

# 2016 YEAR-END TAX LETTER

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## IT'S TAX TIME AGAIN...

Once again, it's time to file and pay your taxes. Your mailbox should be filling up with the information you will need to get the job done.

This letter is full of information designed to help you prepare your tax documents so you will pay only the tax that you rightfully owe.

## Time to get organized

*The following checklist will help you collect the documents needed to file your tax return. When all of the boxes are checked, you're ready.*

- Your last 3 years' tax returns (*new client*). Maybe we can amend and save money.
- Social Security numbers and dates of birth are needed for all taxpayers, spouses and dependents.
- W-2 Forms.
- Your last paycheck stub of the year is full of information.
- 1099 Forms for interest, dividends, retirement, Social Security, and unemployment need to be entered correctly to comply with the IRS matching program.
- Property tax statements contain important information. They list the tax (deductible) and special assessments (not deductible).
- Forms 1098 for mortgage interest need to be entered as printed. The IRS cross checks.
- Year-end statements from investment accounts with transaction details for the year
- Assets held outside the USA. Bring statement(s). Such assets must be disclosed even if they do not generate income.
- Purchase and sale information, including dates, relating to anything sold during 2016 is needed. Include sales denominated in ANY type of currency (including virtual currencies like Bitcoin).
- Child care provider information (name, address, SS#, amount paid) is needed for the child care credit (*even if you are reimbursed at work*).
- Names, addresses, and Social Security numbers from whom you received interest, or to whom you paid interest.
- Bankruptcy or divorce papers (if applicable).
- If you paid an individual person \$600 or more for services rendered in connection with your business, please provide their name, address, and tax ID number.
- Records showing income and expense for any small business or rental property you own will be needed.
- If you have an investment in a Partnership, S Corporation, Estate or Trust you will need to bring Form K-1.
- Bring IRA year-end statements.
- Bring all other statements of income, whether you think they are taxable or not.
- Forms 1098-T amounts paid for post-secondary tuition are sent to the student. If the student is your dependent you must get it from them. Bring receipts.
- Bring your records of estimated taxes paid.
- Student loan interest forms 1098-E.
- Adoption costs if applicable. Also bring the legal adoption documents.
- Form 1098-C for donations of automobiles or boats.
- Details on all noncash donations greater than \$500. Include date, place, fair market value, and original cost.
- If you purchased a new fuel cell or electric plug-in vehicle in 2016, bring the year, make and purchase date.
- Bring a voided check for direct deposit of any refunds you expect to receive.
- Noncustodial parents claiming children need a signed IRS Form 8332 to claim the child.
- If your mortgage was forgiven due to foreclosure, bring Form 1099-C or 1099-A.
- If you bought a new home or refinanced your existing home bring the closing papers.
- Information on energy saving home improvements might get you a tax credit.
- If you were an investor caught in a Ponzi-type scheme, bring the details.
- If you received Forms 1099-K for internet or credit card sales please bring them.
- Proof of health insurance is needed. Bring Form 1095 if you received one.
- Health Savings Account (HSA) contributions and distributions. Bring forms 5498-SA and 1099-SA.
- Out of pocket medical expenses may be deductible (if large). Bring details.



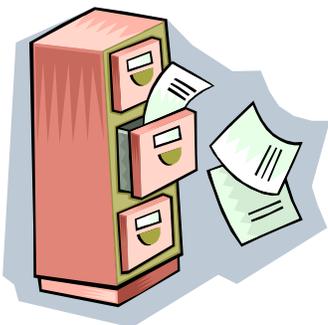


**Caution:** the IRS is very attentive to taxpayers who write off local travel costs.

A daily log of business use is essential. Also, don't forget to record the beginning and the year-end odometer readings.

To avail yourself of tax deductions, you need to be organized and well documented.

Save proof of all tax deductible purchases.



## DEDUCTING MILEAGE?

**Did you drive for charity?** If so, you can deduct 14¢ for every mile you drove.

**If your medical expenses are substantial,** you may want to calculate a mileage deduction. Medical miles for 2016 are calculated at 19¢ per mile.

