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Tax Tips for Website

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2017 YEAR-END PLANNING AND SAVINGS IDEAS

For 2017, it is important to review with your advisor your potential personal and business opportunities to take advantage of year-end tax savings ideas. Due to the changes in the economy, recent law changes and those yet to come, and a Congress that can't seem to agree on much, strategies previously used may not be suitable for the current year or future years. Also, there are key tax breaks that lapsed after 2016 and it is not likely Congress will address these and they aren't in the proposed legislation to be extended by Congress at the time of this writing. Taxpayers should not overlook several recent and proposed law changes and clarifications that could significantly impact their situation. The following ideas should be considered and discussed with your tax advisor to determine which strategies are appropriate to implement and when.

Complying with the Affordable Care Act (ACA)

The ACA is still in place for 2017 and 2018 as of now. Lower income individuals may be eligible for a tax credit (called the Premium Tax Credit) to help pay for health insurance coverage through an Affordable Insurance Exchange, also known as the "Exchange" or "Marketplace". The credit is refundable, so even those with little or no tax liability may benefit. You must file a tax return to be able to claim the credit, even if otherwise you would not be required to file. The credit also can be paid in advance to the insurance company to help cover the cost of premiums.

The individual shared responsibility provision (called the individual mandate at times) requires each household individual to have minimum essential coverage for each month, qualify for an exemption or make a payment for not having this coverage when filing his or her federal income tax return. The penalty for **2017** for not complying is the greater of $695/person ($347.50 per child under 18 or $2,085 maximum per family) or 2.5% of household income over the filing threshold amount.

A clear majority of people who have health insurance through their employer or are on a government plan, such as Medicare or Medicaid, will not be affected by this.

Planning points>

- **All persons that participated in the marketplace in 2017 will be mailed a Form 1095-A by January 31, 2018 showing premiums paid and advance premium credits paid, if any. This will be needed to complete the portion of an individual's tax return dealing with this.**

- **Review with your tax advisor if you may qualify for an exemption to the minimum essential health coverage so you do not have a penalty to pay. Also, the open enrollment period to purchase health insurance coverage for 2018 through the exchange is only open through December 15, 2017 so review your coverage needed and visit healthcare.gov for further information.**
- **Forms 1095-B and 1095-C issued by employers to taxpayers will indicate insurance coverage periods to tell the IRS when a household had minimum essential coverage during the year. These forms, however, may be issued to taxpayers as late as February 28, 2018. This could cause some difficulty in return preparation early in the filing season.**
- **It is also unknown what form the ACA will take in the future or if it will survive at all under the new administration. This throws uncertainty into the above provisions going forward.**

Payroll surtax

An additional .9% Medicare tax is imposed on high earnings workers and self-employed taxpayers in 2017. It applies to wages in excess of $250,000 for joint return filers and $200,000 for single filers. The tax also applies to self-employment income for the year in excess of the above amounts. This additional amount will be withheld from employees' paychecks or, if self-employed, will be paid with the individual's income tax return.

Planning points>

- **Consideration must be given to taking bonuses or delaying self-employed income into 2018 instead of 2017 if it looks like you may fall into this high wage income category. Of course, all tax rates need to be taken into consideration before deciding to shift income between 2017 and 2018.**
- **With current tax reform pending, what Congress will do with tax rates or even this surtax in the future is not certain. Rates will go down for some and up for others. This surtax, as proposed, will remain in place after 2017.**

Gifts

You can save gift and estate taxes by making gifts sheltered by the annual gift tax exclusion before the end of the year.

Planning points>
There was no change in the limits from 2016 to 2017. You can gift up to $14,000 in 2017 ($28,000 for married couples who split gifts) to an unlimited number of individuals but can't carry over unused exclusions from one year to the next. So, there is no doubt when the gift was made, it is suggested for gift of money given close to year end, the donee should be urged to deposit the check before year end. The annual gift exclusion will go up to $15,000 per individual in 2018.

