2016 YEAR-END TAX PLANNING

Time is running out to make important planning moves before the year's end, so don't delay.

The changes in various tax provisions brought about with the 2012 Tax Act continue to make planning for 2016 and future years more complex and challenging. We created this tax planning guide to help you understand how these changes may affect you.

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THE CURRENT ENVIRONMENT

Congress is scheduled to adjourn for the year on Dec. 16, 2016. Major tax policy changes this year are highly unlikely as a result of the November 2016 elections and attention to the economy and job growth. With Donald Trump elected as president and taking office in 2017, time will tell how national priorities may change.

PLANNING FOR SAME-SEX COUPLES

Newly married same-sex couples have new tax planning opportunities to consider, as well as a host of new financial and estate planning issues that should be addressed.

In 2013, the Supreme Court held that Section 3 of the 1996 Defense of Marriage Act (DOMA) was unconstitutional. Section 3 of DOMA provided that marriage, for federal purposes, was to be defined only as a legal union between one man and one woman. The 2013 Supreme Court decision allowed same-sex marriage to be recognized at the federal level. The Treasury Department and the Internal Revenue Service announced that same sex-couples, regardless of where they live, will be recognized as married for federal tax purposes so long as the couple was legally married in a state that sanctions same-sex marriages.

As of the date of this ruling, only 13 states and Washington D.C. sanctioned same-sex marriages. In 2015, the Supreme Court held that every state must permit same-sex marriages.

The results of both Supreme Court decisions mean that same-sex marriages are legally recognized in every state of the Union. Same-sex married couples now enjoy federal and state tax benefits afforded to all married couples. The 2015 ruling not only applies to same-sex couples' right to marry (and enjoy all federal and state tax benefits), but it applies to same-sex couples' rights with regard to divorce, adoption and child custody, separation agreements, marital property, spousal survivorship benefits, inheritance through intestacy, priority rights in guardianship proceedings, contract rights, and many other state rights afforded to spouses.

HIGHLIGHTS FROM THE 2016 TAX REFORM PLAN

Under the United States Constitution, all tax legislation must originate in the House of Representatives. To that end, in June 2016, House Republicans released a tax reform plan. This blueprint is the likely starting point for reform when Congress reconvenes in January 2017. With Republicans controlling both the House and Senate, and now the White House, prospects for significant tax reform are stronger than they have been in years. Key provisions of the House blueprint include:

Proposed Changes to the Individual Income Tax

- Consolidates the current seven tax brackets into three, with rates of 12 percent, 25 percent and 33 percent.
- Taxes capital gains and dividends as ordinary income and provides a 50 percent exclusion of capital gains, dividends and interest income. This is equivalent to taxing capital gains, dividends and interest income at half the rate of ordinary income, with three brackets of 6 percent, 12.5 percent and 16.5 percent.
- Increases the standard deduction from $6,300 to $12,000 for singles; from $12,600 to $24,000 for married couples filing jointly; and from $9,300 to $18,000 for heads of household.
- Eliminates the personal exemption and creates a $500 non-refundable credit for dependents who are not children.
- Increases the Child Tax Credit to $1,500 per child, limits the refundability of the credit to $1,000, and raises the phase-out threshold for the Child Tax Credit for married households from $110,000 to $150,000.
- Eliminates all itemized deductions besides the mortgage interest deduction and the charitable contribution deduction.
- Eliminates the individual alternative minimum tax.

Proposed Changes to Business Income Taxes

- Reduces the corporate income tax rate from 35 percent to 20 percent.
- Eliminates the corporate alternative minimum tax.
- Taxes income derived from pass-through businesses at a maximum rate of 25 percent.
- Allows the cost of capital investment to be fully and immediately deductible.
- Eliminates the deductibility of net interest expenses on future loans.
- Restricts the deduction for net operating losses to 90 percent of net taxable income and allows net operating losses to be carried forward indefinitely, and increased by a factor reflecting inflation and the real return to capital. Does not allow net operating losses to be carried back.
- Eliminates the domestic production activities deduction (section 199) and all other business credits, except for the research and development credit.
- Creates a fully territorial tax system, exempting from U.S. tax 100 percent of dividends from foreign subsidiaries.
- Enacts a deemed repatriation of currently deferred foreign profits, at a tax rate of 8.75 percent for cash and cash-equivalent profits and 3.5 percent on other profits.
- Modifies all business income taxes to be border-adjustable, disallowing the deduction for purchases from nonresidents and exempting export profits and foreign-derived profits from taxation.

