



# 2017

## YEAR-END TAX PLANNING GUIDE

**rkl** LLP  
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# 2017 YEAR-END TAX PLANNING GUIDE



**At RKL, helping our clients save on taxes isn't a once and done exercise.**

It's a year-round effort of strategic analysis and proactive planning that gives individuals and businesses a competitive advantage. This requires ongoing evaluation and assessment of changes and factors that may impact tax exposure. With a new year on the horizon, now is a perfect time to examine your unique circumstances to uncover new opportunities to minimize income taxes.

As part of our ongoing effort to help clients achieve a more secure financial position, we're proud to present our first year-end tax planning guide. In this edition, we provide an overview of critical tax rates and information, outline key considerations for business owners and individual taxpayers and highlight actions to take before the end of the calendar year to reap savings at tax filing time.

As tax reform and legislation swirl through the halls of power in Washington D.C., you can count on your RKL tax team to monitor the latest changes and assess the impact of any tax policies on you and your business.

After reviewing this 2017 guide, contact your RKL advisor before taking any actions. Our diverse expertise means we're able to help you navigate the complex tax code, identify opportunities and execute accordingly in the context of your personal financial circumstances.

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## 2017 HEADLINE: **DISASTER RELIEF**

Devastation from recent hurricanes, tropical storms and wildfires affected millions of individuals and businesses across California, Florida, Georgia, Louisiana, Puerto Rico, South Carolina, Texas and the U.S. Virgin Islands, with cleanup and recovery efforts still ongoing. Upon the declarations of federal disaster, the IRS issued a number of tax relief provisions intended to support taxpayers not only located in the impacted regions, but also individual and business taxpayers with ties to these areas.

**Additional time to file and expedited request for copies:** The IRS is postponing deadlines on or after August 23, 2017 until January 31, 2018. This includes tax returns, estimated taxes and payroll. Additionally, the IRS will expedite any requests for copies of tax returns from taxpayers in affected areas. Use Form 4506 to request a copy of a return and Form 4506-T to request a transcript of a return.

**Casualty losses:** The IRS is also providing an opportunity for taxpayers in a federally declared disaster area to claim casualty losses on their current year returns or a prior year return.

**Leave-based donation programs and relief payments:** The IRS tax relief provisions permit employees to elect to forgo vacation, sick or personal leave in exchange for employer contributions to charities. The IRS deemed in situations related to hurricane relief, cash payments made by an employer will not constitute wages. In such cases, payments must be made by January 1, 2019, for the express purpose of assisting Hurricane Harvey and Irma victims. Employers should not include these donations in Box 1, 3 or 5 of Form W-2; instead, employers may deduct the payments as ordinary and necessary business expenses under Internal Revenue Code Section 162.





# KEY 2017 TAX FIGURES & LIMITS

## QUICK REFERENCE GUIDE

### STANDARD DEDUCTION

<b>MARRIED FILING JOINTLY</b>	\$12,700
<b>SINGLE</b>	\$6,350
<b>HEAD OF HOUSE HOLD</b>	\$9,350
<b>MARRIED FILING SEPARATELY</b>	\$6,350

### PERSONAL EXEMPTION

\$4,050

### IRA CONTRIBUTION

(TRADITIONAL & ROTH)

\$5,500 (with additional \$1,000 catch up over age 50)

### FEDERAL ESTATE TAX

40% maximum tax rate

\$5.49 million per individual lifetime exclusion

### ANNUAL GIFT TAX EXCLUSION

\$14,000 per recipient

### HSA CONTRIBUTION

(EMPLOYER & EMPLOYEE)

\$3,400 | **Self only** (with additional \$1,000 catch up over age 55)  
 \$6,750 | **Family**

## DEADLINES FOR 2017 INDIVIDUAL & BUSINESS TAX FILINGS

The IRS updated several tax return and extension deadlines during the summer of 2017 that will affect upcoming filings. The below chart outlines key dates to keep in mind. Also, when a regular tax date falls on a weekend or legal observed holiday observed in Washington, D.C., the tax return is pushed to the next business day. This practice will impact several due dates, including the individual, C Corporation and Partnership extension deadlines.

TAX TYPE	DUE DATE (for calendar year entities)
Partnerships (Form 1065) & S Corporations (Form 1120S)	March 15, 2018
Individuals (Form 1040), C Corporations (Form 1120), Foreign Bank and Financial Reporting Form (FBAR) FinCEN Report 114 and Trusts and Estates (Form 1041)	April 17, 2018
Tax-exempt Nonprofit Organizations (Form 990)	May 15, 2018
Filing extensions for Partnerships & S Corporations	September 17, 2018
Filing extension for Trust and Estates	October 1, 2018
Filing extensions for Individuals, Foreign Financial Reporting & C Corporations	October 15, 2018
Filing extension for Tax-exempt Nonprofit Organizations	November 15, 2018

# INDIVIDUAL TAXPAYERS



## A lot can happen in a year.

That's why individuals should start year-end tax planning by assessing the changes that took place to their personal situation over the past 12 months. Whether it's a new job, a new house or a new member of the household, life events can impact tax exposure in a variety of ways. This section of the guide contains an overview of common individual tax provisions as well as key tax rates and considerations to get year-end planning off to a solid start.

## LIFE CHANGES WITH TAX IMPACT

- Marriage, divorce or death that changes filing status
- Birth of a child
- Child outgrows tax credit eligibility
- Changes in health
- Relocation/moving/new home purchase
- Higher education and associated expenses
- Starting or closing a business
- Inheritance
- Changes in employment status
- Retirement

## Understanding the impact of various tax planning strategies starts with knowing your tax rate.

Another key factor is the personal exemption and itemized deduction phase out. It's important to recognize the limitations for itemized deductions and when your personal exemption starts to decrease. The charts that follow provide the necessary information for finding out where you stand on these areas. Keep in mind, the tax brackets and rates are adjusted for inflation each year.

