

TAX TIPS & news

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Time to Start Thinking About Year-End Tax Moves

With year-end just around the corner, it is time to think about those last-minute actions you can take to improve your tax situation for 2016. Year-end tax planning is probably something you will want to deal with before the holiday season crush arrives.

There are numerous steps that can be taken before January 1 to save a considerable amount of tax. Not all actions recommended in this article will apply to your particular situation, but you will likely benefit from many of them.

Maximize Education Tax Credits – If you qualify for either the American Opportunity or Lifetime Learning education credits, check to see how much you will have paid in qualified tuition and related expenses in 2016. If it is not the maximum allowed for computing the credits, you can prepay 2017 tuition as long as it is for an academic period beginning in the first three months of 2017. That will allow you to increase the credit for 2016. This technique is especially helpful when a student has just started college in the fall.

Roth IRA Conversions – If your income is unusually low this year, you may wish to consider converting some or all of your traditional IRA into a Roth IRA. The lower income results in a lower tax rate, which provides you an opportunity to convert to a Roth IRA at a lower tax amount.

Don't Forget Your Minimum Required Distribution – If you are over 70.5 years of age and have not taken your 2016 required minimum distribution from your IRA or qualified retirement plan, you should do that before December 31 to avoid possible penalties. If you turned 70.5 this year, you may delay your 2016 distribution until the first quarter of 2017, but that will mean a double distribution in 2017 that will be taxed.

Advance Charitable Deductions – If you regularly tithe at a house of worship or make pledges to other qualified charities, you might consider pre-paying part or all of your 2017 tithing or pledge, thus advancing the deduction into 2016. This can be especially helpful to individuals who marginally itemize their deductions, allowing them to itemize in one year and then take the standard deduction in the next. If you are age 70.5 or over, you can also take advantage of a direct IRA-to-charity transfer, which will count toward your RMD and may even reduce the taxes on your Social Security income.

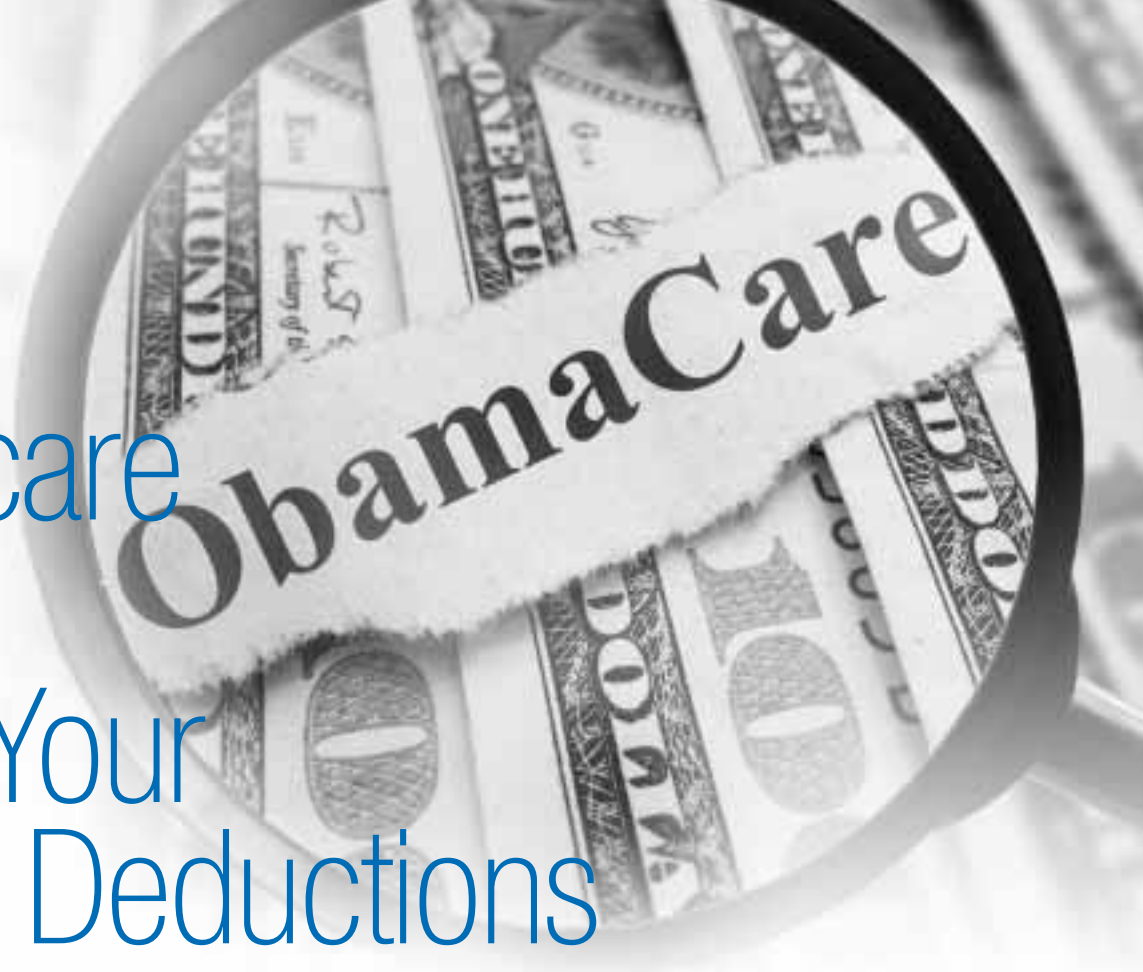
Maximize Health Savings Account Contributions – If you become eligible to make health savings account (HSA) contributions late this year, you can make a full year's worth of deductible HSA contributions even if you were not eligible to make HSA contributions earlier in the year. This opportunity applies even if you first become eligible in December.

