

Tax-Saving Tips

December 2018

2018 Last-Minute Section 199A Strategies

Starting now, this year (2018), you have to consider your Section 199A deduction in your year-end tax planning. If you don't, you could end up with a big fat \$0 for your deduction amount.

If your taxable income is above \$157,500 (or \$315,000 on a joint return), then your type of business, wages paid, and property can reduce and/or eliminate your Section 199A tax deduction.

Strategy 1: Harvest Capital Losses

Capital gains add to your taxable income, and taxable income is the income that

- determines your eligibility for the Section 199A tax deduction,
- sets the upper limit (ceiling) on the amount of your Section 199A tax deduction, and
- establishes the thresholds above which you need wages and/or property to obtain your maximum deductions.

If the capital gains are hurting your Section 199A deduction, you have time before the end of the year to harvest capital losses to offset those harmful gains.

Strategy 2: Make Charitable Contributions

Since the Section 199A deduction uses taxable income for its thresholds, you can use itemized deductions to reduce and/or eliminate threshold problems and increase your Section 199A deduction.

Charitable contribution deductions are the easiest way to increase your itemized deductions before the end of the year.

Consider doing one or both of the following:

- Donate appreciated stock.
- Prepay (before December 31) your planned 2019 charitable contributions so you can claim them as deductions this year.

Strategy 3: Make Retirement Contributions

Any retirement contributions you make directly reduce your taxable income—and you still have the money inside the retirement account, growing free of taxes until you take it out of the account.

If you are a sole proprietor, your retirement contributions don't reduce your qualified business income (QBI). Therefore, as long as your QBI is the basis for your Section 199A deduction, you can put away as much as you want using a traditional IRA, SIMPLE IRA, SEP-IRA, or individual 401(k) without damaging your Section 199A deduction.

If you are an S corporation owner, your retirement strategy can achieve the same result as the proprietor's by using an employee salary or wage contribution to the retirement plan and no contribution by the S corporation.

Strategy 4: Buy Business Assets

Thanks to 100 percent bonus depreciation and Section 179 expensing, you can write off the entire cost of most assets you buy and place in service before midnight, December 31, 2018.

This can help your Section 199A deduction in two ways:

1. The big asset purchase and write-off can reduce your taxable income and increase your Section 199A deduction when the write-off gets your taxable income under the threshold.
2. The big asset purchase and write-off can contribute to an increased Section 199A deduction if your Section 199A deduction currently uses the calculation that includes the 2.5 percent of unadjusted basis in your business's qualified property (UBIA). In this scenario, your asset purchases increase your UBIA, which in turn increases the deduction you already depend on.

2018 Last-Minute Year-End General Business Deductions

Your year-end tax planning doesn't have to be hard. Outlined below are five strategies that will increase your tax deductions or reduce your taxable income so that Uncle Sam gets less of your 2018 cash.

1. Prepaying your 2019 expenses right now reduces your taxes this year, without question. While it's true you kicked the can down the road some, perhaps you have an offset with a big deduction planned for next year. And even if you don't have such a plan at the moment, you have plenty of time to create one or to put more big deductions in place for 2019.
2. The easiest year-end strategy of all is simply to stop billing your customers, clients, and patients. Once again, this kicks the can down the road some and makes your 2019 tax planning more important.
3. With 100 percent bonus depreciation and increased Section 179 expensing in 2018, you can make significant purchases of equipment, machinery, and furniture and write off 100 percent of the value. Make sure you place the assets in service on or before midnight, December 31, 2018, to get the deduction this year.
4. Charges to your credit cards can create deductions on the day of the charge. This is absolutely true if you are a sole proprietor or you operate as a corporation and the credit card is in the name of the corporation. But if you operate as a corporation and the credit card is in your personal name, your corporation needs to reimburse you before midnight, December 31, to create the 2018 deduction at the corporate level.
5. And finally, claim all your legitimate deductions. Don't think you have too many, and don't try to guess which of your too-many deductions could be a red flag. First, it's unlikely you could have enough deductions to create a red flag. Second, no one knows what those red flags are. Third, if the deduction is legitimate, it doesn't matter if the IRS audits it—you'll win.

