces the best result varies widely on a "case-by-case basis since the TCJA Kiddie Tax brackets are unique to each child based on the mix of earned and unearned income." (JA -July 2020). And becomes more complex if the parents' or siblings' returns also need to be amended.

This means, unless the income is substantial, we can't justify the cost of performing the analysis.

- 2020 - For 2020 and beyond, the Old Kiddie Tax rules apply.

B. REQUIRED MINIMUM DISTRIBUTIONS - We mentioned the new Required Minimum Distribution (RMD) rules last year. Those rules indicated that if you reached age 70.5 during 2019, the prior rules still applied and you were required to take your RMD by April 1, 2020, at least until the CARES Act suspended all 2020 RMDs.

So now, those who reached age 70.5 in 2019 will be required to take their first RMD by April 1, 2021.

But those who reached age 70.5 during 2020 or later can delay their first RMD until April 1 of the year after they reach age 72.

C. PELL GRANT INCOME - We also mentioned the special PELL grant rules last year. But we found this very useful and wanted to mention it again. A student who receives a PELL grant may choose to recognize the grant as paying for "living expenses;" even if the institution applies the PELL grant against tuition and fees. If the student makes this choice, they must recognize the PELL grant as taxable income, but may not actually owe any tax. And then, their parents won't have to reduce the qualified education expenses by the PELL grant amount.

D. CANCELED STUDENT LOANS - In Rev. Proc. 2020-11, the IRS expanded its earlier rules (Rev. Proc. 2015-57, 2017-24 and 2018-39) allowing students to avoid Cancellation-of-debt (COD) income if their loans were discharged because of fraud or a schools closing.

E. IRS AUDIT & AMENDMENT WINDOW - On June 26, 2020, a "written advice" from the IRS Chief Council revised prior treatment, and now, an original return (i.e.: filed by April 15th), and not a subsequent on-time "extension" return, starts the "three-year statutory period for assessment under Sec. 6501 or for filing a refund claim under Sec. 6511."

"A superseding return is a return filed subsequent to the originally filed return and filed within the filing deadline. Under Sec. 6501(b)(1), if both ... return[s] are filed before the original deadline, ... there is no effect on the limitation period because both returns are deemed filed on the due date."

But, "a return filed on extension is considered filed when it is received."

SECTION 5. BUSINESS

A. MINIMUM WAGE - On January 1, 2021, the Illinois Minimum Wage increases from \$10.00 to \$11.00 per hour. On January 1st each year thereafter the rate will increase again to \$12.00 in 2022, \$13.00 in 2023, \$14.00 in 2024, and \$15.00 in 2025. New employees may be paid 50 cents less during their first 90 days. Tipped employees may be paid 60% of the minimum wage. Chicago and Cook County each have separate rates.

The minimum wage for employees under the age of 18, working less than 650 hours per year, increases from \$8.00 to \$8.50 on January 1, 2021, then \$9.25 in 2022, \$10.50 in 2023, \$12.00 in 2024 and \$13.00 in 2025.

Federal law generally exempts salaries of \$684 per week (\$35,568 annually) from the minimum wages requirements.

B. NEW FORM 1099-NEC - Beginning in 2020, payments for Non-Employee Compensation will be reported on Form 1099-NEC.

C. ENTERTAINMENT EXPENSES - Final regulations clarify that entertainment expenses are generally not deductible. Some exceptions include:

- a. Employee Party - Employee recreational or social expenses for non-highly compensated employees,
- b. Business Meeting - Expenses directly related to employee, stockholder, agent or director meetings,
- c. Convention - Expenses directly related and necessary to attendance at a convention of any 501(c)(6) entity like a business league or chamber of commerce,
- d. Public Expenses - Expenses for goods or services made available to the general public, and
- e. Entertainment Sold - Entertainment expenses sold in a bona fide transaction for full & adequate consideration.

D. MEALS & DRINKS - Though entertainment is no longer deductible, food and beverages are still 50% deductible if:

1. the expense is an ordinary & necessary business expense,
2. the expense is not lavish or extravagant,
3. the expense is provided to a current or potential client, customer or similar business contact,
4. the taxpayer or an employee is present,
5. the cost of food or beverages provided at entertainment activities, including tax, tips and delivery fees, is stated and paid for separately.

E. AUTO EXPENSES - The value of an automobile, truck or van must not exceed the annual inflation-adjusted threshold in order to qualify for the:

- a. the cents-per-mile valuation rule, or
- b. the fleet-average valuation rule.

The amount increased from \$50,000 in 2018 to \$50,400 in 2019. But IRS Notice 2020-05 kept that amount unchanged for 2020.

