

2008 TAX SEMINAR



YEAR-END TAX PLANNING TECHNIQUES



Tax Planning - General

- What is "Tax Planning"
 - Internal 2000 memo – included with materials
- Tax Planning Procedures
 - Why
 - When
 - Who
 - How



Tax Planning - General

- Why
 - Reduce or defer taxes
 - Add value
 - Expectation
 - Peace of mind
- When
 - Ongoing at all times with emphasis on year-end
- Who
 - All clients



Tax Planning - General

- How
 - Utilize our resources and apply thorough planning techniques
 - Individualized – Client by client planning
 - Know / understand the business and the business owner(s)
 - Know / understand current business operations and current family status
 - Know / understand future business operations / goals and owner's individual / family goals
 - Prepare taxable income and tax liability projections***



Tax Planning - General

- Four areas of tax planning
 - Timing / deferral
 - Permanent reduction / savings
 - Rate differential planning
 - Tax credits
- Note: Always better to apply tax planning techniques before committing to and entering into a transaction, rather than afterwards



Tax Planning - General

- Tax planning should never override or be the driving force behind your overall business objectives
- Tax planning should never override or be the driving force behind your overall financial / investment policy



Tax Planning - General

- Tax planning strategies discussed today are based on the premise that we want to LOWER your 2008 income tax liability and will include basic year-end type strategies
- Continue to have your best interests in mind and constantly wish to explore planning issues such as:
 - Entity selection planning
 - Proper fiscal year-end selection planning
 - Adoption of or change in accounting method opportunities



Tax Planning - Business

- Fixed Asset Additions & Depreciation
 - Depreciation – Book vs Tax
 - Proper asset classification
 - Plan year-end fixed asset acquisitions – accelerate into 2008?
 - Amounts paid by credit card are considered “purchased”
 - IRC Section 179 deduction
 - 50% bonus depreciation
 - Vehicle depreciation limits
 - Cost Segregation Study – Real Estate – Added value due to IRC Section 179 and Bonus depreciation opportunities and energy deduction studies***



Tax Planning - Business

- Fixed Asset Additions & Depreciation
 - IRC Section 179 Deduction
 - Election to deduct as an expense the cost of qualifying property in the year the property is placed in service
 - Making the election
 - Must be placed in service in 2008 – doesn't matter when – no proration required
 - Qualifying property
 - Tangible personal property (excludes real property)
 - Computer software



Tax Planning - Business

- Fixed Asset Additions & Depreciation
 - IRC Section 179 Deduction – continued
 - 2008 annual expense limit - \$250,000
 - 2008 investment limit - \$800,000
 - Business income limit – The deduction is limited to aggregate taxable income from trade or business activities.
 - Individuals – wages are included as business income



Tax Planning - Business

- Fixed Asset Additions & Depreciation
 - IRC Section 179 Deduction – continued
 - Planning to avoid permanent loss of elected 179 expense – ownership in multiple entities
 - State tax implications
 - No AMT adjustment required
 - Proper planning is critical
 - Timing
 - Amounts
 - Whether to elect or not



Tax Planning - Business

- Fixed Asset Additions & Depreciation
 - IRC Section 179 Deduction - continued
 - I'm impressed when someone informs me they have not elected IRC Section 179 or Bonus Depreciation and explains supportable reasons why
 - Your tax professional should never make a blanket statement claiming they were able to save you \$\$ by electing IRC Section 179. If the statement is made, ask them if they fully considered all opportunities for making, or not making the election. IRC Section 179 is a deduction "there for the taking" and only becomes a true utilization of strategy with proper planning



Tax Planning - Business

- Fixed Asset Additions & Depreciation
 - 50% Bonus Depreciation
 - What is bonus depreciation?
 - How does it work?
 - Bonus depreciation is automatic – must "elect-out" if we don't want rules to apply
 - Eligible property
 - Tangible property with a recovery period not exceeding 20 years
 - Purchased computer software
 - Water utility property
 - Qualified leasehold improvements (certain interior improvements to non-residential property)



