BLUME KEENEY PLLC

Trusted Tax Advisors

2016 Year-End Tax Planning Guide

INTRODUCTION

With the election now officially over, at Blume Keeney we can't think of a better remedy for your political headache than a discussion about year-end tax planning. If you are reading this from your new home in Canada, proudly wearing a "make America great again" hat, or somewhere in-between, the myriad of taxes and complicated rules are undoubtedly a worthwhile and welcome respite from the disagreements, mudslinging and negative discourse that this election seemed to feature…at least from our perspective. To that end, the 2016 edition of the Blume Keeney Year-End Tax Planning Guide features some "wholesome" tax planning topics to consider in your search for tax-efficiency - and that's an outcome we can all agree with.

Thanks to tax legislation passed at the end of 2015 that extended or made permanent many popular tax provisions, for the time being we have a tax environment that is actually stable and predictable. Consequently, tax planning for 2016 is a much easier process than what we have experienced in the recent past when provisions had expired and we were unsure when (or even if) they would be extended. While President-elect Trump has proposed significant tax reform, any potential changes will not impact your 2016 taxes.

Major tax reform has been discussed by politicians and taxpayers for many years. With a Republican president and continuing Republican control of both the House and Senate, the stars may align enough that tax reform is actually a possibility within the next few years. However, even with Mr. Trump's

INTRODUCTION (continued)

tax policy outlined below, it's important to remember that tax law is initiated by Congress; not the president. While there appears to be enough discontent within Congress that it may take some time before any meaningful legislation materializes, it is possible that tax law changes will impact the 2017 tax year.

In general, Mr. Trump's proposed tax policy focuses on reducing taxes, both for businesses and individuals, in order to stimulate economic growth. However, the enthusiasm to reduce taxes will have to be tempered with the pressure from Republican constituents to reduce the federal deficit, as his proposed tax cuts would add significantly to the national debt without offsetting revenue raisers and/or major budget cuts. Furthermore, tax legislation originates in the House of Representatives, which has its own version of tax policy that will need to be reconciled with Mr. Trump's proposals.

Specifically, Mr. Trump's tax policy would consolidate tax rates into three brackets: 12 percent, 25 percent, and 33 percent, with a business tax rate of 15 percent. At this point, it is not entirely clear if the 15 percent rate is only applicable to C-corporations or if it will also apply to income from pass-through entities (partnerships, LLCs, S-corporations) and sole proprietors.

The Affordable Care Act (aka Obamacare) would likely be repealed or significantly modified, which would likely eliminate the 3.8% surtax on net investment income and the additional 0.9% Medicare tax. In addition, Mr. Trump has proposed a repeal of the estate tax, GST tax, and gift tax. However, this would also eliminate the step-up in basis for inherited assets; effectively adding a tax on realized capital gains when inherited assets are sold by heirs.

Other specific proposals include:
- Increase the standard deduction;
- Add an above-the-line deduction for child care and elder care expenses;
- Limit the tax value of itemized deductions;
- Limit the tax benefit from employer-provided health insurance, and tax-exempt interest;
- Repeal the alternative minimum tax;
- Expand the earned income tax credit;
- Repeal most business tax incentives except the R&D credit; and
- Add a one-time opportunity to repatriate corporate cash held overseas at a discounted tax rate.

We will continue to monitor developments as they relate to tax legislation, and pass along updates if these proposals become likely. In the meantime, you will want to spend some time thinking about your taxes for 2016 and the potential impact of proposals for 2017. Your particular situation changes from year to year so it is important to read through the guide and identify any areas that might apply. Give Jenny or Ryan a call so that we can personally talk with you about your opportunities.