Cents Per Mile - The cents-per-mile rule allows for the determination of personal use based on the standard mileage rate.

Fleet Average - The fleet average rule allows employers operating a fleet of 20 or more vehicles to use an average annual lease value for every vehicle in the fleet, when applying the annual lease valuation rules.

F. TRAVEL ON COMPANY PLANE - Rev. Rul. 2020-21 set the new rates for flights taken between July 1 and December 31, 2020, at:

- a. \$42.62 as a terminal charge, plus
- b. the Standard Industry Fare Level (SIFL) mileage rate used for determining the value of noncommercial flights employer-provided aircraft of:

- up to 500 miles - \$0.2331 per mile
- 501 - 1500 miles - \$0.1778 per mile
- Over 1500 miles - \$0.1709 per mile

G. QUALIFIED BUSINESS INCOME DEDUCTION - When the IRS introduced Form 8995 to calculate the Qualified Business Income (QBI) deduction allowed on 2019 tax returns, their instructions for that form expanded the factors to be included in the QBI calculation to include:

- (a) the charitable contributions of the business, and
- (b) unreimbursed partnership expenses.

Neither of those had been mentioned in the Code Sec. 199A statutory language or the final regulations.

H. WAYFAIR NEXUS EFFECT - Fallout from the 2018 Wayfair case that created sales tax nexus in South Dakota after \$100,000 of annual sales or 200 annual transactions continues to evolve. So far every state that imposes a sales tax - except Florida, Louisiana, and Missouri - has implemented similar rules.

And, if sales tax is owed, income tax may also be owed.

I. 100% BONUS DEPRECIATION - The final 100% Bonus Depreciation Regulations clarified that prior ownership - having a depreciable interest during the five calendar years immediately prior to the current placed-in-service year - will disqualify the property for 100% bonus depreciation purposes.

SECTION 6. PASSIVE ACTIVITIES & RENTALS

- A. MATERIAL PARTICIPATION - In Barbara (T.C. Memo. 2019-50), the Tax Court ruled that the taxpayer, who spent 40% of his time in Florida but continued working "remotely" on his Chicago business, could use that remote time to qualify as material participation, because of the substantial nature of such remote work.
- B. LATE ELECTION TO TREAT RENTALS AS SINGLE ACTIVITY - In two cases, taxpayers were given an extension to elect to treat all interests in rental real estate as a single activity. In each case, the taxpayers had inadvertently filed their returns without the required election.

SECTION 7. FARMERS

- A. CORONAVIRUS FOOD ASSISTANCE PROGRAM - The Coronavirus Food Assistance Program (CFAP) provides payments for producers of certain agricultural commodities adversely affected by the pandemic. CFAP payments are taxable income.
- B. FARMERS CAN REVOKE UNICAP ELECTION - New Rev. Proc. 2020-13 will allow farmers with annual gross receipts of \$25 million or less, to revoke a prior election out of the uniform capitalization (UNICAP) rules, with respect to pre-productive plant expenditures.

The original election "out" of the UNICAP rules avoided the burden of those honerous rules; but required the taxpayer to use the MACRS "ADS" straight-line depreciation method.

SECTION 8. PARTNERSHIP STUFF

- A. AMENDED RETURNS - The Bipartisan Budget Act of 2018 (BBA) changed the partnership audit rules effective January 1, 2018, where taxes owed on any adjustment, are taxed to the partnership at the highest tax rate in effect that year, instead of to the individual partners at their tax rates. Partnerships can elect "out" of those BBA rules and have the audit rules for individuals apply instead.
- Those BBA procedures also requires partnerships subject to the BBA regime to file an Administrative Adjustment Request (AAR) before they can file an amended partnership return.
- However, IRS Rev. Proc. 2020-23 released on April 8, 2020, allowed eligible partnerships to file amended 2018 and 2019 returns by September 30, 2020, without filing an AAR.
- B. PRIORITY PROFITS - A Priority Profit Allocation (PPA) designates a specified percentage of the partnership income to be paid to one or more partners. Unlike "fixed" Guaranteed Payments (GP), the amount of a PPA payment will "fluctuate" from year-to-years depending on the partnership income. But, while GPs are not eligible for the 20% Code Sec. 199A - Qualified Business Income, but PPAs do qualify.
- PPAs, like GPs, are subject to self-employment tax.
- C. TAX BASIS REPORTING - IRS Notice 2019-66 requires partnerships to report partner capital accounts on the "tax" basis beginning with their 2020 returns.
- D. 704(c) GAIN/LOSS - IRS Notice 2019-66 requires any Code Sec. 704(c) gain or loss, created whenever a partners "contributes" property into a partnership and attaching to that partner upon any subsequent disposition, must be reported on the partnership tax return beginning in 2019.
- E. AT-RISK REPORTING - IRS Notice 2019-66 clarifies that, in spite of the 2019 Form 1065 instructions that indicate otherwise, the new Code Sec. 465 "at-risk" reporting is not required until 2020. Reporting for each separate "at-risk" activity will include: (1) the amount of income or loss, and (2) the amount of partnership liabilities.