## 2017 INCOME TAX RATES & BRACKETS

RATE	SINGLE	HEAD OF HOUSEHOLD	MARRIED FILING JOINTLY	MARRIED FILING SEPARATELY
<b>10%</b>	\$0 to \$9,325	\$0 to \$13,350	\$0 to \$18,650	\$0 to \$9,325
	<b>TAX OWED</b> 10% of Taxable Income	<b>TAX OWED</b> 10% of Taxable Income	<b>TAX OWED</b> 10% of Taxable Income	<b>TAX OWED</b> 10% of Taxable Income
<b>15%</b>	\$9,326 to \$37,950	\$13,351 to \$50,800	\$18,651 to \$75,900	\$9,326 to \$37,950
	<b>TAX OWED</b> \$932.50 plus 15% of the excess over \$9,325	<b>TAX OWED</b> \$1,335 plus 15% of the excess over \$13,350	<b>TAX OWED</b> \$1,865.00 plus 15% of the excess over \$18,650	<b>TAX OWED</b> \$932.50 plus 15% of excess over \$9,325
<b>25%</b>	\$37,951 to \$91,900	\$50,801 to \$131,200	\$75,901 to \$153,100	\$37,951 to \$76,550
	<b>TAX OWED</b> \$5,226.25 plus 25% of the excess over \$37,950	<b>TAX OWED</b> \$6,952.50 plus 25% of the excess over \$50,800	<b>TAX OWED</b> \$10,452.50 plus 25% of the excess over \$75,900	<b>TAX OWED</b> \$5,226.25 plus 25% of excess over \$37,950
<b>28%</b>	\$91,901 to \$191,650	\$131,201 to \$212,500	\$153,101 to \$233,350	\$76,551 to \$116,675
	<b>TAX OWED</b> \$18,713.75 plus 28% of the excess over \$91,900	<b>TAX OWED</b> \$27,052.50 plus 28% of the excess over \$131,200	<b>TAX OWED</b> \$29,752.50 plus 28% of the excess over \$153,100	<b>TAX OWED</b> \$14,876.25 plus 28% of excess over \$76,550
<b>33%</b>	\$191,651 to \$416,700	\$212,501 to \$416,700	\$233,351 to \$416,700	\$116,676 to \$208,350
	<b>TAX OWED</b> \$46,643.75 plus 33% of the excess over \$191,650	<b>TAX OWED</b> \$49,816.50 plus 33% of the excess over \$212,500	<b>TAX OWED</b> \$52,222.50 plus 33% of the excess over \$233,350	<b>TAX OWED</b> \$26,111.25 plus 33% of excess over \$116,675
<b>35%</b>	\$416,701 to \$418,400	\$416,701 to \$444,550	\$416,701 to \$470,700	\$208,351 to \$235,350
	<b>TAX OWED</b> \$120,910.25 plus 35% of the excess over \$416,700	<b>TAX OWED</b> \$117,202.50 plus 35% of the excess over \$416,700	<b>TAX OWED</b> \$112,728.00 plus 35% of the excess over \$416,700	<b>TAX OWED</b> \$56,364 plus 35% of excess over \$208,350
<b>39.6%</b>	\$418,401+	\$444,551+	\$470,701+	\$235,351+
	<b>TAX OWED</b> \$121,505.25 plus 39.6% of the excess over \$418,400	<b>TAX OWED</b> \$126,950 plus 39.6% of the excess over \$444,550	<b>TAX OWED</b> \$131,628.00 plus 39.6% of the excess over \$470,700	<b>TAX OWED</b> \$65,814 plus 39.6% of excess over \$235,350

# STANDARD DEDUCTION

## FILING STATUS

## STANDARD DEDUCTION

Single/Married Filing Separately	\$6,350
Married Filing Jointly	\$12,700
Head of Household	\$9,350

## PERSONAL EXEMPTION FOR 2017: \$4,050

Taxpayers can reduce 2017 taxable income by \$4,050 for each personal exemption claimed for themselves, their spouse and any dependents. This amount is unchanged from 2016. The personal exemption starts to decrease, however, as adjusted gross income (AGI) exceeds a certain threshold. The below chart breaks down the phase out ranges by filing status for 2017.

## PERSONAL EXEMPTION PHASE OUT

### FILING STATUS

### PHASE OUT BEGINS

### PHASE OUT COMPLETE

Single	\$261,500	\$384,000
Married Filing Jointly	\$313,800	\$436,300
Head of Household	\$287,650	\$410,150
Married Filing Separately	\$156,900	\$218,150

# ITEMIZED DEDUCTIONS & LIMITATIONS



Despite tax proposals swirling around Washington aimed at curbing or repealing certain itemized deductions, individual taxpayers must still adhere to the “Pease Rule,” which phases out the value of most itemized deductions once taxpayer’s adjusted gross income (AGI) reaches a certain amount, as outlined in the chart below. This results in a three percent reduction of the amount exceeding an AGI threshold, capped at 80 percent overall.

The Pease Rule applies to key itemized deductions, including home mortgage interest, state and local taxes and charitable contributions, but keep in mind that it does not encompass other significant deductions like investment interest, medical expenses and nonbusiness casualty and theft losses.

FILING STATUS	“PEASE RULE” INCOME THRESHOLD
Single	\$261,500
Married Filing Jointly	\$318,800
Head of Household	\$287,650
Married Filing Separately	\$156,900



## KEY ITEMIZED DEDUCTIONS

The Protecting Americans from Tax Hikes (PATH) Act of 2015 pushed back the expiration or permanently extended a number of popular tax deductions. Here are several ways individual taxpayers can lower their taxable income by deducting significant expenditures throughout the year.

### BEWARE AMT

Keep the AMT trigger in mind when using these or other deductions (see page 13 for more details).

## MEDICAL

- **Tax-Deductible Medical Expenses:** Individual taxpayers may still deduct qualified medical expenses that exceed 10 percent of their adjusted gross income (AGI) for the year. Any medical expense for which the taxpayer is reimbursed, by an employer or insurance policy, cannot be deducted. From January 1, 2013 to December 31, 2016, taxpayers age 65 or older and their spouses could deduct expenses that exceeded 7.5 percent of AGI. However, this exemption expired at the end of 2016; these individuals are now subject to the standard 10 percent AGI limit.
- **Deduction for Long-Term Care Insurance Premiums:** Another way the IRS favors saving for future medical costs is permitting the deduction of a portion of long-term care insurance premiums. Long-term care insurance premiums, subject to the age-based limitations below, are included as medical expenses, subject to the 10 percent AGI limitation. Deductibility limits also apply according to the taxpayer's age, as outlined in the below table.

AGE AT CLOSE OF TAX YEAR	DEDUCTION LIMITED TO
Age 40 or younger	\$410
Between 40 and 50	\$770
Between 50 and 60	\$1,530
Between 60 and 70	\$4,090
70 or older	\$5,110 (maximum deduction)

## STATE AND LOCAL INCOME TAX/SALES TAX

Individual taxpayers can elect to deduct state and local general sales taxes instead of state and local income taxes, but they cannot deduct both. Consult with a tax advisor to determine the most advantageous method. Examples of taxpayers who may benefit from deducting sales tax over state and local income taxes are retirees who do not have state or local taxes withheld from a paycheck or residents of states without an income tax.

## MORTGAGE INTEREST

For most taxpayers, the value of their homes is their most significant financial asset. The tax code as it currently stands provides individuals several options to wring tax savings from their residences.

- **Mortgage or home equity interest deduction:** The interest paid on mortgages up to \$1 million can be deducted in one year for original acquisition debt on a primary or secondary residence. This limit drops to \$500,000 for married taxpayers that file separately. Any mortgage interest over these thresholds is not deductible. For home equity debt, the annual limit is \$100,000. Interest expenses on second mortgages are deductible only if they're used for substantial improvements to an existing residence.
- **Mortgage points deduction:** The "points," or prepaid interest, paid on a home are deductible in full during the year in which the home is purchased or built. This deduction may also be spread out over the life of the loan.



# CHARITABLE DONATIONS

As with all deductions, substantiation is critically important for charitable donations. But scrutiny is higher than ever, thanks to a recent court case that disallowed tens of thousands of dollars in donations because receipts did not describe the items donated. The documentation requirements vary depending on the size and type of donation, as outlined in the below chart.

