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# Tax & Business Alert

OCTOBER 2015

## TIME TO START YEAR-END TAX PLANNING

The federal income tax rates for 2015 are the same as last year: 10%, 15%, 25%, 28%, 33%, 35%, and 39.6%. However, the rate bracket beginning and ending points are increased slightly to account for inflation. For 2015, the maximum 39.6% bracket affects singles with taxable income above $413,200, married joint-filing couples with income above $464,850, heads of households with income above $439,000, and married individuals who file separate returns with income above $232,425. Higher-income individuals can also get hit by the 0.9% additional Medicare tax on wages and self-employment income and the 3.8% Net Investment Income Tax (NIIT), which can both result in a higher-than-advertised marginal federal income tax rate for 2015.

What we've listed below are a few money-saving ideas to get you started that you may want to put in action before the end of 2015:

- For 2015, the standard deduction is $12,600 for married taxpayers filing joint returns. For single taxpayers, the amount is $6,300. If your total itemized deductions each year are normally close to these amounts, you may be able to leverage the benefit of your deductions by bunching deductions, such as charitable contributions and property taxes, in every other year. This allows you to time your itemized deductions so they are high in one year and low in the next. However, the alternative minimum tax (AMT), discussed later in this article, should be considered when using this strategy.
- If you or a family member own traditional IRAs and reached age 70½ this year, consider whether it's better to take the first required minimum distribution in 2015 or by April 1 of next year.


- If your employer offers a flexible spending account arrangement for your out-of-pocket medical or child care expenses, make sure you're maximizing the tax benefits during the upcoming enrollment period for 2016.
- If you have a 401(k) plan at work, it's just about time to tell your company how much you want to set aside on a tax-free basis for next year. Contribute as much as you can stand, especially if your employer makes matching contributions. You give up "free money" when you fail to participate with the maximum amount the company will match.

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- If it looks like you are going to owe income taxes for 2015, consider bumping up the federal income taxes withheld from your paychecks now through the end of the year.
- Between now and year-end, review your securities portfolio for any losers that can be sold before year-end to offset gains you have already recognized this year or to get you to the $3,000 ($1,500 married filing separate) net capital loss that's deductible each year.

*Without a multiyear outlook, you can't be sure maneuvers intended to save taxes on your 2015 return won't backfire and cost additional money in the future.*

- If you own any securities that are all but worthless with little hope of recovery, you might consider selling them before the end of the year so you can capitalize on the loss this year.
- Don't overlook estate planning. For 2015, the unified federal gift and estate tax exemption is a generous $5.43 million, and the federal estate tax rate is a historically reasonable 40%. Even if you already have an estate plan, it may need updating to reflect the current estate and gift tax rules. Also, you may need to make some changes that have nothing to do with taxes.
- If you are self-employed, consider employing your child. Doing so shifts income (which is not subject to the Kiddie tax) from you to your child, who normally is in a lower tax bracket or may avoid tax entirely due to the standard deduction. There can also be payroll tax savings and the ability to contribute to an IRA for the child.
- If you own an interest in a partnership or S corporation that you expect to generate a loss this year, you may want to make a capital contribution (or in the case of an S corporation, loan it additional funds) before year-end to ensure you have sufficient basis to claim a full deduction.

Remember that effective tax planning requires considering at least this year and next year. Without a multiyear outlook, you can't be sure maneuvers intended to save taxes on your 2015 return won't backfire and cost additional money in the future.

And finally, watch out for the AMT in all of your planning because what may be a great move for regular tax purposes may create or increase an AMT problem. There's a good chance you'll be hit with AMT if you deduct a significant amount of state and local taxes, claim multiple dependents, exercise incentive stock options, or recognize a large capital gain this year.

Again, these are just a few suggestions to get you thinking. If you'd like to know more about them or want to discuss other ideas, please feel free to call us. ■

## TAX CALENDAR

**October 15**

- Personal returns that received an automatic six-month extension must be filed today and any tax, interest, and penalties due must be paid.
- Electing large partnerships that received an additional six-month extension must file their Forms 1065-B today.
- If the monthly deposit rule applies, employers must deposit the tax for payments in September for social security, Medicare, withheld income tax, and nonpayroll withholding.

**November 2**

- The third quarter Form 941 (Employer's Quarterly Federal Tax Return) is due today and any undeposited tax must be deposited. (If your tax liability is less than $2,500, you can pay it in full with a timely filed return.) If you deposited the tax for the quarter in full and on time, you have until November 10 to file the return.
- If you have employees, a federal unemployment tax (FUTA) deposit is due if the FUTA liability through September exceeds $500.

**November 16**

- If the monthly deposit rule applies, employers must deposit the tax for payments in October for social security, Medicare, withheld income tax, and nonpayroll withholding.