Other Proposed Changes

- Eliminates federal estate and gift taxes.

IMPACT OF THE TAX ACT OF 2012 TAX LAW CHANGES

Income tax rates

The Tax Act of 2012 imposed a new top tax rate of 39.6 percent. For 2016, top rate is imposed on taxable income in excess of $415,051 for single taxpayers, $441,001 for heads of household, and $466,951 for married taxpayers filing jointly ($233,476 for each married spouse filing separately).

Dividends and capital gains

A 20 percent tax rate applies to qualified dividends and long-term capital gains for taxpayers in the top income tax bracket, while the 15 percent rate is retained for taxpayers in the 25 percent through 35 percent brackets.

A zero percent rate applies to taxpayers in the 10 percent through 15 percent brackets.

Itemized deduction and personal exemption phase-outs

The itemized deduction phase-out and personal exemption phase-out apply to taxpayers with Adjusted Gross Income (AGI) above $259,400 for single taxpayers, $285,350 for heads of household, $311,300 for married taxpayers filing jointly ($155,650 for each married spouse filing separately).

Additional hospital insurance tax on high-income taxpayers

The employee portion of the hospital insurance of the Federal Insurance Contributions Act (FICA), normally 1.45 percent of eligible wages and self-employment income, is increased by 0.9 percent on wages and self-employment income that exceed a threshold amount.

In the case of a joint tax return, the additional tax is imposed on the combined wages and self-employment income of both the taxpayer and the taxpayer's spouse.

The threshold amount is $250,000 for a joint return or surviving spouse, $125,000 for a married individual filing a separate return, and $200,000 for all other filers.

Medicare tax on investment income

Since Jan. 1, 2013, Sec. 1411 of the Internal Revenue Code imposes a tax on individuals equal to 3.8 percent of the lesser of the individual's net investment income* for the year or the amount the individual's Modified Adjusted Gross Income (MAGI) exceeds a threshold amount.

For estates and trusts, the tax equals 3.8 percent of the lesser of undistributed net investment income* or AGI over the dollar amount at which the highest trust and estate tax bracket begins.

The threshold amount is $250,000 for married individuals filing a joint return and surviving spouses, $125,000 for married taxpayers filing separately, and $200,000 for other individuals.

*Net investment income is investment income reduced by deductions properly allocable to that income. Investment income includes income from interest, dividends, royalties, rents, and net gain from disposition of property (other than such income derived in the ordinary course of a trade or business). However, income from a trade or business that is a passive activity and from a trade or business of trading in financial instruments or commodities is included in investment income.

STRATEGIES TO CONSIDER

Annual year-end planning is most often focused on income taxes. Other considerations that should be reviewed and discussed with your advisor include:

Current asset allocations and portfolios

Work with your advisor to ensure that your allocation is aligned with your goals and time horizon for both your taxable and tax-deferred accounts. Make any adjustments as necessary.

Estate planning documents

Make sure your documents and beneficiary designations are still appropriate for your plans and goals, especially if you have had a recent life change – marriage, birth of a child, moved to a new state or had an increase in wealth.

Timing of income and deductions

Higher income tax rates and limitations on personal exemptions and itemized deductions merit a discussion with your tax advisor regarding the timing of income, including income type and deductions.

IRAs

If you reached age 70½ in 2016, you will be required to take a minimum distribution from your traditional IRA by April 1, 2017. Keep in mind that if you wait until 2017 to take your first required minimum distribution, you will be required to take two required minimum distributions in 2017 (your first distribution that you chose to delay until April 2017, plus the required minimum distribution for 2017 distributed by December 31, 2017). If you were over age 70½ before 2016, you must take your 2016 required minimum distribution by December 31. If you are under 70½, consider converting some or all of your traditional IRA to a Roth IRA. Any decision on your retirement accounts should be based on your individual situation. A conversion can occur in one year or over several years.