DONATION TYPE	DONATION AMOUNT <sup>1</sup>			
	UNDER \$250	\$250 to \$500	\$501 to \$5,000	OVER \$5,000
<b>Cash</b>	Bank record or written receipt from charity	Acknowledgment	Acknowledgment	Acknowledgment
<b>Publicly Traded Stock</b>	<ul style="list-style-type: none"> <li>Receipt</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> <li>Form 8283, Section A</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> <li>Form 8283, Section A</li> </ul>
<b>Nonpublicly Traded Stock</b>	<ul style="list-style-type: none"> <li>Receipt</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> <li>Form 8283, Section A</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> <li>Qualified appraisal (if FMV &gt; \$10,000)</li> <li>Declaration of appraiser and donee acknowledgment (Form 8283, Section B)</li> </ul>
<b>Artwork</b>	<ul style="list-style-type: none"> <li>Receipt</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> <li>Form 8283, Section A</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> <li>Qualified appraisal (must attach, if FMV &gt; \$20,000)</li> <li>Declaration of appraiser and donee acknowledgment (Form 8283, Section B)</li> </ul>
<b>Autos, Boats and Planes</b> (charity sells without significant use or material improvement)	<ul style="list-style-type: none"> <li>Receipt</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Form 1098-C or other acknowledgment</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Form 1098-C (attached to tax return)</li> <li>Written records</li> <li>Form 8283 Section A</li> </ul>	<ul style="list-style-type: none"> <li>Form 1098-C (attached to tax return)</li> <li>Written records</li> <li>Donee acknowledgment (Form 8283, Section B)</li> </ul>
<b>Autos, Boats and Planes</b> (significant use or material improvement by charity OR charity gives or sells at discounted price to needy individual in qualified transfer)	<ul style="list-style-type: none"> <li>Receipt</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Form 1098-C or other acknowledgment</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Form 1098-C (attached to tax return)</li> <li>Written records</li> <li>Form 8283 Section A</li> </ul>	<ul style="list-style-type: none"> <li>Form 1098-C (attached to tax return)</li> <li>Written records</li> <li>Declaration of appraiser and donee acknowledgment (Form 8283, Section B)</li> </ul>
<b>All Other Noncash Donations</b>	<ul style="list-style-type: none"> <li>Receipt</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> <li>Form 8282, Section A</li> </ul>	<ul style="list-style-type: none"> <li>Acknowledgment</li> <li>Written records</li> <li>Qualified appraisal [attach to return if deduction &gt;\$500,000 or any amount if a donation of a façade easement in a registered historic district (along with photographs and certain other information)]</li> <li>Declaration of appraiser and donee acknowledgment (Form 8283, Section B)</li> </ul>
<b>Payroll Deduction</b>	<ul style="list-style-type: none"> <li>Paystub, W-2 or other written record from employer</li> <li>Pledge card</li> </ul>	<ul style="list-style-type: none"> <li>Paystub, W-2 or other written record from employer</li> <li>Pledge card</li> </ul>	<ul style="list-style-type: none"> <li>Paystub, W-2 or other written record from employer</li> <li>Pledge card</li> </ul>	<ul style="list-style-type: none"> <li>Paystub, W-2 or other written record from employer</li> <li>Pledge card</li> </ul>
<b>Volunteer Out-of-Pocket Expenses</b>	Receipt, canceled check or other written records	<ul style="list-style-type: none"> <li>Receipt, canceled check or other written records</li> <li>Acknowledgment</li> </ul>	<ul style="list-style-type: none"> <li>Receipt, canceled check or other written records</li> <li>Acknowledgment</li> </ul>	<ul style="list-style-type: none"> <li>Receipt, canceled check or other written records</li> <li>Acknowledgment</li> </ul>

<sup>1</sup> Cash: Amount given in a single donation; Noncash – combined amount of all similar items of property donated to any charity during the year.

# CAPITAL GAINS & DIVIDENDS

The maximum tax rate for qualified (long-term) capital gains and dividends remains at 20 percent for 2017, and decreases to 15 percent and then zero percent depending on the individual's income tax bracket, as outlined in the chart below. Keep in mind that short-term gains and nonqualified dividends are taxed at ordinary income tax rates, which can be as high as 39.6 percent. The capital gains rate applies for purposes of regular tax and the alternative minimum tax.

INCOME TAX BRACKET	CAPITAL GAINS RATE
39.6%	20%
35%	15%
33%	15%
28%	15%
25%	15%
15%	0%
10%	0%

## STRATEGY: CAPITAL LOSSES TO OFFSET INCOME

Individual taxpayers may deduct up to \$3,000 of capital losses in excess of capital gains (\$1,500 for married filing separately). If no capital losses naturally occur during the tax year, individuals might consider cashing out stocks with built-in losses to counteract any liability from capital gains tax. Also, keep in mind that excess capital losses may be carried forward to future tax years indefinitely, subject to the above dollar limitations.

# MEDICARE SURTAXES

## NET INVESTMENT INCOME TAX

Regardless of taxable threshold, certain higher income individual taxpayers are also subject to an additional 3.8 percent net investment income (NII) tax. NII is applied to the lesser of (1) net investment income or (2) excess of modified adjusted gross income (AGI) over the applicable threshold amount. Modified AGI thresholds are \$250,000 (married filing jointly), \$125,000 (married filing separately) and \$200,000 (all other filers).



Examples of net investment income include interest, annuities, dividends, net capital gain, rents and passive business or trade activities. Strategies to mitigate net investment income are also outlined in the “Individual Tax Planning Strategies” section on page 21 of this guide, but here are some of the key ways taxpayers can keep income below the threshold to lessen NII exposure before the end of the year:

- Shift taxable investments to tax-free vehicles
- Offset the income with deductions
- Group similar categories of investment income activities

## ADDITIONAL MEDICARE TAX

Beyond income investment, high-income salaried or self-employed individuals must pay a 0.9 percent additional Medicare tax on any wages, compensation or self-employment income exceeding the threshold amount of \$250,000 (married filing jointly) or \$200,000 (single). For wage earners, this tax may be withheld by employers. Both self-employed individuals and wage earners must report this tax via filing of Form 8959.

# ALTERNATIVE MINIMUM TAX INFO & CONSIDERATIONS

The alternative minimum tax (AMT) was implemented to make sure that taxpayers pay a minimum amount of income tax, regardless of how many credits, deductions and exclusions they take. Nearly all tax actions can trigger the AMT, so taxpayers must always be aware of this potential when planning which deductions to apply, credits to take or other tactics to reduce tax liability.

An AMT rate of 26 percent applies to alternative minimum taxable income (AMTI) up to \$187,800 (\$93,900 for married filing separately). The 28 percent AMT rate applies to AMTI in excess of \$187,800 for all taxpayers. The AMT exemption amounts and phase out at certain thresholds for 2017 are broken out below by filing status:

FILING STATUS	EXEMPTION AMOUNT	THRESHOLD
Single	\$54,300	\$120,700
Married Filing Jointly	\$84,500	\$160,900
Head of Household	\$42,250	\$80,450
Married Filing Separately	\$24,100	

# KEY INDIVIDUAL TAX CREDITS



The IRS rewards individual taxpayers with tax credits for a variety of activities related to their family lives or improvements made to their homes. Tax credits can be refundable or nonrefundable. With nonrefundable tax credits, the resulting tax savings cannot exceed the amount of taxes owed. Refundable tax credits are considered as payments of tax made during the year, so if the total of these types of credits is greater than the tax owed, it results in a refund from the IRS. Below, we outline some of the most common credits individuals can utilize as a dollar-for-dollar reduction of their tax liability.

## FAMILY-RELATED CREDITS

- **Child Tax Credit:** This credit allows individuals to reduce their federal income tax bill for each qualifying child under age 17. The amount remains at \$1,000 per child for 2017. To the extent the child tax credit exceeds the taxpayer's income tax liability, the taxpayer is eligible for a refundable credit (the additional child tax credit) equal to 15 percent of earned income in excess of \$3,000, not to exceed the maximum child tax credit of \$1,000. The Child Tax Credit has an income phase out, so for every \$1,000 that modified adjusted gross income (MAGI) exceeds \$75,000 (single or head of household filers), \$110,000 (married filing jointly) or \$55,000 (married filing separately), the credit reduces by \$50.
- **Child and Dependent Care Credit:** Differing slightly from the Child Tax Credit, the Child and Dependent Care Credit covers expenses related to the care, well-being or protection of a child under the age of 13 at the end of the tax year or an individual physically or mentally incapable of self-care who resides with the taxpayer for more than half of the year. The credit equals \$1,050 per child or dependent, or 35 percent of expenses up to \$3,000. For filers with two or more children, 35 percent of expenses up to \$6,000 may be claimed. Higher income taxpayers will see this credit reduced to 20 percent instead of 35 percent. Keep in mind that this credit may not be claimed if a Flexible Spending Account provided by an employer is used for dependent care.

