Gianno & Freda
Financial Center

It's Not What You Earn, It's What You Keep

THE TIME IS NOW!

HIGHLIGHTS OF YEAR END TAX SAVINGS MOVES

But, you must move quickly, year-end 2019 looms

(Dec. 2019 by Mark Gianno and our crack tax staff!)

The shortened days and crisp New England air remind us of the rapid approach of the end of the tax year for most businesses and all individuals. December finds the tax professionals at the Gianno and Freda Financial Center focusing on determining the year-to-date income of our business and individual clients and projecting the likely income tax effect on that income. Right now, we can recommend strategies for you to defer income or accelerate expenses if you are in higher tax brackets. Or, perhaps you find yourself in an unusually low tax bracket allowing you to accelerate income, such as increasing retirement distributions, at a low tax cost.

But, the window for benefitting from most of those strategic moves in 2019 will close on December 31. The point is, ***call us now to learn what your 2019 tax bill may look like, and take steps to manage your tax liability.***

Of course, this year-end letter doesn't afford us the luxury of covering the vast array of tax issues you might face. For now, let's summarize some of the most prominent issues and strategies. First, some issues for businesses, then a discussion of strategies for individuals.

I hope you will call me to discuss areas of tax and financial concern to you.

FOR BUSINESSES

By now, every business owner should be aware of their likely 2019 business income and the related income tax impact. If this is a high income year, there are a few things you ***must*** consider before the year closes. One is the accelerated depreciation on qualified business property placed in service by purchase/lease before year end. Another important deduction is a contribution to your retirement account(s) (this can even be done *after* year end). A third is to maximize your Qualified Business Income deduction, a major benefit for closely held businesses created in the 2017 tax law.

Accelerated Depreciation Deduction

For many years businesses could immediately write-off (under Internal Revenue Code Sec. 179) the purchase/lease of new or used equipment and furniture and fixtures that otherwise had to be depreciated (expensed) over the years it was used in the business. The property must be purchased/leased and put into service in the year in which you claim the deduction. Putting an asset into service means that you have it set up and working and you are using it in your business. The 2017 tax law extended this Sec. 179 benefit to deductions for nonresidential real property (buildings) improvements. These improvements must be made after the building is in use. The 2017 tax law also put a new limit on the first-year deduction available for the purchase/lease of SUVs. This immediate write-off helps your business reduce income in higher tax brackets by allowing you to take a depreciation deduction for certain assets (capital expenditures) in one year, rather than depreciating them over a longer period of time.

Retirement Account Contributions

Perhaps the best application of our firm's motto, "It's not what you earn, it's what you keep", is maximizing your contributions to your retirement account(s). ***Where else in the tax code do you get a deduction for paying yourself?***

There is a wide variety of retirement plans available to your business. Whether a SIMPLE IRA, SEP IRA, 401(k), Roth 401(k) or a combination of retirement plans is best suited to you varies based on many factors, including the size of your workforce, the age of the workforce, and the amount you are willing to invest. Call me to discuss how you can maximize what you keep by intelligent retirement planning.

Qualified Business Income Deduction

A major benefit in the 2017 tax law for closely-held businesses is the 20% deduction for qualified business income (QBI). This deduction benefits most operating business entities and rental real estate. Entities taxed as S corporations are especially well suited for this deduction. Certain professions (law, medicine, accounting, etc.) are ineligible for the deduction at higher incomes. At higher incomes all businesses face limitations for this deduction based on wages paid and/or the value of real estate in the business. There is an ideal balance to be struck between wages and profits. It is well worth your time to determine ***before*** year end how this deduction might apply to

your business. Give me a call to help you calculate your deduction.

Reasonable Compensation

One of the tax benefits available to owners of S corporations is the elimination of Social Security or self-employment taxes that apply to wages, or to profits from a partnership or sole-proprietorship. Many sole-proprietors regularly pay more in self-employment taxes than income taxes. By electing to be taxed as a Subchapter S Corporation (S Corp), income from sources other than your personal work efforts can legitimately escape self-employment taxes.

However, success in this strategy is completely dependent on the owner receiving a reasonable wage for their work effort. The concept of a reasonable level of wage compensation to business owners is often ignored to the detriment of the taxpayer. I repeatedly see situations in which a business owner incorporates their business, or creates an LLC, makes an S election for the new entity, then fails to pay a wage to themselves for their work effort. **By this method they attempt to shelter ALL of their income from self-employment and Social Security taxes. The IRS regularly challenges this structure, and almost always wins**. The result? Retroactive tax bills with substantial penalties and interest applied.

The IRS and the courts have developed formulas to determine reasonable salary levels for business owners. While these formulas are based on facts and circumstances, and are more art than science, we have studied the formulas in the various rulings and use them to benefit our many business clients. I am happy to work with you to determine your reasonable compensation level compliant with the IRS while maximizing your benefit in the balance between wages and business profit.

Sundry Business and Personal

-Qualified Small Business Stock sales can avoid tax on 50% to 100% of taxable gain to a maximum of $10 million. Restrictions apply.

-Capital gains from the sale of any type of capital asset can be deferred by reinvesting the sale proceeds in an Opportunity Zone Fund. There are complex requirements, but the benefits far exceed the benefits provided by deferral under Code Sec. 1031.

-Cost Segregation studies can provide tax savings by increasing the depreciable portion of a purchase comprising buildings, machinery and equipment and non-depreciable land. In addition, the cost segregation analysis can allocate more value to faster depreciating assets.

We are closely watching developments in business taxation strategies for you. Give me a call to discuss your personal concerns.

For Individuals

It's important to be ever-mindful of your potential income tax liability in order to make smart adjustments ***before*** year end. At higher income levels you should ensure that you implement traditional tax reduction strategies such as maximizing retirement plan contributions, harvesting losses (if there are any!) in your investment portfolios, deferring income into next year and accelerating deductible expenses into this year.

Alternatively, you may find yourself in an unusually low, even zero income tax bracket. This presents a different set of excellent planning opportunities. For instance, remember that the success of all of our retirement planning hinges on being taxed in a ***lower bracket*** when you receive your retirement benefits than your bracket when you deferred the income by contributing to the account. In this case, accelerated IRA withdrawals and converting an IRA to a Roth IRA can effectively use up the lower tax brackets. **It is a terrible waste to leave a zero or 10% tax bracket unused.** Working together before year end we can identify your most beneficial strategies.

Capital Gains

Our long-standing clients know that I consider paying taxes on capital gains a voluntary tax contribution. The reason is that there are multiple ways to avoid recognizing a taxable capital gain. I immediately count six different ways that you can defer or avoid paying capital gains taxes. **Call me *before* you sell.**

Each year I run out of space in this year-end newsletter before I run out of tax saving opportunities to report. While I may not have included a topic of particular interest to you, I am most happy to hear your concerns. **We are honored to be your trusted adviser and partner. Please contact us when you are ready to talk through year-end planning.**

Best wishes for good health and good fortune to you and your family in 2020. I hope you enjoy your holiday celebrations with those you love.