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Tax Newsletter

Seven Tax Traps in the New Law
New individual tax pitfalls to avoid

The new **One Big Beautiful Bill Act** (OBBBA), a follow-up to the Tax Cuts and Jobs Act (TCJA) passed during President Trump's first term, contains numerous tax breaks for individuals. But the massive new law also poses several potential tax "traps" for the unwary. Consider the following.

1. Itemized deductions: Among a slew of other changes for individuals, the TCJA suspended several itemized deductions, including the following:

- Miscellaneous expenses;
- Casualty and theft losses (except for qualified disaster-area losses);
- Mortgage interest paid on up to $100,000 of home equity debt; and
- Job-related moving expenses (except for active-duty military personnel).

The OBBBA extends these changes and makes them permanent. It also extends and modifies other itemized deduction rules (e.g., retaining the $750,000 threshold for deducting mortgage interest on acquisition debt).

2. Personal exemptions: Previously, you could claim a personal exemption for yourself, your spouse and each of your dependents. The TCJA suspended personal exemptions from 2018 through 2025 in conjunction with various other changes for individuals. Under the OBBBA, personal exemptions are permanently eliminated.

3. Charitable deduction floor: For the first time ever, the new law imposes a "floor" of 0.5% of adjusted gross income (AGI) on charitable donations. This operates like the 7.5%-of-AGI floor for medical deductions. For instance, if your AGI is $100,000 and you donate $10,000, your deduction is limited to $9,500. (The law also imposes a 1% floor on corporate donation deductions.)

4. SALT payments: The TCJA capped the annual deduction for state and local tax (SALT) payments at $10,000 for 2018 through 2025. Although the new law increases the cap to $40,000, beginning in 2025, and adds 1% each succeeding year, the higher threshold is phased out for high-income taxpayers for 2025 through 2029. The OBBBA reduces the cap by 30% of the amount by which modified adjusted gross income (MAGI) exceeds $500,000, with an annual 1% increase in the threshold. The rules revert to prior law in 2030. **Note:** We will have more on SALT "workarounds" in the next issue.

5. Pease rule: The "Pease rule" required certain high-income taxpayers to reduce certain itemized deductions—including those for charitable donations—by 3% for every dollar of taxable income above an annual threshold, up to a total reduction of no more than 80%. This rule was suspended from 2018 through 2025. Now the OBBBA revives a modified version reducing deductions for taxpayers in the top 37% tax bracket, beginning in 2026.

6. EV credits: Currently, you can claim a credit of up to $7,500 for acquiring a new electric vehicle (EV) or plug-in hybrid that meets certain consumption requirements. The maximum credit for a used vehicle is $4,000. But the OBBBA ends the EV credits once and for all for vehicles acquired after **September 30, 2025**. You must move fast if you intend to beat this deadline.

7. Home energy credits: Similar to EV credits for car buyers, homeowners may qualify for one or two home energy credits for qualified installations. Both the energy efficient home improvement credit and the residential clean energy credit are available for up to 30% of qualified expenses, subject to certain limitations. The OBBBA repeals both credits in 2026.

Finally, the new law also cracks down on losses from gambling activities (see related article), among other adverse provisions hidden in the fine print. **The upshot**: Be aware of all the OBBBA pros and cons for taxpayers as we head into the end of the year.

How to Bridge a Retirement Shortfall
Practical ideas for closing the gap

People are living longer than they did "back in the day." Of course, that is good news, but it also means you may have to build up a bigger cushion in retirement than you had initially intended. Furthermore, uncertainty over future Social Security benefits adds to the concerns. As a result, you could face a personal shortfall, especially if you incur unforeseen expenses from a health-related issue or some other emergency.

First step: Do not panic. Even if retirement is imminent, you may be able to make up lost ground quickly or take other steps to protect yourself. Here are several practical ideas to review.

- **Ramp up your retirement savings.** For example, if you participate in a 401(k) plan at work, you can generally defer up to $23,500 to your account in 2025. This figure is increased to $31,000 for those age 50 or over. **Special rule:** If you are age 60 through 63, you can tack on a "super catch-up contribution" for a grand total of $34,750. Just a few years of contributions at or near the maximum level can significantly bolster your account.

