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Year-End Tax Planning for 2016

PERSONAL

Well, we waited for another end of year, last minute, tax law change but due to the election results one won't be coming. One thing is for sure, next year will bring such change. We are expecting lower capital gain rates, lower tax rates, possible repeal of the alternative minimum tax, elimination of some deductions, and possible estate tax changes or even a repeal. While considering likely 2017 changes into year-end decisions makes sense, it's important not to weight them excessively. We are expecting changes based on campaign remarks which usually change once the elected take office.

While little happened in the way of tax legislation in 2016, there are certain tax breaks from which you may benefit and certain strategies that can be employed to help minimize taxable income and your federal tax liability.

For 2016, the **top tax rate of 39.6 percent** will apply to incomes over $415,050 (single), $466,950 (married filing jointly and surviving spouse), $233,475 (married filing separately), and $441,000 (heads of households). However, high-income taxpayers are also subject to the **3.8 percent net investment income tax and/or the .9 percent Medicare surtax.** Finally, as discussed below, there are several tax breaks which expire this year. If you think you may qualify for any one of them, we should nail down what actions need to be taken to get a jump on them before they disappear.

Retirement Plans Considerations

Fully funding your company **401(k)** with pre-tax dollars will reduce current year taxes, as well as increase your retirement nest egg. For 2016, the maximum 401(k) contribution you can make with pre-tax earnings is **$18,000**. For taxpayers **50 or older**, that amount increases to **$24,000**.

If you have a **SIMPLE 401(k)**, the maximum pre-tax contribution for 2016 is **$12,500**. That amount increases to **$15,500** for taxpayers **age 50 or older**.

If certain requirements are met, contributions to an **individual retirement account (IRA)** may be deductible. For taxpayers under 50, the maximum contribution amount for **2016 is $5,500**. For taxpayers **50 or older** but less than age 70 1/2, the maximum contribution amount is **$6,500**. Contributions exceeding the maximum amount are subject to a 6 percent excise tax. Even if you are not eligible to deduct contributions, contributing after-tax money to an IRA may be advantageous because it will allow you to later convert that traditional IRA to a Roth IRA. Qualified withdrawals from a Roth IRA, including earnings, are free of tax, while earnings on a traditional IRA are taxable when withdrawn.

If you already have a traditional IRA, we should evaluate whether it is appropriate to convert it to a Roth IRA this year. You'll have to pay tax on the amount converted as ordinary income, but subsequent earnings will be free of tax. And if you have a traditional 401(k), 403(b), or 457 plan that includes after-tax contributions, a new rule allows you to generally rollover these after-tax amounts to a Roth IRA with no tax consequences. A rollover of a SIMPLE 401(k) into a Roth IRA may also be available. As with all tax rules, there are qualifications that apply to these rollovers that we should discuss before you take any actions.

Alternative Minimum Tax

The alternative minimum tax (AMT) continues to burden more than just high-income taxpayers; middle-income taxpayers can also be affected. Certain deductions taken on your personal tax return - such as personal exemptions, state income taxes, property taxes, miscellaneous itemized deductions - cannot be deducted in calculating the AMT.

If it looks like you may be subject to the AMT this year, we should discuss what actions can be taken to reduce your exposure. Since the calculation of the AMT begins with adjusted gross income, lowering your adjusted gross income by maximizing contributions to a tax-deferred retirement plan (e.g., 401(k)) or tax-deferred health savings account may be appropriate. Additionally, if you use your home for business, related expenses (e.g., a portion of your property taxes, mortgage interest, etc.) allocable to Schedule C will also reduce your adjusted gross income.

Avoiding the Net Investment Income Tax

A 3.8 percent tax applies to certain net investment income of individuals with income above a threshold amount. The threshold amounts are $250,000 (married filing jointly and qualifying widow(er) with dependent child), $200,000 (single and head of household), and $125,000 (married filing separately). In general, investment income includes, but is not limited to: interest, dividends, capital gains, rental and royalty income, non-qualified annuities, and income from businesses involved in trading of financial instruments or commodities. Thus, while the top tax rate for qualified dividend income is generally 20%, the top rate on such income increases to 23.8% for a taxpayer subject to the net investment income tax.