## ENERGY TAX CREDITS

- **Residential Alternative Energy Credit:** Recently extended through 2021, this credit covers up to 30 percent of the cost of eligible solar water heaters, solar electricity equipment or fuel cell plants. The maximum amount of credit for these installations tops out at \$500 per half kilowatt hour. It's important to note that the home served does not have to be the taxpayer's principal residence.
- **Nonbusiness Energy Credit:** As of the date of publication, the nonbusiness energy credit is expired; however, it is expected that this credit will be renewed retroactively for 2017. This credit allowed taxpayers to receive 10 percent of the cost of qualified energy efficient improvements to their principal residence located in the United States. This credit has a lifetime limitation of \$500, with a provision that only \$200 may be used for window installation. The eligible improvements include insulation, energy efficient exterior windows and doors, certain roofs, high efficiency heating and air conditioning systems and high efficiency water heaters and stoves that burn biomass fuel.

## EDUCATION TAX SAVINGS OPPORTUNITIES

For many families, education represents one of their most significant expenditures. Thankfully, the tax code offers several opportunities for individual taxpayers to recoup these expenses incurred by students of all ages through a variety of deductions and credits.

There are several things taxpayers should keep in mind when assessing eligibility for the below deductions and credits. First, educational institutions are legally required to file a Form 1098-T for each enrolled student to report qualified tuition payments and related expenses, so taxpayers should make sure they receive this information when gathering tax documents. Next, understand that if expenses are paid by the dependent or by a third party on behalf of the dependent, they are considered paid by the filing taxpayer. Finally, don't forget to consider the student's income tax return when taking credits as this may affect eligibility.

### AMERICAN OPPORTUNITY TAX CREDIT

- Broadened the previously enacted Hope Credit
- Made permanent through the December 2015 PATH Act
- Maximum credit is \$2,500 per student
  - 100% of the first \$2,000 of qualified tuition, fees and course materials
  - Plus 25% of the next \$2,000 paid
  - 40% of the credit is refundable (nonrefundable if claimed on a dependent return)
- Available for the first four years of post-secondary education
- Phases out for taxpayers with adjusted gross income in excess of \$80,000 (single filers) and \$160,000 (married filing jointly)
- Calculated and reported on Form 8863

## LIFETIME LEARNING CREDIT

- Maximum credit up to \$2,000 per return
  - Calculation is 20% of the first \$10,000 of expenses
- Phases out for taxpayers with adjusted gross income above \$65,000 (single filers) and \$131,000 (married filing jointly)
- Available for all years of higher education, including all post-secondary education and courses to acquire or improve job skills
- Eligible qualified expenses include tuition and fees required for enrollment and course-related books, supplies and equipment
- Calculated and reported on Form 8863

## STUDENT LOAN INTEREST DEDUCTION

- Maximum deduction is \$2,500
- No longer limited to interest paid during the first 60 months of repayment
- Deduction is phased out at modified adjusted gross income in excess of \$65,000 for single filers or \$135,000 for married filing jointly

## TEACHERS' CLASSROOM EXPENSE DEDUCTION

- Above-the-line deduction capped at \$250
- Allows primary and secondary education professionals to deduct qualified expenses
- This deduction will be adjusted for inflation annually

# HEALTH CARE CONSIDERATIONS FOR TAXES

Since the passage of the Patient Protection and Affordable Care Act (ACA) in 2014, health care and taxes have been inextricably linked. In addition to the Medicare surtaxes mentioned previously in this guide, the individual mandate also impacts an individual's tax situation. There are ways individuals can maximize tax-advantaged savings for medical expenses or earn credits or deductions for expenses or planning for future health needs.



## ACA IMPACT

The ACA makes qualified individuals and small business employers eligible to purchase private health insurance through state or federal exchanges. Certain individuals may qualify for premium tax credit in order to make the insurance affordable, a determination calculated via Form 1040.

The ACA assesses a penalty for individuals who do not have health insurance, which is paid on Form 1040 and imposed at the higher of either 2.5 percent of household income or the “per person penalty,” which is \$695 per adult and \$347.50 per child under age 18. The maximum per person penalty is \$2,085.

## HEALTH SAVINGS ACCOUNT (HSA)

An HSA is a tax-advantaged savings vehicle used to pay current or future medical expenses for a taxpayer, spouse and qualified dependents. Using an HSA provides three levels of tax benefits: contributions are tax-deductible (or pre-tax if made through payroll deduction), the interest earned on the account is tax-free and account owners can take tax-free withdrawals for qualified medical expenses.

Medical expenses funded through the HSA must not be reimbursed by insurance and cannot be deducted on Schedule A. An individual using an HSA must be covered by a high-deductible health plan (HDHP) and must not be covered by any other major medical insurance plan (with an exception for separate accident, disability, dental, vision or long-term care policies). The qualified HDHP must have a deductible of at least \$1,300 for self-coverage or \$2,600 for family coverage. An HSA limits the out-of-pocket expenses of the beneficiary to \$6,500 for self-coverage and \$13,100 for family coverage.

For 2017, the limits on HSA contributions by both employer and employee are \$3,400 (self-only) and \$6,750 (family plan). Taxpayers age 55 and older are eligible for a \$1,000 contribution to the plan.

## FLEXIBLE SPENDING ACCOUNT (FSA)

An FSA is another tax-advantaged savings vehicle to help individuals and families cover out-of-pocket medical costs. Generally speaking, money saved in an FSA must be spent by the end of the calendar year or at the end of the plan’s grace period, if applicable; otherwise, it must be forfeited. Taxpayers using an FSA should understand their plan’s terms and conditions and be sure to spend down funds within the allotted time to ensure no tax-free savings are lost.

# SAVING FOR RETIREMENT

For most individuals, saving for a secure and enjoyable retirement is a top financial priority. It is important to make sure those assets are set aside in a tax-advantaged vehicle to maximize financial benefits now and at the time of use in retirement. The IRS provides several ways for retirement savers to get the most bang for their buck, in accordance with a slate of rules and requirements, the most significant of which are outlined in this section.

The IRS caps the amounts that can be contributed to different types of plans during the tax year. Consider contributing as much as possible each year to stay on pace with retirement planning overall and enjoy as much benefit as possible from the favorable tax treatment of funds dedicated for this purpose.

