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## Immediate Tax Benefits for Business Property

Section 179 provides generous tax break

There is a unique tax break for business entities of all shapes and sizes contained in Section 179 of the Internal Revenue Code. Under this section, a business can elect to “expense,” or currently deduct, the cost of qualified property placed in service during the year, up to a maximum level. It is near-instant tax gratification.

Although the maximum deduction has increased in recent years, it became an annual rite of passage for Congress to extend the most recent generous amount. Now the Protecting Americans from Tax Hikes (PATH) Act of 2015 has ended the uncertainty. Under the PATH Act, the maximum deduction of \$500,000 is permanently preserved, subject to inflation indexing.

Background: When your business buys certain property (e.g., equipment or machinery), it generally can recover the costs over time through depreciation deductions. For instance, if your company buys computers for the business, it may be able to write off the cost over five years. Other types of business property have longer recovery periods.

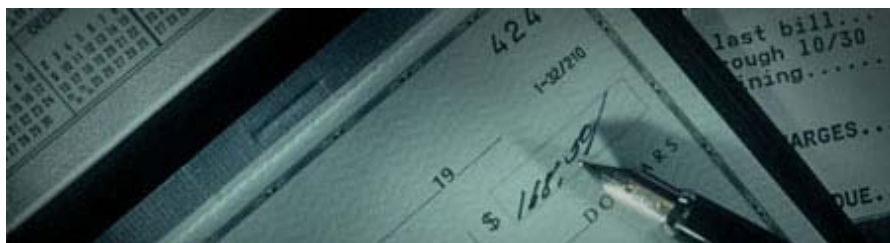
With Section 179, you do not have to wait as long. This provision enables you to claim a deduction of up to \$500,000 in the year the property is placed into service (indexed to \$510,000 in 2017). Furthermore, the Section 179 election is wide open to most business taxpayers—ranging from corporate heavyweights to self-employed individuals—but two important rules may limit annual deductions.

1. Annual business income limit: The expensing deduction cannot exceed the net taxable income from all the businesses you actively operate. For this purpose, net income is figured without regard to expensing, the 50% deduction for self-employment tax and any net operating loss (NOL) carryforwards or carrybacks.
2. Annual dollar cap: If the total cost of qualified property placed in service during the year exceeds an annual threshold, the maximum expensing allowance is reduced on a dollar-for-dollar basis. In the past, this dollar threshold was increased in lockstep with the maximum Section 179 allowance. However, the threshold was set at the lofty figure of \$2 million by the PATH Act, subject to inflation indexing. The indexed amount for 2017 is \$2.03 million. While this reduction rule does not affect many small businesses, you still should be aware of it.

Taxes are an important factor when you consider purchases of business property. Make sure you are aware of how the two tax law limits may affect your Section 179 deductions this year.

In addition, other special rules may apply to specific types of business property, such as vehicles. Generally, there is a \$25,000 cap on deductions for heavy-duty vehicles used in business, and there are other annual limits for “luxury cars.”

Finally, a proposal by the new Trump administration would double the maximum \$500,000 Section 179 allowance to \$1 million, as a stimulus for business growth and expansion.



*Stay abreast of any developments regarding the maximum allowance. You can rely on your professional tax advisers to provide guidance as you proceed.*

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## How to Bridge a Retirement Shortfall

Practical ideas for closing the gap

People are living longer these days than they did five, 10 or 20 years ago. Of course, that is good news, but it also means that you may have to provide a bigger cushion in retirement than you had initially intended. What's more, uncertainty over future Social Security benefits as baby boomers continue to swell the rolls adds to the concerns. As a result, you could face a personal shortfall, especially if you incur unforeseen expenses from a medical condition or some other situation.

What should you do? The first thing is not to panic. Even if retirement is imminent, you may be able to make up lost ground quickly or take other steps to protect yourself. Here are several practical ideas to consider.

- Ramp up your retirement savings. For example, if you participate in a 401(k) plan where you work, you can generally defer up to \$18,000 to the plan in 2017. This figure is increased to \$24,000 for those who are age 50 or older. Just a few years of contributions at or near the maximum level can significantly bolster your account.
- Work on the budget. Now that you are aware of a potential shortfall, you might want to dial down your expectations. Make realistic estimates of your expected income and the expenses going out. Although you will likely pay less for housing (see below) and other items such as life insurance—especially if your children are already adults—consider the impact of potential increases in some expenses, such as travel.
- Move to a smaller home. For most people, housing is the largest overall cost, representing on average more than one-third of overall spending. If your children have flown the coop but you're still living in the large home where you raised them, it may be time to downsize. In addition, you might want to move to a state with a different climate, taking state income taxes into account. Of course, various other factors—such as proximity to family and personal preferences—will come into play.
- Refinance your current home. If you decide to stay put, you should probably refinance your existing mortgage if you're paying a rate higher than the current rates. At the beginning of 2017, mortgage rates are at near-historic lows. Even if rates rise slightly, as projected, you may save tens of thousands of dollars over time by refinancing. Note that your interest payments will generally continue to be tax-deductible.
- Do not quit for good. Just because you've reached retirement age does not mean you have to stop working completely. If needed, you could pursue part-time employment, preferably in a line of work you enjoy. For some individuals, working full time a little longer is also a viable option.

*Because everyone's situation is different, not all of these ideas may be right for you. The most important thing is to assess your financial status and go forward from there.*

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## Do You Have to Pay the NII Tax?

Computing tax liability on 2016 returns

As the deadline for filing 2016 tax returns approaches, some taxpayers are still struggling with the rules for the 3.8% tax on "net investment income" (NII). The tax law provision authorizing this special tax was included in the Affordable Care Act (ACA), the law known as Obamacare. Although the ACA may be repealed by the new Trump administration, it would not likely be retroactive to 2016.