If it appears you may be subject to the net investment income tax (NIIT), the following actions may help avoid the tax. We should discuss whether any of these options make sense in light of your financial situation.

(1) Donate or gift appreciated property. By donating appreciated property to a charity, you can avoid recognizing the appreciation for income tax purposes and for net investment income tax purposes. Or you may gift the property so that the donee can sell it and report the income. In this case, you'll want to gift the property to individuals that have income below the $200,000 (single) or $250,000 (couples) thresholds.

(2) Replace stocks with state and local bonds. Interest on tax-exempt state and local bonds are exempt from the NIIT. In addition, because such interest income is not included in adjusted gross income, it can help keep you below the threshold for which the NIIT applies.

(3) If you are in the real estate business, we should review the criteria for being classified as a real estate professional. If you meet these requirements, your rental income is considered nonpassive and thus escapes the NIIT.

(4) If you intend to sell any appreciated assets, consider whether the sale can be structured as an installment sale so the gain recognition is spread over several years.

(5) Since capital losses can offset capital gains for NIIT purposes, consider whether it makes sense to sell any losing stocks, but keeping in mind the transaction costs associated with selling stocks.

(6) If you have appreciated real property to dispose of and are not considered a real estate professional, a like-kind exchange may be more advantageous. By deferring the gain recognition, you can avoid recognizing income subject to the NIIT.

Because the NIIT does not apply to a trade or business unless (1) the trade or business is a passive activity with respect to the taxpayer, or (2) the trade or business consists of trading financial instruments or commodities, we may want to look at ways in which a venture you are involved with could qualify as a trade or business. However, such classification could have Form 1099 reporting implications whereas personal payments are not reportable.

Liability for the .9 Percent Medicare Tax

An additional Medicare tax of 0.9 percent is imposed on wages, compensation, and self-employment income in excess of a threshold amount. The threshold amounts are $250,000 (joint return or surviving spouse), $125,000 (married individual filing a separate return), and $200,000 (all others). However, the threshold amount is reduced (but not below zero) by the amount of the taxpayer's wages. Thus, a single individual who has $145,000 in self-employment income and $130,000 of wages is subject to the .9 percent additional tax on $75,000 of self-employment income ($145,000 - $70,000 (the $200,000 threshold - $130,000 in wages)). No tax deduction is allowed for the additional Medicare tax.

For married couples, employers do not take a spouse's self-employment income or wages into account when calculating Medicare tax withholding for an employee. If you and your spouse will exceed the $250,000 threshold in 2016 and have not made enough tax payments to cover the additional .9 percent tax, you can file Form W-4 with the IRS before year end to have an additional amount deducted from you paycheck to cover the additional .9 percent tax. Otherwise, underpayment of tax penalties may apply.

New Compliance Requirement for Claiming Educational Tax Credits

Beginning in 2016, in order to claim an American Opportunity or lifetime learning credit or a deduction for education-related tuition and fees, you must have received a Form 1098-T. The form reports qualified tuition and related expenses received by the educational institution. The information reported on this form will be matched against the information reported to the IRS. If you have educational expenses eligible for the credit or deduction, you should receive Form 1098-T from the educational institution to which you made payments by January 31, 2017.

While the form is supposed to report the aggregate amount of payments received by the educational institution, there is a one year transition period where institutions may report the amount billed for 2016 rather than the amount paid.

Because the form only reports qualified tuition and related expenses, you may see a discrepancy between the amounts you paid and the amounts reported. This is due to the fact that certain expenses, such as fees for room, board, insurance, medical expenses, transportation, etc. are not considered qualified tuition and related expenses and thus are not reported on Form 1098-T.

Foreign Bank Account Reporting

If you have an interest in a **foreign bank accounts**, it must be disclosed; failure to do so carries stiff penalties. You must file a Report of Foreign Bank and Financial Accounts (FBAR) if: (1) you are a U.S. resident or a person doing business in the United States; (2) you had one or more financial accounts that exceeded **$10,000** during the calendar year; (3) the financial account was in a foreign country; and (4) you had a financial interest in the account or signatory or other authority over the foreign financial account. If you are unclear about the requirements or think they could possibly apply to you, please let me know.