Gifting plans

The 2016 annual gift exclusion is $14,000 for direct gifts to individuals (i.e., cash, property, loan forgiveness). Gifts not subject to the annual gift exclusion include education costs and medical costs if the payment is made directly to the educational institution or medical provider. Taxpayers also have the highest lifetime gifting exemption in history this year. In 2016, you can gift $5.45 million (per individual) tax free either during your life or at death.

Dividend-paying assets (in taxable accounts)

Preferential treatment on qualified dividends still exists. The tax rate on qualified dividends (15 or 20 percent) is dependent on your income tax bracket. In addition, all dividends may be subject to the 3.8 percent Medicare Contribution Tax. Assuming it complements your financial goals, you may consider working with your advisor to rebalance your portfolio with less of an emphasis on dividend paying stocks.

Gains and losses in taxable accounts

Preferential treatment on long-term capital gains still exists. The tax rate on long-term capital gains (15 or 20 percent) is dependent on your income tax bracket. In addition, some gains may be subject to the new 3.8 percent Medicare Contribution Tax. If the investment analysis requires changes in taxable accounts, review possible gains and losses and the timing of such in tax years 2016 and 2017 in conjunction with the: 1) Individual income tax bracket, 2) Pease and Personal Exemption phase-outs, and 3) Medicare Tax on investment income.

BUSINESS TAX STRATEGIES

Affordable Health Care Act

The “employer shared responsibility” provision of the Affordable Health Care Act requires large employers to offer affordable health insurance that provides minimum value to all full-time employees. If such coverage is not provided, the employer will be assessed a penalty.

- Employers with 100 or more full-time employees were subject to the “employer shared responsibility provisions” in 2016. The penalty is applied if minimum essential coverage is not offered to 95 percent or more of their full-time employees, so large employers may need to assess their health plan offerings to maintain compliance.
- Employers with between 50 and 99 full-time employees will be subject to the “employer shared responsibility provisions” in 2016 with the 95 percent threshold applying immediately.
- Employers (both with 50-99 and 100 or more employees) who are subject to reporting requirements must report to the employee by Mar. 2, 2017. This deadline was previously Jan. 31 and is an extension for tax year 2016 only. Reporting required to be furnished to the IRS must be filed by Feb. 28, 2017 (or March 31 if filed electronically).

Defer or accelerate income and deductions

For pass-through entities such as sole proprietorships, S corporations, partnerships and LLCs, the owners’ share of income is taxed at personal income tax rates.

- If the owner expects to be in the same or lower tax bracket in 2017 as they were in 2016, deferring income to 2017 and accelerating deductions in 2016 will cause some tax to be deferred.
- If the owner expects business income to increase in 2017, thereby putting the owner in a higher personal tax bracket for 2017, the business might consider accelerating income in 2016 and pay tax at the lower 2016 bracket, while deferring deductions to 2017 and offsetting income taxed at the higher 2017 bracket.

For C corporations, compare 2017 income and tax rates to 2016 income and rates.

- If the corporation expects to be in the same or lower bracket in 2017, the corporation might defer income to 2017 and accelerate deductions in 2016.
- If the corporation expects to be in a higher bracket in 2017, the corporation might accelerate income in 2016 and defer deductions to 2017.

Section 179 expensing

Section 179 allows businesses to expense part or all of the cost of new and used qualified property they acquire in the year when the assets are placed in service. There is an annual limit of $500,000 on the amount of expenses that can be deducted under Section 179.

Bonus depreciation

Bonus depreciation allows businesses to claim additional first-year (or bonus) depreciation for eligible property acquired and placed in service in that year. In 2015, Congress passed the PATH Act, which included an extension of bonus depreciation through the end of 2019. However, the bonus depreciation allowance will be gradually phased out as follows:

- 50 percent bonus depreciation allowance through 2017
- 40 percent in 2018
- 30 percent in 2019

Other tax credits

In addition to the Section 179 and bonus depreciation provisions, many other deductions and credits enjoyed in prior years have been extended or made permanent. The PATH Act of 2015 extended or made permanent the following provisions:

- Research and Development Tax Credit was made permanent.
- New Markets Tax Credit extended through 2019.
- Work Opportunity Tax Credit extended through 2019.
- 15-Year Straight-Line Cost Recovery for Qualified Business Improvements was made permanent.

