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CERTIFIED PUBLIC ACCOUNTANTS

November 3, 2016 – Year-End Tax Planning for 2016

As the tax law grows more complex, year-end becomes an increasingly important time to take inventory of your tax situation and, then, take action. Income and deductions for the entire year usually become more clear as we move ever closer to the end of the year. The final months of the year provide a valuable "last chance" to change the course of your tax year before it closes for good. Launching some traditional year-end techniques designed to accelerate deductions and delay income (or vice versa, depending upon prospects for next year) may help to maximize your tax savings and minimize your tax liability for 2016.

Year-end has also become a time when there is an increasing need to take inventory of what's changed within the tax law itself since the beginning of the year. Opportunities and pitfalls within these recent changes – as they impact each taxpayer's unique situation—should not be overlooked. This is particularly the case during year-end 2016. Last year, Congress passed a far-reaching tax bill: the *Protecting Americans from Tax Hikes Act of 2015* (PATH Act). The impact of the PATH Act was not limited to 2015. Many of its provisions could play an important role in your year-end tax planning for 2016. We'll discuss the PATH Act in more detail later.

Data, including 2015 return

Year-end planning should start with data collection and a review of your prior year returns. This review includes losses or other carryovers, estimated tax installments, and items that were unusual. Conversations about next year should include review of any plans for significant purchases or dispositions, as well as any possible life cycle plans. Alternative minimum tax (AMT) liability also needs to be explored as well as potential liability for the net investment income (NII) tax and the Additional Medicare Tax. Do not assume, for example, that because last year, you were not liable for the NII tax you will not be liable this year. Every individual's situation is unique. There is no "one size fits all" when it comes to tax planning.

Investments

Taxpayers holding investments toward the end of the year, whether in the form of securities, real estate, collectibles, or other assets, may have an opportunity to reduce their overall tax liability by some strategic buying and selling (or like-kind exchanging). Balancing the existing tax rates within those considerations is part of that challenge. The ordinary income tax rates, the capital gain rates, the NII tax rate, and the AMT, all play a role.

Income caps on benefits

Monitoring adjusted gross income (AGI) at year-end may also realize a number of tax benefits. Often tax savings can be achieved by lowering income in one year at the expense of recognizing a bit more income in the other year: in this case, either 2016 or 2017. Some of the tax benefits that may be phased-out depending upon the taxpayer's AGI level include:

- itemized deductions;

- personal exemptions;
- education savings bond interest exclusion;
- maximum child's income on parent's return (Form 8814);
- medical savings account adjustments;
- education credits; student loan interest deduction;
- adoption credits;
- maximum Roth IRA contributions; and
- maximum IRA contributions for individuals.

Personal changes

Changes in your personal and financial circumstances—marriage, divorce, a newborn, a change in employment, a new business venture, investment successes and downturns—should all be noted for consideration as part of an overall year-end tax plan. A new child, for example, may not only entitle the proud parents to a dependency exemption, but also a child tax credit and possible child care credit as well. As with any "life-cycle" change, your tax return for this year may look entirely different from what it looked like for 2015. Accounting for that difference now, before year-end 2016 closes, should be an integral part of your year-end planning.

New developments

Recent tax law changes—made by legislation, the Treasury Department and IRS, or the courts—should be integrated into specific 2016 year-end plans. A strategy-focused review of 2016 includes, among other developments:

- the PATH Act, which permanently extended many provisions but temporarily extended others only through 2016;
- growing IRS interest in the liabilities and responsibilities of participants in the "sharing economy;"
- a clarified definition of marriage as applied by new IRS guidance;
- changing responsibilities of individuals and employers under revised rules within the *Affordable Care Act;*
- new de minimis and remodel-refresh safe harbors within the ground-breaking and far-reaching "repair regulations" that impact virtually all businesses;
- new opportunities for small businesses to gain immediate writeoffs for equipment purchases through an expanded "Section 179 deduction;" and
- the impact of recent Treasury Department regulations on retirement planning, including those affecting late rollover relief, changes to deferred compensation plans, partial annuity payment options from qualified plans, and more.