The deadline for filing the form was moved up and it is now due April 15. However, a six-month extension is available. If an individual is abroad, the due date is automatically extended until June 15, with an additional four-month extension available until October 15.

Penalty for Failing to Carry Health Insurance

Under Obamacare, there is a penalty, known as the "shared responsibility payment," for not having health insurance coverage. **You may be liable for this penalty if you or any of your dependents didn't have health insurance for any month in 2016**. The penalty is 2.5 percent of your 2016 household income exceeding the filing threshold or $695 per adult, whichever is higher, and $347.50 per uninsured dependent under 18, up to $2,085 total per family. Depending on your income, you may be eligible for an exemption from the penalty.

Lower AGI Limitation on Medical Expense Deductions for Individuals 65 or Older

You can deduct medical and dental expenses that exceed a certain percentage of your adjusted gross income (AGI) for the year. In 2016, that percentage is **10 percent** for most taxpayers. However, that floor is reduced to **7.5 percent** if you or your spouse have **turned 65** before the end of the year. Because that reduced AGI floor is scheduled to end after 2016, if this lower limitation applies to you for 2016, you should determine whether you can **accelerate any medical expenses expected to be incurred in 2017 into 2016.**

Deduction for Qualified Tuition and Related Expenses

If your modified adjusted gross income (MAGI) does not exceed a certain amount, **2016 is the last year** that you may deduct qualified education expenses paid during the year for yourself, your spouse, or your dependents. You can deduct up to $4,000, $2,000, or $0 of tuition and fees paid, depending on the amount of your modified adjusted gross income (MAGI). The $4,000 limit applies if your MAGI does not exceed $65,000 ($130,000 on a joint return). The $2,000 limit applies if your MAGI exceeds $65,000 ($130,000 on a joint return) but does not exceed $80,000 ($160,000 on a joint return). No deduction is allowed if your MAGI exceeds $80,000 ($160,000 on a joint return).

Exclusion of Income Relating to Discharge of Indebtedness on a Principal Residence

If there was a discharge of qualified debt relating to your principal residence in 2016, you can exclude such debt from income. **This is the last year this tax break is available**.

Deduction for Mortgage Insurance Premiums

If you paid qualified mortgage insurance this year, it is deductible as qualified residence interest. The insurance must have been paid in connection with acquisition debt for a qualified residence. **No deduction is available** for amounts paid or accrued **after December 31, 2016.**

Last Year for Certain Energy-Related Credits

Some of the following energy-related credits **expire at the end of 2016**. If you think you may be eligible to take any of these credits, we should discuss that when we meet.

Nonbusiness Energy Property Tax Credit. You are entitled to an energy property tax credit if you made certain **energy efficiency improvements** during the year. The **credit is equal to 10 percent** of the amounts you paid for residential energy property expenditures (such as electric heat pumps, central air conditioners, and certain water heaters that achieve specified efficiency ratings), and is equal to the amounts you paid for qualified energy efficiency improvements (such as insulation, exterior windows and skylights, exterior doors, and certain types of roofs) installed during the tax year. There are various limitations, based on the type of property purchased, with a total $500 lifetime limitation on this credit.

Residential Energy Efficient Property Credit. You may be entitled to claim a credit for expenditures made in 2016 on residential energy efficient property. The credit is equal to the sum of **30 percent** of what you paid for certain **solar** electric property (extended through 2019 at 30%), solar water heating property, **fuel cell** property, small **wind energy** property, and **geothermal** heat pump property. While the credit for expenditures made for qualified fuel cell property is limited to $500 for each one-half kilowatt of capacity of the property, the amounts of the other qualified expenditures eligible for the credit are not limited.