TAX PLANNING CHECKLIST FOR INDIVIDUALS

Income Planning

- ☐ Tax-Exempt Income – Review investment portfolios to consider exposure to municipal bonds. Not only is the interest tax-exempt, it's also not subject to the 3.8% Net Investment Income Tax (NIIT) that might apply to other taxable income.
- ☐ 0% Tax Rate Income – For taxpayers in the 10% or 15% income tax brackets, long-term capital gains and qualified dividend income is taxed at 0%. So if you are in one of these tax brackets, consider capital gain harvesting before year-end to increase basis within a portfolio. Note that wash sale rules that limit capital losses do not apply to gains.
- ☐ Suspended Passive Losses – Review your passive loss carryovers if selling real estate or business interests. Losses from a passive activity that are not allowed to offset current income due to the passive loss rules are suspended and carried forward. Disposing of a passive activity with suspended losses allows the current year losses and suspended losses to offset income.
- ☐ Income Deferral – When possible, recognize income after year-end. For example, defer bonuses or delay stock option exercises and asset sales.
- ☐ Passive Income – Explore ways to increase the level of participation with passive entities or rental properties to avoid the additional NIIT. Income from passive activities may be subject to the NIIT 3.8% surtax in addition to income tax. However, this can be mitigated if taxpayers can meet one of the tests for material participation.
- ☐ IRA Conversion Strategy – Evaluate your IRA and anticipated income level for 2016 to determine if a portion of your IRA should be converted to a Roth IRA. This conversion will create additional taxable income in the current year but the distributions from the converted account will be income tax free in future years.
- ☐ Installment Sale – Consider deferring gain recognition with assets sold on installment until the tax year when proceeds are actually received.

2016 TAX RATES			
Single	**Married Filing Jointly**	**Marginal Rate**	**Long-Term Capital Gain & Qualified Dividends Tax Rates**
$0 to $9,275	$0 to $18,550	10%	**0%**
$9,275 to $37,650	$18,550 to $75,300	15%	**0%**
$37,650 to $91,150	$75,300 to $151,900	25%	15%
$91,150 to $190,150	$151,900 to $231,450	28%	15%
$190,150 to $413,350	$231,450 to $413,350	33%	15%
$413,350 to $415,050	$413,350 to $466,950	35%	15%
Over $415,050	Over $466,950	39.6%	20%

TAX PLANNING CHECKLIST FOR INDIVIDUALS (continued)

Income Planning (continued)

- [ ] Age 70.5 Initial Required Minimum Distribution – If you turn age 70.5 during 2016, you have until April 1, 2017 to take your initial required minimum distribution (RMD) from retirement plans. However, if you do wait until 2017, you will then have a double distribution in the same year potentially causing negative tax implications. To avoid that, consider taking your age 70.5 RMD prior to year-end.
- [ ] Like-Kind Exchange – Consider using a like-kind exchange on the sale of rental or business property to defer taxable gains.
- [ ] Long-Term Capital Gains and Qualified Dividends – Review investment portfolios to take advantage of the preferential income tax rate for long-term capital gains and qualified dividends.
- [ ] Foreign Bank Accounts – With some exceptions, bank accounts, securities, mutual funds, online poker accounts, or insurance policies with cash value that are physically located outside the U.S. must disclose the foreign account to avoid penalties. This applies to employees with signature authority and foreign retirement accounts.

Top Tax Rates for 2016	
Ordinary earned income	39.6%
Net investment income and passive income(1)	43.4% (2)
Long-term capital gains	23.8%(2)
Qualified dividends	23.8%(2)
Estate and gift tax	40%

(1) Includes interest, dividends, royalties, net rental income and other passive income
(2) Includes 3.8% surtax on the lesser of a) net investment income or b) adjusted gross income over the applicable threshold of $200,000 for single taxpayers, $250,000 for joint taxpayers or $12,400 for estates and trusts.

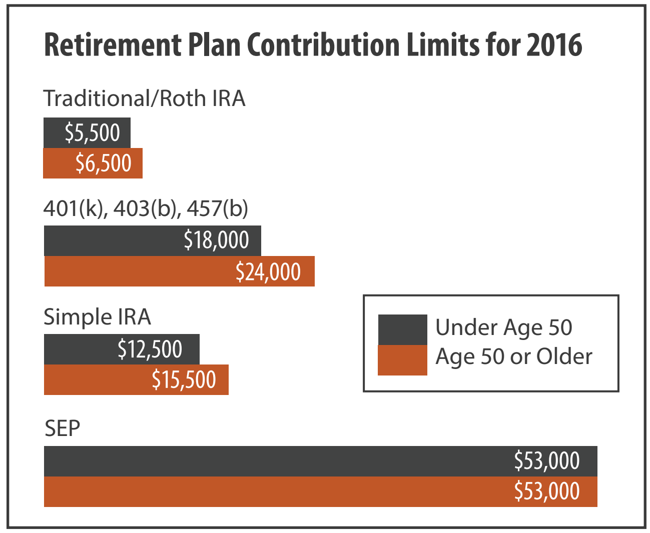
Capital Loss Harvesting – Market volatility during the year may have created unrealized losses. Review your portfolio to ensure that capital losses have been taken (when appropriate) to mitigate capital gains. Capital losses can be used to offset capital gains, and unused losses are carried forward to offset future capital gains. However, the wash sale rules impact the benefit if the same asset is reacquired within a specified time period.

