



2018 YEAR-END TAX PLANNING CHECKLIST



Year-end tax planning for 2018 takes place against the backdrop of legislative changes that fundamentally alter the tax rules for individuals and businesses. For 2018, the Tax Cuts and Jobs Act (TCJA) does away with many familiar, longstanding tax rules and introduces a host of new ones.

For businesses, the corporate tax rate is cut to 21%, the corporate AMT is gone, there are new limits on business interest deductions, and significantly liberalized expensing and depreciation rules. Plus, the domestic production activities deduction is repealed, although there is a new deduction for non-corporate taxpayers with qualified business income from pass-through entities.


For individuals, there are new, lower income tax

rates, a substantially larger standard deduction that for some makes up for severely limited itemized deductions and eliminated personal exemptions, an increased child tax credit, and a watered-down alternative minimum tax (AMT), among many other changes.

Below are a few key changes impacting your 2018 income taxes:

For businesses:

- A flat 21% tax rate for C corporations
- 20% deduction for pass-through business owners
- Repeal of the AMT
- 100% bonus depreciation and increased Section 179 expense
- A disallowance of entertainment expenses
- Net operating loss (NOL) cannot be carried back. Losses are subject to an 80% limitation



YEO & YEO'S YEAR-END TAX PLANNING CHECKLIST OF ADDITIONAL ACTION ITEMS MAY HELP YOU SAVE TAX DOLLARS IF YOU ACT BEFORE YEAR-END.

These are just some of the year-end steps that can be taken to save taxes. Not all actions may apply in your particular situation, but you or a family member can likely benefit from many of them.

Your Yeo & Yeo tax professional can help narrow down the specific actions you can take and tailor a tax plan for your current situation and future changes. Please review the following list and contact us at your earliest convenience so that we can help advise you on which tax-saving moves to make.

Visit the [Tax Resource Center](http://yeoandyeo.com) at yeoandyeo.com for additional tax planning resources including:

- Tax Reform Resources and Webinars
- Tax and Estate Planning Guides Online
- Weekly Tax Bites on Yeo & Yeo's Blog
- Tax Planning Calendars

- Business interest expense is now limited to 30% of the adjusted taxable income. Small businesses with \$25 million or less in gross receipts are exempt from this limitation.

For individuals:

- Standard deduction increases to \$24,000 for married filing jointly (\$12,000 for single)
- \$10,000 maximum itemized deduction for income, property and sales taxes
- No deduction for home equity loans unless used for acquisition indebtedness
- No deduction for miscellaneous itemized deductions

(i.e., investment fees, unreimbursed employee business expenses, tax preparation fees)

- Repeal of the personal exemptions
- Increase in the alternative minimum tax (AMT) exemption amount will eliminate AMT for most taxpayers
- Increase in child tax credit to \$2,000 (subject to phase-out at much higher income limitations than in the past). A new \$500 tax credit for each non-child dependent, which includes a child 17 and older, an ailing elderly parent or an adult child with a disability
- Major overhaul in the actual tax forms!



YEAR-END PLANNING BUSINESSES AND OWNERS

Consider the new deduction for pass-through income. Generally for tax years beginning after Dec. 31, 2017, a non-corporate taxpayer, including a trust or estate, who has qualified business income (QBI) from a partnership, S corporation, or sole proprietorship is generally allowed a deduction equal to:

- The lesser of 20% of QBI (not including net capital gains), or
- 50% of W-2 wages paid by the partnership, S corporation, or sole proprietorship (or 25% of W-2 wages paid plus 2.5% of the unadjusted cost basis of the business's assets, subject to limitations).

But the deduction can't exceed the taxpayer's taxable income, reduced by net capital gain. The calculation for this deduction is complicated and some planning before year-end is required to maximize the benefit.

Keep your entertainment and meals expenses separate. The TCJA disallows deductions for entertainment, amusement, or recreation that are directly related to (or, in certain cases, associated with) the active conduct of the taxpayer's trade or business. There are a few exceptions to this rule, such as an office outing. Business meals, however, are still eligible for a 50% deduction. Therefore, it will be important to keep your entertainment and meals expenses separate so that you do not miss the 50% deduction for the meals.

Due to the TCJA, there are a few new **accounting method changes** available if your annual average gross receipts do not exceed **\$25 million** for the three prior taxable years. These changes are:

- The cash method of accounting is available to any business (other than tax shelters).
- You may be exempt from inventory accounting.
- You may be exempt from UNICAP rules.
- You may be exempt from using the percent-of-completion method for the construction or improvement of real property if the contract is less than two years.

All changes require additional filing requirements for the first year.

Businesses should consider **buying and placing in service new or used machinery, equipment and software** before year-end to qualify for the 100% bonus first-year depreciation allowance. Businesses may take **100% bonus depreciation on qualifying improvement property** placed in service after the date the building was placed in service. Qualified improvement property is any improvement to an interior portion of a building that is nonresidential real property; this includes not only qualified leasehold improvements but may include improvements to the interior of a building that would otherwise be depreciated over 39 years.

