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Balance sheet

Year-End Tax Planning Under The New Administration

By Ann E. Woolum, CPA/ABV, CBA

As the end of the year approaches, it is a good time to think of planning moves that will help lower your tax bill for this year and possibly the next. Factors that compound the planning challenge this year include Congress' all too familiar failure to act on a number of important tax breaks that will expire at the end of 2016, the far-reaching Affordable Care Act and whatever changes the new Congress and Administration may make to the Tax Code in 2017.

Some of the expiring tax breaks will likely be extended, but perhaps not all, and as in the past, Congress may not decide the fate of these tax breaks until the very end of 2016 or later. For individuals, some of these breaks include the treatment of mortgage insurance premiums as deductible qualified residence interest, the 7.5% of adjusted gross income floor beneath medical expense deductions for taxpayers age 65 or older, and the deduction for qualified tuition and related expenses. There is also a host of expiring energy provisions including the residential energy property credit.

Individual Tax Strategies:

- Keep in mind that effective tax planning requires considering both this year and next year—at a minimum. If you believe the President-elect's promise that a major tax bill lowering taxes in the U.S. will be implemented, give consideration to year-end tax moves to make the most of what might be windfall savings next year. The upshot of the tax-reduction changes would be reduced taxes for middle and upper income taxpayers. The standard year-end tax-savings wisdom always has been to defer income, where possible, into the upcoming year. Currently, this standard approach would make even more sense and here are some ways to defer income until 2017:
- An employee with no ownership in the employer who may be eligible for a bonus may request that the employer delay payment of the bonus until early in 2017.
- Income that a cash basis taxpayer earns by providing services is not taxed until the customer pays and the taxpayer receives the cash. If the taxpayer waits to send the bill until very late in the year or next year so that no payment can be received in 2016, the income will be deferred until 2017.
- A taxpayer that is considering a traditional IRA to Roth IRA conversion which generally is subject to tax may want to defer the conversion from 2016 to 2017 if the tax will be lower next year.

If the Affordable Care Act (Obamacare) is repealed, the 3.8% surtax on investment income would also be repealed as well as the penalties for failure to have health insurance. The 3.8% surtax potentially applies if your adjusted gross income exceeds $250,000 for joint returns, and $200,000 for unmarried taxpayers. Managing your adjusted gross income can help you avoid (or reduce the impact of) the 3.8% net investment income tax. For example, if you are planning the sale of property that would generate a large investment gain, consider postponing the sale until 2017 or, if possible, structure an installment sale.

If you turned age 70½ in 2016, you can delay the first required minimum distribution (RMD) to 2017, but if you do, you will have to take a double distribution in 2017, the amount required for 2016 plus the amount required for 2017. This could be beneficial to take both distributions in 2017 if you will be in a substantially lower bracket next year, for example, because you plan to retire late this year. Although lower tax rates are expected for 2017, think twice before delaying 2016 distributions to 2017, bunching income into 2017 might push you into a higher tax bracket or have a detrimental impact on various income tax deductions that are reduced at higher income levels. In addition, failure to take a required withdrawal can result in a penalty of 50% of the amount of the RMD not withdrawn.

An investment strategy that can help lower your tax bill is to review your securities portfolio for any losers that can be sold before year-end to offset gains you have already recognized this year or to get you to the $3,000 net capital loss that is deductible each year. Do not worry if your net loss for the year exceeds $3,000, because the excess carries over indefinitely to future tax years. Be mindful, however, of the wash sale rule when you dump losers—your loss is deferred if you purchase substantially identical securities within the period beginning 30 days before and ending 30 days after the sale.

The new administration has proposed to more than double the standard deduction to $15,000 for single individuals and $30,000 for joint filers while eliminating the deduction for personal exemptions. There is also a proposal to limit the total amount of itemized deductions. Therefore, taxpayers may want to consider accelerating itemized deductions. Consider the following items and using a credit card to prepay expenses that can generate deductions for the 2016 year.