**December 15**

- Calendar-year corporations must deposit the fourth installment of estimated income tax for 2015.
- If the monthly deposit rule applies, employers must deposit the tax for payments in November for social security, Medicare, withheld income tax, and nonpayroll withholding.

# SHARED EQUITY FINANCING ARRANGEMENTS FOR HOME OWNERSHIP

Adult children may be able to acquire a more expensive home than they might otherwise afford by using a shared equity financing arrangement, under which parents or other relatives share in the purchase and cost of maintaining a house used by the children as a principal residence. The nonresident owner rents his or her portion of the home to the resident owner and obtains the annual tax benefits of renting real estate if the statutory requirements are satisfied. Since the child does not own 100% of the home, he or she is the relative's tenant as to the portion of the home not owned and rents that interest from the relative at a fair market rate.

*One drawback to shared equity arrangements is that the nonresident owners will not qualify for the gain exclusion upon the sale of the residence.*

A shared equity financing arrangement is an agreement by which two or more persons acquire qualified home ownership interests in a dwelling unit and the person (or persons) holding one of the interests is entitled to occupy the dwelling as his or her principal residence, and is required to pay rent to the other person(s) owning qualified ownership interests.

Under the vacation home rules, personal use of the home by a child or other relative of the property's owner is normally attributed to the owner. However, an exception to the general rule exists when the dwelling is rented to a tenant for a fair market rent and serves as the renter's principal residence. When the tenant owns an interest in the property, this exception to the general rule applies only if the rental qualifies as a shared equity financing arrangement.

**Example: Shared equity financing arrangement facilitates child's home ownership.**

Mike and Laura have agreed to help their son, Bob, purchase his first home. The total purchase price is $100,000, consisting of a $20,000 down payment and a mortgage of $80,000. Mike and Laura pay half of the down payment and make half of the mortgage payment pursuant to a shared equity financing agreement with Bob. Bob pays them a fair rental for using 50% of the property, determined when the agreement was entered into.

Under this arrangement, Bob treats the property as his personal residence for tax purposes, deducting his 50% share of the mortgage interest and property taxes. Because his use is not attributed to his parents, Mike and Laura, they treat the property as rental. They must report the rent they receive from Bob, but can deduct their 50% share of the mortgage interest and taxes, the maintenance expenses they pay, and depreciation based on 50% of the property's depreciable basis. If the property generates a tax loss, it is subject to, and its deductibility is limited by, the passive loss rules.

One drawback to shared equity arrangements is that the nonresident owners will not qualify for the gain exclusion upon the sale of the residence. The result will be a taxable gain for the portion of the gain related to the deemed rental. The gain may also be subject to the 3.8% Net Investment Income Tax (NIIT). Parents should consider guaranteeing or co-signing the mortgage, instead of outright joint ownership, if excluding potential future gain is a major consideration.


If it is anticipated that the resident owner will ultimately purchase the equity of the nonresident owner and the rental will generate losses suspended under the passive loss rules, special care must be taken when the lease terms are agreed to because suspended passive losses normally allowed at disposition are not allowed when the interest is sold to a related party. This problem can be minimized by making a larger down payment that decreases mortgage interest expense, or by charging a rent at the higher end of the reasonable range for the value of the interest being rented to the resident owner. ■

## DUE DATE CHANGES FOR PARTNERSHIP AND C CORPORATION RETURNS

On July 31, 2015, the President signed the "Surface Transportation and Veterans Health Care Choice Improvement Act of 2015" (the Highway Act) into law, providing a three-month extension of the general expenditure authority for the Highway Trust Fund (HTF). Part of the HTF extension was paid for by changes to tax compliance provisions, the most significant of which is a change to the longstanding due date for C corporation [Form 1120 (U.S. Corporation Income Tax Return)] and partnership [Form 1065 (U.S. Return of Partnership Income)] returns.

For tax years beginning after 2015, the Highway Act switches the Form 1120 and Form 1065 initial due dates. Thus, beginning with 2016 returns—

- The Form 1065 due date will be accelerated by a month to two and a half months after the close of the partnership's tax year (March 15 for calendar-year partnerships). A six-month extension (through September 15 for calendar-year partnerships) will also be allowed.
- The Form 1120 due date will generally be deferred by a month to three and a half months after the close of the corporation's tax year (April 15 for calendar-year corporations). However, under a special transition rule, for C corporations with fiscal years ending on June 30, the change won't apply (it will continue to be September 15) until tax years beginning after 2025. An automatic six-month extension will generally be allowed. However, until 2026, an automatic five-month extension (to September 15) applies to calendar-year corporations and an automatic seven-month extension (to April 15) applies to June 30 fiscal year corporations.

Note that the filing deadline for S corporations has not changed. So, for years beginning after 2015, S corporations and partnerships will have the same March 15 filing deadlines. Also, for calendar-year entities, the revised deadlines will first apply to 2016 returns filed in 2017. ■