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2018

DMJ & Co., PLLC PRESENTS

# Year-End Tax Planning for Business



CERTIFIED PUBLIC ACCOUNTANTS | BUSINESS CONSULTANTS | WEALTH ADVISORS | HEALTHCARE PRACTICE CONSULTANTS

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**November 28, 2018**

**Dear Clients and Friends:**

The purpose of this letter is to bring business year-end tax information to your attention as the calendar year 2018 draws to a close. Please carefully consider these items, how they may affect your business, and do not hesitate to contact us for further clarification on any of these matters.

First, please note for 2018 business tax returns, our default delivery method remains electronic. Many of our clients already prefer an electronic copy because it is easier to store, secure, and share a copy with banks or other interested parties. Just let us know what email address is good to use for confidential matters, and we will email you a secure link that will allow you to download a PDF copy of your returns. If you prefer to receive a USB with a copy, let us know and we will do that instead. We can also set you up on our portal where a copy will be available. You can, of course, continue to opt for a paper copy.

**One policy note.** *Please return your engagement letter when it arrives in the mail. Our firm policy does not allow us to release your e-filed tax return until we have this signed document.*

**THE TAX CUTS AND JOBS ACT OF 2017**

The Tax Cuts and Jobs Act of 2017 (“TCJA”) made many business tax changes, most effective with 2018 tax returns. A comprehensive discussion of the TCJA is beyond the scope of this memo, but here are a few items to consider which may impact your year-end planning –

- “C” corporation tax rates are reduced to a flat 21% from a graduated system of 15% to 35%. The corporate alternative minimum tax is repealed.
- Other businesses that are taxed to their individual or trust owner are instead eligible for a 20% deduction on qualified business income. This is also known as the Section 199A deduction. A discussion of this is beyond the scope of this memo – please contact us to see how it could apply to you. This deduction expires on 12/31/2025.

- Depreciation –
  - Section 179 expensing maximum is doubled to \$1 million.
  - Section 168(k) “bonus” depreciation is available for 100% of the cost of property acquired, both new and used.
  - The maximum depreciation on autos that are subject to personal use is greatly increased.
  - Many technical details have changed in the depreciation of real property.
- Small business simplification. Certain businesses under \$25 million of gross receipts can stop complying with certain requirements for –
  - Use of the accrual method of accounting.
  - Compliance with section 263A uniform capitalization.
  - Use of the completed contract method of accounting.
- Beginning in 2018, only real estate transactions can qualify for Section 1031 like-kind exchange treatment.
- The deduction for domestic production has been repealed.
- The rules around the use of net operating losses have changed.
- Business entertainment is no longer deductible. If you combine meals and entertainment in your general ledger, you need to separate those items on your accounting records.
- Local lobbying is no longer deductible.

### **PLEASE NOTE THE WAYFAIR COURT DECISION**



If your company is making sales out of state, it is now easier for those other states to force you to collect sales tax on those sales. Many states are beginning the enforcement of this rule in 2018, so this is the ideal time to take a look at whether your company is correctly complying with these rules.

**Action item.** Consult with us soon on whether you have sales tax assessment and withholding requirements for your sales out-of-state.

### **NEW TAX ISSUE FOR PARTNERSHIPS, INCLUDING LLPs and LLCs**

On November 2, 2015, The Bipartisan Budget Act was enacted, making radical changes to the partnership audit rules that, as their primary goal, make it easier for the IRS to audit partnerships and collect tax from those audits. The new partnership audit rules are effective beginning in 2018.



The summary of these rules is that if the IRS audits the partnership for a particular tax year, and finds that additional income should be reported, now the partnership remits the tax on behalf of its partners instead of assessing a number of different partners. This sounds simpler but has many problematic aspects, including (1) what is the appropriate rate to use, (2) what if certain partners have since left and thus are not paying their share of the tax through the partnership, and (3)

what if new partners have been since admitted who would be paying the tax on income from a prior year that they did not receive.

These rules require these entities to address certain new issues, including –

1. Amending your operating agreement to comply with these issues.
2. Designation of a partnership representative (“PR”). This person is denoted on your 2018 tax return, and officially designates who is authorized to speak on behalf of the entity with the IRS, should the IRS contact the entity for an audit or other tax correspondence.
3. Small entities may be able to opt out of these rules with their 2018 tax return. This may or may not be a good idea depending on your situation. Entities that are eligible to opt out are those with 100 or fewer direct or indirect partners, and no partners that are trusts, foreign entities, or other partnerships.

Expect us to ask our partnerships, LLPs, and LLCs, at a minimum, how the prior two items should be addressed in your filing.

**Action item.** Partnerships, general partners, managers, and their partners should consult with their legal counsel, and re-examine existing partnership, LLP, LLC, etc. operating and governance agreements to determine what revisions will need to be made in light of the new partnership audit rules. This includes the process of designating a PR, what actions of the PR are approved by the partnership, how and when is the PR replaced, etc.

