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Client Information Bulletin

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Last Chance for Key Tax Deductions?

Opportunities vanishing after 2017 returns

The new tax law enacted at the end of last year—the Tax Cuts and Jobs Act (TCJA)—provides numerous tax changes for individuals, including tax rate cuts and a higher standard deduction. Significantly, the TCJA also eliminates or modifies certain deductions, including the majority of itemized deductions, beginning in 2018. As a result, fewer taxpayers are expected to itemize returns in the future.

However, these deductions are still available on the 2017 returns being filed in 2018, based on prior law. The following is a brief summary.

State and local taxes (SALT): For 2017, you can deduct your (1) state and local property taxes *and* (2) state and local income taxes *or* state and local sales taxes. Beginning in 2018, the SALT deduction is limited to $10,000 annually for any combination of the two.

Mortgage interest: Generally, you are able to deduct interest paid on the first $1 million of acquisition debt and $100,000 of home equity debt. For loans that were made after December 15, 2017, the acquisition debt level is reduced to $750,000, and the home equity debt deduction is repealed after 2017.

Casualty and theft losses: Under pre-TCJA law, losses are limited to the excess above 10% of adjusted gross income (AGI), after subtracting $100 per event. After 2017, this deduction is eliminated, except for disaster-area losses.

Miscellaneous expenses: On 2017 returns, taxpayers can deduct miscellaneous expenses, including unreimbursed employee business expenses, to the extent the annual total exceeds 2% of AGI. Beginning in 2018, this deduction has been eliminated.

Moving expenses: Prior to 2018, you could claim qualified job-related moving expenses as an above-the-line deduction. This deduction, available on 2017 returns, has been repealed by the new tax law, except for expenses incurred by active-duty military personnel.

Domestic production activities: Under Section 199 of the tax code, an above-the-line deduction is allowed in 2017 for qualified domestic production activity expenses. This Section 199 deduction, which is often claimed by manufacturing operations, is no longer available after 2017.

Alimony deductions: For 2017, payers of alimony may deduct the payments, while the income is taxable to the recipients. The TCJA repeals this above-the-line deduction, eliminating the tax consequences for recipients, for divorce or separation agreements entered into

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Do You Need More Time to File?

Are you having trouble getting all your tax return information together in time for the April 17 deadline? Don't despair.

You can request an automatic six-month filing extension—with no questions asked by the IRS. This gives you until October 15, 2018, to file your 2017 return.

Caveat: A filing extension is not an extension to pay tax. Make a reasonable estimate of the amount you owe, and pay the IRS by April 17.

after 2018. (Thus, this deduction is essentially extended for one more year.)

Note that the TCJA retains itemized deductions for charitable donations, gambling losses and medical expenses. In fact, the medical deduction threshold is lowered to 7.5% of AGI for 2017 and 2018 (see below). In addition, the new law preserves above-the-line deductions for student loan interest, IRA contributions and educator expenses, to name a few.

The TCJA changes for individual taxpayers are generally scheduled to sunset after 2025, but that is a long way off. Practically speaking, this may be the last year you are entitled to claim certain deductions in full or at all. Consult your tax adviser to maximize the tax benefits.

Favorable Tax Treatment for Medical Expenses

New law creates retroactive tax break

The Tax Cuts and Jobs Act (TCJA) repeals or cuts back many deductions on personal returns (see page 1), but the medical expense deduction survived the chopping block. In fact, the new law temporarily enhances the deduction, retroactive to the 2017 tax year. In other words, you can benefit from this tax-favored treatment on the 2017 return you file in 2018.

Background: The deduction for medical expenses is limited to the unreimbursed expenses above an annual threshold based on adjusted gross income (AGI). The Affordable Care Act (ACA) increased the threshold from 7.5% of AGI to 10% of AGI (except for a temporary reprieve for senior citizens). Now the TCJA restores the lower 7.5%-of-AGI threshold for all taxpayers, but only for the 2017 and 2018 tax years.

For example, if you have an AGI of $100,000 for 2017 and $9,500 of unreimbursed medical expenses, you can deduct $2,000. Previously, your deduction would have been zero.

Thus, scour your records to find expenses that may help you qualify for a deduction in 2017 or increase your existing deduction. Here are some common examples of expenses you might have missed:

♦ **Transportation costs:** The deductible amount is not limited to the actual cost of the physician's or hospital's services. You may also deduct the cost of traveling to and from the treatment (even if similar treatment is available nearby). If you travel by car, you can either deduct your actual automobile expenses or a flat rate of 17 cents per mile in 2017 (increased to 18 cents per mile in 2018). While the flat-rate method is more convenient, you may come out ahead by keeping track of your actual expenses.

♦ **Lodging costs:** You can also deduct the cost of staying at a hotel or motel while you are receiving medical care away from home. However, the accommodations cannot be "lavish or extravagant." The deductible amount for lodging is limited to $50 per day. If a companion's presence on the trip is required, the cost of the companion's lodging is also deductible (subject to the $50-per-day limit).

♦ **Nursing care:** If a family member needs nursing services in the home, the cost of such services is a deductible medical expense. The medical care does not have to be provided by a registered or trained nurse. In other words, you can pay someone else (e.g., another family member) to provide the care, and you can deduct the expense.

♦ **Capital improvements:** You can deduct the cost of a home improvement if the improvement is made for a medical reason. For instance, the cost of installing central air conditioning to alleviate a child's asthma is deductible. The amount eligible for the deduction is the cost above the increase in the value of your home.

Side benefit: The cost of maintaining and operating the improvement also qualifies for the deduction.

Of course, medical expense deductions are available only if you itemize instead of claiming the standard deduction. For many taxpayers, this may be the last year these expenses are deductible, in light of the TCJA changes.