Prepay Taxes – Both state income and property taxes are deductible if you itemize your deductions and you are not subject to the AMT. Prepaying them advances the deductions onto your 2016 return. So if you expect to owe state income tax, it may be

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Seniors Beware, Obamacare Will Be Cutting Your Medical Deductions



You are allowed to include medical expenses, reduced by a percentage of your adjusted gross income (AGI), as part of itemized deductions. Back in 2013, as part of the Affordable Care Act, the percentage of AGI that reduces medical expenses was increased to 10% but was retained at 7.5% for taxpayers age 65 and over (and for married seniors if either spouse is age 65 or over). However, this lower percentage of AGI for seniors expires after 2016, which could result in a substantially lower medical deduction for some seniors.

Although there is nothing that can be done about the higher percentage of AGI reduction that begins in 2017, seniors can still take advantage of the lower 7.5% of AGI limit by maximizing their medical deductions for 2016. If you have any unpaid medical expenses, discretionary medical treatments, prescriptions you can stock up on, prescription eyeglasses that need to be replaced, dental work that needs to be done or other medical expenses that you can take care of and pay for in 2016, you may be able to benefit from the 7.5% limit in its last year. Don't go crazy, though – costs of that face-lift or tummy tuck you've been thinking about and other elective cosmetic surgery don't qualify as deductible medical expenses.

You are also cautioned to make sure you will benefit tax-wise by incurring medical expenses ahead of when you normally would. For example, if you ordinarily claim the standard deduction instead of itemizing deductions on your return, accelerating your medical expenses into 2016 may not result in any tax savings for you.

WARNING – Latest IRS Scam



There are reports of taxpayers receiving bogus CP-2000 notices, which duplicate the look of official IRS notices that demand immediate payment. To the untrained eye, they look like real IRS notices. The fake notices ask that payments be made to the Internal Revenue Service (IRS), not to the United States Treasury, as the real ones do. Scams are rampant, and like all of the recent ones, they rely on a taxpayer's fear of the IRS to steal your money. Don't be a victim. Always allow this office to review any notice or other communication you receive before acting on it. You can view a copy of the phony notice at:

<https://www.calt.iastate.edu/sites/default/files/files-page/SCAMletter.pdf>

(Time to Start Thinking About Year-End Tax Moves Cont'd...)

appropriate to increase your state withholding tax at your place of employment or make an estimated tax payment before the close of 2016, and if you are paying your real property taxes in installments, pay the next installment before year-end.

Pay Tax-deductible Medical Expenses – If you have outstanding medical or dental bills, paying the balance before year-end may be beneficial, but only if you already meet the 10% of AGI floor for deducting medical expenses, or if adding the payments would put you over the 10% threshold. You can even use a credit card to pay the expenses, but if you won't be paying off the full balance on the card right away, do so only if the interest expense on the credit card is less than the tax savings. You might also wish to consider scheduling and paying for medical expenses such as glasses, dental work, etc., before the end of the year. See the "Seniors Beware" article if you or your spouse is age 65 and over.