Long term Care Savings Plan

For Nebraska filers, there is a deduction for contributions to the Long-Term Care Savings Plan in 2017 up to $2,000 per joint return for Nebraska taxes only.

Planning points>

- **There are age restrictions and withdrawals must be used for long term care expenses or LTC insurance premiums. It must be funded by 12/31/17 to get the deduction for 2017.**
- **This law is set to expire at the end of 2017.**

Estate Planning

The estate exemption is at $5.49 million at a top marginal rate of 40% effective for 2017.

Planning points>

- **Opportunities such as lifetime gifting, Grantor Annuity Trusts should be looked at. Discussion with your advisor is imperative. A married couple will be able to shield just shy of $11 million form federal estate and gift taxes with proper filing and the d marital exclusion.**
- ***Current proposed federal legislation eliminates the estate tax, starting in 2024 under the House plan with the Senate just raising the exemption amount but not repealing the tax. Keep watch with your advisor on what finally passes into law.***

Investment tax rates

The tax rate on long-term capital gains and qualified dividends is reduced to 0% for individuals and trusts in less than a 25% tax bracket for ordinary income.

High-income households pay a 3.8% surtax on at least a portion of their investment income (see discussion following).

The top long-term capital gains and dividends rate is 20% for taxpayers with income exceeding $418,400 single ($470,700 joint). The rate remains at 15% for others.

The long-term portion of capital gains alone is eligible for the favorable tax rates. Net capital losses, regardless of how long they were held, are available to offset up to $3,000 ($1,500 if married filing separately) of other types of income. Any excess loss is carried forward to future years, where it retains its short-term or long-term character.

Planning Points>

- **For many taxpayers, it may make sense to recognize long-term capital gains in 2017 to take advantage of the lower current rates or if they have unused capital losses to take against those gains. It may pay to defer recognition of those gains if the investment surtax will come into play for the higher income individuals in 2017 (see discussion below). If you want to keep the same investment strategy, you could sell your appreciated assets and immediately reinvest in the same or similar assets. You would then hold the new assets until you would have otherwise sold them.**
- **Individuals and trusts who can utilize the 0% capital gains tax rate in 2017 should consider selling capital gain securities.**
- **If your ordinary income tax bracket is greater than 15%, consider making gifts of capital gains and dividend paying assets in 2017 to family members who are eligible for the 0% capital gains tax rate.**
- **Remember passing along high investment income property to a child in 2017 subject to the "kiddie tax" rules may not pay off if they may pay tax at the parent's tax rate anyway.**
- **Depending if you will be subject to higher capital gains rates in 2017 or 2018 or subject to the surtax on investment income (as discussed below) either year, could dictate your strategy of when to recognize capital gains. It is best to have your tax advisor run different scenarios for you to see the overall tax between years.**
- **The netting rules provide an opportunity to manage net taxable capital gain or loss, making it wise to review your security gains and losses before year end to determine whether additional transactions may improve your tax situation.**
- ***Proposed tax legislation does not touch these rates for 2018 but the brackets each kicks in may change of tax brackets changed as proposed.***

3.8 Percent Net Investment Tax

For 2017, a 3.8% surtax in net investment income (NII) applies to most investment income. For individuals, the amount subject to the tax is the lesser of:

1. Net Investment income; or
2. The excess of modified adjusted gross income over the applicable threshold amount which is $200,000 for single and head of household or $250,000 for married filing joint returns.

NII includes dividends, interest, rents, capital gains, royalties, annuities and activities where you are a passive participant (passive activities). Self-employment income, income from an active trade or business and potions of gain on sale of business interests and well as IRA or qualified retirement plan distributions, are not subject to the NII tax.