As you can see from the five strategies above, there's much you can do to control your tax bite.

2018 Last-Minute Year-End Tax Strategies for Your Stock Portfolio

The beauty of tax planning your year-end stock portfolio is that it might cost you pennies in commissions but allow you to pocket real money.

Here's the basic strategy:

- Avoid the high taxes (up to 40.8 percent) on short-term capital gains and ordinary income.
- Lower the taxes to zero—or if you can't do that, then lower them to 23.8 percent or less by making the profits subject to long-term capital gains.

Think of this: you are paying taxes at a 71.4 percent higher rate when you pay at 40.8 percent rather than the tax-favored 23.8 percent.

Strategy 1

Examine your portfolio for stocks that you want to unload, and make sales where you offset *short-term* gains subject to a high tax rate such as 40.8 percent with *long-term* losses (up to 23.8 percent). In other words, make the high taxes disappear by offsetting them with low-taxed losses, and pocket the difference.

Strategy 2

Use *long-term* losses to create the \$3,000 deduction allowed against ordinary income. Again, you are trying to use the 23.8 percent loss to kill a 40.8 percent tax (or a 0 percent loss to kill a 12 percent tax, if you are in the 12 percent or lower income tax bracket).

Strategy 3

As an individual investor, avoid the wash-sale loss rule. Under the wash-sale loss rule, if you sell a stock or other security and purchase substantially identical stock or securities within 30 days before the date of sale or after the date of sale, you don't recognize your loss on that sale. Instead, the code makes you add the loss amount to the basis of your new stock.

If you want to use the loss in 2018, then you'll have to sell the stock and sit on your hands for more than 30 days before repurchasing that stock.

Strategy 4

If you have lots of capital losses or capital loss carryovers and the \$3,000 allowance is looking extra tiny, sell additional stocks, rental properties, and other assets to create offsetting capital gains. If you sell stocks to purge the capital gains, you can immediately repurchase the stock after you sell it—there's no wash-sale "gain" rule.

Important. Don't die with large capital loss carryovers—they'll disappear.

- If your carryover originated from you only, then it all goes away if not used on your joint return in the year of your death.
- If your carryover came from joint assets, then your surviving spouse gets 50 percent of the carryover to use going forward.

Strategy 5

Do you give money to your parents to assist them with their retirement or living expenses? How about children (specifically, children not subject to the kiddie tax)? If so, consider giving appreciated stock to your parents and your non-kiddie-tax children. Why? If the parents or children are in lower tax brackets than you are, you get a bigger bang for your buck by

- gifting them stock,
- having them sell the stock, and then
- having them pay taxes on the stock sale at their lower tax rates.

Strategy 6

If you are going to make a donation to a charity, consider appreciated stock rather than cash because a donation of appreciated stock gives you more tax benefit. It works like this:

- **Benefit 1.** You deduct the fair market value of the stock as a charitable donation.
- **Benefit 2.** You don't pay any of the taxes you would have had to pay if you sold the stock.

Strategy 7

If you could sell a publicly traded stock at a loss, *do not* give that loss-deduction stock to a 501(c)(3) charity. Why? If you sell the stock, you have a tax loss that you can deduct. If you give the stock to a charity, you get no deduction for the loss—in other words, you can just kiss that tax-reducing loss goodbye.

Solution. Sell the stock first to create your tax-deductible loss. Then give the charity the cash realized from your sale of the stock to create your deduction for the charitable contribution.