Take Advantage of the Annual Gift Tax Exemption – You can give \$14,000 to each of an unlimited number of individuals without paying gift tax each year, but you can't carry over unused amounts from one year to the next. (The gifts are not tax deductible.)

Avoid Underpayment Penalties – If you are going to owe taxes for 2016, you can take steps before year-end to avoid or minimize the underpayment penalty. The penalty is applied quarterly, so making a fourth-quarter estimated payment only reduces the fourth-quarter penalty. However, withholding is treated as paid ratably throughout the year, so increasing withholding at the end of the year can reduce the penalties for the earlier quarters.

There are additional factors to consider for a number of the strategies suggested above, and you are encouraged to contact this office prior to acting on any of the advice to ensure that you will benefit given your specific tax circumstances.

Some 2016 Refunds to Be Delayed

The IRS, as required by a late 2015 tax law change and in an effort to combat tax fraud, will not be issuing tax refunds for any 2016 returns that include an earned income tax credit (EITC) or refundable child tax credit (CTC) before February 15, 2017, even if the return was e-filed earlier.

A long-standing problem has been Internet thieves filing returns with stolen IDs and counterfeit W-2s just as the IRS opens e-filing in the later part of January and before employers are required to file W-2s. Delaying payment of these refunds will give the IRS the opportunity to verify income and withholding tax on W-2s reported on a tax return before issuing the refund.

This means refunds will be issued up to a month later than in past years for early-filing taxpayers claiming the credits mentioned, so be prepared for delays.



Little-Known Tactic Increases Child Care Credit

When both spouses in a married couple are jointly involved in the operation of an unincorporated business (generally a Schedule C), it is fairly common – but incorrect – for all of that business's income to be reported as just one spouse's income, even when they both work in the business.

In such cases, the spouse not taking credit for his or her portion of the earned income loses out on the chance to accumulate his or her own eligibility for Social Security benefits. In addition, to claim a child care credit, both spouses on a joint return must have earned income (or imputed income if one of the spouses is a full-time student or is disabled), so unless the spouse not including a portion of the income from the joint business has another source of earned income, the couple will not be allowed a child care credit.

There are ways to remedy this situation, however. One option is to file a partnership return for the activity, in which case each spouse will receive a K-1 that reports his or her share of the net profit. An approach that avoids the necessity of filing a partnership return, and that is probably less complicated, is a qualified joint-venture election, in which each spouse elects to file a separate Schedule C for his or her respective share of the business. This gives both spouses self-employed income for the purposes of the self-employment tax and for claiming the child care credit.

A qualified joint venture refers to any joint venture involving the conduct of a trade or business if:

- (1) The only members of the joint venture are husband and wife,
- (2) Both spouses materially participate in the trade or business, and
- (3) Both spouses elect to apply this rule.

Generally, to meet the material participation requirement, each spouse will have to participate in the activity for 500 hours or more during the tax year.

If the net income from the business exceeds the annual cap on income subject to the Social Security tax, the combined self-employment tax for the spouses with split Schedule Cs will exceed what a single spouse would have paid if he or she had filed a single Schedule C.

An additional benefit when filing split Schedule Cs is the opportunity for both spouses to participate in IRAs and self-employed retirement plans.

November-December 2016: It's time for 2016 year-end and 2017 tax planning. Please call for an appointment.

December 31, 2016: Last day to pay deductible expenses for 2016. This doesn't apply to IRA, SEP, or Keogh contributions, which can be made after December 31, 2016.

- Last day to set up a Keogh Retirement Account if you plan to make a 2016 contribution. ⁽¹⁾
- For individuals who turned 70½ during 2015 or in a prior year, this is the last day to withdraw the required minimum distribution (RMD) from their IRA for 2016. ⁽¹⁾
- Last day for small business owners to establish an accounting procedure allowing them to elect up to a \$2,500 de minimis expense deduction for 2017.

January 1, 2017: The first day for 2017 health insurance coverage. Unless exempt, individuals and families without qualified coverage may incur penalties on their 2017 tax returns.

January 17, 2017: Fourth-quarter 2016 federal individual estimated tax payment is due, unless the 2016 return is filed by January 31, 2017, and the entire balance due is paid with the return. ⁽²⁾

January 31, 2017: The Open Enrollment period for purchasing 2017 health care coverage through a Marketplace ends. If you don't enroll in a 2017 plan by January 31, 2017, you can't enroll in a health insurance plan through a Marketplace for 2017 unless you qualify for a Special Enrollment Period.