Planning points>

- **To the extent your NII is income from a passive activity, increasing your participation in that activity now and in the future, could reduce the amount of this income subject to the tax.**
- **Depending if you will be subject to the surtax on investment income either year, could influence your strategy of when to recognize capital gains. It is best to have your tax advisor run different scenarios for you to see the overall tax between years.**
- **This is another reason to look at ways to reduce your adjusted gross income. Income, even not subject to the NII, could cause your gross income to increase enough to make the NII applicable.**
- ***Tax reform proposals in both the House and Senate leave this in place going forward.***

<u>Cash-basis method for prepaid business expenses</u>

For businesses, tax regulations allow for the immediate expensing of certain prepaid expenses, including insurance premiums, warranty and service contract costs and taxes, licenses and permits. The following conditions must be met for the prepaid expenses to be immediately expensed for tax purposes for the cash-basis method taxpayer:

- First, the benefit cannot extend beyond 12 months.
- Second, the benefit cannot extend beyond the year following the year of payment.
- Third, a legal liability to make the payment must have existed in the year paid.

Planning Points>

- **Timing of certain expense payments and cash flow can give rise to this opportunity to get immediate deductions for benefits later received.**
- ***Note, there is proposed legislation that expand the availability to use the cash-basis method for tax starting in 2018.***

<u>Conversion of traditional IRA to a Roth IRA</u>

If your traditional IRA account values have declined significantly due to the economic downturn and you have been considering a conversion of your traditional IRA into a Roth IRA, now may be the time to do it. Your lower traditional IRA accounts converted may yield a lower tax on conversion than they would have when they were higher, since you are taxed on all or a portion of the traditional IRA amount converted. Remember your converted amount creates taxable income, but no premature withdrawal penalty, in the year of conversion.

Who should make IRA-to-Roth IRA conversions? Consider this if you; (1) have a number of years to go before retirement) and therefore able to recoup the dollars that are lost to taxes on account of the conversion; (2) anticipate being taxed at a higher bracket in the future than you are now; and (3) can pay the tax on the conversion, hopefully with monies other than the IRA monies.

If you find at tax time you really didn't want to do a conversion or it was adverse tax wise to do so, you can always elect to do a re-characterization back to a traditional IRA. There are certain steps and deadlines to do this, so see your tax advisor if you need further advice. See note on possible legislative change to this below.

Planning Points>

- **Discuss with your advisor the tax consequences of this opportunity, the pros and cons of Roth IRAs and to see if you qualify to convert to a Roth IRA. The investment surtax of 3.8% comes into play. Although IRA conversions are not subject to the surtax, the income from them is part of the adjusted gross income total to determine if the surtax applies. Delaying recognition of income on conversion until after 2017 should be reviewed for possible tax consequences.**
- **Roth IRAs have two major advantages over traditional IRAs: (1) distributions from traditional IRAs are taxed as ordinary income. By contrast, Roth IRA distributions can be tax free if they are "qualified distributions" (2) traditional IRAs are subject to minimum distribution rules when the taxpayer reaches age 70 ½. Roth IRAs have no such requirement.**
- ***Proposed legislation eliminates the option to do re-characterization of an IRA between traditional and Roth IRAs after 12/31/17. Thus, you must consider re-characterization pre 12/31/17. Doesn't affect conversions, just re-characterizations.***

<u>Donating appreciated securities</u>

For individuals, consider donating appreciated securities instead of cash. If you have held the security for at least one year and two days, your charitable deduction (before certain limitations) is equal to the value of the securities, and you are not taxed on the appreciation.

Planning points>
Make sure the security is transferred prior to 12/31/17. The donation is an itemized deduction on an individual's income tax return.

<u>IRA qualified charitable distributions.</u>

Consider the opportunity for individuals age 70 ½ or older to make qualified charitable contributions of up to $100,000 directly from an IRA to a qualified charity. The IRA distributions will not be included in your income (may help on the investment surtax calculation). They also will not be shown as charitable itemized deductions either.

Planning points>
This provision in the law is important for several reasons. Not including the IRA withdrawal as income on page 1 of your tax return may cause less of your social security benefits to be taxable or may keep you from moving into a surtax situation discussed previously.