*Credits for **Certain Motor Vehicles** and Vehicle-Related Property*. Various credits are available for certain energy efficient vehicles. A credit is available **through 2016** for vehicles propelled by chemically combining oxygen with hydrogen and creating electricity (i.e., fuel cell vehicles). This credit potentially applies to four separate categories of vehicles: (1) fuel cell vehicles, (2) advanced lean burn technology vehicles, (3) hybrid vehicles and (4) alternative fuel vehicles.

The base credit is $4,000 for vehicles weighing 8,500 pounds or less. Heavier vehicles can get up to a $40,000 credit, depending on their weight. An additional $1,000 to $4,000 credit is available to the extent a vehicle's fuel economy exceeds certain fuel economy standards.

Additionally, the purchase of certain refueling property for alternative fuel vehicles may be eligible for a credit of 30 percent of the cost of such property. The credit is limited to $1,000.

Finally, if you acquired a qualified plug-in electric drive motor vehicle during the year, you may be eligible for a credit of up to $7,500. This generally applies to large four-wheel electric vehicles. A separate credit applies to qualified two- or three-wheeled plug-in electric vehicles.

Gifting Appreciated Stock to Kids

If you have children, particularly college age kids, we should consider if there is any **income that can be shifted to them so that the tax on the income is paid at the child's tax rate.** One strategy is gifting appreciated stock to the child. Where a child has earned income and is taxed at the bottom two income brackets, capital gains generated on the stock sale are taxed at 0 percent, instead of the 15 percent or more that the parent would pay. However, if the child has little or no earned income, the **kiddie tax** could be a factor. In this case, you will want to limit the child's unearned income to $2,100 or less for 2016 in order to avoid having your top tax rate apply to the child's income.

Accelerating Income into 2016

Depending on your projected income for 2017, it may make sense to accelerate income into 2016 if you expect 2017 income to be significantly higher. Options for accelerating income include: (1) harvesting gains from your investment portfolio, keeping in mind the 3.8 percent NIIT; (2) converting a retirement account into a Roth IRA and recognizing the conversion income this year; (3) taking IRA distributions this year rather than next year; (4) if you are self-employed and have clients with receivables on hand, try to get them to pay before year end; and (5) settle any outstanding lawsuits or insurance claims that will generate income this year.

Deferring Income into 2017

If it looks like you may have a significant decrease in income next year, it may make sense to defer income into 2017 or later years. Some options for deferring income include: (1) if you are due a year-end bonus, having your employer pay the bonus in January 2017; (2) if you are considering selling assets that will generate a gain, postponing the sale until 2017; (3) delaying the exercise of any stock options; (4) if you are planning on selling appreciated property, consider an installment sale with larger payments being received in 2017; and (5) consider parking investments in deferred annuities.

Deferring Deductions into 2017

If you anticipate a substantial increase in taxable income, it may be advantageous to push deductions into 2017 by: (1) postponing year-end charitable contributions, property tax payments, and medical and dental expense payments, to the extent deductions are available for such payments, until next year; and (2) postponing the sale of any loss-generating property.

Accelerating Deductions into 2016

If you expect a decrease in income next year, accelerating deductions into the current year can offset the higher income this year. Some options include: (1) prepaying property taxes in December; (2) making January mortgage payment in December; (3) if you owe state income taxes, making up any shortfall in December rather than waiting until the return is due; (4) since medical expenses are deductible only to the extent they exceed 10 percent (7.5 percent for individuals age 65 before the end of the year) of adjusted gross income, bunching large medical bills not covered by insurance into one year to help overcome this threshold; (5) making any large charitable contributions in 2016, rather than 2017; (6) selling some or all loss stocks; and (7) if you qualify for a health savings account, setting one up and making the maximum contribution allowable.

Life Events and Miscellaneous Other Items

Certain life events can also affect your tax situation. If you got **married or divorced**, had **a birth or death** in the family, **lost or changed jobs**, or **retired** during the year, we need to discuss the tax implications of these events.

Other miscellaneous items to consider are the following:

(1) Spend any remaining health **flexible spending account** balances before year end (unless your employer allows you to go until March 15, 2017, in which case you'll have until then). You should check with your employer to see if they give employees the optional grace period to March 15.

