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# Year-End Tax Planning for 2017



**SPECIAL REPORT**



## Year-End Tax Planning for 2017

This Special Report contains year-end tax planning tips that highlight the opportunities and challenges faced by taxpayers in today's uncertain legislative environment. While tax reform is a major topic of discussion in Washington nowadays, nobody knows when tax reform legislation might be enacted and what the new rules may be.

In spite of this uncertainty, the best year-end tax planning strategy for many taxpayers will be to follow the time-honored approach of deferring income and accelerating deductions to minimize 2017 taxes. This approach may turn out to be even more valuable if Congress succeeds in enacting tax reform that reduces tax rates beginning next year in exchange for slimmed-down deductions. But regardless of whether tax reform is enacted, deferring income also may help a taxpayer minimize or avoid phaseouts of various tax breaks for 2017 that are based on adjusted gross income (AGI).

However, year-end tax planning doesn't occur in a vacuum. It must take account of each taxpayer's particular situation and planning goals, with the aim of minimizing taxes to the greatest extent possible. Thus, while most taxpayers will come out ahead by following the traditional approach described above, others with special circumstances may do better by accelerating income and deferring deductions. In some situations, total combined taxes for 2017 and 2018 will be reduced if income is accelerated from 2018 into 2017 and certain expenses are deferred to 2018 where they may give a greater tax benefit in that year.

This Special Report provides two checklists of actions that can cut taxes for taxpayers for this year and in the years to come — one that describes actions individuals can take to save taxes and one that describes actions businesses and business owners can take to save taxes.

This year's lists also include a number of new items for taxpayers that qualify for special tax relief on account of hurricanes Harvey, Irma and Maria.



## Year-End Tax Planning Moves for Individuals

- Higher-income earners must be wary of the 3.8% surtax on certain unearned income. The surtax is 3.8% of the lesser of: (1) net investment income (NII) or (2) the excess of modified adjusted gross income (MAGI) over a threshold amount (\$250,000 for joint filers or surviving spouses, \$125,000 for a married individual filing a separate return and \$200,000 in any other case). As year-end nears, an individual's approach to minimizing or eliminating the 3.8% surtax will depend on his or her estimated MAGI and NII for the year. Some taxpayers should consider ways to minimize (e.g., through deferral) additional NII for the balance of the year; others should try to see if they can reduce MAGI other than NII and others will need to consider ways to minimize both NII and other types of MAGI.
- The 0.9% additional Medicare tax also may require higher-income earners to take year-end actions. It applies to individuals for whom the sum of their wages received with respect to employment and their self-employment income is in excess of an unindexed (i.e., not inflation-adjusted) threshold amount (\$250,000 for joint filers, \$125,000 for married couples filing separately and \$200,000 in any other case). Employers must withhold the additional Medicare tax from wages in excess of \$200,000 regardless of filing status or other income. Self-employed persons must take it into account in figuring estimated tax. There could be situations where an employee may need to have more withheld toward the end of the year to cover the tax. For example, if a taxpayer earns \$200,000 from one employer during the first half of the year and a like amount from another employer during the balance of the year, he or she would owe the additional Medicare tax, but there would be no withholding by either employer for the additional Medicare tax since wages from each employer don't exceed \$200,000.



- A taxpayer should consider postponing income until 2018 and accelerating deductions into 2017 to lower his or her 2017 tax bill. This strategy may be especially valuable if Congress succeeds in lowering tax rates next year in exchange for slimmed-down deductions. Regardless of what happens in Congress, this strategy could enable an individual to claim larger deductions, credits and other tax breaks for 2017 that are phased out over varying levels of AGI. These include child tax credits, higher education tax credits and deductions for student loan interest. Postponing income also is desirable for those taxpayers who anticipate being in a lower tax bracket next year due to changed financial circumstances. Note, however, that in some cases, it may pay to actually accelerate income into 2017. For example, this may be the case where a person will have a more favorable filing status this year than next (e.g., head of household versus individual filing status).
- A taxpayer should consider whether he or she would benefit from realizing losses on stock while substantially preserving his or her investment position. There are several ways this can be done, for example, by selling the original holding then buying back the same securities at least 31 days later.
- If a taxpayer believes that a Roth IRA is better than a traditional IRA, he or she may consider converting traditional-IRA money invested in beaten-down stocks (or mutual funds) into a Roth IRA if eligible to do so. Keep in mind, however, that such a conversion will increase the taxpayer's AGI for 2017.



A taxpayer may want to consider using a credit card to pay deductible expenses before the end of the year. Doing so would increase his or her 2017 deductions even if the credit card bill isn't paid until after the end of the year.