January 31, 2017: Deadline for businesses to provide 1099-MISCs (nonemployee compensation payments - box 7) and W-2s to the people they paid during 2016. This is also the due date ⁽³⁾ for filing these forms with the government. The 1099-MISC forms are required if the business paid \$600 or more for the services of individuals (other than employees) during the year.

February 28, 2017: This is the deadline for filing paper 2016 Forms 1099 (other than 1099-MISC forms that were due January 31, 2017).

March 1, 2017: This is the last day for a farmer or fisherman who owed, but did not pay, estimated tax by January 17, 2017, to file a 2016 calendar-year income tax return to avoid a late payment penalty.

March 15, 2017: Due date ⁽²⁾ for filing 2016 calendar year partnership returns or request an extension. ⁽³⁾

March 31, 2017: If filed electronically, this is the deadline for filing 2016 Forms 1099 (other than 1099-MISC forms that were due January 31, 2017).

April 1, 2017: This is the last day for taxpayers who turned 70½ during 2016 to withdraw their IRA RMD for 2016.

April 15, 2017: For individuals with an interest in, or a signature authority over a foreign financial account, this is the due date ⁽²⁾ for filing form FinCEN 114 (FBAR) with the U.S. Government or to file an extension.

April 18, 2017: Deadline for -

- Individuals to file a 2016 federal income tax return or request a filing extension. ⁽³⁾
- Fiduciaries of estates and trusts to file a 2016 calendar-year income tax return or request an extension.
- Paying the first installment of the 2017 federal individual estimated tax. ⁽³⁾
- The first installment of the 2016 defined benefit pension plan contributions.

(1) This is a Saturday. Many financial institutions are not open on weekends; make arrangements in advance. (2) This is an earlier due date than prior years. (3) Some states have different due dates.

Tax Calendar

TAX TIPS & news

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The purpose of this newsletter is to provide current information on tax, financial and business developments. It suggests general tax planning ideas that may only be appropriate when claiming tax benefits in a manner consistent with the statutes and Congressional purpose. The information and opinions are generalizations and may not apply to all taxpayers and cannot be used by a taxpayer for the purpose of avoiding penalties that may be imposed on the taxpayer. Therefore, it is important that you seek appropriate advice before implementing any of the ideas suggested.

You Asked: I am 60 years old and thinking about retirement. However, I am concerned whether I have enough financial resources to make the move now. Do you have any guidelines?

Answer: Generally, retirees need between 70 and 80 percent of their pre-retirement salary to maintain their current standard of living once they retire. This includes income from company pension plans, Social Security benefits, your own retirement plans such as IRAs, 401(k) plans, etc., and other investments. Do you plan to stay in your existing home or are you planning to downsize? Downsizing and relocating may provide additional cash and reduce expenses. How is your health, and do you have reasonable medical coverage? Most workers can't collect Social Security benefits until age 62 or have Medicare coverage until age 65. What will supplement those benefits until you are eligible? These are some of the major concerns that need to be considered.

You Asked: I am a co-owner with another unrelated individual of a house that is our home. We purchased it a little over a year ago and it needed a lot of TLC. With hard work we have fixed it up. However, the other co-owner now has to move because of a company transfer and wants to sell the home. It is now worth considerably more than we paid for

it, but we will not have owned and lived in it the required two years. Will I end up paying taxes on the gain?

Answer: A homeowner who is required to sell a home because of a job move (at least 50 miles) is entitled to a reduced prorated gain exclusion. For example, if the home was owned and occupied one year (half the required time) prior to the sale, then the reduced exclusion would be \$125,000 (half of \$250,000). The law also allows a co-owner to claim the same partial exclusion.

You Asked: I am a working mother. My child attends kindergarten in the morning and goes to an after-school care program for the remainder of the day. What portion of my expenses for kindergarten and after-school care can be used toward the child care credit?

Answer: Per IRS regulations, expenses for programs at the level of kindergarten and above aren't employment related and thus don't count toward child care expenses. However, those same regulations do allow expenses for before- and after-school care of a child in kindergarten or a higher grade (up to age 13), as well as nursery, preschool, or similar programs below the kindergarten level.



Since You Asked...