(2) If you **rent out a vacation home**, we should review at the number of days it was used for business versus pleasure to see if there are ways to maximize tax savings with respect to that property.

(See www.veselycpa.com for tax articles and updates)

Year-End Tax Planning for 2016

BUSINESS

Several significant tax law changes took effect in 2016 that may affect your business's federal tax filings in 2017. As the year draws to a close, we should review these changes, as well as your business's projected taxable income or loss to see what actions might be appropriate before year end to reduce taxes. It's also important to ascertain whether enough estimated taxes have been paid to avoid any underpayment of estimated tax penalties.

Accelerated Filing Deadlines for Forms W-2, W-3, and Form 1099-MISC

The 2017 deadline for filing 2016 electronic and paper Forms W-2 (and related forms) to employees and to the Social Security Administration (SSA) **is <u>January 31, 2017</u>.** Previously, the deadline was the end of February to file paper Forms W-2 with the SSA and until the end of March to make electronic filings.

If you are filing any Forms **1099-MISC and reporting an amount in Box 7, Nonemployee Compensation, the deadline for filing these forms has also been moved up to January 31, 2017.** If you are not reporting an amount in Box 7, the deadline remains February 28 for paper filings and March 31 for electronic filings.

Extensions of time to file Forms W-2 with the SSA are no longer automatic. For filings due on or after January 1, 2017, you may request one 30-day extension and **the IRS will only grant the extension in extraordinary circumstances or catastrophe.** An extension of time to furnish Forms W-2 to employees may be requested by sending a letter to the IRS, but if an extension is for more than 10 employees, the request must be filed electronically. Requests for an extension of time to furnish Forms W-2 to employees are not automatically granted. If approved, an extension will generally be for no more than 15 days from the due date, unless the need for up to a total of 30 days is clearly shown.

Increased Penalties for Failure to Timely File Certain Information Returns

In addition to the accelerated filing deadlines for 2016 Forms W-2, Forms W-3, and Forms 1099-MISC, **higher penalties apply for (1) the failure to file correct Forms W-2 by the due date; (2) the intentional disregard of filing requirements; (3) the failure to furnish Forms W-2; and (4) the intentional disregard of payee statement requirements. In addition to applying to Forms W-2, W-3, and 1099-MISC, other common forms subject to these increased penalties include: Schedules K-1 for Forms 1041, 1065, and 1120S.**

Penalties for the late filing of these information returns have also increased. For each information return or payee statement with respect to which a failure occurs, the **penalty** has increased to **$250**, and the maximum penalty that may be imposed has been increased from **$1,500,000 to $3,000,000. <u>The penalty for intentionally disregard the filing requirements is now $500 PER 1099 FORM NOT FILED</u>.**

Change in Return and Extension Due Dates for C Corporations and Partnerships

In general, **C corporations** with tax years ending in 2016 now have an extra month to file their federal income tax returns. Such **returns are due by the 15th day of the fourth month following the close of the tax year**, rather than the 15th day of the third month following the close of the tax year. Thus, 2016 calendar-year C corporation federal income tax returns are due April 18, 2017, due to April 15 falling on a Saturday and Monday, April 17 being Emancipation Day in the District of Columbia.

A special rule exempts C corporations with fiscal years ending on June 30 from this change until tax years beginning after December. 31, 2025. Thus, the filing deadline for such corporations remains September 15 until 2026 (when it will change to October 15).

Partnerships with tax years ending in 2016 are now required to file their federal income tax returns by the 15th day of the third month following the close of the tax year, rather than the 15th day of the fourth month following the close of the tax year. Thus, 2016 calendar-year partnership federal income tax returns are **due March 15, 2017**.

Along with the changes in tax return deadlines, many of the automatic extension periods have also changed. For calendar year C corporations, the new rules provide for a five-month automatic extension. The extension period is a month shorter, but results in the same September 15 extended deadline for a calendar year C corporation because of the new due date for C corporation returns (i.e., April 15).

