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Tax & Business Alert

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WALK THE PATH TO TAX SAVINGS FOR 2015

Like many taxpayers, you may have been expecting to encounter a few roadblocks while traversing your preferred tax-saving avenues. If so, tax extenders legislation signed into law this past December may make your journey a little easier. Let's walk through a few highlights of the Protecting Americans from Tax Hikes Act of 2015 (the PATH Act).

OF INTEREST TO INDIVIDUALS

If you're a homeowner, the PATH Act allows you to treat qualified mortgage insurance premiums as interest for purposes of the mortgage interest deduction through 2016. However, this deduction is phased out for higher income taxpayers. The law likewise extends through 2016 the exclusion from gross income for mortgage loan forgiveness.

Those living in a state with low or no income taxes (or who make large purchases, such as a car or boat) will be pleased that the itemized deduction for state and local *sales* taxes, instead of state and local *income* taxes, is now permanent. Your deduction can be determined easily by using an IRS calculator and adding the tax you actually paid on certain major purchases.

Investors should note that the PATH Act makes permanent the exclusion of 100% of the gain on the sale of qualified small business stock acquired and held for more than five years (if acquired after September 27, 2010). The law also permanently extends the rule that eliminates qualified small business stock gain as a preference item for alternative minimum tax (AMT) purposes.

BREAKS FOR BUSINESSES

The PATH Act gives business owners much to think about as well. First, there's the enhanced Section 179 expensing election. Now permanent (and indexed for inflation beginning in 2016) is the ability for companies to immediately deduct, rather than depreciate, up to $500,000 in qualified new or used assets. The deduction phases out, dollar for dollar, to the extent qualified asset purchases for the year exceeded $2 million.

The 50% bonus depreciation break is also back, albeit temporarily. It's generally available for new (not used) tangible assets with a recovery period of 20 years or less, and certain other assets. The 50% amount will drop to 40% for 2018 and 30% for 2019, however.

In addition, the PATH Act addresses two important tax credits. First, the research credit has been permanently extended, with some specialized provisions for smaller businesses and start-ups. Second, the Work Opportunity credit for employers that hire members of a "target group" has been extended through 2019.

GOOD NEWS FOR GENEROUS IRA OWNERS

The recent tax extenders law makes permanent the provision allowing taxpayers age 70½ or older to make direct contributions from their IRA to qualified charities up to $100,000 per tax year. The transfer can count toward the IRA owner's required minimum distribution. Many rules apply so, if you're interested, let us help with this charitable giving opportunity.

Does your company provide transit benefits? If so, note that the law makes permanent equal limits for the amounts that can be excluded from an employee's wages for income and payroll tax purposes for parking fringe benefits and van-pooling / mass transit benefits.

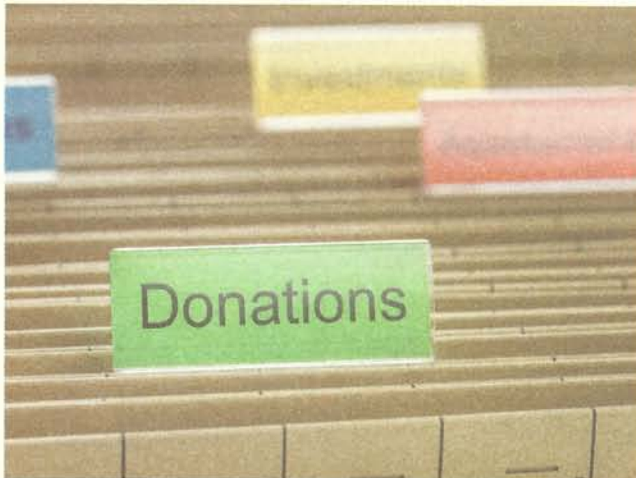
MUCH, MUCH MORE

Whether you're filing as an individual or on behalf of a business, the PATH Act could have a substantial effect on your 2015 tax return. We've covered only a few of its many provisions here. Please contact us to discuss these and other provisions that may affect your situation. ■

5 THINGS TO KNOW ABOUT SUBSTANTIATING DONATIONS

There are virtually countless charitable organizations to which you might donate. You may choose to give cash or to contribute noncash items such as books, sporting goods, or computers or other tech gear. In either case, once you do the good deed, you owe it to yourself to properly claim a tax deduction.

No matter what you donate, you'll need documentation. And precisely what you'll need depends on the type and value of your donation. Here are five things to know:



1. Cash contributions of less than $250 are the easiest to substantiate. A canceled check or credit card statement is sufficient. Alternatively, you can obtain a receipt from the recipient organization showing its name, as well as the date, place and amount of the contribution. Bear in mind that unsubstantiated contributions aren't deductible anymore. So you must have a receipt or bank record.