## 2017 CONTRIBUTION & BENEFIT LIMITS

RETIREMENT PLAN BENEFITS	2017
SEP contribution	\$54,000
Elective deferrals under 401(k) and 403(b)	\$18,000
Catch up contributions for 401(k) and 403(b)	\$6,000
IRA deduction	\$5,500
IRA catch up contributions	\$1,000
SIMPLE contributions	\$12,500
SIMPLE catch up contributions	\$3,000
Maximum compensation for defined contribution plans	\$270,000

## TRADITIONAL IRA CONTRIBUTIONS

Individual taxpayers can make pre-tax IRA contributions for the 2017 tax year up until the April 2018 deadline for filing tax returns. These contributions may be deductible on federal income taxes, with no income limitation unless the taxpayers or their spouses are covered by an employer-sponsored retirement plan. In that case, the tax deduction for IRA contributions phases out once modified gross adjusted income (MAGI) reaches a certain level. For 2017, the phase outs are:

- MAGI between \$62,000 and \$72,000 (single filers)
- MAGI between \$99,000 and \$119,000 (married filing jointly)
- MAGI between \$186,000 and \$196,000 (married filing jointly if IRA contributor is not covered by an employer plan but spouse is)

## ROTH IRA CONTRIBUTIONS

Unlike the traditional IRA, a Roth IRA is funded with after tax money. This means contributions are not tax deductible, but savers won't be taxed upon withdrawal of funds. Eligibility to save with a Roth IRA depends on income. For 2017, the MAGI phase out ranges are:

- MAGI \$118,000 to \$133,000 for single and head of household filers
- MAGI \$186,000 to \$196,000 for married filing jointly
- MAGI \$0 to \$10,000 for married filing separately

## TRADITIONAL TO ROTH IRA CONVERSIONS

If an individual's income is too high to open and contribute to a Roth IRA, another possibility is converting a traditional IRA to a Roth. This mechanism pays no regard to the taxpayer's income or filing status, and the 10 percent tax on early distributions from the traditional IRA does not apply in this situation. Keep in mind, however, that the amount converted is taxable in the year of the conversion, so this may trigger a larger tax bill. Non-deductible basis comes into play in this situation.

To lessen the tax impact, individual taxpayers may convert a traditional IRA to a Roth IRA. In this case, the traditional IRA must be non-deductible. If so, a taxpayer can contribute to the traditional non-deductible IRA and then recharacterize the account to a Roth IRA. Timing is key to this transaction and there are several additional caveats that may apply, so individuals should consult with an accountant or financial advisor to make sure it is beneficial for their unique circumstances.

## SOCIAL SECURITY TAXABILITY

Recipients of Social Security must be aware of the "provisional income" thresholds that determine if and how much their benefits will be taxed. Provisional income is defined as modified adjusted gross income plus half of Social Security benefits. If this total is more than the base amount for an individual's filing status below, some of their benefits may be taxable at a rate of 50 or 85 percent.

- \$25,000: single, head of household, qualifying widow or widower with a dependent child or married filing separately and lived apart from spouse for the entire year
- \$32,000: married filing jointly
- \$0: married filing separately and lived with spouse at any time during the year

Income and transactions throughout the year can bump an individual into a different provisional income threshold, so it is important to monitor finances carefully, particularly as the end of the year approaches. In some cases, it may make sense to defer income until the start of a new year.

# TOP INDIVIDUAL TAX STRATEGIES

As individuals prepare for another tax filing season, here are some key tax-minimizing strategies to keep in mind.



## HARVEST CAPITAL LOSSES

Taxpayers may consider generating enough capital losses to offset their capital gains during the tax year, in addition to taking advantage of the \$3,000 capital loss permitted in the tax code. This can also help offset long-term capital gain from sale of rental property. Be sure to avoid a wash sale by waiting the full 30-day period to repurchase stock.

## DONATE APPRECIATED STOCK

Individuals who donate appreciated stock to a charity do not pay capital gains on the appreciation. They can also take the fair market value of the stock as a charitable deduction on their federal income tax return. Keep in mind that the donated stock must be held long-term. Avoid donating stock that would result in a capital loss.

## DEFER INCOME AND ACCELERATE DEDUCTIONS

Analyze the current year and look ahead to next year to discern if there are taxes that can be paid in advance, such as real estate or state and local taxes. Another tip is to group expenses into one year instead of spreading out over several, which can provide several medical and miscellaneous tax deductions. In both of these scenarios, beware the AMT trigger.

## DEFER INITIAL RMD OF IRA

Taxpayers over age 70½ who own an IRA must take an annual required minimum distribution (RMD) from the account. This annual RMD must begin the year the taxpayer turns 70½, but receipt of the distribution can be delayed until April 1 of the following year the taxpayer turned 70½. The subsequent RMD must be made by December 31.



## QUALIFIED CHARITABLE DISTRIBUTION FROM IRA

In addition to deferring the annual RMD, another way for taxpayers age 70½ or over to avoid a tax hit on this distribution is to make a direct transfer from the IRA to a charity. The yearly limit on such a transfer per person is \$100,000. The Qualified Charitable Deduction is not included in AGI, and is not deductible as a charitable contribution. There are several benefits to this maneuver, including the reduction of federal and state estate taxes since this transfer of wealth occurs during the taxpayer's lifetime; a potential reduction in the amount of Social Security benefits that are taxable; higher itemized deductions since thresholds are lower; and Medicare B and D premiums may be lowered as a result.

## MITIGATE NET INVESTMENT INCOME

As discussed earlier in this guide, certain higher income individual taxpayers are subject to a 3.8 percent net investment income (NII) tax. There are several ways taxpayers can mitigate NII, the most significant of which are outlined below. Individuals should consult their tax advisor for the full slate of options available to reduce NII exposure that apply to their unique financial situation.

- **Shift taxable investments to tax-free:** Investments that generate tax-exempt income are exempt from NII. Consider rebalancing your portfolio to add municipal bonds, stocks that pay out lower dividends and investments in sectors such as real estate, energy and natural resources that are protected from depreciation or depletion.
- **Convert passive income to active income:** The classification of income-generating activities, as either active or passive, and how they are grouped with other activities can impact whether they are subject to the NII. Taxpayers can increase the number of hours spent participating in an entity's affairs to convert passive income to active income that is not subject to NII tax. Your tax advisor can help identify the optimal way to increase material participation or group activities.
- **Shift or defer income with like-kind exchanges and installment sales:** Like-kind exchanges used in place of cash transactions can help taxpayers avoid triggering a taxable gain in business or rental real estate. Additionally, using the installment method to sell qualified assets can spread out gains, thereby preventing the NII trigger in a particular tax year. Be sure to contact your tax advisor before engaging in these transactions, as there are specialized rules that apply.
- **Place investible assets in a "wrapper vehicle":** Money put into a qualified retirement plan, like an IRA, 401(k) or other deferral plan reduces modified adjusted gross income, which in turn reduces NII exposure. Keep in mind that distributions from retirement plans are not subject to NII. Other wrappers include investments, like real estate, private loans or mortgages, or an LLP or LLC business entity. NII does not apply to collectibles or cash value life insurance, so consider those as an alternate option for asset placement.

# ESTATE PLANNING TAX CONSIDERATIONS

Estate planning allows individuals to develop a strategy to maintain financial security throughout their lifetime as well as ensure the intended transfer of property and assets at death. Planning for a financial legacy must be handled with care, however, to avoid tax penalties and to maximize available tax benefits.

**Estate Tax:** The maximum federal estate tax rate is 40 percent. For the 2017 tax year, it is only levied on estates of \$5.49 million or more. A portability provision allows the estate of a decedent who is survived by a spouse to make an election to transfer unused exemption to the surviving spouse. Each state has its own set of laws regarding estate/inheritance taxes.

**Gift Tax:** The annual exclusion for taxable gifts per taxpayer is \$14,000 per recipient and \$28,000 (if married) per recipient. Exclusions must be used by December 31 of each year, with no carryover. Keep in mind for 2018, the annual exclusion will rise to \$15,000 per recipient or \$30,000 if married.