For fiscal year C corporations with tax years ending on dates other than June 30, the length of automatic extensions remains unchanged at six months. For fiscal year C corporations with tax years ending on June 30, a special seven-month automatic extension applies for tax years beginning after 2015 and ending before 2026.

While partnerships were previously allowed a five-month extension of time in which to file their tax returns, they are now allowed a six-month extension so that the extended due date is the same as under prior law (i.e. September 15).

The filing deadline for **S corporation** returns remains unchanged, meaning that partnerships and S corporations will now share the same due dates.

Code Sec. 179 Expense Deduction and Bonus Depreciation

Two of the biggest deductions available to a business are the Code **Sec. 179 expense** deduction and bonus depreciation. For 2016, the maximum amount of qualifying property that your business can expense is **$500,000**. That amount is reduced one-for-one to the extent qualifying property purchased **exceeds $2,020,000.**

New for 2016 tax returns, **air conditioners and heating units now qualify** for the Code Sec. 179 expense deduction.

The 50 percent bonus depreciation deduction is again available for 2016. Combined with the Code Sec. 179 deduction, bonus depreciation can provide your business with significant reductions in taxable income. For example, if your business purchased $800,000 of qualifying equipment, the total first year deduction would be $680,000 ($800,000 - $500,000 (maximum

Code Sec. 179deduction) - $150,000 (50% depreciation x remaining basis of $300,000) - $30,000 (normal depreciation of 20% x remaining basis of $150,000).

In addition, if your business filed its 2014 return (or its 2015 short year return) before the enactment of last year's tax extenders bill on December 18, 2015, your business may be able to retroactively elect to take the 50-percent bonus depreciation deduction for qualified property placed in service during the 2015 portion of fiscal years beginning in 2014. If you think you might be eligible, we should meet to discuss the possibility of electing the retroactive bonus depreciation.

Safe Harbor for Deducting Remodeling Costs Incurred by Retail and Restaurant Businesses

Late last year, the IRS provided a safe harbor that allows a **retail or restaurant business** to **deduct 75 percent** of the qualified costs incurred in performing a **remodeling project** on a qualified building. The business **must capitalize the remaining 25 percent** of the costs and recover them through depreciation. Previously, the deductibility of such costs were controversial and the subject of scrutiny in an audit. There are a number of conditions on using this safe harbor so, if you think you have costs that may qualify for this safe harbor, we should review the requirements that must be met in order to deduct such costs.

Increase in De Minimis Repair Amounts That May Be Expensed

Under a safe harbor in the repair and capitalization rules that took effect in 2014, certain amounts that a business pays for tangible property acquired or produced during the tax year **may be deducted**, rather than capitalized, provided certain requirements are met and the cost of the property does not exceed a de minimis amount. **Effective for 2016**, the IRS increased the de minimis amount that is deductible by such businesses from $500 to **$2,500**.

The new $2,500 threshold applies to items substantiated by an invoice. As a result, your business may be eligible to immediately deduct many expenditures that would otherwise need to be spread over a period of years through annual depreciation deductions. Whether you can benefit from this change in the current year depends on your financial picture. In addition, if your business does want to take advantage of the increase in the de minimis limitation, **an election must be made** and the business's **accounting procedures** may need to be modified.

Research Tax Credit Made Permanent

Last year's tax extender legislation permanently extended the popular research tax credit. Additionally, beginning in 2016, small businesses may claim the credit against alternative minimum tax (AMT) liability. Also beginning in 2016, this credit can be utilized by certain qualifying startup businesses against the employer's payroll tax liability.

And, it is worth noting that two taxpayer-favorable court cases rejected IRS attempts to rein in taxpayers' ability to take full advantage of this credit. If you've taken research tax credits in the past couple of years, it may be worthwhile to review the calculation of those credits in light of these cases to see if additional expenses can be claimed based on the court holdings.