College Education Savings Plan

Contribute to a section 529 tuition plan for higher education. There is no federal tax deduction but investments grow tax free, and if you invest in the NEST plan for Nebraska, you could get up to a $10,000 deduction for Nebraska income tax purposes only. Distributions are tax free 100% if used for qualified educational expenses including, tuition, books, fees, room & board (if at least a ½ time or greater student).

Planning points>

- **The plan must be funded by 12/31/17 to receive the state only deduction for 2017. It is recommended any distributions are taken in the same year as the qualifying expenses are paid. Since the annual contributions count towards the gifting annual exclusion amounts, beware of the rules regarding the gift tax return filing options and requirements if you contribute more than the annual gift exclusion amount to a 529 plan in any one year.**
- **Even if you must take a distribution and not use it for qualified education expenses, you will only be taxed on any earnings on the distribution, not the amount contributed that is considered part of the distribution.**

Home Office expenses

There is an option of an easier path to claiming the home office deduction. The optional deduction is capped at $1,500 per year based on a $5 per square foot for up to 300 square feet of office. The current restrictions on the home office deduction, such as the requirement that a home office must be used exclusively for business and the limit tied to the income derived for the business, still apply.

Planning point>

- **The optional deduction may be less of a reporting burden but there is a good chance it will produce a lesser deduction than doing it the previous way, with not that much return preparation time savings to do the deduction calculation and based upon the restrictions on the deduction amount and office size limitation in the new optional method. It is recommended you work with your advisor to see which method will produce the largest deduction.**

College Education credits and deduction

For 2017, the American Opportunity Tax Credit creates an up to $2,500 higher education tax credit (direct reduction in tax) that is available for the first four years of college and is based on amounts paid for tuition, fees and books for a student enrolled at least on a one-half time basis at a qualified educational institution. This credit can be up to 40% refundable. The credit has an adjusted gross income limit subjecting it to phase out at $180,000 on a joint return or $90,000 on a single return. Qualified education expenses not only include tuition and fees and books but equipment used for college use such as computers.

The Lifetime Learning credit remains unchanged at a maximum $2,000 and is available for any college year, not limited to just the first four. Unlike with the American Opportunity credit, nothing but tuition and fees is included in determining eligible expenses.

Planning points>

- **One way to take advantage of the credit is to prepay the spring semester 2018 tuition, including books, by 12/31/2017 if you haven't reached the maximum eligible expenses amount already in 2017. This can be a good way to fund higher education and get some sort of tax break for doing it.**
- ***Under proposed legislation the American Opportunity Tax credit would remain after 2017 but the Lifetime Learning Credit option disappears.***

Itemized deductions

Consider these federal itemized deduction related ideas.

Planning Points>

- **If you expect you might owe state income tax for 2017 or if you are paying state quarterly tax estimates, if you pay and mail (postmark in 2017) your expected state balance due for 2017 in with your 4th quarter estimated tax payment that is due January 2018, you can write off the payment as a federal itemized deduction in 2017.** ***See proposed tax legislation note below.***
- **Like state income taxes, real estate taxes due in early 2018 can often be prepaid in 2018. For real estate taxes on your personal residence, just be mindful of the alternative minimum tax (AMT). Reals estate tax on rental property is deductible (subject to the passive loss rules) whether or not you are subject to AMT.** ***See proposed tax legislation note below.***
- **Making the January 2018 mortgage payment on your personal residence before the end of 2017 enables you to deduct the interest portion of the payment in 2017.** ***See proposed tax legislation note below.***
- **For gifts to charity, you deduct them in the year the check is mailed or money handed over to the charity, not when you pledge. Donations made by credit card are considered made when posted to your charge account, not in the year the charge account is paid.**

