What's interesting, what's new & what now……

WHITE & COMPANY, PC
CERTIFIED PUBLIC ACCOUNTANTS

Presented by:
Ivan White, CFP®, CPA, PFS, Thomas White, CFP®, CPA, PFS and Eric Parker, CPA
PO Box 898
Sunnyside, WA 98944
Phone: (509)837-6700 or 800-405-4158
Email: advisers@whitecocpa.com

January 2017

WHAT'S INTERESTING……

1. Taxpayer must determine whether an expenditure related to tangible property is currently a deductible expense or a non deductible but depreciable capital expenditure
2. Step 1 - Determine the proper unit of property (UOP) for buildings. UOP is the building and its structural components & eight separately defined building systems *i.e. the plumbing, electrical, HVAC, escalator, fire protection, alarm, gas distribution and security systems*
3. Step 2 - Determine if there is an improvement to the UOP that needs capitalized. The UOP is improved only if the amounts paid are:
   I. For a <u>betterment</u> to the UOP
   II. To <u>restore</u> the UOP
   III. To <u>adapt</u> the UOP to a new or different use

4. Definitions:
   I. A **Betterment** is anything that (a) ameliorates a material condition or defect that either existed before the acquisition of the unit of property or arose during production, (b) is for a material addition that enlarges, expands, extends or adds a major component to a unit of property or increases capacity of the unit of property or (c) is reasonably expected to increase productivity, efficiency, strength, quality or output of a unit of property
   II. A **Restoration** is an amount paid to (a) restore a unit of property to its ordinarily efficient operating condition if it has deteriorated to a state of repair, (b) returns the unit of property to a like new condition after the end of its class life or (c) replaces a part or combination of parts that comprise a major component or major structure or building system.
   III. An **Adaptation** is an improvement to adapt a unit of property to a new or different use

5. To qualify as a repair –a good rule of thumb is replace less than 33% of a major component of a unit of property (UOP) and less than 30% of the building or its structural component
6. Tax elections under the final tangible property regulations
   I. De minimis expensing safe harbor
   II. Safe harbor election for small taxpayers
   III. Routine maintenance safe harbor
   IV. Elect to capitalize
7. If the de minimis safe harbor is elected, taxpayers won't have to capitalize the cost of acquisition or improvements under $2,500

8. The de minimis amount is determined at the invoice or item level
    I. Taxpayer is not required to include the additional costs of acquiring or producing unless included on the invoice
    II. An amount in excess of the de minimis amount does not automatically have to be capitalized, the other rules then apply
    III. Anti-abuse rule –prohibits a taxpayer from manipulating a transaction to avoid the applicable per-item limit
9. Another safe harbor is the Small Taxpayer safe harbor to immediately deduct improvements (repairs)
    I. Annual amount per building is limited to the lesser of 2% of building's unadjusted basis (original purchase cost & capitalized improvements less land cost) or $10,000
    II. If total improvements, repairs, etc. exceed the 2% then the safe harbor is not available
    III. Election must be timely & applies to each property
    IV. Small taxpayer: Gross receipts under $10 million

10. Routine maintenance safe harbor –
    I. Recurring activity to maintain operating condition during property's useful life
    II. Includes -inspection, cleaning and testing
    III. Specific to buildings –reasonably expected to be needed more than once in ten years after purchase –only has to be expected
    IV. Considerations –
        a. recurring nature of activity
        b. Manufacturer's recommendations
        c. Industry practice –HUD carpeting every 7 years
        d. Taxpayer experience
11. Elect to capitalize everything
    I. Creates added basis
    II. Does not increase Passive Activity Loss (PAL)
12. IRS Position –Publication 527, Residential Rental Property ****See IRS Publication 527 on following page**

Repairs and Improvements

Generally, an expense for repairing or maintaining your rental property may be deducted if you are not required to capitalize the expense.

Improvements. You must capitalize any expense you pay to improve your rental property. An expense is for an improvement if it results in a betterment to your property, restores your property, or adapts your property to a new or different use. Table 1-1 shows examples of many improvements.

Betterments. Expenses that may result in a betterment to your property include expenses for fixing a pre-existing defect or condition, enlarging or expanding your property, or increasing the capacity, strength, or quality of your property.

Restoration. Expenses that may be for restoration include expenses for replacing a substantial structural part of your property, repairing damage to your property after you properly adjusted the basis of your property as a result of a casualty loss, or rebuilding your property to a like-new condition.

Adaptation. Expenses that may be for adaptation include expenses for altering your property to a use that is not consistent with the intended ordinary use of your property when you began renting the property.

