

# Client Bulletin

Smart Tax, Business & Planning Ideas *from your Trusted Business Advisor*<sup>SM</sup>

## Deducting Taxes Paid



When you file your 2015 federal income tax this year, you can take a standard deduction. For 2015, that's \$6,300 for single taxpayers and for married individuals filing separately; \$12,600 for couples filing jointly and for certain widow(er)s; and \$9,250 for those filing as heads of household. The beauty of taking the standard deduction is that it's simple: There's no need to gather information and scant risk of triggering an audit.

However, taking the time to itemize deductions can be a tax saver. If your itemized deductions exceed the standard amounts, you'll generally come out ahead by listing them on Schedule A of Form 1040. Indeed, the amount you can claim under "Taxes You Paid" may be enough to justify itemizing.

### Property tax

You can itemize the property tax you pay for your home. If you have a second home, the tax on that property also can be deducted. In fact, you can deduct any amount of tax you pay on any number of homes that were not used for business, even if they're in different states or out of the United States.

The key here is to deduct the payment for the year in which it was paid. If you had a property tax payment due in January or February 2016, for instance, and you sent in the payment in December 2015, that amount can be an itemized deduction in 2015.

If you make monthly mortgage payments on a home, a portion of each payment might go into an escrow account for eventual forwarding to the property tax collector. In this scenario, the property tax payments are deductible for the year in which the money is actually paid out of the escrow account to the taxing authority.

So-called "local benefits taxes" paid by property owners may or may not be deductible, depending on how the money is used. Our office can determine whether you can deduct such taxes. You also may be able to deduct personal property tax, assessed on the value of items, such as boats or cars.

January 2016

## What's Inside

- 1 Deducting Taxes Paid
- 2 Deducting IRA Contributions
- 3 Going Outside to Sell Your Company
- 4 Tax Calendar

### Down to Zero

*The 0% cost-of-living adjustment (COLA) for Social Security benefits in 2016 follows COLAs of only 1.7% in 2013, 1.5% in 2014, and 1.7% in 2015, far below the 4.1% historical average.*

### Safe Harbor LLP

5812 Geary Blvd.,  
San Francisco, CA 94118  
ph. (415) 742 - 4249  
fx. (415) 742 - 4924

## Trusted Advice

### Not Deductible

Following is a list of taxes and other expenses that are not deductible taxes:

- Federal income and most excise taxes
- Social Security, Medicare, federal unemployment (FUTA), and railroad retirement (RRTA) taxes
- Customs duties
- Federal estate and gift taxes
- Tax on gasoline
- Car inspection fees
- Assessments for sidewalks or other improvements to your property
- License fees (marriage, driver's, dog, etc.)

### To be decided

State and local income tax you paid also can be deducted on Schedule A. That includes amounts withheld from paychecks as well as any estimated state or local estimated income tax you paid during the calendar year.

For the past decade, taxpayers have had the option of deducting state and local *sales* tax instead of state or local *income* tax, if that provides a greater deduction. This provision has expired several times, only to be renewed. As of this writing, the sales tax deduction opportunity is not in effect for 2015, but it's likely that Congress will have restored it by the end of the year.

A sales tax deduction obviously appeals to residents of states or localities with no income tax. If you live in an area with an income tax—and if you are itemizing deductions—you should see which choice provides the greater tax savings.

**Example 1:** Marge Collins pays enough property tax to make itemizing worthwhile. When getting her records together for tax preparation, Marge discovers that she paid a total of \$3,000 in state income tax in 2015. Assuming the sales tax deduction has been restored for 2015, Marge should see how much sales tax she paid last year. If the total exceeds \$3,000, she probably should deduct sales tax instead of state income tax.

How can Marge determine the amount of sales tax she paid, throughout 2015? One way is to go through all of her receipts for the year, and calculate the sales tax she paid on purchases.

Many people don't keep all their receipts, though. If you're in that category—and if the rules for 2015 are the same as they were for 2014—you can use the optional sales tax

table provided by the IRS, in the instructions to Form 1040.

That table shows the amount of the sales tax you're estimated to have paid in the relevant year, depending on your income, where you live, and the exemptions you claim. Note that "income," for this purpose, includes not only your adjusted gross income but also inflows such as tax-exempt interest and nontaxable Social Security benefits. The greater your income, the more sales tax you're presumed to have paid.