## **GENERAL BUSINESS PLANNING CONCEPTS**

 Cash basis businesses that want to defer 2018 income into 2019 should consider sending end of year invoices very late so that customers do not remit their payment until 2019. Also, try to avoid having unpaid bills on hand at the end of the year so as to garner a 2018 deduction. Remember that expenses paid with a credit card are considered paid when charged, even if the credit card bill is outstanding at year end.

Accrual basis businesses that want to defer 2018 income into 2019 should defer providing goods and services until next year. This may or may not be a wise business decision – you will need to decide that for yourself.

However, note that the constructive receipt rules dictate that income is received when you have the right to it – just choosing to not take it does not defer the tax on it.

For additional deductions, consider establishing a retirement plan this year. A 2019 retirement plan contribution for 2018 is deductible in 2018, whether your business reports on the accrual or cash basis, as long as the payment is made by your business tax return deadline, including extensions.

If losses are expected, S corporation business owners should make sure that they have sufficient basis to deduct the losses on their tax return. Please see us for how to increase your basis before year end.

## YEAR-END FORM W-2 REMINDERS

Remember that several year-end adjustments are needed for your W-2 filings. These include the following – contact us if you need assistance in calculating these amounts:

- If you provide a company vehicle to any employee (including company owners), the value of the personal use of the vehicle must be included in the W-2. This is income for federal and state withholding, FICA, Medicare, and federal and state unemployment tax purposes.
- For this and similar non-cash compensation, you obviously cannot withhold tax when there is no cash payment. Therefore, you need to calculate this additional W-2 income before the last payroll of the year so that you can withhold additional tax from the last payroll, if needed.

**Action item.** Include the income from personal auto use in the W-2 of any employee with personal auto use. Get with us and we will be happy to assist you with this calculation.

- If you provide group-term life insurance in excess of \$50,000 to employees, the value of the life insurance in excess of the \$50,000 must be included in the W-2. We can help with this calculation. Note that this should not be taken to read that the employer's payment of the life insurance premium for anyone does not represent taxable compensation. A life insurance plan must meet specific requirements to be considered group-term life.

**Action item.** Include the income from excess group-term life insurance in the W-2 of all employees. We can assist with this calculation.

- For "S" corporations, the amount the company paid for accident and health insurance (including dental, cancer, long-term care, and other policies) must be included in the W-2 of certain shareholders (those owning more-than-2% directly or indirectly of the company, including spouses, children, parents, and grandchildren). The amount paid is taxable for federal and state withholding purposes, but is not taxable for FICA, Medicare, or federal and state unemployment tax purposes.

**Note:** The IRS has stated its intention to disallow the deduction for health insurance for more-than-2% "S" corporation shareholders if the company fails to include this health insurance in the W-2 of the shareholder.

**Action item.** Include the amount paid by the company for health, dental, and long-term care insurance for more-than-2% "S" corporation direct and indirect shareholders in their W-2 for 2018.

- Note that if the business pays for country club dues or similar social clubs for owners or officers and that membership is actually in the name of the individual instead of the business, then this payment is additional compensation and should be included in the W-2. It does not matter that the primary purpose of such use is for business marketing.

## YEAR-END FORM 1099 INFORMATION REPORTING REQUIREMENTS

This requirement includes payments of \$600 or more for –

- Fees and other compensation for services.
- Commissions reduced by any repayment of current year's (but not prior year's) commissions.
- Interest and dividends. If the company pays dividends or is in the business of paying interest, the threshold is reduced to \$10 or more.
- Rents except for those paid to real estate agents. Rent paid by the real estate agent to the landlord is reportable gross (not net) of any commissions retained.
- Taxable prizes and awards paid in the course of business, such as by radio and television broadcasting companies, and incentive awards, such as those given to distributors by manufacturers.
- Fees paid for professional services to attorneys, physicians, and similar service providers.
- Royalties, annuities, pensions, and other gains, profits, and income.

This requirement does not apply to the following types of payments –

- Wages or other compensation reported on Form W-2.
- Payments of any type to corporations other than medical and healthcare payments and attorney fees.
- Payments of bills for merchandise, telephone, freight, storage, and similar charges. This exception does not apply when the merchandise is incidental to the receiving of services, such as auto or copier repairs from unincorporated providers.
- Payments to employees under an "accountable" plan of expense reimbursement.
- Salaries or profits paid or distributed by a partnership to the individual partners.
- Trust or estate payments to beneficiaries.
- Personal (non-business) payments for rent, interest, services, etc.
- Qualified achievement or safety awards of tangible personal property valued at \$400 or less.

Some other rules of note –

- For legal services, all payments of \$600 or more for legal services must be reported, even if the payments are to a corporation. For reporting purposes, it does not matter that the attorney retains only a portion of the payment as his or her fee, but that the payment is made to the attorney.
- Payments which included backup withholding must be reported on a 1099, regardless of the amount.
- Sometimes the structure of the business arrangement makes it difficult to determine when the payment was made. For information reporting purposes, amounts that are credited to, or set aside, for a taxpayer during a calendar year are constructively received and should be reported, although not actually received by the taxpayer. For this rule to apply, there must be no substantial limitation or restriction as to the time or manner of payment, or condition upon which payment is to be made. The amount payable must be available to the taxpayer so that

he may draw it at any time and its receipt brought entirely within his own control and disposition.