Depreciation of Rental Property

Table 1-1. **Examples of Improvements**

Additions	**Miscellaneous**	**Plumbing**
Bedroom	Storm windows, doors	Septic system
Bathroom	New roof	Water heater
Deck	Central Vacuum	Soft water system
Garage	Wiring upgrades	Filtration system
Porch	Satelite dish	
Patio	Security system	
Lawn & Grounds	**Heating & Air Conditioning**	**Interior Improvements**
Landscaping	Heating system	Built-in appliances
Driveway	Central air conditioning	Kitchen modernization
Walkway	Furnace	Flooring
Fence	Duct work	Wall to wall carpeting
Retaining wall	Central humidifier	
Sprikler system	Filtration system	**Insulation**
Swimming pool		Attic
		Walls, floor
		Pipes, duct work

13. Options to use to expense improvement

    I. Safe harbor for items $2,500

    II. Small Taxpayer safe harbor

    III. Routine maintenance safe harbor

    IV. Improve less than 30% of UOP

    V. Consider the improvement a refresh

What's New….

14. A taxpayer owned an S Corp that held a horse breeding business operated at a loss. The S Corp paid the landlord $80k rent per year for the land and buildings. IRS classified the horse breeding business as a hobby & disallowed the loss and the rent paid. However, the landlord received the rent and had to pay tax on the rent income of $80k and could not deduct the hobby loss!
15. Taxpayer held all business receipts for Nov & Dec and deposited them in January. This put three-months income into January. Under IRS audit, Nov & Dec were pulled back to the open year under audit. January of the same open year had three-months income resulting in fourteen-months of income. The IRS did not allow a corresponding deduction to the previous closed year.

16. Taxpayer was depositing cash under the $10k amount multiple times and acting suspicious to the teller. The bank voluntarily filed Form 8300 (Report of Cash Payments Over $10k Received in a Trade or Business) even though the total was under $10k. Since Form 8300 was filed voluntarily, no copy was required to be given to the taxpayer –but the IRS had one! Ouch!
17. Bitcoin –The IRS considers Bitcoins an asset, not currency. If you buy Bitcoins for $600 and use them to pay for an asset or an expense worth $800, you have a short-term gain of $200
18. If you deduct employee business expenses on Form 2106 (Employee Business Expenses) when they are reimbursable from the employer, there is no deduction.

19. State of WA estate tax exclusion amount for 2017 = $2,129,000. Filing threshold is $2M even if no tax is due. WA has *no* gift tax laws. Federal estate or gift exclusion for 2017 is $5,490,000.

20. Only 14 states impose an estate tax and six states impose an inheritance tax. WA is rated the #7 worst for estate tax by Kiplinger. Oregon is rated the #1 worst for estate tax!

21. All W-2s and 1099s have been due to the taxpayers by January 31st. Now, the W-2 and Form 1099MISC filing deadline with the IRS & Social Security Administration for all issuers is also January 31st (was March 1)

22. In an effort to recoup overdue taxes owed, the IRS will be turning inactive receivables over to private debt collectors starting in the spring 2017. All of these taxpayers will be sent a letter from the IRS informing them of the turnover to a private collection agency. Then they can be contacted by phone. Think this will be a problem?

23. An IRS emphasis point: You need the proper documentation to deduct charitable contributions, per IRS regs. Without it, no deduction….period!

I. A single cash contribution under $250 –a cancelled check, bank record, credit card statement or written acknowledgement from charity
II. A cash contribution of more than $250 –written acknowledgement from the charity
III. A payroll deduction –a paystub and pledge card
IV. Noncash contribution less than $250 –written acknowledgement from the charity
V. Noncash contribution of $250-$500 –same written acknowledgement from the charity
VI. Noncash contribution of $500- $5,000 –same written acknowledgement and Form 8283 (Noncash Charitable Contributions)
VII. Noncash over $5,000 –same written acknowledgement , appraisal by qualified appraiser attached to Form 1040 and Form 8283
VIII. Noncash contribution of more than $500,000 -written acknowledgement from the charity, appraisal must be attached to the return and Form 8283, part B

IX. Noncash contribution of auto, boat or airplane with a value of more than $500 -written acknowledgement from the charity, attach Form 1098-C and Form 8283 to the return

X. Noncash contribution of publicly traded stock -written acknowledgement from the charity and Form 8283, part A

XI. Noncash contribution of privately traded stock of more than $5,000 -written acknowledgement from the charity, Form 8283 part B. Appraisal is required to be attached if the privately traded stock is valued at $10,000 or more

XII. Noncash contribution of art valued at more than $20,000 -written acknowledgement from the charity, appraisal, Form 8283 part B. The appraisal and a photo must be attached to the return

XIII. IRA owners over age 70.5 that do Qualified Charitable Distributions (QCD) need a written acknowledgement also from the charity!