- [ ] Same-Sex Marriage – New guidance relating to same-sex marriage has changed tax return filing requirements for certain individuals and created opportunities to potentially reduce income taxes. Furthermore, these changes apply retroactively so it is important to consider prior year tax returns in light of these changes
- [ ] Child's Income – Transfer income producing assets, or appreciated property to kids to utilize their (generally) lower tax bracket. However, the Kiddie Tax could eliminate a majority of the tax savings if the child is under age 18, or under age 24 and a full time student.

TAX PLANNING CHECKLIST FOR INDIVIDUALS (continued)

Deduction Planning

- ☐ Retirement Plan Contributions – Certain plans, such as 401(k) and Keogh plans allow larger tax deductions than IRAs or SEP IRAs but they must be established by year-end.
- ☐ Over Age 50 Retirement Plan Contributions – If over age 50, be sure to utilize the "catch-up contribution" that allows for an additional $6,000 contribution to a 401(k) and a $1,000 contribution to an IRA in addition to the regular contribution limits.
- ☐ Health Savings Account (HSA) Contributions – If eligible, contributions to a HSA are tax deductible and eligible distributions are tax-free.
- ☐ Qualified Charitable Distribution (QCD) – If over age 70.5, you can make tax-free distributions from your IRA of up to $100,000 directly to charitable organizations. These distributions are excluded from your taxable income.
- ☐ Charitable Miles – A deduction of $0.14 per mile is allowed when using a vehicle for charitable purposes, plus parking fees and tolls.
- ☐ Charitable Contributions – Consider giving appreciated property to a charity instead of cash to receive a deduction for the fair market value and avoid paying tax on the capital gain. Conversely, depreciated investment assets should be sold first, and the cash donated to charity to receive the benefit of the capital loss.



- ☐ Timing of Charitable Contributions – Credit card charges and checks mailed on or before December 31, though not actually paid until 2017, are still considered deductions in 2016.
- ☐ Substantiation of Charitable Contributions – The IRS has been disallowing charitable contribution deductions when taxpayers are unable to completely meet the substantiation requirements. When giving over $250 to charity, be sure to get an acknowledgement letter from the charity. It would even be advisable to take a photo of non-cash items contributed.

VALUE	CHARITABLE CONTRIBUTION SUBSTANTIATION REQUIREMENTS		
	Cash Donations	Non-Cash Donations	Publicly Traded Stock Donations
$249 or less	Maintain records to support contribution	Maintain records to support contribution	Maintain records to support contribution
$250 - $500	Maintain written acknowledgement from the charitable organization	Maintain written acknowledgement from the charitable organization	Maintain written acknowledgement from the charitable organization
$501 - $5,000		In addition to maintaining acknowledgement letter, must report date that property was acquired, adjusted cost basis, and method of acquisition	In addition to maintaining acknowledgement letter, must report date that property was acquired, adjusted cost basis, and method of acquisition
More than $5,000		In addition to requirements above, must obtain an appraisal from a qualified appraiser	
$500,000 or greater		Obtain an appraisal from a qualified appraiser for assets other than cash or publicly traded securities AND attach a copy of the appraisal to your return along with a confirmation letter from the charity	

TAX PLANNING CHECKLIST FOR INDIVIDUALS (continued)

Deduction Planning (continued)

