GROWERTALKS

Features

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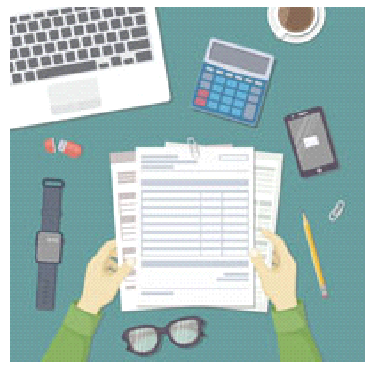
It’s Never Too Late

Mark E. Battersby



Although tax planning should be a year-round strategy, with year-end planning a good backup, even as the tax filing deadline fast approaches, it’s not too late to reap tax savings. The goal of any planning should be to keep the tax bill at a legal minimum, year-after-year, keeping in mind that a business owner’s obligation is to pay their fair share of taxes—not a dollar more.

Don’t overlook depreciation—and alternatives

Consider depreciation, for example, the income tax deduction that allows growers to recover the cost or other basis of property. It’s an annual allowance for the wear and tear, deterioration or obsolescence of business property, such as buildings, machinery, vehicles and equipment. Also depreciable is intangible property, such as patents, copyrights and computer software.

The “extenders” bill passed late in 2015 permanently set the amount of the Section 179, first-year expensing write-off. Expenditures of as much as $500,000 for newly-acquired equipment and business property, with a $2 million overall investment limit, can be “expensed” and immediately written-off rather than depreciated. While there’s no increase in the dollar amount of asset purchases that qualify, thanks to the inflation adjustment, the investment limit for 2016 increased to $2,010,000 before the phase-out begins.

The same extenders bill also extended the 50% “bonus” depreciation write-off for equipment placed in service between 2015 and 2017, with a lower percentage kicking in for an additional two years. That means a write-off of 50% of the purchase price in the first year, plus the regular depreciation rate on the remaining 50%.

Although depreciation can only be claimed for assets placed in service prior to the end of the tax year, claiming or ignoring depreciation write-offs should be given some thought. For instance, while taking the bonus depreciation write-off is the rule, you can elect out for all property within a “class.” Thus, if you purchase five trucks (five-year property) and $65,000 in office furniture (seven-year property), the choice can be made to not take bonus depreciation on the trucks or the furniture, or both, but selecting which trucks to use the election on is a no-no.

Calculating business expense

Just as all income should be reported to keep the tax folks at bay, all of your expenses should be reported in order to keep the tax bill low. That is, the expenses should be claimed unless the rules permit postponing them to a later, more profitable tax year when they might be better used to reduce income.

Rarely is it easy finding and documenting all of your business expenses. Despite the fact that the IRS doesn't usually require receipts for expenditures of less than $75, receipts, records and other documentation can help uncover expenditures and deductions that might otherwise have been overlooked.

Not too surprisingly, some of the most lucrative deductions for small businesses are also some of the most complicated. The home office deduction, for instance, requires compiling multiple expenses and calculating percentages, while the deduction for auto expenses requires extensive recordkeeping that should have begun at the beginning of the year. Other often overlooked, neglected or misunderstood deductions include:

• Repairs: As a general rule, whenever possible, repairs and maintenance expenses should be deducted immediately, rather than capitalized and depreciated. Several changes to the repair guidelines largely ignore the difference between a repair and a capital expenditure with unique "safe harbors."

Small businesses lacking so-called "applicable financial statements" (AFS) can use a new de minimis safe harbor by electing to deduct smaller purchases ($500 or less per purchase or per invoice). Businesses with the required financial statements can deduct as repairs up to $5,000 per purchase or invoice. A small business with gross receipts of $10 million or less can also take advantage of a safe harbor for repairs, maintenance and improvements made to eligible buildings.

• Work Opportunity Tax Credit: Thanks to the tax "extenders" bill, the Work Opportunity Tax Credit has been extended through 2019 for employers hiring members of targeted groups. That same bill also added qualified long-term unemployment recipients to the roster of targeted groups effective January 1, 2016.

• The Domestic Manufacturing Deduction: Confusing, complex and frequently ignored, Section 199 of our tax law—sometimes referred to as the "domestic manufacturing deduction," "U.S. production activities deduction" or "domestic production deduction"—allows even non-traditional "manufacturers" to claim a deduction equal to 9% of income from so-called "qualified production activities."

It's a tax break, pure and simple, that any business with both employees and income from qualified "production" can claim. Naturally, every grower should weigh the benefit of this unique tax deduction against the cost of calculating and supporting it.

• Advertising and promotion: The cost of advertising your goods or services—business cards, yellow page ads and so on—is deductible as a current expense. Promotional costs that create business goodwill, such as sponsoring a pee-wee football team, are also deductible as long as there's a clear connection between the sponsorship and your business.

• Software: As a general rule, software purchased for your business must be depreciated over a 36-month period—with some important exceptions. When, for instance, software comes with a computer and its cost isn't separately stated, it's treated as part of the hardware and is depreciated over five years. However, under Section 179, a whole computer system (including bundled software) can be written off in the first year if the total cost is within the Section 179 annual deduction.

Keeping it real

The way the IRS views "reasonable compensation" has changed significantly over the years. The IRS's goal is to prevent S corporation owners from exploiting a payroll tax loophole. As a result, when the IRS examines the tax returns of an S corporation, the focus is usually on determining whether the compensation paid to the S corporation owner was "reasonable" based on the services provided.

In a number of Revenue Rulings regarding S corporations—the most common entity in the United States today—the IRS and the U.S. Treasury Depart-ment have determined that to the extent the owners of S corporations perform services for their business, the business should pay that owner a reasonable salary as compensation for those services. In addition—and crucially—that reasonable salary is subject to self-employment tax.

Losses and more losses

Casualty and theft losses are deductible if they result from a sudden, unexpected and unusual cause. Of course, a tax deduction for a casualty loss is only allowed in the year of the loss and no deduction can be taken if reimbursement is anticipated. When it comes to theft losses, a deduction can be taken only in the year the theft was discovered.

There are also strict time limits for a business to claim a Net Operating Loss (NOL) carryback, as well as electing to forego the carryback and just carry the loss forward. The typical statute of limitations for filing an NOL tax refund claim is three years from the time the return was filed or two years from the time the tax was paid, whichever period expires later.

Lawmakers also have enacted special rules requiring the claim for a refund to be filed within three years of the date on which the return was actually due (including extensions)—for the taxable year of the net operating loss, which results in the carryback.

Overlooked state and local tax obligations

Don't forget that state and local governments impose their own filing and payment responsibilities with various income, sales and property taxes. Recently, states have become more aggressive in taxing corporations that aren't physically present in their states, but have significant sales to customers in those states. While there may be exceptions for limited business activities in particular states, it's wise to check on your operation's cross-border activities to ensure you're filing all state corporate tax returns as needed.

Extending the pain, if not the payment

Anyone who has tried, but can't, get their taxes prepared by the filing deadline can file a Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return or use an online service. The IRS grants extensions of as much as six months to file taxes. Unfortunately, while the extension provides more time to file your tax returns, it doesn't grant more time to pay the tax bill—or a good estimate of the final tab.

Although taxes should never be the primary reason behind any strategy, purchase or move made by a business owner, taking advantage of our tax rules is important. It's never too late to plan on saving taxes and any grower changing his or her mind after the return is filed can amend or change an already-filed tax return. Remember that in order to achieve a low tax bill either before or after the return is prepared, professional assistance may be required. **GT**

Mark E. Battersby is a freelance writer who specializes in business finance. He can be reached at mebatt12@earthlink.net.