- If a taxpayer converted assets in a traditional IRA to a Roth IRA earlier in the year and the assets in the Roth IRA account declined in value, he or she could wind up paying a higher tax than is necessary if things are left as is. A taxpayer can back out of the transaction by recharacterizing the conversion — that is, by transferring the converted amount (plus earnings or minus losses) from the Roth IRA back to a traditional IRA via a trustee-to-trustee transfer. A taxpayer can later reconvert to a Roth IRA.
- It may be advantageous for a taxpayer to try to arrange with his or her employer to defer, until early 2018, a bonus that may be coming their way.
- A taxpayer may want to consider using a credit card to pay deductible expenses before the end of the year. Doing so would increase his or her 2017 deductions even if the credit card bill isn't paid until after the end of the year.
- A taxpayer who expects to owe state and local income taxes at filing time next year may want to ask his or her employer to increase withholding of state and local taxes (or pay estimated tax payments of state and local taxes) before year-end to pull the deduction of those taxes into 2017 if the taxpayer won't be subject to alternative minimum tax (AMT) in 2017. Pulling state and local tax deductions into 2017 would be especially beneficial if Congress eliminates such deductions beginning next year, which is a distinct possibility.
- A taxpayer may want to take an eligible rollover distribution from a qualified retirement plan before the end of 2017 if the taxpayer is facing a penalty for underpayment of estimated tax and having his or her employer increase withholding is unavailable or won't sufficiently address the problem. Income tax will be withheld from the distribution and applied toward the taxes owed for 2017. A taxpayer can then timely roll over the gross amount of the distribution, i.e., the net amount received plus the amount of withheld tax, to a traditional IRA. No part of the distribution will be includible in income for 2017, but the withheld tax will be applied pro rata over the full 2017 tax year to reduce previous underpayments of estimated tax.



- A taxpayer should estimate the effect of any year-end planning moves on the AMT for 2017, keeping in mind that many tax breaks allowed for purposes of calculating regular taxes are disallowed for AMT purposes. These include the deduction for state property taxes on a taxpayer's residence, state income taxes, miscellaneous itemized deductions and personal exemption deductions. If a taxpayer is subject to the AMT for 2017 or suspects he or she might be, these types of deductions should not be accelerated.
- A taxpayer may be able to save taxes by applying a bunching strategy to pull "miscellaneous" itemized deductions, medical expenses and other itemized deductions into this year. This strategy would be especially beneficial if Congress eliminates such deductions beginning in 2018.
- A taxpayer may want to pay contested taxes to be able to deduct them this year while continuing to contest them next year.
- A taxpayer may want to settle an insurance or damage claim in order to maximize his or her casualty loss deduction for this year.
- Taxpayers who must take required minimum distributions (RMDs) from their IRAs or 401(k) plans (or other employer-sponsored retirement plans) should make sure that they take the required withdrawal, as failure to do so can result in a penalty of 50% of the amount of the RMD not withdrawn. RMDs from IRAs must begin by April 1 of the year following the year a taxpayer reaches age 70½. That start date also applies to company plans, but non-5% company owners who continue working may defer RMDs until April 1 following the year they retire. However, although RMDs must begin no later than April 1 following the year in which the IRA owner attains age 70½, the first distribution calendar year is the year in which the IRA owner attains age 70½. Thus, if a taxpayer turns age 70½ in 2017, the first required distribution can be delayed to 2018, but a taxpayer who chooses to do so will have to take a double distribution in 2018 — i.e., the amount required for 2017 plus the amount required for 2018. Taxpayers should think twice before delaying 2017 distributions to 2018, as bunching income into 2018 might push them into a higher tax bracket or have a detrimental impact on various income tax deductions that are reduced at higher income levels. However, it could be beneficial for a taxpayer to take both distributions in 2018 if he or she will be in a substantially lower bracket that year.
- A taxpayer should consider increasing the amount set aside for next year in his or her employer's health flexible spending account (FSA) if the taxpayer set aside too little for this year.
- If a taxpayer becomes eligible in December of 2017 to make health savings account (HSA) contributions, he or she can make a full year's worth of deductible HSA contributions for 2017.
- A taxpayer should consider making gifts sheltered by the annual gift tax exclusion before the end of the year and thereby saving gift and estate taxes. The exclusion applies to gifts of up to \$14,000 made in 2017 to each of an unlimited number of individuals. A taxpayer can't carry over unused exclusions from one year to the next. Such transfers 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.
- If a taxpayer was affected by Hurricane Harvey, Irma or Maria, keep in mind that he or she may be entitled to special tax relief under recently passed legislation, such as relaxed casualty loss rules and eased access to retirement funds. In addition, qualifying charitable contributions related to relief efforts in the Hurricane Harvey, Irma or Maria disaster areas aren't subject to the usual charitable deduction limitations.