PATH Act "extenders"

The PATH Act plays a particularly prominent role in year-end tax planning for 2016. Enacted immediately before the start of 2016, the PATH Act permanently extended many tax incentives that were previously temporary, removing a lot of uncertainty.

Not all of these "extenders" provisions were extended beyond 2016, however; and some were modified in the process. Others were extended for up to five years, deferring to "tax reform" a more lasting solution.

Here's a list of some of the major changes made by the PATH Act, especially focused on how they impact year-end transactions: For individual taxpayers, these include (among others) the:

- American Opportunity Tax Credit (made permanent);
- Educators' $250 "classroom" expense deduction (made permanent);
- State and local sales tax deduction election, in lieu of state income taxes (made permanent);
- Exclusion for direct charitable donation of IRA funds of up to $100,000 for qualified individuals (made permanent);
- Code Sec. 25C residential energy property credit (generally through 2016 only but with special rules for some solar property);
- Fuel cell motor vehicle credit (through 2016 only);
- Mortgage insurance premium deduction (through 2016 only); and
- Tuition and fees "above-the-line" deduction (through 2016 only).

For businesses, the PATH Act extender provisions include (among others):

- Code Section 179 expensing (made permanent);
- Bonus depreciation (five years, with phase-out);
- Work Opportunity Credit (through 2019);
- 100-percent gain exclusion on qualified small business stock (made permanent);
- Reduced, five-year recognition period for S corporation built-in gains tax (made permanent);
- 15-year straight-line cost recovery for qualified leasehold improvements, restaurant property and retail improvements (made permanent);
- Film and TV production expense elections (through 2016 only);
- Energy efficient commercial buildings deductions (through 2016 only);
- Mine safety equipment expense elections (through 2016 only); and
- Additional depreciation for biofuel plant property (through 2016 only).

Timing

Once December 31, 2016 has come and gone, there is very little that you can do to lower your tax liabilities for 2016. True, there are some retirement plan contributions if made early in 2017 that may offset 2016 liabilities; and some accounting-oriented elections may be made when filing a 2016 return. But those opportunities are limited. There is much greater potential savings on most fronts if action is taken by December 31, 2016.

Knowing the ins and outs of timing rules become critical to some year-end strategies. For example, it may not be necessary to pay cash upfront in order to attain a deduction or other tax benefit for 2016. Taxpayers can write a check or charge an item by credit card and treat these actions as payments. It also may not matter when the recipient receives a check mailed by the payor, when a bank honors the check, or when the taxpayer pays the credit card bill, as long as done or delivered "in due course." However, in some business situations, a write-off is not only dependent upon purchasing a particular asset but also in having the asset "placed in service." For more details about these business rules, please contact our office.

Accelerate or delay? Year-end tax planning, especially if done "at the eleventh hour," requires some understanding of the timing rules: when income becomes taxable and when it may be deferred; and, likewise, when a deduction or credit is realized and when it may be deferred into next year or beyond.

Those taxpayers, individuals and small businesses alike, using the cash method basis of accounting can defer or accelerate income using a variety of strategies. These may include:

For income acceleration or deferral:

- sell or hold appreciated assets;

- sell outstanding installment contracts;
- redeem U.S. Savings Bonds or hold them;
- accelerate or delay debt forgiveness income; and
- seek or avoid mandatory like-kind exchange treatment.

For deduction acceleration or deferral: A cash basis taxpayer generally deducts an expense in the year it is paid, although prepayment of an expense generally would not accelerate a deduction. There are exceptions, including, among others, those made in connection with:

- up-front package payment;
- some tuition prepayments; and
- fourth quarter estimated state taxes.

New Administration

Whenever a new Administration and new members of Congress move into Washington, it is clear that changes will follow. How these changes will impact upon your long-term tax situation remains to be developed. The change in Administration and an eventual groundswell for tax reform make the future more difficult to read than in prior years. Nevertheless, in looking toward the future, you should not lose sight of the tax dollars that may be saved immediately through 2016 year-end strategies in response to these changes.

Please feel free to call our offices if you have any questions about how year-end tax planning might help you maximize your tax savings. Our tax laws operate largely within the confines of "the taxable year." Once 2016 is over, tax savings that are specific to 2016 may be gone forever.