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Tax & Business Alert

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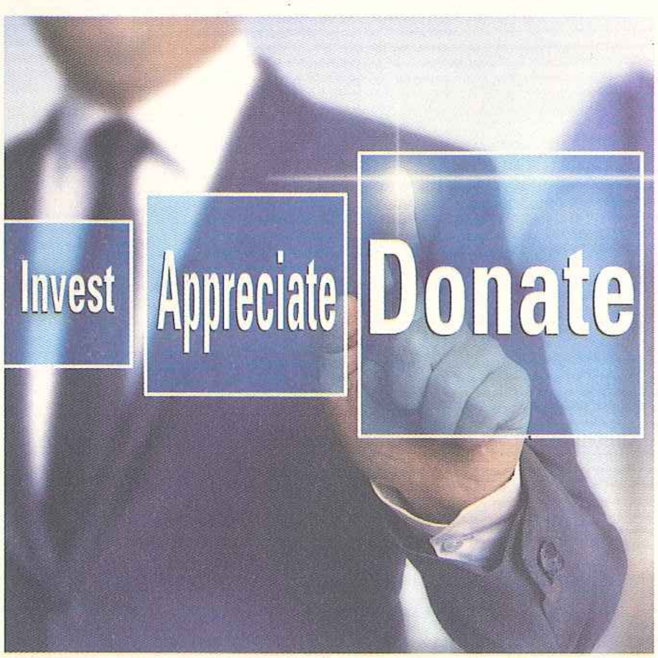
DONATING APPRECIATED STOCK OFFERS TAX ADVANTAGES

When many people think about charitable giving, they picture writing a check or dropping off a cardboard box of nonperishable food items at a designated location. But giving to charity can take many different forms.



One that you may not be aware of is a gift of appreciated stock. Yes, donating part of your portfolio is not only possible, but it also can be a great way to boost the tax benefits of your charitable giving.

NO PAIN FROM GAINS

Many charitable organizations are more than happy to receive appreciated stock as a gift. It's not unusual for these entities to maintain stock portfolios, and they're also free to sell donated stock.

As a donor, contributing appreciated stock can entitle you to a tax deduction equal to the securities' fair market value — just as if you had sold the stock and contributed the cash. But neither you nor the charity receiving the stock will owe capital gains tax on the appreciation. So you not only get the deduction, but also avoid a capital gains hit.

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The key word here is "appreciated." The strategy doesn't work with stock that's declined in value. If you have securities that have taken a loss, you'll be better off selling the stock and donating the proceeds. This way, you can take two deductions (up to applicable limits): one for the capital loss and one for the charitable donation.

INEVITABLE RESTRICTIONS

Inevitably, there are restrictions on deductions for donating appreciated stock. Annually you may deduct appreciated stock contributions to public charities only up to 30% of your adjusted gross income (AGI). For donations to nonoperating private foundations, the limit is 20% of AGI. Any excess can be carried forward up to five years.

So, for example, if you contribute $50,000 of appreciated stock to a public charity and have an AGI of $100,000, you can deduct just $30,000 this year. You can carry forward the unused $20,000 to next year. Whatever amount (if any) you can't use next year can be carried forward until used up or you hit the five-year mark, whichever occurs first.

Moreover, you must have owned the security for at least one year to deduct the fair market value. Otherwise, the deduction is limited to your tax basis (generally what you paid for the stock). Also, the charity must be a 501(c)(3) organization.

Last, these rules apply only to appreciated *stock*. If you donate a different form of appreciated property, such as artwork or jewelry, different requirements apply.

INTRIGUING OPTION

A donation of appreciated stock may not be the simplest way to give to charity. But, for the savvy investor looking to make a positive difference and manage capital gains tax liability, it can be a powerful strategy. Please contact our firm for help deciding whether it's right for you and, if so, how to properly execute the donation. ■

IS THE SALES TAX DEDUCTION RIGHT FOR YOU?

As the year winds down, many people begin to wonder whether they should put off until next year purchases they were considering for this year. One interesting wrinkle to consider from a tax perspective is the sales tax deduction.

MAKING THE CHOICE

This tax break allows taxpayers to take an itemized deduction for state and local sales taxes in lieu of state and local income taxes. It was permanently extended by the Protecting Americans from Tax Hikes Act of 2015.

The deduction is obviously valuable to those who reside in states with no or low income tax. But it can also substantially benefit taxpayers in other states who buy a major item, such as a car or boat.

CONSIDERING THE BREAK

Because the break is now permanent, there's no urgency to make a large purchase this year to take advantage of it. Nonetheless, the tax impact of the deduction is worth considering.

For example, let's say you buy a new car in 2016, your state and local income tax liability for the year is $3,000, and the sales tax on the car is also $3,000. This may sound like a wash, but bear in mind that, if you elect to deduct sales tax, you can deduct *all* of the sales tax you've paid during the year — not just the tax on the car purchase.