2016 TAX SHEET

MARRIED, JOINT		
If Taxable Income Is Between:	*Your 2016 Tax Is:*	*Of Amount Over:*
$0-$18,550	10%	$0
$18,551-$75,300	$1,855 + 15%	$18,550
$75,301-$151,900	$10,367.50 + 25%	$75,300
$151,901-$231,450	$29,517.50 + 28%	$151,900
$231,451-$413,350	$51,791.50 + 33%	$231,450
$413,351-$466,950	$111,818.50 + 35%	$413,350
$466,951 and above	$130,578.50 + 39.6%	$466,950
SINGLE		
$0-$9,275	10%	$0
$9,276-$37,650	$927.50 + 15%	$9,275
$37,651-$91,150	$5,183.75 + 25%	$37,650
$91,151-$190,150	$18,558.75 + 28%	$91,150
$190,151-$413,350	$46,278.25 + 33%	$190,150
$413,351-$415,050	$119,934.75 + 35%	$413,350
$415,051 and above	$120,529.75 + 39.6%	$415,050
MARRIED FILING SEPARATELY		
$0-$9,275	10%	$0
$9,276-$37,650	$927.50 + 15%	$9,275
$37,651-$75,950	$5,183.75 + 25%	$37,650
$75,951-$115,725	$14,758.75 + 28%	$75,950
$115,726-$206,675	$25,895.75 + 33%	$115,725
$206,676-$233,475	$55,909.25 + 35%	$206,675
$233,476 and above	$65,289.25 + 39.6%	$233,475
HEAD OF HOUSEHOLD		
$0-$13,250	10%	$0
$13,251-$50,400	$1,325 + 15%	$13,250
$50,401-$130,150	$6,897.50 + 25%	$50,400
$130,151-$210,800	$26,835 + 28%	$130,150
$210,801-$413,350	$49,417 + 33%	$210,800
$413,351-$441,000	$116,258.50 + 35%	$413,350
$441,001 and above	$125,936 + 39.6%	$441,000
ESTATES AND TRUSTS		
$0-$2,550	15%	$0
$2,551-$5,950	$382.50 + 25%	$2,550
$5,951-$9,050	$1,232.50 + 28%	$5,950
$9,051-$12,400	$2,100.50 + 33%	$9,050
$12,401 and above	$3,206 + 39.6%	$12,400

CORPORATIONS	
$0-$50,000	15%
$50,001-$75,000	25%
$75,001-$100,000	34%
$100,001-$335,000	39%[1]
$335,001-$10,000,000	34%
$10,000,001-$15,000,000	35%
$15,000,001-$18,333,333	38%
$18,333,334 and above	35%

[1] *Reflects a 5% surtax which phases out the benefit of the 15% and 25% rates.*

STANDARD DEDUCTION	
Married, Joint	$12,600
Single	$6,300
Head of Household	$9,300
Married, Separate	$6,300
Blind or over age 65: Married - add $1,250; Single - add $1,550	

ITEMIZED DEDUCTIONS PHASE OUT BEGINS	
Married, Joint	$311,300
Single	$259,400
Married, Separate	$155,650
Head of Household	$285,350

Personal Exemption	$4,050

Kiddie Tax Exclusion	$2,100

PERSONAL EXEMPTION PHASE OUT BEGINS	
Married, Joint	$311,300
Single	$259,400
Married, Separate	$155,650
Head of Household	$285,350

ALTERNATIVE MINIMUM TAX EXEMPTION AMOUNT	
Married, Joint	$83,800
Single	$53,900
Married, Separate	$41,900
Head of Household	$53,900

FICA/SECA RATES	
Employee OASDI Component	6.2%
Self Employed OASDI Component	12.4%

3.8% MEDICARE SURTAX ON UNEARNED INCOME BEGINS	
Married, Joint	$250,000
Married, Separate	$125,000
Others	$200,000

0.9% ADDITIONAL MEDICARE TAX ON WAGES BEGINS	
Married, Joint	$250,000
Married, Separate	$125,000
Others	$200,000

