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CERTIFIED PUBLIC ACCOUNTANTS | CONSULTANTS CLIENT PLANNING ADVISORY FALL 2016

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YEAR END PAYROLL MANUAL

Our Small Business Resource Group creates a yearly "Year End Payroll Manual" that can help you with W-2 preparation, 1099 reporting, fringe benefits, year-end payroll tax forms and more. If you are interested you can download a copy from our website at www.atkinsoncpa.com, or you can call Christina Holcomb, Marketing Coordinator at 505-843-6492 to send you a digital copy. The payroll manual will be available in mid-December. If you need a trusted partner, our Small Business Resource Group is ready to help.

Atkinson & Co.'s Small Business Resource Group is a team composed of certified bookkeepers, IT personnel and accountants. They can assist you with bookkeeping needs, payroll, tax strategies, accounting software issues, compliance and needs specific to your business.

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Drawing Down Your Portfolio in Retirement

Retirees often need money from their investment portfolio, if they have little or no earned income. For many seniors, tax efficient withdrawals require two levels of decisions. First, should the dollars come from regular taxable accounts or from tax-deferred accounts such as IRAs? Second, regardless of where the money is coming from, how will a portfolio be liquidated to provide spending money?

TAXABLE OR TAX-DEFERRED?

Some people enter retirement holding an IRA as well as a taxable account. If cash is needed, they often choose to take the money from the taxable account.

Example 1: Joy Larson needs $4,000 a month from her portfolio in retirement to supplement her Social Security income. The money in her traditional IRA was rolled over from Joy's 401(k) plan at work. All the money in her 401(k) was pretax, so IRA withdrawals will be taxed at ordinary income rates. Consequently, Joy decides to take money from her taxable account. Those withdrawals may be tax-free, if no investment gains are triggered. And, even if Joy takes some gains, they may be taxed at favorable long-term capital gains rates.

Drawing down the taxable account may be a common practice for retirees. However, there may be drawbacks. In time, the taxable account might be depleted, leaving only pretax IRA money for distributions later in retirement. Those distributions may be heavily taxed at whatever tax rates apply in the future.

continued on page 2

Year-End Business Tax Planning

The PATH Act's many provisions also include a permanent increase in the amounts allowed under IRC Section 179, which permits rapid deduction (expensing) of funds spent for business equipment. For 2015, expensing up to $500,000 of equipment was allowed with no phaseout beginning at $2 million of purchases. For 2016, the inflation adjusted amount is $2,010,000. In addition, the PATH Act makes permanent the treatment of off-the-shelf computer software as Sec. 179 property.

The bottom line is that small companies can confidently purchase equipment and software this year. As long as total outlays don't top $2.01 million, expenses up to $500,000 can be deducted for 2016 rather than spread over several years. To qualify for the IRC Section 179 tax break, the equipment or software must be purchased, financed or leased, and placed into service by December 31. The deduction will equal the full purchase price.

For companies that spend more on equipment than the IRC Section 179 deduction allows, the PATH Act's extension of "bonus depreciation" may help. For 2016 as well as 2017, a taxpayer may generally deduct 50% of qualifying equipment's cost (reduced by the amount of any Sec. 179 expense deduction taken for the cost of the equipment). However, bonus depreciation applies only to new equipment while the first-year IRC Section 179 deduction applies to new and used equipment.

PAPERWORK NOW, PAYMENT LATER

The end of the year is also a good time to review your company's retirement plan situation. If you have one, should you make a change? If you don't have a company-sponsored retirement plan, do you want to establish one? Such a plan not only will benefit your employees, it will enable you to put aside funds for your own retirement on a tax-favored basis.

Today, a 401(k) can be considered the "standard" company plan. Many prospective employees expect to have a 401(k) at work, so offering such a plan may enable you to attract good people and retain valued workers. Contributions generally are funded by the employees themselves, but many companies provide matching contributions in some form.

December 31 is the deadline for establishing a 401(k) plan for 2016, assuming your company uses a calendar year. Employee contributions for 2016 must be withheld from 2016 paychecks and must be sent to the relevant financial firm as soon as possible. Employer contributions, deductible for 2016, can be made up to the company's tax return due date, including extensions.

A variation of the basic 401(k) is often known as the solo 401(k) or the individual 401(k). Other names may apply. However the plan is titled by the financial firm involved, it is open only to business owners and their spouses who are employed by the company. For 2016, the maximum contribution to a solo 401(k) is $53,000 per participant, if certain conditions are met, or $59,000 for those age 50 or older. Basic 401(k) plans have contribution limits of $18,000 or $24,000 before any employer match.

Again, the deadline for establishing a solo 401(k) in 2016 is December 31 of this year. Some tax deductible contributions may be made up to the tax return deadline, including extensions, in 2017.

