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Year End 2017 – Tax Planning Letter

Professional services include:

- Tax Compliance
- Audit & Assurance
- Litigation Support
- Estate & Gift
- Succession Planning
- Valuation
- IRS Representation
- Family Foundations
- Bookkeeping & Accounting

Our mission is to provide our clients with exceptional services by taking initiative to be proactive advisors. We pride ourselves in developing tailored strategies to meet the specific needs of our clients.

We have a diverse commercial and individual accounting, auditing, tax and business consulting practice.

Our partners and staff are available to meet the needs of our clients and offer to meet with owners and management periodically throughout the year to discuss plans and to consult on a broad range of financial and business topics.

AICPA

Considerations for Year End Planning

In anticipation of the next tax preparation season, we hope that the following letter will alert you to changes in the tax laws that may affect you. Further, if you would like to discuss strategies that would help you save taxes and accomplish your estate planning goals, please contact us in November of this year to schedule a planning appointment.

Tax Brackets: With the net investment income tax, the highest marginal rate is now a whopping **44.70%**, which starts at taxable income of $418,400 for single filers. The tax rate on long-term capital gains and qualified dividend income remains at 15% for many single filers, but rises to **24.70%** for those with the net investment income tax when income exceeds $418,400.

Health Insurance: The penalty for not having health insurance continues, at 2.5% of income, or $695 per adult/$347.50 per child, capped at $2,085. If your income is under $48,240 for a single and $64,960 for a two-person household, you may qualify for assistance via a premium credit to reduce the cost of health insurance purchased through the www.healthcare.gov exchange.

Auto Mileage Allowance: The IRS set the mileage allowance at $0.535 per mile for business driving in 2017, and at $0.17 per mile for medical purposes. The charitable mileage rate remains at $0.14 per mile. Those who use their cars regularly for business should track their total mileage and business mileage using a mileage log and notations on their business calendar. One easy method to track total mileage is to document your mileage on January 1st and save your oil change service receipts showing total vehicle mileage. Note this on your tax organizer for our use in calculating your mileage deduction.

IRA Withdrawals: If you are over 70½, you can take your minimum required withdrawal by making a direct transfer to charity via your IRA custodian. This could save on your overall tax liability by reducing the impact of itemized deductions phase outs, net investment income tax, and higher rates of incomes and capital gains tax.

Tuition & Fees Deduction: This deduction expired at the end of 2016. Students can still claim the American Opportunity Credit or the Lifetime Learning Credit, but the above-the-line deduction for tuition/fees is gone.

<u>Bunching of Itemized Deductions:</u> If your income is stable, your taxes may be minimized if you shift deductions from year to year to overcome the thresholds. Maneuver your controllable deductions so that every other year you exceed the threshold and can itemize. Controllable expenses such as real estate taxes, state income taxes (if applicable) and charitable contributions are common expenses that can be paid either before or after the end of the tax year. In the alternating years, you use the standard deduction. This technique is called "bunching" deductions and could be applicable depending on your itemized deductions and the relevant phase outs. There are three important itemized deduction thresholds to keep in mind when bunching deductions:

1. <u>Itemized deductions</u> don't count until you exceed the standard deduction amount. For 2017, the standard deduction is $12,700 for married people and $6,350 for singles (over 65, this is increased by $1,250 each if married; $1,550 if single). Unless your total itemized deductions exceed the standard, they will not benefit you.

2. <u>Medical deductions</u> have their own threshold. Often we can control in which year these expenditures are paid. Only medical expenses that total more than 10% of AGI are deductible as itemized deductions. (Previous 7.5% of AGI for over 65 expires for year 2017.) When it is possible to time the payment of elective medical expenses such as dental bills (orthodontist, caps, crowns, dentures, periodontist) or elective surgery for which you will pay the bill (or a large deductible), bunching these payments in the same year may help your tax situation.

3. <u>Miscellaneous deductions</u> are also subject to a similar threshold, as only those expenses which exceed 2% of AGI are deductible. This includes employee business (auto and travel) expenses, investment expenses and tax preparation fees. You could pay investment magazines, safe deposit box rent, and tax preparation fees, etc., two years at once (the current year and the following year). In the next year, when you use the standard deduction, none of these expenses will be incurred.