Pressing Needs for Corporate Minutes

Protection for your company

Naturally, it takes some time to record corporate minutes in a business setting. But it is usually time well spent. Plus, it is now easier to have minutes prepared than it was years ago, due to improvements in computer software.

Significantly, corporate minutes can serve as the proof you need in order to back up your position if the IRS challenges an item on your return. Furthermore, they can help shield business owners from personal liability for corporate debts. In particular, corporate minutes can be especially valuable in three key areas:

***1.* Executive compensation:** Your company can deduct compensation—salaries, bonuses and so on—paid to corporate officers as a business expense. However, the compensation must be "reasonable in amount" for the services rendered. If the IRS considers the compensation unreasonable (i.e., a disguised dividend), the deduction may be denied. There are a few steps you can take via the corporate minutes to justify the deductibility of compensation paid:

♦ Set down the salaries of all officers, and specify the procedures for salary adjustments and bonuses.

♦ Have the board of directors declare a dividend and specify the return on its capital investments.

♦ Spell out the details of any unusual circumstances (e.g., an officer who takes on additional responsibilities in an understaffed office).

♦ Describe the nature and complexity of each officer's duties.

***2.* Accumulation of earnings:** If a company retains earnings beyond the reasonable needs of the business, it may have to pay a 20% penalty tax. This tax is not imposed unless the accumulated earnings exceed $250,000 (the limit is $150,000 for personal service corporations).

However, corporate minutes may be able to protect your company from this penalty. For example:

♦ The minutes can show detailed expansion plans that justify retention of earnings.

♦ They can point out extenuating business circumstances (e.g., a cyclical sales flow or the threat of a strike).

♦ The minutes can reflect the intent to retain earnings only to cover working capital for the year, based on a precise formula.

***3.* Records of board meetings:** Whenever the board of directors meets, a record of the discussions should be included in the corporate minutes. **Reason:** If a dispute arises later on, the minutes can be used to settle the controversy. For instance, minutes can be valuable in the following situations: election of officers, declaration of dividends, acceptance of contracts, approval for mergers, authorization of loans, project reports and compliance with governmental regulations.

Of course, there is no absolute guarantee that a dispute will be settled in your favor, but the corporate minutes are probably the best proof you can have.

In summary: It is important that your corporate minutes be accurate and precise. But that's not enough. You also must make sure that they are updated to reflect any changes.

Give Us A Call!

*Do you have any questions or comments about **Client Information Bulletin** or your individual situation? Please do not hesitate to contact our office. We would be glad to serve you in any way we can.*

Compare the Two Types of IRAs

Distinguishing traditional IRAs from Roths

There are two basic types of IRAs: the traditional IRA and the Roth IRA. With either one, the deadline for contributions for the 2017 tax year is April 17, 2018. There are no extensions for making IRA contributions for 2017, even if you obtain an extension for filing your return (see page 2).

It is important to know the similarities and distinctions of the two types of IRAs. For starters, the annual limit for contributions to either IRA for the 2017 tax year is $5,500. (It remains the same in 2018.) Plus, you can add another $1,000 if you are age 50 or older. There is no current tax on the contributions' earnings within any account.

Generally, you can contribute to an IRA if you receive earnings or other compensation from a job. However, the ability to contribute to a Roth IRA is limited or eliminated for certain high-income taxpayers. Here are the other main differences to keep in mind:

1. Traditional IRAs: Contributions may be wholly or partially deductible. But deductions are phased out if your modified adjusted gross income (MAGI) exceeds a specified level and you (or your spouse, if you are married) are an active participant in an employer-sponsored retirement plan. Therefore, for many individuals, no part of the contribution to a traditional IRA is tax-deductible.

When you receive distributions from a traditional IRA, you are taxed at ordinary income tax rates on the portion representing deductible contributions and earnings. In addition, you will have to pay a 10% penalty tax on withdrawals made before age 59½ unless one of the special tax law exceptions applies.

2. Roth IRAs: Unlike contributions to a traditional IRA, contributions to a Roth are never tax-deductible, regardless of your MAGI. But there is a potential payoff on the back end that you cannot realize with a traditional IRA: Qualified distributions from a Roth in existence for at least five years are 100% tax-free. For this purpose, qualified distributions include withdrawals made after age 59½, those made on account of death or disability, or those used to pay qualified first-time homebuyer expenses (up to a lifetime limit of $10,000).

Other distributions are taxed as ordinary income under "ordering rules." Contributions are treated as coming out first, followed by conversion and rollover amounts and then earnings. Thus, even if you do not receive qualified distributions, part or all of the payout may be tax-free.

Due to the lure of tax-free distributions, you might consider converting some or all of the funds in your traditional IRA to a Roth IRA. But be aware that the conversion itself is taxable at ordinary income rates, just like a withdrawal. Also, if you must use funds being transferred to pay the resulting conversion tax, it will dilute some of the tax benefit.

Which type of IRA is best for you? It depends on a number of variables, such as your current and future expected tax rates and your personal circumstances. Rely on your professional advisers to provide guidance.

Facts and Figures

Timely points of particular interest

➡**Tax Review**—The IRS imposes strict recordkeeping requirements for travel expenses. **Case in point:** To save money, a movie producer spent nights at his ex-wife's and aunt's homes while away on business. He did not pay lodging costs, but he supplied groceries and other household items. The Tax Court limited the deduction due to a lack of substantiation.

➡**SIMPLE Does It**—As with other retirement plans, older participants in a Savings Incentive Match Plan for Employees (SIMPLE) can boost contributions. The regular contributions limit for SIMPLEs is $12,500, but those age 50 or older can add another $3,000, for a total of $15,500. (Both figures are the same as they were in 2017.) This increases the retirement nest egg.

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