- State and local income taxes are one of the easiest deductions to manipulate. Mailing your fourth quarter estimate that is due in January 2017 in late December 2016 lets you claim the deduction in 2016.
- You can also accelerate charitable contributions planned for 2017 into 2016. Try to make your contribution with appreciated stock that you have owned for over a year. This way, you deduct the full value and never pay capital gains tax on the appreciation. In addition, if you own an IRA and are age 70½ or older, and are thinking of making a charitable gift, consider arranging for the gift to be made directly by the IRA.
- Beginning in 2013, the threshold for deducting medical expenses rose from a maximum 7.5 percent of adjusted gross income to 10 percent unless you are age 65 or older (the age 65 exception applies through December 31, 2016). When thinking about medical expenses that may be deductible, do not forget to consider health insurance premiums (if not deducted from your wages pretax), long-term care insurance premiums (age-based limits apply), medical and dental services and prescription drugs that are not reimbursable by insurance or paid through a tax-advantaged account, and miles driven for health care purposes.
- If you make your January 2017 mortgage payment on your residence before the end of 2016, you can deduct the interest portion in 2016. However, unless you do the same thing in 2017, you will deduct only eleven months of interest in 2017.
- The alternative minimum tax (AMT) can throw a monkey wrench into your bunching of itemized deductions. State and local taxes including real estate taxes, some medicals, and most miscellaneous itemized deductions are not deductible for AMT purposes and may provide no tax reduction benefit if subject to AMT. The new administration has proposed eliminating the AMT.

Many tax deductions and credits are subject to adjusted gross income based phase-out, which means only taxpayers with adjusted gross income below certain levels benefit. Adjusted gross income is the amount at the bottom of page 1 of your Form 1040—basically your gross income less certain deductions, but before itemized deductions and deduction for personal exemptions. Unfortunately, the applicable adjusted gross income amounts differ depending on the particular deduction or credit. The following table shows a few of the more common deductions and credits and applicable adjusted gross phase-out ranges for 2016:

Deduction or Credit	Adjusted Gross Income Phase-out Range		
	Joint Return	Single/Head of Household (HOH)	Married Filing Separate
Child Tax Credit	Begins at $110,000	Begins at $75,000	Begins at $55,000
American Opportunity Tax Credit	$160,000—$180,000	$80,000—$90,000	No credit
Itemized Deduction and Personal Exemption Reduction	Begins at $310,300	Begins at $259,400, $285,350 HOH	Begins at $155,650
Lifetime Learning Credit	$111,000—$131,000	$55,000—$65,000	No credit
Passive Rental Loss ($25,000) Allowance	$100,000—$150,000	$100,000—$150,000	No allowance unless spouses live apart
Student Loan Interest Deduction	$130,000—$160,000	$65,000—$80,000	No deduction

Make gifts sheltered by the annual gift tax exclusion before the end of the year and thereby save gift and estate taxes. You can give $14,000 in 2016 to each of an unlimited number of individuals but you cannot carry over unused exclusions from one year to the next. The transfers also may save family income taxes where income-earning property is given to family members in lower income tax brackets who are not subject to the kiddie tax.

Business Owners Tax Strategies

Under Section 179, an eligible business owner can claim significant first-year depreciation write-offs for the cost of new and used equipment, software, qualified costs for restaurant buildings, and improvements to interiors of retail and leased nonresidential buildings. For tax years beginning in 2016, the maximum limitation is $500,000, but this amount is reduced to the extent qualified purchases exceed $2,010,000 (this is now permanent with both being indexed for inflation). Also, limits apply to the amount that can be deducted for most vehicles. Businesses should also consider making expenditures that qualify for 50% bonus first-year depreciation if bought and placed in service during 2016.

If your business does not already have a retirement plan, now might be the time to begin a plan. Even if your business is only part-time, contributing to a SIMPLE IRA or another type of plan can reduce your current tax while increasing your retirement savings.

If you own an interest in a partnership or S corporation, your ability to deduct any losses it passes through is limited to your basis. Although unused losses can be carried forward indefinitely, you may want to make a capital contribution (or in the case of an S corporation, also loan it additional funds) which will increase your basis in the entity so you can deduct the loss this year.

These are just some of the year-end steps that can be taken to save taxes. By contacting us, we can tailor a particular plan that will best fit your needs.