

Enclosed please find your organizer for the 2016 filing season. The organizer will assist you in gathering your tax information by showing you what was reported on your 2015 return. Below we have highlighted some 2016 tax changes and year-end reminders. If you should have any questions, please don't hesitate to contact us.

Like last year, most individuals are required to have minimum essential health insurance coverage or pay a penalty. Included in this packet of information is an Affordable Care Act checklist which you must complete, sign and return to us with your other tax information. **We also need copies of any 1095 forms you receive.**

The IRS has expanded enforcement efforts by increasing reporting requirements on tax preparers. Due diligence checklists that we must complete have grown to include questions regarding education and child tax credits. In addition the IRS is intensifying requirements for electronic information security for tax preparers. These changes, along with ever expanding tax regulations, are significantly increasing costs to tax preparers. We are doing our best to mitigate these added expenses, but you may see fee increases this year as we strive to maintain the highest quality work for our valued clients.

### Important Tax Law Items - Individual

- The standard mileage rate for business use of a vehicle was 54 cents-per-mile for 2016.
- The maximum rate for long-term capital gains for 2016 remains at 15% for many taxpayers; however, if you are in the 39.6% bracket (see above) your maximum rate is 20%. Qualified dividend income continues to qualify for capital gain treatment in 2016.
- An additional Medicare tax of 0.9% was added for 2013 and remains in effect. This tax applies to wages, self-employment income, and railroad retirement compensation **in excess of \$250,000** (married filing jointly), \$125,000 (married filing separately), and \$200,000 (any other filing status).
- Similarly a Net Investment Income (NII) tax of 3.8% was added for 2014 which also remains. This tax applies to the smaller of your net investment income or your modified AGI **in excess of \$250,000** (married filing jointly and qualifying widow(er)), \$125,000 (married filing separately), and \$200,000 (any other filing status). NII generally consists of interest, dividends, capital gains, passive investments and rental income. However, there are exceptions on rental income for "real estate professionals" and in self-rental situations.
- Rental properties require more disclosures than in the past. **For each property**, the physical location, the type of property (single family, duplex, commercial, etc.), the number of days rented, the number of days used for personal purposes, and any Form 1099-Ks received must be reported.
- Reminder – All charitable deductions of any amount must have a receipt. Any individual contribution over \$250 must also have an acknowledgement letter from the charity. Several recent court cases have emphasized the importance of documentation in this area. Note: most "go-fund-me" donations are not deductible because the contribution is not to an IRS recognized charity.
- We are required to report on your income tax return the amount of any distributions from a health savings account (HSA), even if the funds were properly used for qualified medical costs. Please provide us with a copy of the Form 1099-SA from your HSA administrator.
- The IRS is now requiring taxpayers to obtain Form 1098-T for higher education expenses in order to claim education credits and/or deductions. Please provide us a copy of this form if you wish to claim these expenses on your 2016 income tax return.
- Distributions from 529 plans are tax-free when used for tuition, room and board, fees, books, computers and related software. Also keep in mind that Indiana "College Choice" plans are eligible for a credit of 20% of the contribution up to a maximum credit amount of \$1,000.
- Reminder - beginning with 2011 returns, Indiana allows a deduction of up to \$1,000 for K-12 dependents in private or home schools for expenses related to tuition, books, etc.
- Indiana repealed the insulation deduction effective 1-1-2016.
- A teacher's credit (similar to the federal tax break) remains in effect for 2016 equal to the lesser of \$100 or the total amount expended for classroom supplies during the year.
- Planning tip on IRA's: Name specific beneficiaries to allow distributions over the beneficiary's life expectancy. If the IRA simply gets distributed through an estate the funds must be distributed (and taxed) within five years from date of death.
- The gift tax exclusion amount is \$14,000 per donee for 2016. The federal estate tax exclusion is currently \$5,450,000 for 2016. Indiana's inheritance tax has been repealed for individuals who pass away after 12/31/2012.
- US taxpayers with foreign financial accounts to be aware that that the FinCEN 114 (formerly known as the FBAR) is due April 15, 2017. This form is required if the account value exceeds \$10,000 at any time during the year. The form used to be due by June 30<sup>th</sup>.