2018 Last-Minute Vehicle Purchases to Save on Taxes

Two questions:

1. Do you need a replacement business car, SUV, van, or pickup truck?
2. Do you need tax deductions this year?

If you answered “yes” to both questions, here are some ideas for you to consider:

1. Buy a New or Used SUV, Crossover Vehicle, or Van with a GVWR Greater than 6,000 Pounds

Let’s say that on or before December 31, 2018, you or your corporation buys and places in service a new or used SUV or crossover vehicle that the manufacturer classifies as a truck and that has a gross vehicle weight rating (GVWR) of 6,001 pounds or more. This newly purchased vehicle gives you four big benefits:

1. Bonus depreciation of 100 percent (new, thanks to the TCJA)
2. Section 179 expensing of up to \$25,000
3. MACRS depreciation using the five-year table
4. No luxury limits on vehicle depreciation deductions

2. Buy a New or Used Pickup with a GVWR Greater than 6,000 Pounds

If you or your corporation buys and places in service a qualifying pickup truck (new or used) on or before December 31, 2018, then this newly purchased vehicle gives you four big benefits:

1. Bonus depreciation of 100 percent
2. Section 179 expensing of up to \$1,000,000
3. MACRS depreciation using the five-year table
4. No luxury limits on vehicle depreciation deductions

To qualify for full Section 179 expensing, the pickup truck must have

- a GVWR of more than 6,000 pounds, and
- a cargo area (commonly called a “bed”) of at least six feet in interior length that is not easily accessible from the passenger compartment.

Short bed. If the pickup truck passes the more-than-6,000-pound-GVWR test but fails the bed-length test, tax law classifies it as an SUV. That’s not bad. It’s still eligible for the \$25,000 SUV expensing limit plus 100 percent bonus depreciation. See Section 1 above for how this works.

3. Buy a New or Used Qualifying Cargo or Passenger Van with a GVWR Greater than 6,000 Pounds

A new or used cargo or passenger van bought and placed in service on or before December 31, 2018, can qualify for four big tax benefits:

1. Bonus depreciation of 100 percent
2. Section 179 expensing of up to \$1,000,000
3. MACRS depreciation using the five-year table
4. No luxury limits on vehicle depreciation deductions

Cargo van. To qualify for full Section 179 expensing, the cargo van must

- have a GVWR of more than 6,000 pounds,
- fully enclose the driver compartment and load-carrying area,
- not have seating behind the driver's seat, and
- have no body section that protrudes more than 30 inches ahead of the leading edge of the windshield.

If the van passes the GVWR test but fails one of the other qualifying tests listed above, the law deems it an SUV.

Passenger van. If the van has a GVWR of greater than 6,000 pounds and seats more than nine people behind the driver's seat, it is a tax law-defined passenger van, not an SUV, and it qualifies for full Section 179 expensing of up to \$1,000,000 and 100 percent bonus depreciation.

4. Buy a Depreciation-Limited New or Used Car, SUV, Truck, or Van

If you or your corporation buys and places in service a new or used passenger vehicle such as a car (or a pickup, SUV, or van with a GVWR of 6,000 pounds or less) on or before December 31, 2018, then you or your corporation may claim up to \$8,000 in bonus depreciation.

Tax reform increased the 2018 luxury passenger vehicle depreciation limits to

- \$10,000 for the first taxable year in the recovery period,
- \$16,000 for the second taxable year in the recovery period,
- \$9,600 for the third taxable year in the recovery period, and
- \$5,760 for each succeeding year in the taxable period.

Here's how this works: Say you buy a car. You add the \$8,000 in bonus depreciation to the \$10,000 car limit, for a 2018 limit of \$18,000. To get to this limit, you can use a combination of bonus depreciation and regular depreciation. You reduce the \$18,000 limit by any personal use.

2018 Last-Minute Year-End Tax Deductions for Existing Vehicles

It's time to examine your existing cars, SUVs, trucks, and vans for some profitable year-end business tax deductions. Your first step is to identify your gain or loss on sale. Once you have the gain or loss, know these basic rules:

- Gains attributable to depreciation produce ordinary income.
- Gains in excess of original basis produce capital gains. (This is unlikely to happen on most business vehicles, but it can happen with classic and antique business vehicles because they can go up in value.)
- Losses on business vehicles produce ordinary deductions.

In general, at this time of year we suspect you are looking for vehicle loss deductions, so that's where we will look.

1. Take Your Child's Car and Sell It

We know. This sounds horrible. But stay with us. What did you do with your old business car? Do you still have it? Is your child driving it? Or perhaps your spouse has it as a personal car.