- **Work on the budget.** Now that you are aware of a potential portfolio, you might want to dial down your expectations. Make realistic estimates about the income you expect to be coming in and the expenses going out. Although you will likely be paying less for housing and other items like life insurance—especially if your children are already adults—consider the impact of potential increases in some expenses potential increases in some expenses like travel expenditures.

- **Move to a smaller home.** For most people, housing is the largest overall cost, representing on average more than one-third of overall spending. If your kids have flown the coop but you're still living in the large home where you raised them, it may be time to downsize. In addition, you might want to move to a state with a different climate, taking state income taxes into account. Of course, various other factors—such as proximity to family and personal preferences—will come into play.

- **Refinance your current home.** If you decide to stay put, you should probably refinance an existing mortgage if you are paying a rate higher than the current rates. Depending on your situation, you may be able to save tens of thousands of dollars over time by refinancing. **Note:** That your interest payments will generally continue to be tax-deductible under the latest rules.

- **Do not quit for good.** Just because you've reached retirement age does not mean you have to stop working completely. If needed, you could pursue part-time employment, preferably in a line of work you enjoy. For some individuals, working full-time a little longer is also a viable option.

Reminder: Everyone's situation is different. Therefore, maybe none of these ideas or only some of these ideas are right for you. The most important thing to do is to assess your financial status and go from there.

Passing Grade for Educator Deduction
New law rewrites the rules

Although the new One Big Beautiful Bill Act (OBBBA) extends the tax law crackdown on miscellaneous expenses, including unreimbursed employee business expenses, it provides a new tax avenue for other taxpayers. For the first time ever, qualified educators can deduct all their out-of-pocket expenses without any dollar cap.

On the other hand, some educators who previously were able to claim a limited above-the-line deduction may get zero tax benefit.

Background: Prior to the Tax Cuts and Jobs Act (TCJA), you could deduct qualified miscellaneous expenses in excess of 2% of your adjusted gross income (AGI). This included various investment and tax-related expenses as well as unreimbursed employee business expenses. For instance, if you had an AGI of $100,000 and personally spent $3,000 on office supplies for your business, you could deduct $1,000, but only if you itemized deductions.

However, the TCJA suspended the miscellaneous expense deduction from 2018 from 2025. It was scheduled to be reinstated in 2026, but now the OBBBA eliminates it permanently.

Separate and apart from the miscellaneous deduction, educators can deduct up to $300 a year for their unreimbursed classroom expenses (recently raised from $250), whether they itemize or not. This deduction is still available on 2025 returns.

Who is eligible for the deduction? Teachers, of course, but the list of qualified educators goes further. The deduction may be claimed by someone employed as a principal, instructor, counselor or aide for students in kindergarten through senior year in high school. For instance, a guidance counselor who provides college prep materials to students may qualify for the write-off.

Note: That the deduction is not available, however, to preschool and day care teachers, camp counselors, college professors and other higher education instructors, self-employed tutors and part-time school aides. It is also off-limits to parents who homeschool their kids.

Qualified expenses include more than just crayons and glitter. Specifically, the costs of the following expenses are allowed.

- Books;
- School supplies;
- Computer equipment and software;
- Athletic equipment for physical education,
- Professional development courses or conferences related to course curriculum; and
- Any other item that is appropriate for and helpful to the students and classroom.

Reminder: Out-of-pocket classroom expenses are not deductible if you are reimbursed by the school, a teacher's union, a parent-teacher association or some other person or entity.

Now the OBBBA flips the page. Beginning in 2026, it revises the rules for the educator expense deduction. Notably, the new law eliminates the $300 cap, but the deduction is limited to itemizers. For instance, if you itemize and pay $1,500 in classroom expenses out of your pocket, you can deduct the entire $1,500. However, if you claim the standard deduction, there is no tax reward for your generosity.

Lesson to be learned: You may have a decision to make at the end of the year. If you expect to itemize deductions next year, you might postpone deductible expenses until 2026. Conversely, you may pay out of-pocket educator expenses in 2025 to salvage a $300 deduction ($600 for joint filers if each spouse qualifies). Go to the head of the tax class!