Vehicle Deductions and Substantiation

Deductions for **vehicle-related expenses** are an important part of most business tax returns. Whether such **deductions pass scrutiny with the IRS** depends on whether the business complies with the **strict substantiation requirements** necessary for such deductions. With respect to deductions relating to vehicles, we need to ensure that your **business records** include the following information with respect to each vehicle used in the business: (1) the **receipted amount** of each separate expense with respect to the vehicle (e.g., the cost of purchase or lease, the cost of repairs and maintenance); (2) the amount of **mileage for each business or investment use and the total miles for the tax period**; (3) the **date** of the expenditure; and (4) the **business purpose** for the expenditure. The following are considered adequate for substantiating such expenses: (1) **records such as an account book, diary, log, statement of expense, or trip sheets**; and (2) **documentary evidence such as receipts, canceled checks, bills, or similar evidence.**

Records are considered adequate to substantiate the element of an expense only if the records are prepared or maintained in such a manner that each recording of **an element of the expense is made at or near the time the expense is incurred.**

Accountable Plans

By using an accountable plan, your business can reimburse employees for business expenses such as travel, meals, entertainment and other costs without reporting the **reimbursements** as taxable compensation. This can help reduce employment taxes on such payments. However, in order for a plan to be considered an eligible reimbursement plan, it must satisfy certain requirements.

Fringe Benefits

You may want to consider using benefits rather than higher wages to attract employees. However, keep in mind that the **<u>$100 per day, per employee, penalty</u> still applies to many health reimbursement or "health plans" that do not comply with the Affordable Care Act.** Certain fringe benefits paid under a qualified fringe benefit plan are deductible by your business and are not taxable as compensation to the employee, thus avoiding employment taxes that would otherwise be paid on the additional compensation. Retirement plans are particularly attractive to potential employees. By starting a retirement savings plan, you not only help your employees save for the future but also attract and retain quality employees. In addition to providing deductions to your business, a tax credit is available to small employers for the costs of starting a retirement plan.

S Corporation Salaries

For any business operating as an S corporations, it's important to ensure that **shareholders** involved in running the business are paid a **wage amount** that is **commensurate with their workload**. **Distributing profits instead of paying compensation subject to employment taxes is an area that the IRS targets on such returns**. Failing to do so can lead not only to tax deficiencies, but penalties and interest on those deficiencies as well. The key to establishing reasonable compensation **is determining what wage is appropriate on the open market for the work you do for the corporation.**

Last Year for Contractor Credit for Energy Efficient Homes

Eligible contractors have one last chance to claim the energy efficient home credit. A contractor eligible for the energy efficient home credit is any person that constructs a qualifying energy efficient home. The contractor must own and have a basis in the home during its construction. A home qualifies for the energy efficient home credit only if it meets certain energy saving standards. There are two different energy saving standards and the amount of the credit depends on which standard is met. The two standards apply as follows: (1) constructed homes and manufactured homes that meet a 50 percent energy efficient standard qualify for a $2,000 credit; and (2) manufactured homes that meet a 30 percent energy efficient standard qualify for a $1,000 credit. The credit expires on December 31, 2016.

Planning for Revised Partnership Audit Procedures

Effective for partnership tax years beginning after 2017, the current partnership audit procedures will be replaced with a single centralized audit system. While some partnerships may elect out of the new regime, most partnerships will be subject to the new rules. Under the new system, the **IRS will examine a partnership's items of income, gain, loss, deduction, credit and partners' distributive shares for a particular year** of the partnership (i.e., the reviewed year). Any adjustments are taken into account by the partnership, and not the individual partners, in the year that the audit or any judicial review is completed (i.e., the adjustment year). **Thus, it's possible for current year partners to be liable for mistakes or errors committed in prior years when they were not partners.** The new rules provide certain exceptions that can allow current year partners to escape such liability, including an **election that must be made no later than 45 days after the date of a notice of final partnership adjustment.** The bottom line is that partnership agreements should be reviewed and revised to take into account the new audit rules, and that is best done sooner rather than later.

We are here for you if you wish to discuss any of these options, determine whether your tax withholdings and/or estimated tax payments are sufficient for your expected 2016 taxable income and assist with any other tax planning decisions.

With best wishes for the Holiday and year to come,

Jeff

(See www.veselycpa.com for tax articles and updates)