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## Year-End Tax-Planning Moves for Businesses and Business Owners

- Businesses should consider making expenditures that qualify for the business property expensing option. For tax years beginning in 2017, the expensing limit is \$510,000 and the investment ceiling limit is \$2,030,000. Expensing is generally available for most depreciable property (other than buildings), off-the-shelf computer software, air conditioning and heating units and qualified real property — qualified leasehold improvement property, qualified restaurant property and qualified retail improvement property. The generous dollar ceilings that apply this year mean that many small and medium sized businesses that make timely purchases will be able to currently deduct most if not all their outlays for machinery and equipment. What's more, the expensing deduction is not prorated for the time that the asset is in service during the year. The fact that the expensing deduction may be claimed in full (if the business is otherwise eligible to take it) regardless of how long the property is held during the year can be a potent tool for year-end tax planning. Thus, property acquired and placed in service in the last days of 2017, rather than at the beginning of 2018, can result in a full expensing deduction for 2017.
- Businesses also should consider making buying property that qualifies for the 50% bonus first year depreciation if bought and placed in service this year (the bonus percentage declines to 40% next year). The bonus depreciation deduction is permitted without any proration based on the length of time that an asset is in service during the tax year. As a result, the 50% first-year bonus writeoff is available even if qualifying assets are in service for only a few days in 2017.
- Businesses may be able to take advantage of the "de minimis safe harbor election" (also known as the book-tax conformity election) to expense the costs of lower-cost assets and materials and supplies, assuming the costs don't have to be capitalized under the Code Sec. 263A uniform capitalization (UNICAP) rules. To qualify for the election, the cost of a unit of property can't exceed \$5,000 if the taxpayer has an applicable financial statement (AFS; e.g., a certified audited financial statement along with an independent CPA's report). If there's no AFS, the cost of a unit of property can't exceed \$2,500. Where the UNICAP rules aren't an issue, consider purchasing such qualifying items before the end of 2017.
- Businesses contemplating large equipment purchases also should keep a close eye on the tax reform plan being considered by Congress. One current proposal contemplates immediate expensing — with no set dollar limit — of all depreciable asset (other than building) investments made after Sept. 27, 2017, for a period of at least five years. This would be a major incentive for some businesses to make large purchases of equipment in late 2017.
- If a business was affected by Hurricane Harvey, Irma or Maria, it may be entitled to an employee retention credit of up to \$2,400 for wages paid to eligible employees.
- A corporation should consider deferring income until 2018 if it will be in a higher bracket this year than next. This could certainly be the case if Congress succeeds in dramatically reducing the corporate tax rate, beginning next year.
- A corporation should consider deferring income until next year if doing so will preserve the corporation's qualification for the small corporation AMT exemption for 2017. Note that there is never a reason to accelerate income for purposes of the small corporation AMT exemption because if a corporation doesn't qualify for the exemption for any given tax year, it will not qualify for the exemption for any later tax year.



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- A corporation (other than a “large” corporation) that anticipates a small net operating loss (NOL) for 2017 (and substantial net income in 2018) may find it worthwhile to accelerate just enough of its 2018 income (or to defer just enough of its 2017 deductions) to create a small amount of net income for 2017. This will permit the corporation to base its 2018 estimated tax installments on the relatively small amount of income shown on its 2017 return, rather than having to pay estimated taxes based on 100% of its much larger 2018 taxable income.
  
- If a business qualifies for the domestic production activities deduction (DPAD) for its 2017 tax year, consider whether the 50%-of-W-2 wages limitation on that deduction applies. If it does, consider ways to increase 2017 W-2 income, e.g. — by bonuses to owner-shareholders whose compensation is allocable to domestic production gross receipts. Note that the limitation applies to amounts paid with respect to employment in calendar year 2017, even if the business has a fiscal year. Keep in mind that the DPAD wouldn’t be available next year under the tax reform plan currently before Congress.
  
- To reduce 2017 taxable income, a business should consider deferring a debt-cancellation event until 2018.
  
- To reduce 2017 taxable income, a business should consider disposing of a passive activity in 2017 if doing so will allow it to deduct suspended passive activity losses.





## Guidance

Get all the comprehensive tools and learning resources you need to help ensure you're ready to address the unique opportunities and challenges that affect year-end planning and beyond.

### Tax Saving Moves for the Rest of 2017

This 100 page Tax Planning and Practice Guide contains year-end tax planning tips that highlight the unique opportunities and challenges faced by taxpayers in today's complex tax environment. As the end of the year approaches, there is still time to make planning moves that will help individuals and businesses lower their tax bills. Learn more about the moves to make by year-end to achieve maximum overall tax savings for 2017 and later tax years and how to set basic planning goals and adjust income and expenses accordingly.

### 2018 Federal Tax Handbook – Newly Updated

Designed to provide quick and easy answers about 2017 returns and critical tax questions during the 2018 tax year, the RIA Federal Tax Handbook offers comprehensive, insightful guidance on federal tax law, including the latest regulations, rulings and revenue procedures as well as precise explanations about changes that could impact your business or your clients.

### Federal Tax Coordinator

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