We will be happy to discuss whether taking your deductions in 2017 or 2018 is better for you.

<u>Alternative Minimum Tax (AMT)</u>: Congress reset the AMT exemption and permanently adjusted it for inflation. The rate for 2017 is $84,500 for joint filers and $54,300 for individuals. When the AMT applies, your benefit from the itemized deductions for taxes and miscellaneous expenses are diminished. Thus, moving these expenses to 2018 by bunching itemized deductions may result in some benefit if you expect your income to fluctuate.

<u>Estate and Gift Taxes</u>

Leaving the income tax area, there are several ideas to consider when estate taxes are a concern. We can work directly with you or your estate planning attorney to discuss how the following may benefit your estate.

- **<u>Estate Tax Exemption</u>:** The estate tax exemption is now $5,490,000 with the inflation adjustment and is "permanent." Permanent means that the law stays the same until Congress changes it, a vast improvement over temporary measures that revert to an antiquated amount when the law expires. Those with estates under $5 million should not be subject to estate taxes unless there is a legislative change. The estate tax exemption portability system means that trusts for estate tax savings may not be required. Portability is now permanent as well. Portability means that the unused estate tax exemption for one spouse can be used by the surviving spouse. Thus, if the married couple has less than $11 million, estate taxes will not be applicable. Nevertheless, the family of the first spouse to die must file an estate tax return, on time, to establish the unused exemption so that it may be carried over.

- **<u>Gifts</u>:** Annual gifts of up to $14,000 may be given to as many people as you wish. If married, your spouse can join in the gift, which allows the two of you to gift up to $28,000 annually to an individual.

- **Gifts to Heirs:** Direct payments of tuition and medical or dental costs paid to the school or doctor are not treated as gifts. This is a way to benefit children and grandchildren without using your annual gift exemption.

- **Charitable Gifts:** There are a variety of methods for making charitable gifts that may benefit you depending upon your situation.

  ✓ Gift of Appreciated Property. There are no capital gains taxes on gifts of appreciated property to charities. When property is given to charity, a deduction for the fair market value is generally allowed. The capital gains tax does not apply to such a gift because you do not sell the asset. Consider giving five shares of stock to charity rather than cash or better yet, to a donor advised charity or a charitable foundation that will allow you to make the gift now, but determine an ultimate beneficiary in a succeeding tax year.

  ✓ Gifts via IRA Beneficiary. If you are making a gift to charity in your will, often an IRA or other retirement account is the best type of asset to fund these gifts. Not only do you avoid estate tax, it also avoids income tax for your beneficiaries.

  ✓ Charitable Gift Annuity (CGA). If your gift is under $500,000, the use of a CGA may be just the ticket. In this case you give a sum to your favorite charity, it pays you a life annuity and upon your death the charity keeps the money. You make the equivalent of a bequest, you get a charitable deduction to reduce today's income taxes, and you get the honor of benefitting your charity while you are living. The drawback is that your gift is irrevocable. Unlike the charitable remainder trust described below, you cannot change the charitable beneficiary of an annuity, if the charity falls out of your favor.

  ✓ Charitable Remainder Trust - Charitable remainder trusts give the best of all worlds with an income tax deduction now for the gift that takes place upon your death. Such trusts are appropriate when the ultimate gift is expected to be $500,000 or more and when you plan to consume the income from investments. The advantages to a charitable remainder trust are:
    - Charitable trusts do not pay capital gains taxes; and
    - You receive a current income tax deduction for the "remainder value" of the contribution, even though you continue to receive the income from the property contributed.

- **Gift of Life Insurance:** Life insurance policies can be significant tax loopholes. Similar in their income tax ramifications to municipal bonds, when held until death life insurance policies often produce a greater after-tax return. However, you may avoid both estate taxes and income taxes with a life insurance policy, which is not possible with municipal bonds. There are some incredible estate tax savings possible when life insurance policies are acquired through an irrevocable trust, since the proceeds from life insurance held in an insurance trust are not subject to income or estate taxes when inherited by your family.

This annual Tax Planning newsletter is being sent to you to encourage you to utilize all the opportunities the tax law provides to minimize your 2017 taxes as well as offer suggestions for longer range planning. Year-end tax planning can be well worth your time. If you are interested in a tax planning appointment, call our office to discuss these matters further.

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