SECTION 9. MISCELLANEOUS TAX FACTS

| | 2018 | 2019 | 2020 | 2021 |
|---|-------------|-------------|-------------|------------|
| Old personal exemption (used for other purposes) | 4,150 | 4,200 | 4,300 | |
| Standard deduction - Single | 12,000 | 12,200 | 12,400 | 12,550 |
| - Married filing joint | 24,000 | 24,400 | 24,800 | 25,100 |
| - Married filing separate | 6,500 | 12,200 | 12,400 | 12,550 |
| - Head of Household | 9,550 | 18,350 | 18,650 | 18,800 |
| - Dependent | 1,050 | 1,100 | 1,100 | 1,100 |
| Additional amount for Blindness or Age (65) | 1,300 | 1,300 | 1,300 | 1,350 |
| - if unmarried & not a surviving spouse | 1,600 | 1,650 | 1,650 | 1,700 |
| Taxable Social Security (FICA) wage base | 128,400 | 132,900 | 137,700 | 142,800 |
| IRA & Roth IRAs - Maximum contribution | 5,500 | 6,000 | 6,000 | 6,000 |
| - Catch-up if 50 or older | 1,000 | 1,000 | 1,000 | 1,000 |
| IRA contribution - Limited if income exceeds: | | | | |
| - and both spouses covered by retirement plan | 101,000 | 103,000 | 104,000 | 105,000 |
| - only one spouse covered by retirement plan | 189,000 | 193,000 | 196,000 | 198,000 |
| Roth IRA contribution - Limited if income over: | | | | |
| - Single & Head of household | 120,000 | 122,000 | 124,000 | 125,000 |
| - Married filing joint | 189,000 | 193,000 | 196,000 | 198,000 |
| 401(k) 403(b) & 457(b) - Maximum Elect. Deferral | 18,500 | 19,000 | 19,500 | 19,500 |
| - Add'l if 50 or older | 6,000 | 6,000 | 6,500 | 6,500 |
| SIMPLE - Maximum Elective Deferral | 12,500 | 13,000 | 13,500 | 13,500 |
| - Additional if 50 or older | 3,000 | 3,000 | 3,000 | |
| Defined Contribution - Max. annual contribution | 55,000 | 56,000 | 57,000 | |
| Social Security - Earnings limit if under Normal Retirement age | 17,040 | 17,640 | 18,240 | 18,960 |
| HSA - Self-only - Annual contribution limit | 3,450 | 3,500 | 3,550 | 3,600 |
| - Minimum deductible | 1,350 | 1,350 | 1,400 | 1,400 |
| - Maximum out-of-pocket | 6,650 | 6,750 | 6,900 | 7,000 |
| - Family - Annual contribution limit | 6,900 | 7,000 | 7,100 | 7,200 |
| - Minimum deductible | 2,700 | 2,700 | 2,800 | 2,800 |
| - Maximum out-of-pocket | 13,300 | 13,500 | 13,800 | 14,000 |
| Standard Mileage Rates - Business rate (per mile) | .545 | .58 | .575 | |
| - Medical rate | .18 | .20 | .17 | |
| - Charitable rate | .14 | .14 | .14 | |
| Per Diem Rates - Beginning | Oct 1, 2017 | Oct 1, 2018 | Oct 1, 2019 | |
| - For Lodging (low-cost locality) | \$134 | \$134 | \$140 | \$138 |
| - For Meals & Incidentals (low-cost locality) | \$57 | \$57 | \$60 | \$60 |
| - Meals & Incid. (low-cost transport. industry) | | \$66 | \$66 | \$66 |
| Estate & Gift Taxes | | | | |
| Estate & gift tax applicable exclusion amount | 11,180,000 | 11,400,000 | 11,580,000 | 11,700,000 |
| Illinois estate tax applicable exclusion amount | 4,000,000 | 4,000,000 | 4,000,000 | 4,000,000 |
| Annual gift tax exclusion | 15,000 | 15,000 | 15,000 | 15,000 |