Acquire and place in service qualified property, eligible for expensing under Code Section 179. The maximum amount you can expense for 2018 is \$1,000,000. The \$1,000,000 amount is reduced by the amount by which the cost of qualifying property placed in service during 2018 exceeds \$2,500,000 (the investment ceiling). The TCJA expands the definition of qualifying property from equipment and machinery to

include certain depreciable tangible personal property used predominantly to furnish lodging or in connection with furnishing lodging. The definition of qualified real property eligible for expensing includes any of the following improvements to nonresidential real property after the date such property was first placed in service: roofs; heating, ventilation, and air-conditioning property; fire protection and alarm systems and security systems. It also includes any other building improvements that are not elevators or escalators, do not enlarge the structure, and are not attributable to internal structural framework.

Businesses may be able to **take advantage of the “de minimis safe harbor election” to expense the costs of inexpensive assets, materials and supplies**, assuming the costs do not have to be capitalized under the Code Sec. 263A uniform capitalization rules. To qualify for the election, the cost of an expensed unit-of-property cannot exceed \$5,000 if the taxpayer has an applicable financial statement, e.g., a certified audited financial statement. If there is no applicable financial statement, the cost of an expensed unit of property cannot exceed \$2,500. Where appropriate, purchase such qualifying items before the end of 2018.

A corporation, other than a “large” corporation, that anticipates a small net operating loss (NOL) for 2018 and substantial net income in 2019 may find it worthwhile to **accelerate just enough of its 2019 income or to defer just enough of its 2018 deductions** to create a small amount of net income for 2018. This will permit the corporation to base its 2019 estimated tax installments on the relatively small amount of income tax shown on its 2018 return, rather than having to pay estimated taxes based on 100% of its much larger 2019 taxable income.

To reduce 2018 taxable income, consider **disposing of a passive activity** in 2018 if doing so will allow you to deduct suspended passive activity losses.

- If you own an interest in a partnership or S corporation, consider whether you need to **increase your basis in the entity so you can deduct a loss from it for this year.**





YEAR-END PLANNING INDIVIDUALS

Postpone income until 2019 and accelerate deductions into 2018 to lower your 2018 tax bill. This strategy may enable you to claim larger deductions, credits, and other tax breaks for 2018 that are phased out over varying levels of adjusted gross income. 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. However, in some cases it may pay to accelerate income into 2018. For example, this may be the case when a person's marginal tax rate is much lower this year than it will be next year.

Consider “bunching” your 2018 and 2019 charitable contributions in 2018. Due to the increase in the standard deduction and the limitation on deductible taxes, many taxpayers may find that they do not have enough deductions to itemize in 2018. If you are close to the maximum standard deduction, you might want to make your 2019 charitable contributions in 2018. By doing this, you may be able to itemize and take a tax deduction for your contributions in 2018. Then in 2019, you would take the standard deduction.

If you are unsure as to whom you will be making your 2019 charitable contributions, or you would like to maintain annual donations to your favorite charities, try using a Donor Advised Fund (DAF). By using a DAF, you can receive the full deduction in 2018 for the amount you contributed, and then in 2019 decide to whom and when you would like the funds dispersed.

Increase withholding of state and local taxes, or

make estimated tax payments. If you expect to owe state or local income taxes when you file your return next year, consider asking your employer to increase withholding of state and local taxes, or make estimated tax payments before year-end to pull the deduction of those taxes into 2018. Remember that due to tax reform, you are only allowed a maximum \$10,000 itemized tax deduction. This includes state and local income taxes, real estate tax, sales tax and personal property tax. Therefore, this strategy will only be beneficial if you are under the \$10,000 maximum and if you are going to itemize.

Make sure you have the correct amount of taxes withheld. The IRS has a tax withholding calculator at: <https://www.irs.gov/payments/tax-withholding> that will help you with this process.

Increase the amount you set aside for next year in your employer's **health flexible spending account (FSA)** if you set aside too little for this year. The maximum annual contribution to an FSA that a cafeteria plan can allow is \$2,650 for tax year 2018. This amount is scheduled to increase to \$2,700 for 2019.

If you are eligible to make health savings account (HSA) contributions in December of this year, **you can make a full year's worth of deductible health savings account contributions** for 2018. This is so even if you first became eligible on December 1, 2018. The maximum annual contribution to an HSA for 2018 is \$3,450 for self-only and \$6,900 for family coverage. If you are over the age of 55, you can contribute an additional \$1,000 to your HSA. The contribution limit increases in 2019 for

self-only coverage to \$3,500 and for family coverage to \$7,000.

Bulk up 529 plans. The TCJA now allows taxpayers to take up to \$10,000 in distributions per student for public, private, or religious elementary and secondary school tuition costs. If you have young children or grandchildren, consider funding their 529 plans at a higher level to grow tax-free and cover a portion of the cost of elementary and secondary schools in addition to college tuition.