What's more, the IRS tables don't assume you have made any large purchases. Thus, the resulting amount from the tables can be increased by any sales tax you paid for a car (bought or leased), motorcycle, boat, airplane, motor home or similar items.

Last year, a Sales Tax Deduction Calculator was offered at [irs.gov](http://irs.gov). The IRS asked for a few simple entries in order to illustrate the amount of state and local sales tax you could claim. Assuming the sales tax deduction is reinstated for 2015, this calculator may help you get your records ready for tax preparation. ■

## Did You Know?

**A** couple, both aged 65 and retiring in 2015, could expect to spend an estimated \$245,000 on health care throughout retirement, up from \$220,000 in 2014 and \$190,000 in 2005. Those numbers assume enrollment in Medicare but exclude any long-term care expenses. Reasons for the upward trend include longer life expectancies as well as anticipated increases for medical bills and prescription drug costs.

Source: [fidelity.com](http://fidelity.com)

# Deducting IRA Contributions

The deadline for 2015 IRA contributions is April 18, 2016. Workers and their spouses who were under age 70½ at year-end 2015 can each contribute up to \$5,500, or \$6,500 for those 50 and older. For traditional IRAs, income limits don't apply.

That is, those named can make contributions of these amounts to a traditional IRA. Whether those contributions will be tax-deductible is another matter. In any case, investment earnings inside an IRA will be untaxed until money is withdrawn.

## Deduction limits based on plan participation

**Worker not covered by plan.** If a worker was not covered by an employer's retirement plan in 2015, IRA contributions are deductible. Income is not an issue.

**Example 1:** Nora Dixon, age 29, works for a small computer graphics company that does not offer a retirement plan to its employees. Nora's husband Oliver, also 29, is a physical therapist who is not covered by a retirement plan. Both Dixons can deduct traditional IRA contributions up to \$5,500 each for 2015, no matter how much they earn.

**Worker covered by plan.** However, for workers who were

covered by an employer plan, income will determine deductibility. To deduct the maximum amount as a single filer, your modified adjusted gross income (MAGI) for 2015 must be \$61,000 or less; you can take a partial deduction with MAGI up to \$71,000. Over \$71,000 of MAGI, single filers who are covered by an employer plan can't deduct any IRA contribution. (For plan-participating married people filing jointly, the 2015 MAGI ceilings are \$98,000 for a maximum deduction and \$118,000 for a partial deduction.)

**Example 2:** Paul and Rhona Benson, both age 44, are each covered by a retirement plan at their jobs. The Bensons had MAGI of \$108,000 in 2015. That's 50% of the way through the phase-out range for joint tax returns. Thus, Paul and Rhona can each contribute up to \$5,500 to traditional IRAs for 2015, and they can each take a \$2,750 tax deduction: 50% of the maximum.

**One spouse covered by plan.** Among married couples with higher incomes, one spouse might be able to deduct all or part of an IRA contribution. That would be the case if one spouse is covered by an employer plan, but the other spouse isn't. The spouse who is not covered can deduct a full 2015 IRA contribution with joint MAGI up to

\$183,000, or a partial deduction with MAGI up to \$193,000.

**Example 3:** Sheila Ford, age 65, is covered by an employer plan at work, while her husband Greg, 68, is retired. Their 2015 MAGI is \$175,000. Both Fords can make a \$6,500 traditional IRA contribution for 2015. However, because their joint MAGI is over \$118,000, Sheila can't take any tax deduction. Greg, on the other hand, is not covered by an employer plan, so he can take a full \$6,500 tax deduction because their joint MAGI is under \$183,000.

Note that traditional IRA contributions are available only to workers and spouses under age 70½. In this example, Greg would not be able to make any IRA contribution if he were age 72, for example.

## The Roth alternative

A taxpayer that can make a deductible traditional IRA contribution can instead make a contribution to a Roth IRA. Roth IRA contributions are never tax-deductible. However, after you've had a Roth IRA for five years and reach age 59½, all distributions are tax-free. Our office can go over the tax aspects with you to help you decide between a nondeductible Roth IRA and a potentially tax-deductible traditional IRA contribution. ■

# Going Outside to Sell Your Company

For business owners who are seeking a successor, the right person might be obvious. If you have a co-owner or partner, a buy-sell agreement can set the terms; if a younger family member is willing and able, you can decide on a way to transfer control. Otherwise, there may be a key employee who's a logical candidate—

or you might hire someone to take over eventually.