Tax Planning - Business

- Fixed Asset Additions & Depreciation
 - 50% Bonus Depreciation - continued
 - Original use requirement (new)
 - Timely placed in use requirement
 - Half-year, Mid-quarter, and Mid-month depreciation conventions don't apply
 - State tax implications
 - No AMT adjustment required
 - Proper planning is critical
 - Amounts
 - Timing
 - Whether to elect-out or not
 - Housing and Economic Recovery Act of 2008 – Accelerate use of tax credit carryovers in lieu of bonus depreciation



Tax Planning - Business

- Fixed Asset Additions & Depreciation
 - IRC Section 179 / Bonus depreciation example:
 - Assume \$350,000 new equipment purchased 2008:
 - \$350,000 - \$250,000 IRC Section 179 deduction
 - \$100,000 remaining depreciable basis reduced for \$50,000 (50% of basis) bonus depreciation
 - \$50,000 remaining depreciable basis x 20% first year allowable MACRS depreciation = \$10,000
 - With IRC Section 179 election and bonus depreciation - total year one deduction = \$310,000
 - Without IRC Section 179 election – year one deduction \$210,000
 - Without IRC Section 179 election and bonus depreciation – year one deduction \$70,000



Tax Planning - Business

- Fixed Asset Additions & Depreciation
 - Vehicle planning
 - Luxury auto limitations
 - Luxury doesn't mean "luxury" in today's terms – it includes just about every automobile
 - Depreciation significantly limited
 - Bonus depreciation adds \$8,000
 - Avoiding luxury auto limitations
 - Lease vs buy (lease inclusion)
 - Light trucks & vans
 - SUVs > 6,000 lbs loaded GVWR
 - Work vans & trucks – limited seating, names painted, tool boxes, ladder racks, etc
 - Heavy duty trucks
 - \$25,000 IRC Section 179 availability
 - Personal use of auto reporting
 - Proper planning is critical



Tax Planning - Business

- General planning
 - Delay shipping of products or providing services until 2009 – in turn, delay billings
 - Accelerate purchase of necessary miscellaneous office and shop supplies into 2008
 - Perform anticipated fixed asset repairs in 2008 rather than waiting until 2009
 - Make year-end charitable contributions or have your Board of Directors approve charitable contributions, accrue and pay within 2 ½ months after year-end



Tax Planning - Business

- General planning
 - C-corporations - make charitable contributions of inventory (held for sale to customers in the ordinary course of business), or depreciable or real property used in its trade or business to qualified non-profit organizations for the care of the ill, needy, or infants. Two options for inventory, one for all other assets:
 - COGS deduction up to corporation's amount of basis – not subject to a 10% taxable income limitation (only for inventory), or
 - Special deduction of limited to twice the corporation's basis in the asset(s) or basis plus 50% of difference between FMV and basis
 - There are organizations that assist in making these contributions
 - Similar deduction for contributions of food inventory and qualified contributions of book inventory to certain public schools
 - Similar deduction for contributions of computer technology or equipment to schools or libraries for use in the U.S. for educational purposes that is related to the donee's purpose or function.



Tax Planning - Business

- General planning
 - If cash basis of reporting – prepay expenses prior to year-end
 - If accrual basis ensure thoroughness in recording year-end accruals, trade payables, etc.
 - Accrue vacation pay, accrue payroll taxes, year-end wages
 - Accrue year-end bonuses (pay bonuses for > 2% S-corporation s/h's, > 50% corporate s/h's including related owners, s/h's of personal service corporations
 - Write-off obsolete, out of service equipment



Tax Planning - Business

- General planning
 - Consider setting up a retirement plan if you don't have one...or modify the one you have
 - Make or accrue retirement plan contributions
 - Write-off bad debts (Creating or increasing an allowance account doesn't create a current tax deduction)
 - Write-off obsolete inventory



Tax Planning - Business

- General planning
 - S corporations, Partnerships, LLCs – Review status of s/h stock basis, partner basis, member basis, and all around at-risk basis
 - Allows for deductibility of losses
 - Allows for tax-free distributions
 - Allows for deductibility of carry-forward losses
 - Make personal loans to business if necessary



Tax Planning - Business

- General planning
 - Consider pre-tax FSA plan***
 - Consider HSA or HRA***
 - Accelerate income in order to expedite the use of carryovers – NOLs, capital losses, tax credits, etc.