BEYOND 401(K)S

Other retirement plans for small businesses also have a December 31 deadline for signing the forms to receive tax benefits in 2016. These plans also have an extended due date for making contributions. They include profit sharing plans, which are funded by the employer. Profit sharing plans may motivate employees to help the company's earnings grow. Annual employer contributions are discretionary, so companies aren't locked in.

Our office can help you choose among various retirement plans for your business and let you know about any year-end deadlines. ❍

Drawing Down Your Portfolio in Retirement

continued from page 1

In addition, holding on to IRA money can lead to a sizable amount of tax-deferred dollars left to your heirs. Your beneficiaries will have required minimum distributions (RMDs) from the inherited IRA, and those distributions probably will be taxable. (Special rules apply to IRA money left to a surviving spouse, but those dollars eventually may pass to younger relatives.) If the IRA beneficiaries inherit while in their prime working years, the tax on those distributions could be especially steep.

On the other hand, if you take some cash from your IRA and leave highly appreciated assets in your taxable account, you may be able to pass those appreciated assets to your heirs. Under current law, they'll get a basis step-up, usually to a date-of-death value. Then, your heirs can sell the assets and avoid paying tax on the appreciation during your lifetime.

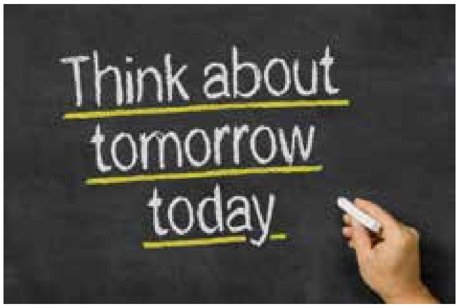
The bottom line is that you might want to use some IRA money as well as money from taxable accounts to cover living expenses in retirement. This approach may be helpful before you reach age 70½, when RMDs from your IRA begin. Withdrawing some money from your IRA before 70½ may help you hold down taxable RMDs in the future.

KNOW HOW TO FOLD 'EM

Regardless of where the money will come from, you should have a plan for drawing down your portfolio in retirement. Your specific circumstances will influence your decisions, but one approach is to start retirement with a sizable "cash bucket." This money can be used for living expenses, regardless of what happens in the financial markets.

Example 2: In example 1, Joy Larson needs $4,000 a month from her portfolio in retirement, or $48,000 a year. Joy decides she wants enough cash to cover three years' outlays, or $144,000. Therefore, in advance of her retirement, Joy puts together $144,000 in bank CDs and money market funds. This money can flow into her checking account to help pay her bills.

From time to time, Joy will liquidate other assets to replenish her cash bucket. There are many ways to do so, so Joy should have a plan. For instance, she may check her asset allocation every year to see whether it's still in keeping with her current wishes. Suppose Joy wishes to keep a 50-50 asset



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allocation between stocks and bonds, but a stock market slide has tilted her portfolio towards bonds, which have been stable. Then, Joy might sell some bonds and bond funds, putting the proceeds into her cash bucket while bringing her portfolio into a better balance.

No portfolio drawdown plan will work for everyone, but you should approach retirement with a well-reasoned plan and attempt to stick with it. Having a substantial amount of cash may enable you to ride out any market downturns, while having a thoughtful mix of equities and fixed income can provide income and growth potential throughout your retirement. ❍

Year-End Retirement Tax Planning

Many people save money for retirement in a traditional IRA. The funds might have come from annual IRA contributions, or from rolling over an employer sponsored retirement account such as a 401(k). Either way, the dollars in your traditional IRA are probably pretax, so they'll be taxed on withdrawal.

You can leave the money in your traditional IRA for ongoing tax deferral. However, you might need cash now, especially if you're retired or have had unexpected expenses. In another scenario, you may expect your traditional IRA to be extremely large by the time you reach age 70½ and RMDs begin. Those RMDs might be so large that they'll be heavily taxed in a high bracket.

Therefore, you might want to take withdrawals from your traditional IRA before year-end 2016, so they'll count in this year's taxable income. With savvy planning, you can minimize the tax bite by staying within your current tax bracket.

Example 1: Greg and Heidi Jackson's taxable income last year was $100,000. They expect their taxable income to be about the same this year. In 2016, the 25% bracket goes up to $151,900. Thus, the Jacksons can take as much as $50,000 from their traditional IRAs before December 31 this year, without moving into a higher tax rate. They might withdraw, say, $20,000 from their IRAs, pay $5,000 in tax at a 25% rate, and have $15,000 left for other purposes.

THE RIGHT SPOT

If you're taking money from a traditional IRA, the best time may be between ages 59½ and 70½. After age 59½, the 10% early withdrawal penalty won't apply; before 70½, you won't be subject to RMDs, which will restrict your flexibility about IRA withdrawals.