In some cases, though, this type of "inside" succession plan won't be possible or practical. You'll have to go outside to find a buyer who will take your place or who will hire someone to run the company. An outside sale can be financially rewarding,

especially if there are multiple bidders, but it also may require more time and effort than a transition to someone you already know.

## Be prepared

An outside buyer will want to know what he or she is getting, in great detail, so be prepared to divulge an enormous

*continued on page 4*

amount of information about your company. One possible approach is to get your books and records in order, then hire a reputable appraiser to value the business. With that valuation you can set an asking price, which may hold down the number of tire kickers and bring out serious buyers.

Negotiations can proceed from there, and not just on the purchase price. The new buyer might want you to stay on for some period of time; in many acquisitions, the ultimate purchase price may involve some type of earnout, where you would receive additional payments based on the business' future performance. The more prepared you are, from a financial as well as a personal commitment standpoint, the more likely the final terms will be agreeable.

## Tax topics

The sale of an asset as valuable as a successful business probably will generate major tax issues. You'll want to maximize the amount you'll receive, but a huge cash inflow in one calendar year is likely to result in a large amount of tax. Even if the amount is favorably taxed as a long-term capital gain, you also might trigger various surtaxes and phaseouts, so that your true after-tax amount winds up being less than you expected.

Accepting an installment sale, with proceeds coming in over several years, could make the transaction less taxing. The buyer may be more comfortable with this arrangement as well. If an earnout is part of the agreement, you might be able to structure the package so that it's heavy on sales

taxed as capital gains rates and lower on earned income, which is generally subject to higher ordinary tax rates.

Keep in mind that the buyer will have tax concerns, too. Often, a business buyer will prefer to acquire the company's assets rather than shares of stock. Those assets may get a new basis, generating larger depreciation deductions. Such a deal structure might not be as favorable to you, the seller, but you might negotiate a plumper purchase price in return for some concessions there.

Expect the buyer to have a tax professional on the team to request favorable terms. If you are selling your company to an outside buyer or to an insider, our office can help you come away with a tax-efficient succession. ■

## TAX CALENDAR

### JANUARY 2016

#### January 15

**Individuals.** Make a payment of your estimated tax for 2015 if you did not pay your income tax for the year through withholding (or did not pay enough in tax that way). Use Form 1040-ES. This is the final installment date for 2015 estimated tax. However, you don't have to make this payment if you file your 2015 return and pay any tax due by February 1, 2016.

**Employers.** For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in December 2015 if the monthly rule applies.

### FEBRUARY 2016

#### February 1

**All businesses.** Give annual information statements (Forms 1099) to recipients of certain payments you made during 2015. Payments that are covered include: (1) compensation for workers who are not considered employees; (2) dividends and other corporate distributions; (3) interest; (4) rents; (5) royalties (6) profit-sharing distributions; (7) retirement plan distributions; (8) original issue discounts; (9) prizes and awards; (10) medical and health care payments; (11) debt cancellations (treated as payment to debtor); (12) payments of Indian gaming profits to tribal members; and (13) cash payments over \$10,000. There are different forms for different types of payments.

**Employers.** Give your employees their copies of Form W-2 for 2015.

For nonpayroll taxes, file Form 945 to report income tax withheld for 2015 on all nonpayroll items, such as backup withholding and withholding on pensions, annuities, and IRAs.

For Social Security, Medicare, and withheld income tax, file Form 941 for the fourth quarter of 2015. Deposit or pay any undeposited tax. If your tax liability is less than \$2,500, you can pay it with the return. If you deposited the tax for the quarter in full and on time, you have until February 10 to file the return.

For federal unemployment tax, file Form 940 (or 940-EZ) for 2015. If your undeposited tax is \$500 or less, you can either pay it with your return or deposit it. If it is more than \$500, you must deposit it. However, if you already deposited the tax for the year in full and on time, you have until February 10 to file the return.

#### February 16

**All businesses.** Give annual information statements (Forms 1099) to recipients of certain payments you made during 2015. Payments that are covered include: (1) amounts paid in real estate transactions; (2) amounts paid in broker and barter exchange transactions; and (3) payments to attorneys.

**Employers.** For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in January if the monthly rule applies.

**Individuals.** If you claimed exemption from income tax withholding last year on the Form W-4 you gave your employer, you must file a new Form W-4 to continue your exemption for another year.

#### February 17

**Employers.** Begin withholding income tax from the pay of any employee who claimed exemption from withholding in 2015, but did not give you a new Form W-4 to continue the exemption for 2016.