PICKING AN APPROACH

To claim the deduction, you need not keep receipts and track all of the sales tax you've paid this year. You can simply use an IRS sales tax calculator that will base the deduction on your income and the sales tax rates in your locale, plus the tax you actually pay on certain major purchases.

Then again, if you retain documentation for your purchases, you might enjoy a larger deduction. The "actual receipt" approach could result in a sizable deduction if you've made a number of notable purchases in the past year that don't qualify to be added on to the sales tax calculator amount. Examples include furnishing a new home, investing in high-value electronics or software, or purchasing expensive jewelry (such as engagement and wedding rings).

SAVING WHILE BUYING

The sales tax deduction offers an opportunity to save tax dollars while buying the items you want or need. Let us help you determine whether it's right for you. ■

MAKE SURE YOU'RE UP TO SPEED ON NONQUALIFIED STOCK OPTION RULES

Many employers look to attract and retain key employees through various investment-related incentives. One example is the nonqualified stock option (NQSO). If your employer provides these to you, or you're considering an employer that does, make sure you're up to speed on the applicable tax treatment and reporting.

HOW DO THEY WORK?

An NQSO is an option that doesn't qualify for the special tax treatment afforded incentive stock options. Let's look at an example: ABC Inc. grants an employee, Steve, NQSOs to buy 100 shares of the company's stock for $100 per share — the fair market value (FMV) on the grant date.

The NQSOs vest over five years and must be exercised within 10 years. In Year 5, the stock's FMV has increased to $150 per share, and Steve exercises all of his NQSOs, buying shares worth $15,000 (100 × $150) for $10,000 (100 × $100).

WHAT'S THE TAX IMPACT?

Generally, there are no tax consequences when NQSOs are granted. That said, the IRS has issued guidance regarding a variety of circumstances under which an NQSO grant requires you to report taxable income. This would be the case if the NQSO itself (as opposed to the underlying stock) has "readily determinable value." But NQSOs granted by employers almost never satisfy this requirement.

When you exercise an NQSO, however, you must report compensation income equal to the spread between the exercise price and the stock's FMV on the exercise date. Going back to the example, when Steve exercises his NQSOs, he must report $5,000 in compensation, which is taxable to him as ordinary income and deductible by his employer. It's included in wages on Steve's Form W-2 and is subject to payroll taxes.

HOW ARE SALES REPORTED?

Reporting income on the exercise of NQSOs is relatively simple. So long as the amount is reported properly on your W-2, it's easy to report it correctly on your tax return.

To calculate and report gain on the sale of NQSO stock, you take the proceeds from the sale (net of any broker's commissions or other expenses) and subtract your basis in the stock. The difference is short- or long-term capital gain, depending on how long you held the stock.

Generally, the basis is equal to the amount you paid for the shares (the exercise price) plus the amount of compensation income you reported upon exercise.

Suppose Steve, from the example above, holds his stock for two years and sells it for $18,000. His basis is $15,000 — the original exercise price of $10,000, plus the $5,000 he reported as wages. When he sells the stock, he will recognize $3,000 in long-term capital gain.

An NQSO is an option that doesn't qualify for the special tax treatment afforded incentive stock options.

WHAT COULD GO WRONG?

NQSOs can be a valuable incentive. But, when selling stock acquired through the exercise of NQSOs, complications regarding the basis of the stock can sometimes arise. So please contact us for help calculating your basis and verifying the accuracy of your tax reporting. ■

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WHAT BUSINESS OWNERS SHOULD KNOW ABOUT COMPANY VEHICLES AND TAXES

If you're self-employed and you or your employees use a vehicle to conduct business, it's important to know the latest tax rules. First, business-related vehicle expenses can generally be deducted using either the:

- Mileage-rate method (54 cents per mile driven in 2016), or
- Actual-cost method (total out-of-pocket expenses for fuel, insurance, repairs and other vehicle expenses, plus depreciation).

When buying new or used vehicles, every size and structure of business should look into expensing under Internal Revenue Code Section 179. Many rules and limits apply.

For example, the normal $500,000 Sec. 179 expensing limit generally applies to vehicles with a gross vehicle weight rating of more than 14,000 pounds. A $25,000 limit applies to vehicles (typically SUVs) rated with a gross vehicle weight at more than 6,000 pounds. Vehicles rated at 6,000 pounds or less are subject to the luxury automobile limits.

For passenger autos placed in service in 2016, the first-year depreciation limit is $3,160. The amount that may be deducted under the combination of Modified Accelerated Cost Recovery System (MACRS) depreciation and Sec. 179 for the first year is limited under the luxury auto rules to $11,160.

In addition, if a vehicle is used for business and personal purposes, the associated expenses, including depreciation, must be allocated between deductible business use and nondeductible personal use. The depreciation limit is reduced if the business use is less than 100%. If business use is 50% or less, you can't use Sec. 179 expensing or the accelerated regular MACRS; you must use the straight-line method.