CPA

Client Bulletin

Smart tax, business and planning ideas from your Trusted Business Advisor℠

January 2019

Double (and triple) IRA season is here

The start of each year might be considered "Double IRA" season. Until mid-April (the 15th, in 2019), you still can make contributions to an IRA for 2018, if you have funds you'd like to save for retirement. Most workers and their spouses may each contribute up to $5,500, or $6,500 for those who were 50 or older at the end of 2018.

If you have additional dollars to invest, you also can put them into an IRA for 2019, now that the year has begun. The sooner you put money into a 2019 IRA and choose investments, the sooner tax-advantaged buildup might begin.

Note that such IRA contributions are permitted even if you also participate in an employer's retirement plan. The same is true if you participate in a SEP-IRA or SIMPLE IRA through your company or self-employment.

Three for the money

Many workers can choose among three types of IRAs.

Deductible IRAs. Whereas most workers and their spouses can contribute to regular (traditional) IRAs, only some people can deduct their contributions. A full deduction is available if you do not participate in an employer's retirement plan; if you do participate, the deduction allowed depends on your income.

Example 1: Paula Adams, a single taxpayer who participates in a 401(k), must have had modified adjusted gross income (MAGI) of $63,000 or less in 2018 for a full deduction on her 2018 tax return. If her MAGI is greater than $63,000 but less than $73,000, a partial deduction is allowed.

Different MAGI numbers apply to married taxpayers filing joint returns, qualifying widows or widowers, and married taxpayers filing separate returns.

Contributions to traditional IRAs are not allowed after you reach age 70½.

Roth IRAs. Contributions to Roth IRAs are never tax deductible. However, once you have had a Roth IRA account for five years and reach age 59½, all withdrawals — including withdrawn investment earnings — are untaxed.

There are no age limits for contributions to a Roth IRA. However, income limits apply.

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Jumbo nest eggs

Assets held in IRAs have increased an average of 10 percent per year over the past 25 years, from under $1 trillion in 1993 to more than $9 trillion in 2018.

Trusted advice

Behind the back door

- Suppose a taxpayer with $26,000 of pretax money in a traditional IRA makes a $6,500 nondeductible contribution to a new traditional IRA.
- That brings the IRA total to $32,500, of which $6,500 (20 percent) is after-tax money.
- Then, a Roth IRA conversion of any amount will be 20 percent tax-free and 80 percent taxable, regardless of which IRA is used for the Roth conversion.
- Such back-door Roth conversions may be most appealing to high income taxpayers with little or no pretax money in traditional, SEP, or SIMPLE IRAs.

Example 2: Rick Baker, a single taxpayer, must have had MAGI of $120,000 or less in 2018 for a full contribution to a Roth IRA for 2018. Rick can make a partial contribution if his MAGI is greater than $120,000 but less than $135,000, and no contribution if his MAGI is $135,000 or more.

Different MAGI numbers for Roth IRA contributions apply to married taxpayers filing joint returns, qualifying widows or widowers, and married taxpayers filing separate returns.

Nondeductible traditional IRAs. Some workers and workers' spouses will not be able to deduct contributions to traditional IRAs or contribute to Roth IRAs because of their income.

Example 3: Carol Davis, a single taxpayer who participates in a 401(k), had MAGI of $220,000 in 2018. That puts her over the upper MAGI limits for traditional IRA deductions ($73,000) and Roth IRA contributions ($135,000), mentioned previously. However, as long as Carol was under age 70½ by the end of 2018, she can make a full nondeductible contribution to a traditional IRA. Any earnings within this IRA will not be taxed until money is withdrawn.

Once money is in a traditional IRA, it can be converted to a Roth IRA, in which future distributions may be untaxed. Roth IRA conversions have no income or age limits.

Tax trap

Roth IRA conversions generate tax bills if pretax dollars are moving into an after-tax account. That may not be the case if only after-tax dollars are being converted.