## Business Deductions and Law Changes

As in previous years we urge you to develop a mindset that you may be asked by taxing agencies to produce your documentation when organizing your records this year end. With that in mind, please take a moment to review the items below and please don't hesitate to contact us regarding specific questions about your business.

- Filing due dates are changing for 2016. C corporations are now due April 15, 2017 (previous due date was March 15<sup>th</sup>). S corporations remain the same, for this year the due date is March 15, 2017. Partnerships are due March 15, 2017 (previous due date was April 15<sup>th</sup>).
- With Notice 2015-82 the IRS raised the threshold for items that required capitalization. The new rules require examination of all repair or maintenance expenditures over \$2,500. Each such item may be written off in total for 2016 if:
  - You expect to perform the activity more than once over the item's tax life; AND
  - The maintenance keeps (rather than puts) the property in operating condition; AND
  - The need for the maintenance results from your own use (not a prior owner's use).
- The Code §179 expensing election for equipment remains \$500,000 for 2016 but the Indiana limit remains only \$25,000. In addition, 50% "bonus" depreciation deductions are available for eligible items purchased as new during for 2016.
- **Be sure to file 1099 forms** for contractors over \$600, for rental payments or attorney fees paid. Intentionally disregarding this responsibility is a \$530 (up from \$520 last year) penalty for each 1099 not filed. Also note that the filing deadline to submit copies to the IRS and the recipient has advanced to January 31, 2017.
- All business expenses must be ordinary and necessary to be deductible. In addition, deductions reported on an income tax return must be verifiable. To corroborate an amount a taxpayer must have a receipt that indicates the vendor, amount, date and a description of the item or service purchased. Merely having a credit card statement (including American Express) that details the charges is not enough. You must have receipts. The backup documents must be maintained for as long as the statute of limitations remains in effect. **We recommend keeping the information for a minimum of six years.**
- Business meals with clients, customers or employees may be deductible only if the meal is (1) directly related to the active conduct of your business and (2) a substantial and bona fide business discussion takes place. Proof that these requirements were met must be documented on the receipt or in a separate journal. Meals where only business owners and their families are present are only deductible when traveling away from home. "Away from home" means requiring an overnight stay.
- Reimbursements to employees for business deductions must fall under an "accountable plan." This means that employees must provide receipts to their employer for the expenses. Reimbursing an employee without substantiating the expense will require treating the amounts as wages, subject to all the related payroll tax burdens.
- The personal portion of automobiles provided to employees must be included in their compensation unless they reimburse the employer for the personal usage. **Contemporaneous logs of automobile usage are required to validate the deduction.** The log should include dates, customers/vendors visited and the business purpose for each trip as well as the total miles driven on the vehicle during the year.
- The IRS continues to scrutinize year-end inventories; therefore, we strongly encourage you to **take a physical count of your inventory** items as of December 31, 2016. Reporting "about the same as last year" may well be a red flag to the IRS.
- Ohio is expanding the small business deduction to include 100% of the first \$250,000 of net income, with a 3% flat rate after the limit is reached.

## Other

In an effort to protect taxpayer personal information the IRS is now requiring that we obtain a written consent signed by our clients in order to release any information to a third party. We are happy to accommodate your request to release copies of tax returns, financial statements or other documents to banks, insurance companies and others, but keep in mind that we will need the consent form before processing your request.

Gillam & Zetzel will continue to provide clients with electronic copies of tax returns (in a PDF format), however paper copies are available if you prefer. If the electronic option is chosen, we will email the returns to you, or provide them on a portable storage device. All electronic returns will be password protected, and can be read with a free Adobe PDF application.

Thank you for the opportunity to be of service to you!

*Happy Holidays from everyone at Gillam & Zetzel, Inc.*