**If you drove for business purposes,** the situation is a little more complicated: First decide which miles qualify.

**Use the following three scenarios to determine how many miles you can deduct:**

Keep in mind the following statement: **In general, commuting is not deductible.**

**If you have an office or regular place of business outside your home,** you may not de-

duct miles commuting to and from work or to your first or from your last stop, but you may deduct mileage to drive to a *temporary work place* (less than one year's duration) and mileage to and from different work locations during the day.

**If you have an office in your home that qualifies for a home office deduction,** all of your business-related mileage is deductible.

**If you work out of your home but do not qualify for the home office deduction,** the distance between home and your first stop and between your last stop and home are nondeductible commuting miles. You should carefully plan to have your first and last stops close to home to maximize the mileage deduction.

A trip to the bank, post office, or a supplier can help increase deductible business miles.

**Once you have determined which miles to count,** you need to decide whether to use the *standard mileage* rate or actual expenses.

The *standard mileage rate for qualified business use* for 2016 is 54¢ per mile (down 3½ cents from 2015).

**Which method is best?**

In general, the standard method works best if your business miles are high or your vehicle is economical to run.

The actual expense method works best if your vehicle weighs over 6000 pounds, is costly to run, or you do not have that many miles in total.

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## DO YOU WORK AT HOME?

**If you are self-employed,** you may qualify for the home office deduction if you use a portion of your home **exclusively** as your principal place of business, to store inventory, or to conduct substantial management or administrative activities. There can be no other fixed location where the above activities can be done.

**If you are an employee,** your home office must be required by your employer.

The office space still needs to be **used regularly and exclusively for business.** You can not have any other usage of the

area whatsoever. Using your office for personal or investment reasons eliminates the deduction as far as the IRS is concerned, so be careful to keep your office space and computer usage all business.

Having a deductible home office means you can deduct all of your local business travel as described earlier, and you will not have to keep a log of computer usage because your computer will be used exclusively for business.

If your office qualifies, you will need additional information: Measure the business space and

the total space. You will also need your mortgage interest, taxes, insurance, association fees, repairs, maintenance, utilities, garbage, security, and rent paid. Also, provide an accounting of the total investment in your home.

**The IRS has provided a simplified home office deduction, if you choose.** Instead of calculating all of the above information, \$5 per square foot can be deducted (maximum \$1,500). The IRS estimates that the new calculation will save taxpayers 1.6 million hours per year.

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## COMPUTER & CELL PHONE GUIDELINES

Did you buy a computer that you would like to deduct? You can use the following guide to determine what is deductible.

**If you are an employee,** a computer must be required as a condition of employment and for the convenience of your employer to be deductible.

**If you are self-employed,** the business percentage of computer usage, measured by time, is deductible.

**If you use your computer for investments,** the business percentage of use may also be deductible if you itemize.

**If you are a student,** the use of a computer is not deductible, but you can tap your 529 plan for a computer purchase.

*Keep a log of computer usage to support your deduction.*

**Cell phone deductions are as follows:**

**Employers providing cell phones** do not have to require records of use to provide tax-free cell phones to employees.

**Employees required to use cell phones for work** can deduct cell phone use to the extent used for business.

**Self employed individuals** can deduct business cell phone usage. The IRS, however, still has a hard time believing a cell phone is 100% for business. It's wise to keep a log of use.

# WHAT'S NEW FOR 2016?

There are plenty of changes now in effect from prior legislation, IRS rulings, and court cases.

**Are you filing early to get a fast refund?** Taxpayers getting the Earned Income Credit or refundable Child Tax Credit will have to wait until Feb. 15<sup>th</sup> for a refund regardless of how early they file.

**Do you have assets outside the US?** The deadline for reporting foreign accounts comes earlier this year. The deadline is now the same as the tax return filing deadline (including extensions). The IRS continues to ramp-up efforts to find foreign account holders. Be sure to give your tax professional a list of all your foreign held accounts and assets.

**Do you give to charity from an IRA?** Good news. Congress permanently extended the provision allowing people over 70<sup>1/2</sup> to make tax free distributions from an IRA to charities. Such distributions count toward your RMDs and are capped at \$100,000.

**Are you uninsured?** More employers are now required to offer affordable health insurance. Employers with 50+ full time equivalent employees are required to offer insurance to 95% of their full time employees. Smaller employers do not have to comply with this rule.