- [ ] School Teachers – Elementary and secondary school teachers are allowed to deduct up to $250 on books, supplies, and materials purchased for their classrooms.
- [ ] Residential Energy Tax Credits – If considering installing energy saving and energy-efficient (Energy Star) improvements to your residence, such as certain insulation materials, roofs; windows; doors; stoves; heat pumps; gas, propane, or oil furnaces; air conditioners; and water heaters, be sure to complete the installation prior to December 31, 2016. This credit has not yet been extended past 2016.
- [ ] Education Credits and Deductions – New for 2016, to be eligible for the American opportunity tax credit, the lifetime learning credit, or the tuition and fees deduction, taxpayers must have a Form 1098-T from the educational institution. Information from the Form 1098-T is needed to claim the credits or deductions.
- [ ] Deduction Phase-Outs – Consider bunching two years of deductions into one year by accelerating or deferring deductions, like medical expenses, mortgage interest, state income taxes, real estate taxes and charitable contributions to exceed the phase-outs and maximize the deduction benefit.

Estate and Gift Planning

- [ ] Annual Exclusion – Every taxpayer has a $14,000 per-recipient annual exclusion from gift tax. Combined with a spouse's annual exclusion, a married couple can give $28,000 per recipient. Consider evaluating your gifting options before year-end.
- [ ] Federal Lifetime Exemption – The federal lifetime exemptions for gift and estate tax is now $5.45 million (this is in addition to the $14,000 per-recipient annual exclusions for lifetime gifts referenced above). The gift and estate tax rate for transfers greater than $5.4 million is 40% for 2016.
- [ ] Valuation Discounts – Discounts have been an extremely valuable tool in the estate planning arena for decades. However, recent Proposed Regulations from Treasury will limit the application of these discounts. Taxpayers seeking to apply these discounts as part of their overall estate, gift and succession plans should evaluate their options now before the Regulations are finalized.
- [ ] State Estate Tax – Some states, including Washington, Oregon, and Massachusetts, have state estate taxes. The state exemptions are lower than the federal exemption so it is important to consider state estate taxes in your estate plans.
- [ ] Charitable Gifts – Taxpayers with significant charitable intent may be able to receive both an income tax benefit and an estate tax benefit with proper planning.
- [ ] Interest Rates – Applicable federal rates (AFRs), minimum interest rates that are required to be charged by related parties, continue to be at historical lows. In some cases, it may be possible to refinance loans between related parties to reduce interest payments.
- [ ] Same-Sex Marriage – New guidance relating to same-sex marriage has created opportunities for certain individuals. Wills and other estate planning documents should be updated to incorporate these new opportunities.

TAX PLANNING CHECKLIST FOR INDIVIDUALS (continued)

Affordable Care Act – Health Insurance

- [ ] Required Insurance – All US citizens and legal residents are required to have qualifying health insurance. There are some exemptions, primarily due to financial hardship or short-term gaps in coverage.
- [ ] Penalties – The penalty for not obtaining qualifying health coverage has increased to the greater of $695 per adult ($347.50 per child) or 2.5% of household income in 2016. Maximum penalties of $2,085 apply.
- [ ] Premium Tax Credits – Taxpayers with household incomes below four times the federal poverty limit ($47,080 for an individual, $97,000 for a family of four) may qualify for a premium tax credit or a premium subsidy.
- [ ] Reporting – A Form 1095-A, 1095-B or 1095-C will be issued to anyone enrolled in health insurance during the year substantiating health insurance coverage for the calendar year. These forms will be needed to complete the Form 1040.

TAX PLANNING CHECKLIST FOR TRUSTS

Tax Planning Checklists for Trusts

- [ ] Distributions – Trusts have a low threshold of $12,400 for the NIIT so most undistributed income in a trust will be subject to the additional tax. Trustees should consider maximizing distributions to beneficiaries, and consider strategies to distribute capital gains.
- [ ] Passive Activities – IRS guidance has clarified the application of NIIT on a trust's business and/or real estate income. In light of this new guidance, consider the role of a trustee in the management of the trust assets and whether additional steps can be taken to mitigate this additional tax.

Taxable Income	Marginal Tax Rate
Not over $2,550	15%
Over $2,551 but not over $5,950	25%
Over $5,951 but not over $9,050	28%
Over $9,051 but not over $12,400	33%
Over $12,400 *	39.6%

*Additional 3.8% tax on investment and passive income in excess of $12,400

- [ ] Income Sources – Similar to the tax planning strategies for individuals, trustees should evaluate the role of tax-exempt income in the trust's investment portfolio given the 3.8% NIIT on taxable income.