Basic premise: The 3.8% tax applies to the lesser of your NII or the amount by which your modified adjusted gross income (MAGI) exceeds an annual threshold of \$200,000 for single filers and \$250,000 for joint filers. The tax is also imposed on trusts and estates with income above the threshold, based on the dollar amount of the highest tax bracket.

For this purpose, NII includes interest and dividends; distributions from annuities (other than tax-deferred distributions); rent and royalties; gains from investments in passive activities; trades of financial instruments and commodities; and net capital gain from the sale of property (other than property held in an active trade or business). Significantly, it does not include salary or wages; distributions from IRAs and qualified retirement plans; taxable Social Security income; active trade or business income; self-employment income; gain on the sale of active interests in a partnership, S corporation or limited liability company; income from tax-exempt municipal bonds; and tax-deferred income from nonqualified annuities.

In some cases, taxpayers may owe the tax based on NII, in other cases tax based on the excess MAGI and in still others they may not have to pay the tax at all.

Example 1: Alice is a single filer with NII of \$25,000 in 2016. When she completes her 2016 return, she determines that her MAGI is \$250,000. Because the NII of \$25,000 is less than the excess MAGI of \$50,000, Alice has to pay a tax of \$950 (3.8% of \$25,000).

Example 2: Bob is a single filer with NII of \$40,000 in 2016. When he completes his 2016 return, he determines that his MAGI is \$220,000. Because the excess MAGI of \$20,000 is less than the NII of \$40,000, Bob has to pay a tax of \$760 (3.8% of \$20,000).

Example 3: Carol and Ted are joint filers with NII of \$100,000 in 2016. When they complete their 2016 return, they determine that their MAGI is \$225,000. Because their MAGI does not exceed the threshold, Carol and Ted do not have to pay the 3.8% tax.

If you owe the tax for 2016, there is not much you can do about it now. Going forward, you may consider several strategies for reducing NII and/or MAGI, including postponing large capital gains, selling real estate on an installment basis, investing in tax-free municipal bonds, converting assets in a traditional IRA to a Roth IRA in a low tax year and using a charitable remainder trust, just to name a few.

*Coordinate these strategies with assistance from your professional advisers. We will keep you posted on any significant developments.*

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## Getting Personal About Personal Exemptions

Tax return benefits for the family

Are you entitled to personal and dependency exemptions on your tax return? It might be the last year you can claim the exemption for someone—say, a child graduating from college—or exemptions may be eliminated altogether by tax reforms that could be coming in conjunction with proposed rate cuts. At the very least, however, the exemptions are still available on 2016 returns.

Basic rules: Every taxpayer is entitled to claim a personal exemption for himself or herself, plus an exemption for a spouse if filing a joint tax return. The exemption amount, which is indexed annually, is \$4,050 for 2016. (It will remain the same in 2017.) In addition, you may claim exemptions for each one of your qualified dependents.

To qualify for a dependency exemption, you must meet all four of the following requirements:

- You are not a dependent of another taxpayer. Individuals who are dependents are not eligible to claim dependents.
- The individual being claimed as a dependent cannot be married and filing a joint return. Exception: A married person can file a joint return and still be claimed as a dependent if the joint return claims only a refund of tax withholding or estimated tax payments and there would be no tax liability for either spouse if they had filed separate returns.
- The individual being claimed as a dependent is a citizen, national or resident alien of the United States, or a resident of Canada or Mexico.
- The dependent meets the definition of being either a qualifying child or a qualifying relative.

Generally, this means that you must provide more than half the annual support being provided to the individual being claimed as a dependent and that person must have less than the personal exemption amount in gross income subject to tax. For a child who is younger than age 19 or a full-time student younger than age 24, the gross income part of the test does not apply.

Key rules: Under the “personal exemption phaseout” (PEP) rule, the total amount of personal exemptions you may claim, including any dependency exemptions, is reduced by 2% for each \$2,500 or portion thereof that your adjusted gross income (AGI) exceeds a specified dollar threshold. For 2016 returns, the threshold is \$259,400 for single filers and \$311,300 for joint filers.

The PEP rule was recently reinstated by the American Taxpayer Relief Act (ATRA) of 2012. At the same time, using the same phaseout ranges, ATRA revived a companion tax provision reducing itemized deductions for high-income taxpayers. Both of these tax rules could have an impact on your 2016 return.

*Reminder: When possible, maximize the available tax benefits on your personal 2016 return by obtaining expert guidance. Do not leave any tax-saving opportunities to chance.*

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## Facts and Figures

Timely points of particular interest

**Business Alliances**—How can you grow your business in 2017? One idea to consider is a business alliance. This is a formal business arrangement between two or more organizations to achieve shared business objectives. This includes joint ventures, franchising, cross-licensing and cross-marketing activities. There are numerous pros and cons to consider, so obtain expert advice.

**Higher Wage Base**—The Social Security Administration has announced that the wage base for Social Security tax purposes is increasing from \$118,500 in 2016 to \$127,200. This significant jump of \$8,700 is based on changes in the Consumer Price Index. However, the tax rate remains at 6.2% on wages up to the wage base and 1.45% on all additional wages.

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## Time Running Out on FSAs

Generally, amounts left over in a flexible spending account (FSA) for health care or dependent care expenses are forfeited at the end of the year. But some companies allow a 2½-month “grace period.”

The grace period for FSAs in 2016 ends on March 15, 2017. If possible, empty out your FSAs by then. Alternatively, an employer may arrange to carry over up to \$500 of a remaining balance.

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