- **There is the option to deduct state and local sales tax instead of state income tax. This is especially helpful in states with no state income taxes imposed. *See proposed tax legislation note below.***
- **All the above should be considered with the possibility that, if you are in an alternative minimum tax situation, these itemized deduction suggestions may not provide any federal tax benefit. Please consult your tax advisor on the alternative minimum tax and how it affects you.**
- **Beware, for higher income individuals, itemized deductions could be partially phased out by 3% of the excess over $313,800 for joint and $261,500 for single filers of AGI**
- ***Beware, proposed legislation may eliminate the deduction for state income taxes and sales taxes as itemized deductions, eliminate or limit the deduction for property taxes, be more restrictive on how much mortgage interest you can take as an itemized deduction, eliminate the employee business expense for unreimbursed expenses and eliminate medical expenses itemized deductions.***

<u>Standard deduction and personal exemptions</u>

Starting in 2018, proposed legislation would raise the standard deduction to $12,000 for single filers and $24,000 joint returns and eliminate the deduction for dependents for all taxpayers.

Planning Points>
One must consider this in planning year end itemized deductions for 2017 and going forward considering the standard deduction change and potential change to a number of itemized deductions.

<u>Bonuses and retirement plan contributions</u>

For a business deduction, if structured correctly, **accrual** method taxpayers can wait and pay 2017 bonuses up to March 15, 2018 and still claim a deduction on a calendar year 2017 tax return. Certain corporate retirement plan contributions can be funded as late as the due date of the return in 2018, including extensions, and still receive a 2017 tax deduction, whether you are an accrual or cash basis taxpayer.

Planning points>
This can help with cash flow issues. Beware, the bonus deferral does not work for owners' bonuses, which must be paid any bonuses by 12/31/17 for the deduction to be allowed for 2017.

Retirement plan options

If you can contribute to a 401k, SIMPLE or other employer sponsored retirement plan, it is a good way to put money away tax deferred. Contributions vary depending on the plan and your age.

Even if not participating in an employer plan consider if you are eligible for contributions into a regular IRA or Roth IRA. 2017 annual contribution limits are the same as 2016 at $5,500 maximum (or $6,500 if over age 50).

Self-employed individuals have several retirement plan options such as Keogh's, SEP's, individual 401k plans and IRAs with contribution limits for 2016 ranging from $18,000 ($24,000 for over age 50) for a 401k plan up to $54,000 for a SEP or Keogh plan.

Planning Points>

- **Take advantage of the retirement options available if your cash flow allows.**
- **For the self-employed, consider setting up one of these plans, some of which don't have to be funded until the filing deadline for 2018 to receive a 2017 tax return deduction. The funding deadline for traditional and Roth IRAs is April 17, 2018. See your tax advisor for your options and contribution limits.**
- ***Watch potential pending legislation affecting this area moving past 2017.***

ACA employer mandate

Rules went into effect starting 2015 affecting health insurance coverage required to be offered to employees and year end reporting to employees by employers, especially those with over 100 full time equivalent employees, but also reporting requirements for those employers with as few as 50 full time equivalent employees.

Planning points>
The rules are complicated but penalties for non-compliance can be severe. Please read up on the extensive information through the IRS website and/or contact your tax advisor to become education on requirements that may affect you as a large or small business employer.

Monitoring passive activities

Complex rules govern the tax treatment of business activities in which the owner does not materially participate. If these "passive activities" produce a loss, that loss may be limited and not currently deductible for tax. If a passive activity is produces income, the income could be subject to the 3.8% surtax on net investment income (see previous discussion on this).

Planning point>

- **If you are the owner of a business, it is a good idea to keep good records of the hours you spend working the business. This is important to be able to prove your level of participation.**

- **Review the passive rules with your tax advisor as it affects all activities you are involved with, whether as a sole proprietor, a rental activity, S corporation or partnerships or trusts. Review the material participation rules with then to know how to avoid being treated as a passive participant in an activity so that when the activity does show losses, you aren't currently limited in deductions**.

<u>Business depreciation & expensing options</u>

The Section 179 expensing election and bonus depreciation provisions provide an immediate deduction for the cost of certain business equipment (in place of slower depreciation deductions).

To qualify for a 50% bonus depreciation write-off in the first year, the equipment must be new and placed in service before year end 2017.