## ESTATE & GIFT TAX REDUCTION STRATEGIES

In the simplest terms, taxpayers have three main options to reduce or eliminate federal estate and gift taxes.

- Take exemptions – use both if married
- Remove assets from estate
- Use life insurance to replace assets given to charity and/or pay remaining estate taxes

Upon the first death of spouse, the estate can elect to permit the surviving spouse to use the remaining estate tax exemption. This must be elected on the estate tax return even if no tax is due and does not apply to generation-skipping transfer tax exemption.

Taxpayers wishing to remove assets from their estates should keep in mind that appreciating assets are best to give away. Other gifting options beyond the annual exclusion is charitable giving, medical or educational expenses paid directly to the provider and contributions to 529 college savings plans. Gifts to grandchildren must be planned carefully so as to not trigger the generation-skipping transfer tax. When gifting interests in a business or family limited partnership, use valuation discounts to minimize tax impact. Gifting via a trust offers another way to achieve tax savings while preserving some control over the gifted assets.

# FOREIGN FINANCIAL ACCOUNT REPORTING

For individual taxpayers with foreign bank accounts or assets, the requirement to report these holdings to the IRS is clear and the penalties for failure to report them are significant. Taxpayers who do not directly own any share in a foreign business or a foreign bank account may still be required to include foreign reporting in their tax returns. For example, an executive or employee that has signature authority over a foreign bank account owned by her company would be responsible for reporting the account to the U.S. Treasury.

**Foreign accounts (FBAR):** Taxpayers that own or have signature authority over foreign accounts with balances in excess of \$10,000 must file Reports of Foreign Bank and Financial Accounts (FBAR) Form 114 electronically with the Treasury Department. Each account is measured at its maximum balance during the year. The \$10,000 figure is the aggregate of all accounts. The IRS defines authority as the ability to withdraw from the account. For the purposes of the FBAR, a financial account includes, but is not limited to, traditional bank accounts and other accounts held with a financial institution, as well as brokerage or commodities accounts, insurance and annuity policies with a cash value and mutual funds.

## DUE DATES & PENALTIES

Starting with tax year 2016, the due date for the FBAR was changed from June 30 to align with the April 15 tax deadline, which due to a weekend and D.C.-observed holiday falls on April 17 for 2018. Six month extensions are available. Penalties for failure to file can range from up to \$10,000 (non-willful) to up to the greater of \$100,000 or 50 percent of account balances, plus possible criminal penalties (willful).

## DUE DATES & PENALTIES

Form 8938 is also due by the federal income tax deadline, with a six-month extension available. Penalties include up to \$10,000 for failure to disclose and an additional \$10,000 for each 30 days of non-filing after receipt of IRS notice up to \$50,000 plus possible criminal penalties.

## Statement of Specified Foreign Financial Assets (Form 8938)

**Form 8938):** Taxpayers holding foreign assets totaling more than \$50,000 on the last day of the tax year or more than \$75,000 at any time during the year must report these holdings on Form 8938, which must be filed with their federal income tax return. These thresholds rise to \$100,000 (last day) or \$150,000 (any point during year) for married filing jointly taxpayers. Different thresholds apply to Americans living abroad. For the purposes of the form, specified foreign financial assets include the foreign accounts required for the FBAR (detailed above), as well as stock or securities (including debt) issued by a non-U.S. person, any ownership interest in a foreign entity or any financial instrument or financial contract issued by a non-U.S. person.

# BUSINESS OWNERS



Positioning a business for sustained profitability and success is a year-round endeavor, but as another tax year draws to a close, there are several opportunities to minimize the taxability of business income. The Protecting Americans from Tax Hikes (PATH) Act of December 2015 provided some certainty and consistency, permanently or significantly extending several key tax provisions that benefit businesses. For a full assessment of the impact of the following strategies, deductions and credits, consult your CPA or business advisor.

## ENTITY TYPE IMPACT & CORPORATE TAX RATES

The structure of a business determines how it is taxed, whether it is a pass-through entity that sees income, deductions, credits and losses flow through to the owners' individual tax returns or an entity taxed at the corporate rate.

### CORPORATE TAX RATE

For C corporations (other than a personal service corporation), the 2017 federal income tax rates are broken out below. **NOTE:** *Qualified personal service corporations pay a flat 35 percent tax.*

Corporate earnings are potentially subject to another layer of tax if paid out in dividends to shareholders. Keep in mind that qualified dividends are taxed at a rate of 15 or 20 percent depending on taxable income levels.

IF YOUR TAXABLE INCOME IS BETWEEN	YOUR TAX IS	OF THE AMOUNT OVER
\$0 - 50,000	0 + 15%	\$0
\$50,001 - 75,000	7,500 + 25%	\$50,000
\$75,001 - 100,000	13,750 + 34%	\$75,000
\$100,001 - 335,000	22,250 + 39%	\$100,000
\$335,001 - 10,000,000	113,900 + 34%	\$335,000
\$10,000,001 - 15,000,000	3,400,000 + 35%	\$10,000,000
\$15,000,001 - 18,333,333	5,150,000 + 38%	\$15,000,000
\$18,333,334 or more	A flat 35%	-----

### WATCH FOR AMT

While small corporations are generally exempt, larger corporations can trigger the Alternative Minimum Tax (AMT). In eligible situations, AMT is applied to corporations at a 20 percent rate, with the first \$40,000 of income excluded. The corporate AMT is phased out when AMT-eligible income falls between \$150,000 and \$310,000.



# TAX CONSIDERATION FOR PARTNERSHIPS

## PREPARE FOR NEW PARTNERSHIP AUDIT RULES

The federal Bipartisan Budget Act of 2015 significantly alters partnership audit rules by transferring liability for payment of audit adjustment assessments from the partners to the partnership itself.

To prepare for compliance with the new rules, which take effect in 2018, partnerships will need to designate a partnership representative, review ownership structure and amend partnership and operating agreements. In addition, partnerships may want to obtain indemnification agreements from partners leaving the partnership in order to maintain the ability to recover the portion of any tax paid at the entity level upon audit for years in which those individuals were partners. There is an annual election to opt out based on size and ownership structure.

## TREAT PARTNERS AS EMPLOYEES

Treating partners as employees delivers several benefits to partnerships or limited liability companies (LLCs), such as the simpler option of reporting wages on Form W-2 versus Schedule K-1. While recent developments have clouded the viability of this option, there are still ways to take advantage of it. Partnerships or LLCs that wish to position partners as employees should consider using a tiered structure in which employees are partners in a holding company instead of the parent company that is the real employer. Be sure to consult with your tax advisor regarding the structural issues and regulatory obstacles to overcome and achieve the desired tax position.

## PARTNER SELF-EMPLOYMENT TAX

Generally speaking, self-employed individuals are taxed on their net earnings. Self-employment tax also applies to the wages paid by a corporation to shareholder-employees. Less clear is the treatment of members of limited liability partnerships (LLPs) and LLCs thanks to recent tax court decisions and proposed regulatory changes. To accommodate the aggressive approach taken by the IRS regarding the applicability of self-employment tax to LLC or LLP members, companies may want to consider altering their operating agreements or governing rules to section off certain amounts of income as return of capital instead of compensation.

# ADDITIONAL FILINGS & DEADLINES FOR BUSINESS TAXPAYERS

In addition to the various dates for individual and business tax returns, which were recapped earlier this guide and are shared again below, there are also some other key tax-related dates that business owners should keep on their radars. Please note that for C Corporations with fiscal years ending on June 30 the due date change is deferred until December 31, 2025, so until then the due date remains the 15th day of the third month after the end of the fiscal year.