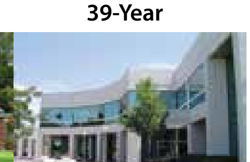
TAX PLANNING CHECKLIST FOR BUSINESSES

Tax Planning Checklists for Businesses

- [ ] Form W-2 – Beginning in 2016, the filing deadline for Forms W-2/W-3 is January 31. Employers are also required to disclose the annual cost of health plan coverage provided to an employee on the W-2.
- [ ] Health Insurance – Employers with 50 or more FTE employees must offer minimum essential coverage starting in 2016 and report insurance coverage for employees on Form 1094-B, 1094-C, 1095-B and Form 1095-C
- [ ] Limitation on Health FSA Reimbursements - The maximum Health FSA reimbursement may not exceed $2,550 per year for 2016 and is expected to remain the same for 2017.
- [ ] Buy-Sell Agreements – Buy-Sell Agreements can act as a will for businesses. Agreements should be reviewed and updated regularly. This is especially important in any business with multiple owners.
- [ ] Section 179 – The Section 179 depreciation deduction for qualifying assets acquired in 2016 is $500,000. This depreciation deduction begins to phase out once total depreciable assets purchased during the year exceed $2,010,000.
- [ ] Bonus Depreciation – 50% bonus depreciation has been extended through 2017, with 40% bonus depreciation in 2018, and 30% bonus depreciation in 2019. Bonus depreciation is scheduled to expire after 2019.

MACRS Depreciation Asset Classes

3-Year	5-Year	7-Year	10-Year
			
Tractor units for over-the-road-use.	Autos, computers, and equipment	Office furniture and fixtures, farm machinery and equipment	Vessels, barges, tugs

15-Year	20-Year	27.5-Year	39-Year
			
Certain land improvements	Certain farm buildings	Residential rental property - apartment buildings, single family	Non-residential real property - office and commercial

TAX PLANNING CHECKLIST FOR BUSINESSES (continued)

Tax Planning Checklists for Businesses (continued)

- [ ] Family Employees – Consider hiring your school-age child to work for your business part-time. Reasonable compensation is deductible, reducing your self-employment income. No Social Security or Medicare tax is due on the child's earnings if they are under age 18 and the business is not a corporation. Also, the child could make a contribution to a traditional or Roth IRA.
- [ ] Employer-Provided Child Care Credit – Employers can claim a credit of up to $150,000 for supporting employee child care or child care resource and referral services.
- [ ] Research and Development Credit – Companies that develop new or improved products or processes may be able to benefit from research tax credit incentives. The research tax credit law was permanently extended.
- [ ] Small Business Health Care Tax Credit for Small Employers – Small employers, generally those with fewer than 25 full-time equivalent employees with average wages of $50,000 or less, are allowed a maximum credit for 50 percent of premiums paid for employees health insurance. Insurance must be purchased through the Small Business Health Options Program (SHOP) or qualify for an exception to the requirement.
- [ ] Form 1099 – Any non-corporate vendor paid over $600 must be issued a Form 1099 to report payments. The Form 1099/1096 is due by January 31 and the penalty for late filing can be as high as $530 per Form 1099 with no maximum penalty. <u>The IRS has emphasized greater enforcement of the Form 1099 compliance process for tax year 2016.</u>

IMPORTANT TAX DUE DATES

For Businessses, Individuals and Trusts

IMPORTANT TAX DUE DATES (changes in bold)		
TAX FORM	**Filing Deadline**	**Extended Filing Deadline**
Form W-2/W-3	January 31	N/A
Form 1099/1096	**January 31**	N/A
Individuals – Form 1040	April 15	October 15
FBAR – Form 116	**April 15**	**October 15**
Trusts – Form 1041	April 15	**September 30**
Partnerships – Form 1065	**March 15**	September 15
C Corporations – Form 1120	**April 15**	September 15
S Corporations – Form 1120S	March 15	September 15

Regardless of your political preferences, there is benefit to being aware of the tax planning opportunities available to you for 2016 and beyond. Decisions you make this year could have a direct impact on your long term financial security, so it pays to plan and take action now to ensure your goals can be achieved.

Contact Jenny Keeney or Ryan Blume for more information.
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