The 179 election allows for $500,000 for qualifying assets put into service in 2017.

Under the luxury vehicle rules, limits are placed on otherwise allowable deductions for autos, light trucks and minivans. The law keeps the increased first year limits by $8,000 on luxury vehicles purchased in 2017.

Businesses have an opportunity to expense otherwise capitalized tangible property costs of the de minimis rule is met. Known as the repair regs. If certain elections made and financial reports prepared, then a set amount of otherwise capital items can be expensed outside of those under section 179 discussed above. If a business prepares applicable financial statements (AFS) they can use the de minimis election to expense up to $5,000 items individually and if no AFS then the limit is $2,500.

Planning Points>

- **Consider any year end purchases to reach this amount allowed for the deduction if your tax savings warrants doing so. Equipment, for example, must not only be purchased but placed into service by 12/31/17 for calendar year taxpayers to qualify for a 2017 deduction. Also, expensing could be limited on certain vehicles so consult your tax advisor if you are considering vehicle purchases.**
- **The bonus depreciation is for new property only, not used. Remember, to take the expensing write-off, the business must show net income. The bonus depreciation rules don't require this. This phases out the next several years.**

- **The repair regs dealing with the de minimis election can be complicated. Review with your tax advisor before implementing as certain elections and documentation is needed. (See following discussion)**
- ***Proposed legislation greatly expands the property that can be expens3ed in the year put into service both under the bonus depreciation and section 179 rules effective for 2018. Keep this in mind when making year end purchasing decisions.***

Repair regulations

For tax years beginning in 2014, new rules are in effect for determining when expenditures can be deducted as a repair expense and when they must be capitalized and depreciation. The rules for 2016 and beyond must be monitored. For example, numerous elections apply on an annual basis, such as the de minimis expensing safe harbor and partial asset dispositions. In addition, the taxpayer should consider how the betterment, restoration and adaptation rules apply to a unit of property when analyzing a repair for capitalization purposes.

Planning Point>
All businesses should review their repair/capitalization policies to assure that they are in compliance with the new rules. This includes an opportunity to do an expensing of certain amounts as repairs of a de minimis amount depending on what type of financial statements a business has, if any. The rules in this area are complicated so work with your tax advisor.

Identity Theft

Thieves often begin their fraud by stealing an individual's Social Security number (SSN) and other personal information. A thief can use this information in many ways but one way is using the information to file a false income tax return usually to obtain a large refund before the IRS and the legitimate taxpayer realizes what has happened. Victims of ID theft might not realize their situation until they file their tax returns and uncover the problems. The IRS has provided a variety of tools and steps to be taken if you think you may be a victim of ID theft. Victims must prove who they are and many times the situation will delay the tax refund the taxpayer s entitled to receive until the mess is cleared up. In addition, you will be assigned a special ID number from the IRS to use on future filings of tax returns.

Planning point>
Know how to reduce your threat and know what to do if you fall victim to identity theft. Consult the resources on the IRS.gov website or contact your tax advisor to help you plot your course if you have been victimized.

Business entity choice

Proposed legislation would drastically cut corporate tax rates, change individual tax rates and allow for lower tax for pass through entity (partnerships, LLCs and S corporations) income to individuals effective in 2018 or later.

Planning point>
Follow the legislation on changes to these areas as it may affect your choice and options for being taxed as particular types of entities for the greatest tax savings. Your tax adviser is essential for consultation in this.

Legislation

As of now, certain tax reform bills are being debated through Congress and some of the areas were mentions above what is proposed. It is difficult at best to know what will come about ultimately as passed law but it is safe to say most of the proposed legislation becomes effective in 2018 or later.

This makes it doubly important to take the proposals into consideration in your decisions for the remainder of 20178 and beyond but also makes it more difficult the longer legislation is not passed to advise the proper courses of action.

Planning point>
Keep your eyes on any legislation extending these provisions as well as new laws or changes to current law.