BUSINESS TAX TYPE	DUE DATE(s) (for calendar year entities)
Forms 1094-C and 1095-C	January 31, 2018 to employees / February 28, 2018 to IRS if filing hard copy / April 2, 2018 to IRS if e-filing
Form 1099	January 31, 2018 to employees / February 28, 2018 to IRS if filing hard copy / April 2, 2018 to IRS if e-filing
Forms W-2, W-3 and 1099-MISC (Box 7 – Nonemployee compensation)	January 31, 2018 to employees, Social Security Administration and IRS if filing hard copy or e-filing
Partnerships (Form 1065) & S Corporations (Form 1120S)	March 15, 2018
Individuals (Form 1040), C Corporations (Form 1120) and Trusts and Estates (Form 1041)	April 17, 2018
Tax-exempt nonprofit organizations (Form 990)	May 15, 2018
Employee Benefit Plans (Form 5500)	July 31, 2018
Filing extensions for partnerships & S Corporations	September 17, 2018
Filing extension for trust and estates	October 1, 2018
Filing extensions for individuals, C Corporations and Employee Benefit Plans	October 15, 2018
Filing extension for tax-exempt nonprofit organizations	November 15, 2018

# KEY INFORMATIONAL **TAX RETURNS**

Some of the tax forms listed prior are informational returns required by the IRS. While there is no tax payment associated with these filings, there are financial penalties and consequences for late submission or failure to file. Information is provided below regarding the most common types of informational returns.

## **FILING DEADLINE FOR FORMS W-2 AND 1099**

The IRS has fairly strict reporting requirements for certain payments made in the course of business or trade. The most common Form 1099s are the Form 1099-INT/1099-DIV and the Form 1099-MISC. A 1099-INT or 1099-DIV is required if you paid \$10 or more of interest or dividends during the calendar year. Form 1099-MISC is required for any unincorporated vendor to whom you paid \$600 or more for services or rent during the calendar year. All Forms 1099, with the exception of 1099-MISC, for tax year 2017 are due to the recipient by January 31, 2018, and the IRS by February 28, 2018 (hard copy) or April 2, 2018 (e-file). Form 1099-MISC is due to the IRS on January 31, 2018.

Employers must also report wages paid to employees and the taxes withheld from them via Form W-2. For tax year 2017, Forms W-2 are due to the recipient and the Social Security Administration by January 31, 2018.

## **1094 & 1095 COMPLIANCE**

These forms are both required under the Affordable Care Act (ACA). 1094-C proves to the IRS that applicable large employers fulfilled their requirements under the ACA's Employer Shared Responsibility Mandate. Employers must provide 1095-C to their employees to help them demonstrate that they met the minimum essential coverage mandate under the ACA. 1095-Cs must be sent to employees by January 31, 2018, and then employers must file their 1094-Cs and copies of all 1095-Cs to the IRS by February 28, 2018 (hard copy) or April 2, 2018 (e-file).

# **ASSET PURCHASES**

## **DE MINIMIS SAFE HARBOR ELECTION**

Businesses that acquire, produce or improve tangible property are likely affected by IRS regulations pertaining to capitalization and deductions for tangible assets, commonly referred to as the tangible property or repair regulations. Effective since the 2014 tax year, the IRS issued additional guidance to expand the dollar amount eligible for this election starting in 2016.

Under this safe harbor election, businesses may expense a certain dollar amount of asset purchases under a specified threshold. For companies with certified audited financial statements, the de minimis threshold can be up to \$5,000. For companies without such statements, the threshold is \$2,500. This write-off amount must conform with the entity's fixed asset capitalization policy and the election must be filed annually with the tax return.

## OTHER SAFE HARBOR PROVISIONS/ELECTIONS

In addition to tangible property investments, businesses may also elect safe harbor status for the remodel or refresh of a building or facility. This election may require filing for a change in accounting method, and its limitations and restrictions may make this undesirable but it should at least be considered for taxpayers operating a retail establishment or restaurant. Up to 25 percent of qualified remodel-refresh costs may be capitalized, along with 75 percent currently deductible as repairs and maintenance, provided the business has applicable financial statements. Auto or other motor vehicle dealers and gas stations are excluded from this election.

Smaller business taxpayers with \$10 million or less in gross receipts have the additional option to elect safe harbor for their buildings. This option allows improvements to be expensed if the total amount of repairs, maintenance and improvements performed on the building during the year does not exceed the lesser of \$10,000 or two percent of the unadjusted basis of the building.

## BONUS DEPRECIATION

In recent years, bonus depreciation was not passed until the tax year almost expired, making it difficult for business owners to plan for capital expenditures. The PATH Act of 2015 extended bonus depreciation through 2019, lowered its recovery period threshold and created a new category for cost recovery. Business owners may now be eligible for greater tax deductions related to improvements made to commercial or rental properties. Despite the many benefits of bonus depreciation, this tool only accelerates deductions. As the percentage of depreciation decreases and with its status unclear after 2019, future taxable income could be higher as a result of taking bonus in current and prior years.

### **Below is the depreciation schedule implemented under the PATH Act:**

- 50% bonus depreciation extended for property placed in service in 2015, 2016 and 2017
- 40% bonus depreciation for property placed in service in 2018
- 30% bonus depreciation for property placed in service in 2019
- Without additional legislation, bonus depreciation expires after 2019

Previously, the cost of buildings and various improvements could only be recovered over 39 years. This prevented companies from receiving bonus depreciation on new properties. The PATH Act made permanent a lower, 15-year depreciation threshold, for qualified leasehold improvements made to the interior portion of non-residential real property. The PATH Act also created a new recovery category: Qualified Improvement Property (QIP). This new category allows companies greater flexibility in accelerating the cost recovery for non-residential building improvements.

## SECTION 179 EXPENSING

Popular with small businesses, a Section 179 election reduces dollar for dollar the amount of qualifying property placed in service exceeding the investment limitation. The PATH Act permanently extended the \$500,000 annual cap on the Section 179 deduction and the \$2 million investment limitation. Starting in 2016, both the annual cap and investment limitation are indexed for inflation, so for 2017 the cap is \$510,000 and the investment limitation is \$2,030,000. When electing Section 179, watch for ordinary income recapture versus capital gain on a sale.

Certain qualified real property is eligible for Section 179 expensing, including qualified leasehold improvements, retail improvements or restaurant property. Portable heating and air conditioning units, computer software purchased off the shelf, and new and used vehicles, machinery or equipment are also eligible for Section 179 expensing.

## COST SEGREGATION STUDIES

A cost segregation study allows companies that recently built, renovated, expanded or purchased a building to identify, segregate and reclassify building-related costs that are currently classified as real property to shorter, depreciable lives. This tax savings strategy offers several benefits for business owners to consider. A cost segregation study identifies the portion of a building's cost that can be considered "personal property" or a "land improvement," and depreciate it over a shorter period of time than the standard depreciation life of 39 years for a commercial building or 27 ½ years for a residential building. This may afford business owners several benefits, including greater tax deductions, accelerated depreciation and increased cash flow.



# KEY BUSINESS TAX CREDITS & DEDUCTIONS

In the course of regular business activities and investments, business owners may find several opportunities to recoup tax savings. Many of these deductions and credits were significantly or permanently extended as part of the December 2015 PATH Act, which gives business owners greater flexibility in timing asset purchases or capital investments as part of strategic, long-term tax planning. Below is a roundup of some of the most significant tax savings opportunities for businesses. Consult an accountant or business advisor to discover if these or other options are viable for your unique situation.