Tax Planning - Business

- General planning
 - Implement a capitalization policy
 - Properly evaluate and segregate meals and entertainment expenditures – 100% vs 50% deductibility
 - Consider installment sale options – elect out – planning opportunities
 - Consider benefits of like-kind exchanges (IRC 1031)
 - Involuntary conversion / casualty loss – gain on reimbursement proceeds - deferral opportunity (IRC 1033)
 - IRC Section 1244 – Small Business Corporation Stock planning



Tax Planning - Business

- General planning
 - Consider Federal, State, municipality - credit and grant opportunities
 - R & D Credit (new and improved – not what you think!)
 - Developing a new process or improving existing process
 - Developing a new product or improving an existing product
 - Any failed attempts at product improvements or process improvements
 - Designing product alternatives
 - Designing, constructing and testing prototypes and models
 - Designing molds, jigs, dies, tools, etc.
 - Designing an innovative product that is new to the market
 - Implement or upgrade systems and/or software
 - Improve or build new manufacturing facilities
 - You do not need to have a patent



Tax Planning - Business

- General planning
 - Consider Federal, State, municipality - credit and grant opportunities - continued
 - Work Opportunity Credit
 - Disabled Access Credit
 - Credit for Small Employer Pension Plan Start-up Costs
 - Empowerment and Enterprise Zone Credits
 - Credit for Tax Paid on Fuels
 - Alternative Motor Vehicle Credits
 - Municipality grants / tax abatements for expansion and / or relocation projects



Tax Planning - Individual

- Charitable giving planning
 - Charitable Giving
 - Highly appreciated stock
 - FMV deduction
 - No gain reporting
 - Appreciated Real Estate
 - IRA
 - No tax on distribution
 - No charitable deduction
 - Must be 70 ½ years of age or older
 - Limited to \$100,000
 - Utilize Charitable Trusts
 - Make year-end charitable contribution utilizing your credit card



Tax Planning - Individual

- Individual retirement account planning
 - Conversion of traditional IRA to Roth IRA
 - 2008 & 2009 – Modified AGI can't exceed \$100,000
 - 2008 & 2009 - Doesn't apply if filing status Married Filing Separately
 - May be good idea with decline in account values – much lower tax implications
 - Taxable transaction
 - Roth non-deductible / earnings non-taxable
 - Use of non-deductible IRA contributions to build up amount of conversion in 2010
 - Better investment tool if utilized long-term
 - If already made a conversion, can re-characterize original conversion
 - Can do this year, by April 15 of next year, or by October 15 of next year if timely filing occurred on April 15 – amended return would be required



Tax Planning - Individual

- Retirement income planning
 - Retirement account required minimum distributions
 - Retirees turning 70 ½ this year
 - With retirement account balances dropping dramatically, this has become a problem for many retirees
 - RMD based upon life expectancy tables and FMV of account balance at end of preceding year
 - Take RMD this year or postpone until next year (April 1, 2009) – hoping market recovers
 - Bunching of income for 2009 – (2) RMDs
 - Proposed tax relief for seniors forced to take RMDs – previously endorsed by both parties' presidential candidates
 - 2 year suspension of RMD requirements
 - Suspension of 50% penalty



Tax Planning - Individual

- Investment income planning (Only if it makes sound investment sense)
 - Sell (recognize) realized loss positions
 - Offset recognized 2008 gains
 - Offset year-end capital gain distributions
 - Sell (recognize) realized gain positions
 - Offset recognized 2008 losses
 - Gamble that capital gain rates will rise with new administration
 - Benefit from zero percent capital gains & qualified dividends income tax rates (2008 – 10)
 - Applies to taxpayers in the 10% and 15% overall tax brackets – very low income earners – approx. \$16,000 MFJ, \$8,000 MFS & Single
 - Net Unrealized Appreciation transactions – complete liquidation of employer stock held in retirement plan – see Whalen Associate if this applies to you