****The written acknowledgement must be received from the charity before the due date of the return (including extensions) and it must include a statement that no goods or services were received in exchange for the contribution*

24. IRS emphasis point – the Real Estate professional. There are three eligibility requirements.

   I. Rental real estate is owned by you
   II. The 50% test. 50% of your personal services for the year are performed in real property trade or business
   III. The 750 hour test. You must perform more than 750 hours in these trades or business

IV. Other requirements –

a. Each spouse must be considered separately for percentage & hours
b. Eligible trade or businesses are: Development, Redevelopment, Construction, Acquisition, Conversion, Rental that you operate, manage, lease or broker trade or business real estate appraisers
c. Mortgage brokers are _not_ in an eligible trade
d. The time test is most difficult because of proof required
e. Even though spouse is treated separately on a jointly filed return, only one spouse needs to be a Real Estate professional to deduct the loss
f. After determining you are a Real Estate professional, you must prove material participation in managing the rentals
g. Most common three out of seven ways to prove material participation:
    i. Doing substantially all the work –more than 70% of all hours
    ii. Managing for more than 500 hours –Grouping needed?
    iii. Work more than 100 hours with no one else participating

25. Another IRS emphasis point –Passive Losses

I. Rentals are "per se" passive and net losses are carried over, not currently deductible

II. "Material participation" avoids passive treatment only if rental activity can be properly grouped within a trade or business

   a. Most common test is more than 500 hours participating in grouped activity

   b. Other tests include "significant participation activities", 100 hours without others spending more hours and 5 other tests

   c. Grouping requires common ownership interest, interdependence, appropriate economic unit and other requirements

III. Active rental real estate exception allows up to $25,000 of overall rental loss

   a. Phased out at AGI between $100,000 and $150,000

   b. Requires substantial involvement in managing the rental (no property manager)

IV. Passive losses are released in year of disposition

V. PAL carryovers do not have a statue of limitations

26. State of Washington definition of employee vs. independent contractor

I. Auditors from Employment Security and Labor & Industries assume an individual is an employee

II. RCW 51.08.195 provides exceptions to treatment of employees

a. The individual is free from control or direction over the performance of the service

b. The individual is customarily engaged in an independent established trade, occupation or business

c. The individual is responsible to file with the IRS for the type of business the individual is conducting.

d. On the effective date of service or reasonable period of time after service, the individual has established an account with the Department of Revenue and has registered and received a UBI number

e. The individual is maintaining a separate set of books and records for the business

III. The auditors are ignoring all of the above except item "d"

WHAT NOW……

27. Trump and Republican proposals include:
    I. Only three tax rates vs. eight right now
    II. Affordable Care Act (ACA) taxes removed
    III. Alternative Minimum Tax (AMT) –gone!
    IV. Estate and gift tax under $10M net –gone!
    V. Net investment income tax –gone!
    VI. Corporate tax rate 15%
    VII. Who knows what else…….


TAXES

How to search for a UBI number.........two choices

Websites:

WA STATE –CORPORATIONS DIVISION

https://www.sos.wa.gov/corps/corps_search.aspx

WA STATE –DEPARTMENT OF REVENUE

http://dor.wa.gov/content/doingbusiness/registermybusiness/BRD/

NOW ON THE TABLE -

A. Affordable Care Act (ACA) Repeal & Replacement
   I. Repeal of the Individual and Employer Penalties
   II. Repeal net investment income tax – equals 3.8% of investment income if modified adjusted gross income (AGI) is over $250,000
   III. Repeal of 0.9% additional Medicare tax on wages or earnings over $250,000
   IV. Repeal of the increased subtraction percentage from medical expense. The repeal of 7.5% to 10%
   V. Repeal of medical devise excise tax of 2.3%
   VI. Repeal of the $2,500 limitation on Sec. 125 Plan
   VII. This is the House version
B. American Health Care Act (AHCA) – Replace
   I. New refundable credit for premium assistance based on age for those without coverage
   II. Increase HSA contribution limit to $6,550 for self only and $13,100 for family

NOW ON THE TABLE - Continued

C. The Trump Plan

I. Reduce tax brackets from 7 down to 3

i. Current brackets: 10, 15, 25, 28, 33, 35 and 39.6%

II. Double the current standard deduction amount:

i. Current standard deduction: MFJ= $12,700 would increase to MFJ= $25,400

III. Eliminate all itemized deductions except contributions and mortgage interest

IV. Tax corporations at a 15% rate versus the current 35%

V. Tax past through businesses at 15% rate versus current at one of the 7 rates mentioned earlier (see C.1.i. above)

VI. Remove all Estate taxes