We ask because that old business vehicle could have a big tax loss embedded in it. If that loss is inside that old business vehicle, your strategy is easy. Take the vehicle and sell it to a third party before December 31 so that you have a tax-deductible loss this year.

Your loss deduction depends on your percentage of business use. That's one reason to sell this vehicle now: the longer you let your spouse or teenager use it, the smaller your business percentage becomes and the less tax benefit you receive.

2. Self-Employed? Use the Buy-and-Sell Strategy

Now, thanks to the TCJA tax reform, all business vehicles have gain or loss on sale or trade-in. Here's how the strategy works:

- The sale to a third party or the "trade-in sale" of your existing business vehicle produces a gain or loss that does not increase or decrease your self-employment taxes.
- The purchase of the replacement vehicle creates depreciation and, if elected, Section 179 expensing deductions. These deductions reduce your self-employment taxes. (Note: This is also true with IRS mileage rates because such rates include depreciation as a component.)

3. Cash In on Past Vehicle Trade-Ins

In the past (before 2018) when you traded vehicles, you pushed your old business basis to the replacement vehicle under the old Section 1031 tax-deferred exchange rules. (But remember—this rule doesn't apply any longer to Section 1031 exchanges of vehicles or other personal property occurring after December 31, 2017.)

Regardless of whether you used IRS mileage rates or the actual expense method for deducting your business vehicles, you could find a big deduction here. Check out how Sam finds a \$27,000 tax-loss deduction on his existing business car. Sam has been in business for 11 years, during which he

- converted his original personal car to business use;
- then traded in the converted car for a new business car (car 2);
- then traded in car 2 for a replacement business car (car 3); and
- then traded in car 3 for another replacement business car (car 4), which he is driving today.

During the 11 years Sam has been in business, he has owned four cars. Further, he deducted each of his cars using IRS standard mileage rates. To get a mental picture of how this one sale produces a cash cow, consider this: when Sam sells car 4, he is really selling four cars—because the old Section 1031 exchange rules added the old basis of each vehicle to the replacement vehicle's basis.

Examine your car for this possible loss deduction. Have you been trading business cars? If so, your loss could be big!

4. Put Your Personal Vehicle in Business Service

Lawmakers reinstated the 100 percent bonus depreciation for 2018, and that creates an effective strategy that costs you nothing but can produce solid deductions. Are you (or your spouse) driving a personal vehicle? If so, you can convert this vehicle to business use before December 31 and qualify it for some hefty bonus-depreciation deductions.

2018 Last-Minute Year-End Medical and Retirement Deductions

When you get busy with your business, it's easy to forget about your retirement accounts and medical coverages and plans. But year-end is approaching, and now's the time to take action.

Included below are six action steps for 2018 that can help you reduce your taxes and pocket extra money.

1. Put your retirement plan in place no later than December 31 so you are absolutely sure that you have a plan. In fact, be sure to make a contribution to the plan before December 31.
2. Convert to a Roth IRA. The long-term savings here can be huge. Make sure to leave the converted funds in the Roth for at least five years.
3. If you have a Section 105 plan in place and you have not been reimbursing expenses monthly, do a reimbursement now to get your 2018 deductions, and then put yourself on a monthly reimbursement schedule in 2019.

4. If you have not reimbursed your qualified small employer health reimbursement account (QSEHRA), make sure to get that done properly now. If you have not yet put a QSEHRA in place and you plan to do so on January 1, do that now and just suffer that \$50-per-employee penalty should you be found out.
5. If you operate your business as an S corporation and you want an above-the-line tax deduction for the cost of your health insurance, you need the S corporation to (a) pay for or reimburse you for the health insurance and (b) put it on your W-2. Make sure that happens before December 31.
6. Claim the tax credit for the health insurance you give your employees. If you provide your employees with health insurance, see whether your pay structure and number of employees put you in a position to claim a 50 percent tax credit for some or all of the monies you paid for health insurance in 2018 and, possibly, prior years.