Individuals without health insurance will face increased penalties for tax year 2016. The penalty for not having insurance increases to the greater of 2.5% of income above the filing threshold or a flat fee of \$695 per adult (up from 2% and \$325 respectively in 2015).

**Do you want to start a ROTH IRA?** Now there is a new kind of ROTH IRA called a myRA (go to myRA.gov for details). It costs nothing to open an account and there are no fees or minimum contributions. The tax rules are exactly the same as a regular ROTH IRA (same contribution and distribution rules and limits).

**Are you part of the 'Sharing Economy'?** The IRS has launched the new "Sharing Economy Tax Center" (enter keyword 'sharing economy' at IRS.gov for a link). The site is designed to help Uber drivers & Airbnb renters (among others) understand their tax obligations. And don't forget... if you rent your home for fewer than 15 days you don't need to report the income on your tax return.

**Do you need a transcript from the IRS?** The IRS's "Get Transcript" service is back online (use keyword "transcript" at IRS.gov for a link). It was suspended last year due to hackers stealing taxpayer transcripts. Now there are extra verification steps to help prevent another hacking incident.

**Are you aware of the latest tax scams?** The IRS saw a 400% surge in scams in 2016. The IRS's "Tax Scams/Consumer Alerts" webpage has the latest (use keyword "scams" at IRS.gov for a link). There are a variety of fake phone calls, eMails, and texts designed to resemble IRS communications. Remember that the IRS never initiates contact by phone, text, or email. Never click on any links and never provide any information. Scammers are also using fake letters that look like IRS audit notices. Ask your tax professional if the letters are legit before taking action.

**Do you own a business?** The IRS has made it easier to write-off items that last longer than one year. Now you can elect to expense items costing less than \$2500. As always, save your receipts because you will need to prove that each item was less than \$2500.

There are other generous provisions if you bought a new truck (6000+ lbs gross vehicle weight) for your business. Legislation passed in December 2015 permanently extended the \$25,000 expensing and 50% bonus depreciation of such vehicles.

**Do you have employees or contractors?** This year the IRS wants your W2 and 1099-misc filings by Jan 31<sup>st</sup>. In prior years you had until March 31<sup>st</sup> (if you e-filed).

**Do you have unpaid medical bills?** Older taxpayers (age 65+) with high medical expenses should pay their bills before the end of 2016. Next year the threshold for being able to deduct medical expenses goes from 7.5% of income to 10% (age 65+).

**Did you or your kids attend college?** This year more schools will be reporting the amounts of tuition paid on form 1098-T. In previous years most schools only reported the amount billed, which is not what is needed to calculate education credits and deductions.

**Did you buy a computer for college?** The tax court has ruled that a computer is not a qualified expense for the American Opportunity Credit unless it was a requirement to attend the college.

**Do you owe the IRS?** The IRS has raised the interest rate on underpayment of income tax to 4% (up from 3%). The IRS has also increased the late filing penalty to \$205 (up from \$135) for returns with a balance due filed greater than 60 days past the deadline. For some taxpayers that have outstanding inactive debts the IRS is switching to private debt collectors starting in spring 2017.

**Are you worried about being Audited?** IRS audits are at historically low rates (0.84% of returns filed). However, there is a greater chance of being audited if you claim the Earned Income Credit (1.75% audited), own a business (2.5% audited), or make more than \$1million/yr (9.5% audited).

**Did you work at the polls this election?** Remember that what you earned is taxable income.

**Did you pay taxes to Cuba?** Good news. Now taxes paid to Cuba qualify for the Foreign Tax Credit.



Typical of an election year, there were no major tax bills passed in 2016. However, plenty of changes went into effect this year due to prior legislation, IRS rulings, and tax court cases.

*Best of all, taxes on the same income as last year are automatically lower due to indexing.*

These are only some of the highlights of the legislation, rulings, and court cases affecting your 2016 tax situation. A good tax professional can help you use these new decisions to their fullest.

Turn the page for some great year-end tax-saving ideas.



# YEAR-END TAX SAVING TIPS

## GIVE TO CHARITY

Not sure of where to start? Try [charitynavigator.org](http://charitynavigator.org) for guidance.