## DOMESTIC PRODUCTION ACTIVITIES DEDUCTION

A deduction of nine percent of qualified production activity income is available to companies not just in the manufacturing industry, but also construction, engineering and architecture. Examples of eligible qualified domestic production activities occurring in the U.S. include:

- Manufacturing
- Building or renovating residential and commercial properties
- Software development (including video games)
- Sale, lease or license of domestically manufactured or produced items (including motion pictures)
- Engineering or architecture services related to construction projects

Keep in mind the deduction cannot exceed 50 percent of W-2 wages allocable to domestic production gross receipts, so consider making year-end bonus payments to company owners to increase the wage threshold if possible.

## RESEARCH & DEVELOPMENT TAX CREDIT

For more than three decades, the R&D credit was temporary, being renewed (often retroactively) or extended for another year by Congress. The PATH Act permanently established the R&D credit as a tax planning option for eligible businesses and removed limitations that previously excluded small or midsized companies from using this credit. There is now an expanded opportunity for all businesses to earn a tax credit for new product development, product improvements and process improvements they are likely already undertaking.

The PATH Act removed the AMT limitation for small businesses, who are often subject to AMT. Now small businesses (defined as having an average of less than \$50 million in gross receipts over the prior three years) may use the R&D credit to offset AMT liabilities. Start-up companies (defined as businesses with less than \$5 million in gross receipts and no more than five years of gross receipts) can now apply the credit against the Federal Insurance Contributions Act (FICA) portion of their payroll taxes up to \$250,000.

To be eligible for the R&D credit, qualifying activities must:

- Use technological processes to make tangible products or improvements to the product
- Develop new or improved software applications for internal or external purposes
- Develop new or improved processes for producing goods

## R&D CREDIT UPDATE:

Start-up companies can now apply the credit against the Federal Insurance Contributions Act (FICA) portion of their payroll taxes up to \$250,000.

## CREDITS AND DEDUCTIONS RELEVANT TO SMALL BUSINESSES

**Work opportunity:** To encourage workplace diversity and facilitate access to employment for workers, the IRS offers the Work Opportunity Tax Credit for businesses that hire individuals from certain target groups. This credit generally equals up to 40 percent of up to \$6,000 of first-year wages paid (per employee).

**FICA tips:** Most relevant for restaurants and food/beverage establishments, companies can deduct the amount of Federal Insurance Contribution Act (FICA) taxes paid on employee tips that exceeds federal minimum wage standards.

**Pension plan startup costs:** Small businesses that set up retirement plans, whether it's a traditional pension, a 401(k) or 403(b), a profit-sharing plan or a SEP or SIMPLE IRA, for their employees may be eligible for a \$500 credit to offset the costs of starting up the plan.

**Commercial solar energy projects:** Recently extended until 2019, the Business Energy Investment Tax Credit (ITC) allows companies to recoup 30 percent of the cost of installing eligible solar technologies, including solar water heat systems, solar space heat, solar thermal electric, solar thermal process heat and photovoltaics. The ITC is not capped by dollar value, so regardless of the cost of a project, companies can take the 30 percent credit.

# BUSINESS TAX PLANNING OPPORTUNITIES



Business owners work throughout the year to maximize profitability and lower tax impact, but there are some key ways to reduce business tax impact before the end of the year. Be sure to discuss these opportunities with your advisor to determine eligibility and applicability to unique circumstances.

**Accounting method impact:** Whether a business uses the cash or accrual tax accounting method, there are opportunities to time payments or income for maximum tax benefit. Cash-method taxpayers might consider deferring income by postponing billing invoices so that payments are not submitted until the start of the new year. Accrual-method taxpayers could defer income by holding off on delivering products or carrying out services until the start of the next tax year.

**Timing of bonus payments:** For businesses that intend to pay employee bonuses in 2017, consider the timing of the payments as it relates to their tax accounting method. Cash-method businesses should consider making the bonus payments before the end of the year in order to deduct the expense on 2017 tax returns. Accrual-method businesses have more flexibility, since they can still take a 2017 deduction for bonuses paid within 2.5 months of year-end, as long as the liability for the bonuses is fixed and determinable by December 31. This additional flexibility, however, is not available for any bonuses accrued for S Corporation shareholders, LLC members or partners. In addition, accruals by C Corporations for bonuses to shareholders with a greater than 50 percent interest are also not deductible.

**Start-up expenditures:** Taxpayers who kicked off a new business venture this year may be able to deduct up to \$5,000 in start-up expenses like travel costs related to business set-up or advertising ahead of a grand opening.

**Retirement plan contributions:** In addition to an owner's personal retirement contributions, contributions made by the business on behalf of employees may also be tax-deductible, subject to yearly contribution limits.

**Reasonable shareholder/employee compensation:** Generally speaking, employee salaries and bonuses are deductible corporate expenses. In the case of S corporations, however, it is more advantageous to draw only “reasonable” compensation from the company. Shareholder/employee compensation should be reviewed to ensure it is reasonable for the services performed and not considered overpayment. Keep in mind additional, nonwage corporate earning distributions are exempt from Social Security, Medicare and self-employment taxes.

**Business expense reimbursements:** Businesses that reimburse employees for mileage, travel or other expenses could save on payroll taxes by using the accountable plan rules for reimbursement. Under this plan, employee reimbursement requests are accompanied by detailed accounting of business expenses. Employees are required to return any excessive or overpayments to the employer within a reasonable period. According to IRS rules, reimbursements made under the accounting plan are not counted in employee wages.

**Bad debts deduction:** If a business extends credit to customers, bad debts are another potential deduction opportunity. Businesses can deduct any debt that is wholly or partially worthless, assuming the amount was already included in income. Before the end of the year, review accounts receivable reports to find any uncollectible debts that may be written off.

**Scrap old or damage physical inventory:** Businesses with damaged, old or unsellable physical inventory can scrap these items and claim a tax deduction for doing so. The IRS permits write-offs of items lost to disaster or theft, or inventory that just won’t sell. Scrutiny is high for these types of claims, so make sure records (including before and after photos) are retained to support any deductions. Under IRS rules, businesses can use lower of either the cost method or “lower of cost or market” method to determine the deduction value of inventory.

**Invest in new equipment:** By acquiring new or updated business equipment before the end of the tax year, business owners may be eligible for deductions and depreciation benefits. This deductibility varies depending on the purpose of the equipment and business type, so be sure to discuss with a professional advisor before making a large equipment purchase.

**Prepay certain fees and expenses:** Businesses that use the cash method for tax accounting should consider prepaying IRS-permitted expenses for the next year, such as insurance payments or professional services fees. This opportunity applies only in cases where the economic benefit of prepayment does not extend past the end of the tax year following the year the prepayment was made. This also provides a great planning opportunity for accrual basis taxpayers who have made, or are considering making, a change in accounting method for their treatment of prepaid items. By requesting an accounting method change with the IRS, accrual method taxpayers are permitted to deduct certain prepaid items in a similar fashion to cash method taxpayers.

# LET'S TALK.



Staying in touch with your RKL advisor throughout the year and seizing opportunities for savings as they arise makes year-end planning smoother and puts you in a stronger position to achieve your financial goals.

Questions about any of the topics presented in this guide? Want to take advantage of any of these tax-savings opportunities before year-end? Contact your RKL advisor, one of our local offices or visit us online at [rklcpa.com](http://rklcpa.com).

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