Tax Planning - Individual

- General planning
 - Arrange with employer to defer compensation (bonuses, etc.) into 2009
 - Pass-thru entity basis planning
 - Consider disposal of passive activities to allow deduction of suspended losses
 - Step-up level of participation in passive activities
 - Pay State and Local income tax prior to year-end
 - Expected balances due
 - Estimated tax payments
 - Real estate taxes
 - Watch for AMT disallowance
 - If expecting 2008 tax balances owed – increase withholding between now and year-end to reduce underpayment penalties
 - If applicable – consider moving debt-cancellation events to 2009



Tax Planning - Individual

- General planning
 - Bunch miscellaneous itemized deductions to exceed 2% requirement
 - Bunch medical costs to exceed 7.5% requirement
 - Mortgage interest deduction limitations
 - \$1 million cap
 - \$100,000 equity loan limit
 - AMT adjustment for boats, RVs, and equity loan interest not used to buy, build, or substantially improve home
 - If planning on making energy saving improvements to your home – wait until 2009. A credit of up to \$500 may be available (doesn't apply for 2008)
 - "Qualified Joint Venture" – Husband & Wife business activities



Tax Planning - Individual

- General planning
 - If considering a hybrid vehicle eligible for a credit – consider doing so in 2008
 - If self-employed and haven't done so – consider a self-employed retirement plan
 - Sep
 - Solo-401(k)
 - Simple
 - Etc.
 - If possible - consider changing state of residency for state income tax planning purposes
 - Advise Whalen Associate if you incur loss on cancellation of investment annuity contract – potential deduction opportunity



Tax Planning - Individual

- Alternative Minimum Tax planning
 - AMT – What is it?
 - AMT is an alternative set of rules used to determine tax liability. It first came into existence as part of the Tax Reform Act of 1969. It was designed to target the rich. Lawmakers who introduced the concept cited a Washington Post article which reported that in 1967, 155 individuals with incomes over \$200,000 did not pay any federal income taxes, and that 20 of these individuals were millionaires. The reason why they paid zero tax was because they used legal tax loopholes to eliminate their tax. AMT was designed to close tax loopholes by imposing an "alternative" set of rules. If this "alternative" way of calculating tax results in a higher tax, then regular tax must be increased by AMT.



Tax Planning - Individual

- Alternative Minimum Tax planning
 - AMT – Why does it threaten the middle class?
 - \$200,000 in 1967 equals \$1,200,550, as adjusted for inflation. If AMT rules had stuck to their original purpose, they would only affect people who make in excess of \$1.2 million. Most tax rules are adjusted for inflation on an annual basis. AMT, however, is not automatically adjusted for inflation. Congress must pass new legislation each time they want to adjust AMT to reflect inflation



Tax Planning - Individual

- Alternative Minimum Tax planning
 - AMT tax relief
 - The Emergency Economic Stabilization Act of 2008 provides AMT relief for individuals – a one year patch
 - 2008 exemptions increased
 - AMT income ranges over which exemptions are phased out have been expanded
 - Incentive Stock Option exercises – unpaid AMT liability, as well as interest and penalties, generated by ISO exercises before 2008, is abated
 - Certain nonrefundable personal tax credits provide benefit against AMT
 - Dependent care credit
 - Hope and Lifetime Learning credits
 - Child credit
 - Adoption credit



Tax Planning - Individual

- Estate / Gifting planning
 - Consider making \$12,000 gifts prior to year-end
 - Can give to unlimited number of individuals
 - \$12,000 gift (per person / per year)
 - Creates no tax liability or reporting requirement
 - Can't carryover unused annual gifting exclusions.



Tax Planning – Q & A

- Question and Answer session