Example 4: Suppose that Carol Davis from example 3 is 55 years old. She contributes $6,500 to a nondeductible traditional IRA for 2018. Carol has no pretax money in any other traditional, SEP, or SIMPLE IRA. If she converts that $6,500 to a Roth IRA, Carol will owe no tax. She will have made what's known as a *back-door Roth IRA contribution* and will get around the income limits. (See **Trusted advice** box.)

Drive cautiously…but carry ample auto insurance

January is a good time to review your insurance coverage. In particular, you should be sure you have adequate auto insurance if you own or lease one or more cars.

Reviewing your current policy might not be simple. You likely will find terms such as *bodily damage liability*, *property damage liability*, *collision*, *comprehensive*, *personal injury protection*, and *underinsured motorist coverage*. Primarily, you should look for substantial liability protection, in case you or a family member is in an accident, and financial coverage for potential damage to your vehicle.

Cover your assets

Liability coverage is designed to pay for expenses relating to personal injury or property damage from an auto accident. Some states might require an auto insurance policy to have a minimum of $25,000 for liability coverage. However, if your policy's liability insurance limit is relatively low, you could, if successfully sued, be liable for any greater damages.

Therefore, you might prefer a policy with bodily injury protection of at least $100,000 per person and $300,000 per accident. You also

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Did you know?

For full coverage ($100,000 for bodily injury/$300,000 per accident/$100,000 property damage, with a $500 deductible), 20-year-olds pay an average of $3,214 a year for auto insurance. That average decreases as drivers gain experience and maturity to $1,363 at age 55. Then, average premiums start to rise, reaching $1,987 at age 85.

Source: carinsurance.com

should consider an excess liability (umbrella) policy to protect you from potentially larger claims.

Damage control

Considering how much it costs to buy or lease a vehicle today, plus the possible cost of repairing any damage, you probably should have collision and comprehensive coverage, as well. The former pays for damages to your own car; the latter may cover theft or non-collision damages, such as repairs after a storm.

One issue here is the deductible amount that you will pay before the insurance takes effect. The higher the deductible you choose, the lower your premiums, but the greater the exposure you will have if you file a claim. Our office can help you evaluate the trade-off between lower premiums and more potential repair costs.

With any type of auto insurance deductible, discounts might be available to drivers with safe records and families with students who have good grades. You also may save money if you use the same company for home insurance as well as your auto insurance.

Be prepared

Having proof of auto insurance coverage whenever you're driving is very important. You should always keep a copy of your insurance card and the contact information of your insurer or agent in the vehicle.

Preparation also can include driving with some way to easily record details of a possible accident. The National Association of Insurance Commissioners has developed WreckCheck, a program designed to guide drivers through the process of documenting relevant details, taking photos, and deciding which personal information to share with others. The accident report that is created can then be emailed to your insurance agent.

IRS says business meal deductions still apply

The Tax Cuts and Jobs Act (TCJA) of 2017 generally disallowed all deductions for business entertainment, amusement, and recreation (see the May 2018 *CPA Client Bulletin*). However, the TCJA did not specifically turn thumbs up or down on the deductibility of business meal expenses.

Example: Jim Morgan, who owns a roof cleaning business, takes a prospect to lunch and pays the $60 bill. Under the old law, Jim could take a $30 (50%) tax deduction.

Is this still the case? In Notice 2018-76, issued in the second half of last year, the IRS clarified that such business meals generally remain 50% tax deductible. Proposed regulations will be published in the future, but business owners can rely on Notice 2018-76 in the interim.

Essentially, this notice confirms that anything that might be considered entertainment won't be a deductible expense. The IRS's list includes night clubs, theaters, country clubs, sports events, and so on. Regular business meals, on the other hand, may still qualify for the 50% deduction.