2018 Last-Minute Year-End Tax Strategies for Marriage, Kids, and Family

Here are five year-end tax-deduction strategies that apply if you are getting married or divorced, have children who did or could work in your business, and/or have situations where you give money to relatives and friends.

1. Put Your Children on Your Payroll

Did your children under age 18 help you in your business this year? Did you pay them for their work? You should pay them for the work—and pay them on a W-2. Why? **First**, W-2 wages paid by the parent to the parent's under-age-18 child for work done on the parent's Form 1040 Schedule C business are both

- deductible by the employer-parent, and
- exempt from federal payroll taxes for both the parent and the child.

Thus, if you operate your business as a sole proprietorship or single-member LLC taxed on Schedule C or as a spousal partnership, then you face no federal payroll taxes on the W-2 wages you pay your under-age-18 child. (And in most states, you also face no state payroll taxes.) Further, your child faces no federal payroll taxes. If you operate as a corporation, your child and the corporation pay payroll taxes. But that does not eliminate the benefits; it simply reduces them.

Second, thanks to tax reform, your child can use the 2018 standard deduction to eliminate income taxes on up to \$12,000 in wages.

Third, your child can contribute up to \$5,500 to either of the following:

1. **A tax-deductible IRA**, and deduct that amount from federal taxation. This is the best strategy to use if the child has more than \$12,000 in W-2 wages and you want the child to have more tax-free money.
2. **A Roth IRA**, which is not tax-deductible, but the child can (a) remove the contributions (money put in) at any time, tax- and penalty-free, and (b) remove the earnings tax-free after age 59 1/2. This is the best strategy to use if the child has less than \$12,000 in total W-2 wages and other earned income, because the child has no need for a tax deduction.

2. Get Divorced after December 31

The marriage rule works like this: you are considered married for the entire year if you are married on December 31. Although lawmakers have made many changes to eliminate the differences between married and single taxpayers, in most cases the joint return will work to your advantage. Thus, wait until next year to finalize the divorce if alimony is not involved.

Warning on alimony! The Tax Cuts and Jobs Act (TCJA) changed the tax treatment of alimony payments under divorce and separate maintenance agreements executed *after December 31, 2018*:

Under the old rules, the payor deducts alimony payments and the recipient includes the payments in income.

Under the new rules, which apply to all agreements executed after December 31, 2018, the payor gets no tax deduction and the recipient does not recognize income. And if you are married on December 31, don't file in April as married, filing separately. In most cases, this is a sure way to overpay your taxes.

3. Stay Single to Increase Mortgage Deductions

Two single people can deduct more mortgage interest than a married couple. If you own a home with someone other than your spouse, and you bought it on or before December 15, 2017, you individually can deduct mortgage interest on up to \$1 million of a qualifying mortgage.

For example, if you and your unmarried partner live together and own the home together, the mortgage ceiling on deductions for the two of you is \$2 million. If you get married, the ceiling drops to \$1 million. If you bought your house after December 15, 2017, then the reduced \$750,000 mortgage limit from the TCJA applies. In that case, your two-person maximum deduction goes down to \$1.5 million.

4. Get Married on or before December 31

Remember, if you are married on December 31, you are married for the entire year. If you are thinking of getting married in 2019, you might want to rethink that plan for the same reasons that apply in a divorce (as described above). The IRS could make big savings available to you if you are married on December 31, 2018.

Again, you have to run the numbers in your tax return both ways to know the tax benefits and detriments for your particular case. A quick trip to the courthouse may save you thousands.

5. Make Use of the 0 Percent Tax Bracket

In the old days, you used this strategy with your college student. Today, this strategy does not work with the college student, because the kiddie tax now applies to students up to age 24. But this strategy is a good one, so ask yourself this question: Do I give money to my parents or other loved ones to make their lives more comfortable?

If the answer is yes, is your loved one in the 0 percent capital gains tax bracket? The 0 percent capital gains tax bracket applies to a single person with less than \$37,650 in taxable income and to a married couple with less than \$75,300 in taxable income. If the parent or other loved one is in the zero capital gains tax bracket, you can get extra bang for your buck by giving this person appreciated stock rather than cash.