If you're younger than 59½, you still might avoid the 10% penalty by qualifying for an exception. Several exceptions are available, including one for higher education expenses.

Example 2: Suppose Greg and Heidi Jackson from example 1 are both younger than 59½. If they take $20,000 from their IRAs this year, as indicated in that example, a $2,000 (10% of $20,000) penalty will be added to their $5,000 (25%) tax bill. However, if the Jacksons pay at least $20,000 in 2016 for their daughter's college bills, they can take that $20,000 from their IRAs and owe the 25% income tax but not the penalty.

CANNY CONVERSIONS

After withdrawing funds from a traditional IRA at a low tax, un-penalized rate, you can use the after-tax dollars to pay college bills or for living expenses in retirement. If there is no immediate need for cash, you can move the money into a Roth IRA. After five years and age 59½, all withdrawals from a Roth IRA will be tax-free.

Converting traditional IRA money to a Roth IRA will trigger income tax. That might not be a major issue if you're staying in the 15%, 25%, or 28% tax brackets. However, if you convert too much, you could wind up moving into a higher bracket and paying more income tax than you'd like.

Fortunately, the tax code offers a solution to this potential problem. You can recharacterize (reverse) a Roth IRA conversion, in whole or in part, by October 15 of the following year, and owe tax only on the amount that stays in the Roth IRA.

Example 3: In the previous examples, Greg and Heidi Jackson expect to have around $100,000 in taxable income this year. Their 25% tax bracket goes up to $151,900 in 2016. The Jacksons, hoping to convert as many dollars as possible at the 25% tax rate, convert $50,000 of Greg's IRA to a Roth IRA by year-end 2016.

When the Jacksons prepare their income tax return for 2017, they learn that their 2016 taxable income was higher than expected. Not including the Roth IRA conversion, their taxable income was $118,500. A full $50,000 Roth IRA conversion would put part of the conversion amount into the 28% bracket, generating more tax than the Jacksons want to pay.

In this situation, the Jacksons could recharacterize enough of Greg's Roth IRA conversion to wind up with a $33,400 conversion, retroactively. They would use up the full 25% tax bracket while the recharacterized dollars would return to Greg's traditional IRA, untaxed. If you are interested in this type of lookback fine tuning, our office can help you with a year-end Roth IRA conversion and a possible 2017 recharacterization.

BEYOND IRAS

The 2016 contribution limit for 401(k) plans is $18,000 per participant plus $6,000 if you're 50 or older by year-end. If you are not maximizing your 401(k) contributions and wish to put more into the plan this year for increased tax deferral, contact your plan administrator. Meanwhile, keep in mind that many retirement plans impose RMDs after age 70½. Make sure you're withdrawing at least the minimum amount, if you're required to do so, in order to avoid a 50% penalty on any shortfall. ❍

New Tax Filing Deadlines

W-2 AND 1099 FORMS

In 2017, both paper and electronic tax year 2016 Forms W-2 and W-3, and those 1099s that include non-employee compensation in Box 7, must be submitted to the SSA and IRS by Jan. 31, 2017. Forms 1099 that do not include an entry in Box 7 will still be due by Feb. 28 (if filed electronically, by Mar. 31). Where you file them remains unchanged: 1099s to the IRS; W-2's and the W-3 to the SSA. All W-2s and 1099s must be mailed to payees by Jan. 31, 2017.

PARTNERSHIP INCOME TAX RETURNS

The new due date for partnerships with tax years ending on December 31 to file federal income tax returns is March 15. For partnerships with fiscal year ends, tax returns are due the 15th day of the third month after the close of the tax year. Under prior law, returns for calendar-year partnerships were due April 15, and returns for fiscal-year partnerships were due the 15th day of the fourth month after the close of the fiscal tax year.

CORPORATION INCOME TAX RETURNS

The new deadline for C corporations to file income tax returns is the 15th day of the fourth month after the close of the corporation's tax year. In other words, C corporations with tax years ending on December 31 must file federal income tax returns on or before April 15. Under prior law, such returns were due on the 15th day of the third month after close. (S corporations must continue to file returns on the 15th day of the third month, after close of the corporation's tax year.)

C corporations with tax years ending on June 30, however, aren't subject to the new due dates until tax years beginning after December 31, 2025.

The revised due dates are generally effective for tax years beginning after December 31, 2015. In other words, they generally apply to the tax returns for 2016 that are due in 2017. ❍

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6501 AMERICAS PARKWAY NE , SUITE 700
ALBUQUERQUE , NM 87110

PO BOX 25246
ALBUQUERQUE, NM 87125

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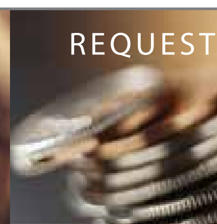

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EDITOR: ROBERTA SALAS
CO-EDITOR: SHERRY STATES, CPA