Five points

Drilling down, the IRS listed five tests that must be passed in order to support the deduction:

1. The expense must be an ordinary and necessary expense, paid or incurred in carrying on a trade or business.
2. The meal can't be considered lavish or extravagant, considering the business context.
3. The taxpayer (or an employee) must be present.
4. The other party must be a current or potential business customer, client, consultant, or similar business contact.
5. In the case of food and beverages provided during or at an entertainment activity, the food and beverages must be purchased separately from the entertainment, or the cost of the food and beverages must be stated separately from the cost of the entertainment on one or more bills, invoices, or receipts and must be priced reasonably.

Example: Carol Clark takes a client to a baseball game, where Carol buys hot dogs and drinks for herself and the client. The cost of the game tickets is not deductible. Carol can deduct 50% of the cost of the food and beverages as long as she can show that these outlays were separate from the ticket cost.

Note that the IRS uses the expression "food and beverages" in this notice. This may imply that the cost of taking a business contact out for coffee or alcoholic drinks may be 50% deductible, even if no meal was served.

It's also worth noting that activities generally perceived to be

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entertainment may be deductible business expenses — if you're in an appropriate business. The IRS gives examples of a professional theater critic attending a play and a garment manufacturer conducting a fashion show for retailers. Our office can let you know if some type of entertainment could be considered deductible advertising or public relations for your company.

Tax calendar

JANUARY 2019

January 15

Individuals. Make a payment of your estimated tax for 2018 if you did not pay your income tax for the year through withholding (or did not pay enough in tax that way). Use Form 1040-ES. This is the final installment date for 2018 estimated tax. However, you don't have to make this payment if you file your 2018 return and pay any tax due by January 31, 2019.

Employers. For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in December 2018 if the monthly rule applies.

January 31

All businesses. Give annual information statements (Forms 1099) to recipients of certain payments you made during 2018. Payments that are covered include (1) compensation for workers who are not considered employees, (2) dividends and other corporate distributions, (3) interest, (4) medical and health care payments, (5) rents, (6) royalties, (7) profit-sharing distributions, (8) retirement plan distributions, (9) original issue discounts, (10) prizes and awards, (11) cash payments for fish to anyone in the trade or business of catching fish, (12) debt cancellations (treated as payment to debtor), (13) payments of Indian gaming profits to tribal members, and (14) cash payments over $10,000. There are different forms for different types of payments.

Individuals who must make estimated tax payments. If you did not pay your last installment of estimated tax by January 15, you may choose (but are not required) to file your income tax return (Form 1040) for 2018 by January 31. Filing your return and paying any tax due by January 31 prevents any penalty for late payment of the last installment.

Employers. Give your employees their copies of Form W-2 for 2018. If an employee agreed to receive Form W-2 electronically, have it posted on a website and notify the employee of the posting.

For nonpayroll taxes, file Form 945 to report income tax withheld for 2018 on all nonpayroll items, such as back-up withholding and withholding on pensions, annuities, and IRAs.

For Social Security, Medicare, and withheld income tax, file Form 941 for the fourth quarter of 2018. Deposit or pay any undeposited tax under the accuracy of deposit rules. If your tax liability is less than $2,500, you can pay it with the return. If you deposited the tax for the quarter in full and on time, you have until February 11 to file the return.

For federal unemployment tax, file Form 940 for 2018. If your undeposited tax is $500 or less, you can either pay it with your return or deposit it. If it is more than $500, you must deposit it. However, if you already deposited the tax for the year in full and on time, you have until February 11 to file the return.

FEBRUARY 2019

February 15

All businesses. Give annual information statements (Forms 1099) to recipients of certain payments you made during 2018. Payments that are covered include (1) amounts paid in real estate transactions,(2) amounts paid in broker and barter exchange transactions, and (3) substitute payments and gross proceeds paid to attorneys.

Employers. For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in January if the monthly rule applies.

Individuals. If you claimed exemption from income tax withholding last year on the Form W-4 you gave your employer, you must file a new Form W-4 to continue your exemption for another year.

February 16

Employers. Begin withholding income tax from the pay of any employee who claimed exemption from withholding in 2018 but did not give you a new Form W-4 to continue the exemption for 2019.

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