**Short of cash? You can still make a last minute gift.** Charge your deductions on a credit card and pay later. Consider giving through [www.justgive.org](http://www.justgive.org). You can privately give to thousands of rated charities with a credit card. Your donation goes directly to the charity, and [www.justgive.org](http://www.justgive.org) will send you a confirmation and a year-end summary to satisfy documentation requirements.

Or, better yet, you don't even have to spend money to take a charitable deduction. Clean out your closets of unwanted items to make a noncash gift. Keep in mind, the items must be in at least good condition. You should omit items of minimal value (socks and underwear), and thoroughly document the donation.

If you plan on donating a vehicle before year-end, beware of the rules. Select a charity that will either use or improve the vehicle, and you will be able to deduct *fair market value*. Otherwise your deduction will be limited to the price the charity got when they sold the vehicle. The charity will give you a 1098C documenting the contribution. The 1098C needs to be attached to your tax return.

If you have a stock or piece of property that has increased in value, you can deduct the full value and avoid paying capital gains tax by donating it to charity. If you want to give stock that has fallen in value, sell the stock, take the loss, and give the money to charity.

If you are over age 70<sup>1/2</sup> you can give directly to charities from your IRA. The distribution counts toward your Required Minimum Distributions (RMDs).

**Keep in mind that proof of payment is needed for donations of any size.**

## CHECK YOUR TAX PAYMENTS TO AVOID PENALTIES

The IRS will charge a penalty if your tax for 2016 is less than 90% prepaid unless your payments are at least equal to last year's tax. (110% of last year's tax if your income exceeds \$150,000).

You can boost your itemized deductions, and possibly save yourself from a penalty, by sending your last state estimated tax payment before December 31<sup>st</sup> or by stepping up your state withholding.

## CHECK YOUR PORTFOLIO

If you are in the 15% tax bracket or lower (gross income under \$47,800 (single) or under \$95,600 (married)) you may be able to sell stocks or property at a gain in 2016 and pay no Federal tax. If you are in the above tax range, or even higher if you itemize and/or have dependents, it might be wise to check out the possibility.

If you missed out on last year's credits or deductions because your income went over the limits, it might be wise to check your portfolio for some losses to reduce your income. You can offset up to \$3,000 of other income with stock losses. If you wish to repurchase the stock again, wait at least 31 days to avoid wash sale rules.

If you are planning on deducting worthless stock, remember that it's not deductible until it's completely worthless.

In buying mutual fund shares, avoid the year-end tax trap. Year-end dividends may include a years worth of capital gain in a large taxable payout. The value of your shares declines by the amount of payout, so you end up paying tax on profits that reduce your share value.

## SELF-EMPLOYED?

**Shelter up to 20% of your net income in a SEP retirement plan.** Besides current tax savings, money grows tax-deferred on these investments. A SEP contribution can be made up to the due date of your 2016 tax return, including extensions.

**Pay all bills already received for operating expenses rather than deferring payment until 2017.** If you need new equipment, save tax dollars now by purchasing before year-end. Remember that you can charge on a credit card and receive a current deduction.

**To channel your income into next year for a cash basis business,** you must be certain it is not constructively received. You can delay your billing to next year to defer income to 2017.

## and...THE FUTURE?

The election is finally over. Let's take a look at where we stand.

### Donald Trump's plans include:

- Dramatically reduced taxes for both individuals and businesses
- Standard deduction up to \$30k (married) and \$15k (single)
- Fewer tax brackets
- 15% business tax rate (including for sole proprietors)
- Eliminating the 0.9% and 3.8% surtaxes
- Eliminating the AMT
- More dependent care tax breaks
- Tax favored accounts for elder care and child development
- Repeal and replace Obamacare

### Will Trump get what he wants?

With Republican control of congress there will be changes. Trump and congressional Republicans will likely compromise on tax reform.

Trump wants to repeal Obamacare. This will be a high priority early in his presidency.

Public outcry will also be a factor. Get involved if you want your voice to be heard. At a minimum, write your congressional representatives.



*The basic strategy for year-end tax planning can be summed up in the following two statements:*

- *Channel your income into the year where it will be taxed at a lower rate.*
- *Channel your deductions to the year where your income will be taxed at a higher rate.*

*If you think that you need year-end tax planning, get in touch with a professional who knows the rules to help answer your questions.*