Don't Be Scared By Zombie Debt
Scavengers are on the lookout

It has nothing to do with the walking dead, but "zombie debt" from years ago can come back to haunt you in the present day. It helps to review your financial records to portray an accurate picture of any liabilities.

Background: The term "zombie debt" is used to describe debt that was purchased from the original creditor or collection agency at a miniscule price. Then the new debt holders stalk the consumers to get them to pay the debt.

This type of scam has been ramping up in recent years. The scavengers may range from Wall Street bigwigs to fly-by-night hustlers. The older the debt, the more likely it is that zombie debt collectors can scoop it up for pennies on the dollar.

What kind of debt is included in zombie debt? It can vary, but these three types of debts are frequently involved.

1. Expired debt: If the statute of limitations has run out on the debt—the length of time it can be legally collected—it is no longer viable. The time allowed differs from one jurisdiction to the next. In any event, the con artists may try to trick you into paying off expired debt.

2. Other people's debt: Zombie debt might not even be yours. Maybe it is debt of a person who has a name similar to you—for example, an "s" is added to or subtracted from your last name—or it could stem from an inaccurate data entry. Plus, someone might come after you for debt that has already been paid off in full.

3. Bankruptcy debt: It is not unusual for scavengers to seek payment for debt that has been discharged in bankruptcy.

How do zombie tax collectors get you to pay? Not surprisingly, they often frighten you into paying debt that you are not legally obligated to address. This can take several forms including the following common scare tactics.

- Accept payment for a portion of the debt. The scavenger may claim they are willing to let you off the hook if you make a partial payment. Unfortunately, this only resets the statute of limitations, so the tax collector can subsequently come after you for the rest.

- Offer to "fix" your credit report. Debt can remain on your credit report for seven years plus 180 days from the date of the delinquency. A scam artist may convince that they can have the debt removed earlier or they can add debt after the 7½-year period has ended.

- Threaten to sue you or garnish wages. Despite having no legal standing, a scavenger may sue you, or more likely threaten to sue you, for unpaid debt. Or they may threaten to have amounts withheld from wages by employers.

- Engage in abuse and harassment. Zombie debt collectors may try to intimidate you into paying by being verbally abusive or hounding you relentlessly. Or a couple could team up against you by playing "good copy, bad cop" roles.

- Pretend to be an attorney. The scavenger may represent themselves as an attorney or another member of a law firm. This often accompanies the threat of legal action. The idea is to scare you into paying a debt you do not owe.

If you are contacted by a zombie debt collector, do not panic. Contact an attorney before you make any moves—especially payments.

Raw Deal for Gambling Losses

Generally, you can deduct the amount of your gambling losses, but only up to the amount of your winnings for the year, if you itemize on your return. The amount of the annual loss includes certain expenses like travel expenditures.

Busted! The new law just changed the tax odds in the IRS' favor. Under the One Big Beautiful Bill Act (OBBBA), the deduction is reduced to 90% of the losses, on top of the other limit. For example, if you have $10,000 in winnings and $8,000 in loses, your deduction is reduced to $7,200 (90% of $8,000).

This change is scheduled to take effect in 2026 but has already met with strong resistance. Proposed legislation would restore prior law. We will keep you posted.

Facts and Figures
Timely points of particular interest

Business Car Warranty—Suppose you buy an extended warranty on a vehicle used for business purposes. Can you deduct the full amount in the year of the purchase? No. Instead you can only deduct the portion of the warranty expense attributable to the months the car is used. For example, if you buy a car on September 1, 2025, and add the warranty, the cost of the warranty attributable to four months is deductible on your 2025 return. **Note:** If the vehicle is also used personally, the deduction is further reduced based on the applicable business percentage.

The OBBBA 2.0—Just because the One Big Beautiful Bill Act (OBBBA) has been signed into law does not mean that Congress will take a break from passing new tax legislation. The drums have already started beating for another reconciliation bill to wend its way through Congress this fall. The proposed legislation could revive provisions proposed in either the House or Senate that fell by the wayside in the final version of the OBBBA. At the very least, expect a "technical corrections act" to clean up unintended results and errors.