QUALIFIED DIVIDENDS AND CAPITAL GAINS	
That would otherwise be taxed at	10% or 15%
Are taxed at	0%
That would otherwise be taxed at	25% - 35%
Are taxed at	15%
That would otherwise be taxed at	39.6%
Are taxed at	20%

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IRA AND PENSION PLAN LIMITS

IRA CONTRIBUTION LIMIT - LESSER OF TAXABLE COMPENSATION OR:	
Under age 50	$5,500
Age 50 and over (Under 70½ for Traditional)	$6,500
PHASE OUT FOR DEDUCTING IRA CONTRIBUTIONS	
Married, Joint	$98,000-$118,000 MAGI
Married, Separate	$0-$10,000 MAGI
Single, Head of Household	$61,000-$71,000 MAGI
Phase out for deducting spousal IRA	$184,000-$194,000 MAGI
PHASE OUT OF ROTH CONTRIBUTION ELIGIBILITY	
Married, Joint	$184,000-$194,000 MAGI
Single, Head of Household	$117,000-$132,000 MAGI
Married, Filing Separately	$0-$10,000 MAGI
SELF-EMPLOYED PENSION (SEP) CONTRIBUTIONS	
Contribution Limit:	
Employees	25% of Compensation up to $53,000
Self-Employed Persons	20% of Earned Income up to $53,000
Annual Compensation Threshold for Requiring SEP IRA Contribution	$600
SIMPLE ELECTIVE DEFERRAL	
Under age 50	$12,500
Age 50 and over	$15,500

401(k), 403(b), 457 and SARSEP elective deferral under age 50	$18,000
401(k), 403 (b), 457 and SARSEP elective deferral age 50 and over	$24,000

QUALIFIED RETIREMENT PLAN EMPLOYER CONTRIBUTION LIMITS	
Annual defined contribution limit	$53,000
Annual defined benefit limit	$210,000
Highly compensated employee	$120,000
Key employee in top heavy plans makes	$170,000
Annual compensation for qualified plans	$265,000

RETIREMENT TAX CREDIT	
Married, Filing Jointly	Below $61,000 AGI
Head of Household	Below $46,125 AGI
Single, Married Filing Separately	Below $30,750 AGI

EDUCATION	
Coverdell Education Savings Account	$2,000
Coverdell contribution eligibility phaseout	
Married, Joint	$190,000-$220,000
All Others	$95,000-$110,000

STUDENT LOAN INTEREST DEDUCTION LIMIT	
Married, Joint	$130,000-$160,000
All Others	$65,000-$80,000

PHASE OUT OF LIFETIME LEARNING CREDIT	
Married, Joint	$110,000-$130,000
All Others	$55,000-$65,000

PHASE OUT OF AMERICAN OPPORTUNITY CREDIT[2]	
Married, Joint	$160,000-$180,000
All Others	$80,000-$90,000

[2] Formerly Hope Credit

TAX FREE SAVINGS BOND INTEREST PHASED-OUT	
Married, Filing Jointly	$116,300-$146,300
All Others	$77,500-$92,500

GIFT AND ESTATE TAX	
Gift Tax Annual Exclusion	$14,000
Gift Tax Rate	Maximum 40%
Lifetime Gift Exemption (Unified with Estate Tax)	$5,450,000
Estate Tax Rate	Maximum 40%
Estate Tax Exemption (Unified with Gift Tax)	$5,450,000
GST Tax Rate	40%
GST Exemption	$5,450,000
Annual exclusion for gifts to non-citizen spouses	$148,000

Unused Exemption Available to Surviving Spouses

SOCIAL SECURITY	
FICA taxable income limit	$118,500

MARRIED, SEPARATE[3]	
50% taxable	$0 MAGI
85% taxable	$0 MAGI

MARRIED, JOINT[3]	
50% taxable	$32,000 MAGI
85% taxable	$44,000 MAGI

SINGLE[3]	
50% taxable	$25,000 MAGI
85% taxable	$34,000 MAGI

Source: Internal Revenue Service

[3] Percentage of benefit taxable above MAGI threshold.

GET STARTED TODAY

It is important to remember that these are just some of the tax planning highlights that affect many of our clients.

Tax laws are extremely complex and fluid, and your personal situation should be considered. However, time is running out to make some of these important planning moves before the year's end.

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