2. Noncash donations of less than $250 require a bit more. You'll need a receipt from the charity. Plus, you typically must estimate a reasonable value for the donated item(s). Organizations that regularly accept noncash donations typically will provide you a form for doing so. Keep in mind that, for donations of clothing and household items to be deductible, the items generally must be in at least good condition.

3. Bigger cash donations mean more paperwork. If you donate $250 or more in cash, a canceled check or credit card statement won't be sufficient. You'll need a contemporaneous written acknowledgment from the recipient organization that meets IRS guidelines.

Among other things, a contemporaneous written acknowledgment must be received on or before the earlier of the date you file your return for the year in which you made the donation or the due date (including an extension) for filing the return. In addition, it must include a disclosure of whether the charity provided anything in exchange. If it did, the organization must provide a description and good-faith estimate of the exchanged item or service. You can deduct only the difference between the amount donated and the value of the item or service.

4. Noncash donations valued at $250 or more and up to $5,000 require still more. You must

get a contemporaneous written acknowledgment plus written evidence that supports the item's acquisition date, cost and fair market value. The written acknowledgment also must include a description of the item.

5. Noncash donations valued at more than $5,000 are the most complicated. Generally, both a contemporaneous written acknowledgment and a qualified appraisal are required — unless the donation is publicly traded securities. In some cases additional requirements might apply, so be sure to contact us if you've made or are planning to make a substantial noncash donation. We can verify the documentation of any type of donation, but contributions of this size are particularly important to document properly. ■

WHY YOU MIGHT WANT TO *NOT* CLAIM YOUR CHILD AS A DEPENDENT

Understandably, many parents get in the habit of claiming their children as dependents on their federal tax returns. You generally may do so as long as your child is either under age 19 (nonstudents) or under age 24 (students). But there is a reason to *not* claim your child as a dependent — and it has everything to do with higher education.

CREDITS AND PHASEOUTS

The two primary college-funding tax credits available are the American Opportunity credit and the Lifetime Learning credit. Thanks to recently passed legislation, the American Opportunity credit now permanently allows eligible taxpayers to take an annual credit of up to $2,500 for the first four years of postsecondary education. Meanwhile, the Lifetime Learning credit provides up to $2,000 in relief to those eligible. (You can't claim both credits in the same year for the same student.)

Thanks to recently passed legislation, the American Opportunity credit now permanently allows eligible taxpayers to take an annual credit of up to $2,500 for the first four years of postsecondary education.

But these credits are subject to "phaseouts" that limit eligibility for higher-income taxpayers. For example, for 2015, eligibility for the American Opportunity credit begins to phase out for taxpayers with modified adjusted gross incomes (MAGIs) beyond $80,000 (single filers) or $160,000 (married couples filing jointly). Similarly, eligibility for the Lifetime Learning Credit begins to phase out for taxpayers with MAGIs beyond $55,000 (singles) or $110,000 (joint filers).

GOOD REASONS

If your income disqualifies you from claiming these credits, your child's income probably doesn't disqualify him or her. Therefore, your child may be able to report payment of education expenses for tax purposes and then claim one of the credits — but only if you don't claim him or her as a dependent.

Under this scenario, the child's tax benefit typically outweighs the value of the dependency exemption to the parents. Why? First, a credit reduces taxes dollar-for-dollar, while an exemption reduces only the amount of taxable income. Second, an income-based phaseout may reduce or eliminate the benefit of the exemption even if you did claim your child as a dependent. For 2015, the phaseout starting points for the exemption are adjusted gross incomes of $258,250 (singles) and $309,900 (joint filers).

THE RIGHT CALL

If your dependency exemption is phased out, it will probably make sense not to claim your child as a dependent so he or she can grab a tax credit. But if your exemption isn't phased out or is only partially phased out, the decision becomes trickier. We can help you make the right call. ■

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RUN A BUSINESS "ON THE SIDE"? MAKE SURE IT'S NO HOBBY

If you run a business "on the side" and derive most of your income from another source (whether from another business you own, employment or investments), you may face a peculiar risk: Under certain circumstances, this on-the-side business might not be a business at all in the eyes of the IRS.

Generally, a taxpayer can deduct losses from profit-motivated activities, either from other income in the same tax year or by carrying the loss back to a previous tax year or forward to a future tax year. But, to ensure some pursuits are really businesses — and not mere hobbies intended primarily to offset other income — the IRS enforces what are commonly referred to as the "hobby loss" rules.

For example, if you haven't earned a profit from your business in three out of five consecutive years, you'll bear the burden of proof to show that the enterprise isn't merely a hobby. If a profit can be proven within this period, the burden falls on the IRS. In either case, the agency uses nine nonexclusive factors to determine whether the activity is a business or a hobby — including management expertise and time and effort dedicated.

If your enterprise is redefined as a hobby, there are many business deductions and credits that you won't be eligible to claim. You may still write off certain expenses related to the hobby, but only to the extent of income the hobby generates. If you're concerned about the hobby loss rules, we can help you evaluate your situation. ■

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