MARKS PANETH

ACCOUNTANTS & ADVISORS

MARKS PANETH TAX ALERT: YEAR-END TAX PLANNING FOR BUSINESSES AND INDIVIDUALS

EXPIRING TAX BREAKS FOR BUSINESSES MAY MERIT ACTION NOW

Although tax legislation signed into law this past January made a wide variety of tax breaks permanent, it extended several valuable breaks for businesses only through Dec. 31, 2013. It's possible that some, or even all, of them could be extended again. But with the battle in Washington over tax reform, it's difficult to predict what will happen with expiring breaks.

So you may want to take steps now to lock in any breaks that can benefit your business while they're still available. Don't, however, ignore traditional year-end strategies for your business — or yourself.

Enhanced depreciation-related breaks

Many businesses may benefit from purchasing assets by Dec. 31 to take advantage of depreciation-related deductions that are scheduled to either become less favorable or disappear in 2014:

***Bonus depreciation*.** For qualified assets acquired and placed in service through Dec. 31, 2013, this additional first-year depreciation allowance is, generally, 50%. Among the assets that qualify are *new* tangible property with a recovery period of 20 years or less and off-the-shelf computer software. With a few exceptions, bonus depreciation is scheduled to disappear in 2014.

***Section 179 expensing*.** This election allows a 100% deduction for the cost of acquiring qualified *new* or *used* assets. But, a couple of rules may make Sec. 179 expensing less beneficial to certain businesses:

- For 2013, expensing is subject to an annual limit of $500,000, and this limit is phased out dollar for dollar if purchases exceed $2 million for the year. So larger businesses may not benefit.
- The election can't reduce net income below zero. So, for businesses that are having a bad year, it can't be used to create or increase a net operating loss for tax purposes.

The expensing and asset purchase limits are scheduled to drop to $25,000 and $200,000, respectively, in 2014.

***Breaks for leasehold improvement, restaurant and retail improvement property*.** All of these breaks are scheduled to expire Dec. 31:

- ***50% bonus depreciation*.** This additional first-year depreciation allowance is available for qualifying leasehold improvements.
- ***Sec. 179 expensing*.** You can use part of your Sec. 179 election to deduct up to $250,000 of qualified leasehold-improvement, restaurant and retail-improvement property.
- ***Accelerated depreciation*.** A shortened recovery period of 15 — rather than 39 — years can be applied to qualified leasehold-improvement, restaurant and retail-improvement property.

Although all of these depreciation-related breaks may offer substantial savings on your 2013 tax bill, it's possible they won't prove beneficial over the long term. Taking these deductions now means forgoing deductions that could otherwise be taken later, over a period of years under normal depreciation schedules. In some situations — such as if in the future your business could be in a higher tax bracket or tax rates go up — the normal depreciation deductions could be more valuable.

Credit for hiring from disadvantaged groups

The Work Opportunity credit is designed to encourage hiring from certain disadvantaged groups. Examples of qualifying groups include food stamp recipients, ex-felons and nondisabled veterans who've been unemployed for four weeks or more, but less than six months. For hiring from these groups, the credit generally equals 40% of the first $6,000 of wages paid, for a maximum credit of $2,400 per qualifying employee.

A larger credit may be available for hiring disabled veterans or veterans who've been unemployed for six months or more in the preceding year.

Currently the Work Opportunity credit is scheduled to expire Dec. 31. So if new hires from one of the eligible groups might make sense for your business, consider making the hires soon to ensure you can benefit from the credit if it's not extended.

Credit for research

The research credit (also commonly referred to as the "research and development" or "research and experimentation" credit) is for increases in a wide variety of research activities, not just laboratory experiments. Wages for researchers, the cost of research supplies and the cost of computer licensing for research purposes are among those expenses that may qualify.

The traditional research credit is equal to 20% of qualified research expenses over a defined base amount related to your gross receipts and previous research spending. The simplified credit is equal to 14% of qualified spending for that year that's over 50% of your qualified research expenses for the previous three years.

Because the research credit is scheduled to expire Dec. 31, if you have the capability of increasing your research activities between now and year end, you may want to do so to help ensure you can take advantage of the credit. Or, if you've already increased your research activities for the year, make sure you're properly tracking those expenses.

Tried-and-true tax strategies for businesses

Considering traditional income and expense timing strategies is always a good idea. If you expect to be in the same or a lower tax bracket next year, it's generally a tax-smart idea to defer income to next year and accelerate deductible expenses into the current year. The opposite approach can save tax overall if you expect to be in a *higher* bracket next year (though it will increase your tax bill this year).

Maximizing tax credits will also help save tax. In addition to the credits mentioned above, examples of credits your business may qualify for include:

- Empowerment zone,
- New markets,
- Energy-related,

- Health care coverage for small businesses, and
- Retirement plan for small businesses.

Some of these credits also are scheduled to expire Dec. 31.

YOUR INDIVIDUALTAX PLAN

Although most tax breaks for individuals were made permanent, year end tax planning is still critical for individuals — especially higher-income taxpayers. Why?

Beginning in 2013, the top ordinary rate of 39.6% and top long-term capital gains rate of 20% return for taxpayers with taxable income that exceeds $400,000 (singles), $425,000 (heads of households), or $450,000 (married couples filing jointly).

Also beginning in 2013, under the 2010 health care act, an additional Medicare tax on earned income and a new Medicare tax on net investment income will be imposed when income exceeds certain levels. The additional 0.9% Medicare tax applies to FICA wages and self-employment income exceeding $200,000 (singles and heads of households) or $250,000 (married couples filing jointly). The new 3.8% Medicare tax applies to net investment income to the extent that modified adjusted gross income exceeds those same thresholds.

Finally, the income-based reductions on itemized deductions and phaseout of personal exemptions return in 2013. The thresholds for them are $250,000 (singles), $275,000 (heads of households) and $300,000 (married filing jointly).

All of these tax increases warrant additional year end planning. You may not be able to avoid these hikes, but you can take steps to help minimize their impact.

DON'T PUT OFF TAX PLANNING

Most steps to reduce your current year's tax bill must be implemented by the end of the year. Acting before year end is especially critical when it comes to breaks that expire this year. So don't put off tax planning. Please contact us today to learn what steps you can take to minimize your business and individual tax bills for 2013 and beyond.

TAX PLANNING GUIDE

To facilitate ongoing access to the latest tax rules and regulations, Marks Paneth offers an online tax guide that is updated on a regular basis.

FOR MORE INFORMATION

If you have questions about anything you read either in this alert or in our tax planning guide, please contact a Marks Paneth tax advisor or Steven Eliach, JD, LLM, the Principal-in-Charge of the Marks Paneth Tax Practice, by phone at 212.503.6388 or by email at seliach@markspaneth.com.

SCHEDULE A YEAR-END TAX PLANNING MEETING

Companies and individuals alike seek to minimize their tax liability while still complying with applicable tax laws and regulations. Year-end tax planning can help achieve these goals as well as facilitate the filing of next year's tax returns.

We encourage you to schedule a tax planning meeting with a Marks Paneth tax advisor. Our online tax planning guide can provide a framework for this discussion.

Our knowledgeable professionals look forward to working with you to develop strategies customized specifically for you.

IRS CIRCULAR 230 DISCLOSURE

Treasury Regulations require us to inform you that any Federal tax advice contained in this communication is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter addressed herein.