Make gifts sheltered by the annual gift tax exclusion before the end of the year and thereby save gift and estate taxes. You can give \$15,000 in 2018 to each of an unlimited number of individuals, but you cannot carry over unused exclusions from one year to the next. The transfers also 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.

Maximize your 401(k) contributions. If you are a participant in a traditional employer-sponsored defined contribution plan, the 2018 contribution limit for a 401(k) is \$18,500, with an additional \$6,000 catch-up allowed for individuals 50 and older. Consider contributing from a year-end bonus to take advantage of the maximum contribution. Beginning in 2019, the contribution limit is set to increase to \$19,000. The catch-up contribution remains the same at \$6,000.

If you are self-employed and will not have employees, **you can establish a “one person” 401(k) plan.** Under this plan, you can make elective contributions of up to \$18,500 for 2018 (\$24,500 if you are over age 50) and can make profit-sharing contributions up to a maximum of \$55,000 counting both the employer and the elective contributions (not counting catch-up contributions). The plan must be established by the end of the year to claim a tax deduction for contributions for that year, although you do not need to make contributions until the due date (with extensions) of your return.

Contribute to an IRA. If your employer does not offer a retirement plan, consider a traditional or Roth IRA. The 2018 contribution limit on IRAs is \$5,500, with an additional \$1,000 catch-up for taxpayers 50 and older. With a traditional IRA you can likely deduct your contributions, though your deduction may be limited if your spouse participates in an employer-sponsored plan. Beginning in 2019, the contribution limit is set to increase



to \$6,000. The catch-up contribution remains the same at \$1,000.

Consider making contributions to Roth IRAs instead of traditional IRAs. Roth IRA payouts are tax-free and thus immune from the threat of higher tax rates, as long as they are made 1) after a five-year period, and 2) on or after attaining age 59½, after death or disability, or for a first-time home purchase.

If you believe a Roth IRA is better than a traditional IRA, and want to remain in the market for the long term, **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 your adjusted gross income for 2018. As a general rule, we advise our clients to pay any taxes resulting from a conversion with non-retirement funds to maximize the future benefit it will produce. Withholding federal and state taxes from a conversion would also generate an additional 10% penalty on the amounts withheld.

Higher-income-earners have unique concerns to address when mapping out year-end plans. Individuals receiving wages and other earned income in excess of \$200,000 (\$250,000 for married couples filing jointly and \$125,000 for married couples filing separately) need to be wary of the additional 0.9% Medicare tax. There is also a 3.8% surtax on certain unearned income. The surtax is

3.8% of the lesser of 1) net investment income, or 2) the excess of modified adjusted gross income over an unindexed threshold amount of \$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, a taxpayer's approach to minimizing or eliminating the 3.8% surtax will depend on the individual's estimated modified adjusted gross income and net investment income for the year. Some taxpayers should consider ways to minimize additional net investment income for the balance of the year, others should try to see if they can reduce modified adjusted gross income other than net investment income, and still others may need to consider ways to minimize both. Net investment income includes taxable interest, dividends and capital gains, as well as passive income, such as income from rental activities that do not constitute a trade or business. We can assist with strategies to minimize or eliminate this additional tax.

Take minimum distributions (RMDs) from your IRA, 401(k) plan, or other employer-sponsored retirement plan if you have reached age 70½. Failure to take a required withdrawal can result in a penalty of 50% of the amount of the RMD not withdrawn. If you turned age 70½ in 2018, you could delay the first required distribution to 2019, but if you do, you will have to take a double distribution in 2019—the amount required for 2018 plus the amount required for 2019. Think twice before delaying 2018 distributions to 2019—bunching income into 2019 might push you into a higher tax bracket or have a detrimental impact on various income tax deductions that are reduced at higher income levels. However, if you will be in a substantially lower bracket in 2019 it could be beneficial to take both distributions in that year.

If you are 70½ or older, **consider making charitable contributions** (up to \$100,000) **directly from your IRA,** referred to as Qualified Charitable Distributions (QCD). While these contributions will not be deductible on Schedule A as itemized deductions, they will not be included in your adjusted gross income either but will go towards satisfying your RMD. They may also have the added benefit of not being taxable in your state of residence.





Give appreciated stock as a charitable contribution.

The value of your donation is the fair market value of the stock on the date of the contribution, and you will not have to pay any tax on the appreciation of the stock. This will also prevent the gain from being subject to the 3.8% tax on net investment income.

Consider realizing losses on the sale of stock to offset other investment gains while substantially preserving your investment position to minimize the burden of the 3.8% tax on net investment income. This

is especially important if your taxable income exceeds \$425,800 (\$479,000 married filing joint), as the long-term capital gain rate increases from 15% to 20% for those individuals. There are several ways this can be done. For example, you can sell the original holding, then buy back the same securities at least 31 days later. It may be advisable for us to meet to discuss year-end trades you should consider making as there are limitations to the amount of capital losses that can be deducted in any given year.

CONTACT YEO & YEO

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