- Where a payment is made in property other than money, the fair market value of the property at the time of payment is the amount subject to reporting.
- Direct sales of at least \$5,000 of consumer products sold to a buyer for resale, anywhere other than a permanent retail establishment, must be reported on Form 1099-MISC.
- Note that those who file 250 or more information returns are required to submit these forms electronically. Failure to comply with this requirement brings a significant penalty. We can assist you with this compliance.
- Rental activities that are considered a business should also consider filing Forms 1099. The IRS has said that failure to file Forms 1099 could jeopardize the position that the rental is a business; thus, the net income from this business would be subject to the 3.8% tax on net investment income.

**Action item.** Make sure that your company is in compliance with Form 1099 disclosure requirements. We can assist as needed. If you need our assistance with your 1099 requirements, please let us know no later than January 15.

**Action item.** Consider auditing your vendor files to make sure that you have a signed W-9 on file for each. If you do not, request one now.

**Note:** Penalties for failure to file correct information returns and/or to furnish correct payee statements have increased in recent years and are now subject to inflationary adjustments. There is no limitation on the penalties for intentional disregard to file. Information returns and payee statements include, for example, Forms 1098, 1099, W-2G, and W-2.

## **SETTING UP NEW EMPLOYEES**



Please make sure that your system for onboarding new employees is following the requirements for items that need to be documented from an immigration perspective.

Consider looking over your employee files to make sure that you have a Form I-9 for all workers. Acquire the form where a copy is missing. Also, consider placing a copy of all I-9s in a separate file for easy access in the event of an immigration employment audit.

We are not human resource professionals and you should consider engaging one for HR matters.

## **EMPLOYEES OR INDEPENDENT CONTRACTORS**



It is critical that business owners correctly determine whether the individuals providing services are employees or independent contractors. Generally, you must withhold income taxes, withhold and pay Social Security and Medicare taxes, and pay unemployment tax on wages paid to an employee. You do not generally have to withhold or pay any taxes on payments to independent contractors.

If you classify some of your workers as independent contractors who are actually employees, please note that the government continues to pursue these issues. Your business could be required to pay unpaid payroll taxes, interest, and penalties. Your company could also be obligated to pay for employee benefits that it did not previously provide, as well as federal penalties.

The basic guidance is an “economic realities test.” How much control does your company have over the way workers perform their jobs? For example:

1. Do the workers in question determine how they accomplish their task, or do you closely supervise them?
2. Do they have other clients, or do they work full-time for you?
3. Do they receive payment for each job, or do you pay them on your schedule?
4. Do they own their own equipment and facilities, or does your company provide equipment, supplies, and office space?

These and other considerations are important in determining a worker’s status. If you have any questions, consult with us about the proper classification of your workers to avoid additional taxes and penalties.

## **NEXUS**



Are you sure that you aren’t doing business in new states? Talk with us if this may be the case. Note that states are increasingly aggressive at pursuing out-of-state businesses for sales/use and income taxes. Some indications that you may be doing business in that state include sending salespersons into that state, having payroll, leasing property, buying assets, etc.

**Action item.** Consult with us if you have activity outside of your home state or if you believe that you may have filing exposure in other states.

## **LIFE INSURANCE**



If your business has purchased and owns life insurance on employees, or is considering doing so, note that your business needs to comply with the “Notice and Consent” procedures. Failure to follow these rules can result in a future collection on the insurance policy becoming taxable income. Contact your insurance representative to make sure that this requirement has been addressed.

**Action item.** If the company carries life insurance on any employee, consult with your life insurance agent to make sure that you are in compliance with the “notice and consent” rules.

## **UNCLAIMED (ESCHEAT) PROPERTY**

Unclaimed property consists of tangible and intangible property that has been abandoned, such as bank accounts, wages, refunds, utility deposits, and others. Any business entity in possession of unclaimed property is a potential “holder” of unclaimed property. North Carolina’s Unclaimed Property Law requires all companies and institutions operating in the State to examine their books and other accounting records on an annual basis to determine whether they are in possession of dormant unclaimed property. Once the holder determines the property held is abandoned, a good faith effort must be made to locate the owner. In some instances, a due diligence letter must be sent to the owner. Please note there are specific due dates that must be adhered to with respect to identifying unclaimed property and notifying owners. Holders must file the Unclaimed Property Verification Report (Form ASD-159) and other necessary forms along with any property to the NC Department of State Treasurer. If a business entity asserts it does not hold any unclaimed property, a Negative Report of Unclaimed Property (Form ASD-NEG) may be filed, to run the statute of limitations on unclaimed property reporting for that year.



North Carolina Department of State Treasurer Unclaimed Property Division encourages holders that are not currently in compliance with Unclaimed Property Laws to participate in a Volunteer Disclosure Program (VDP). This VDP allows a holder to conduct a self-examination of their books and records to determine if they hold property which is past due and reportable to North Carolina, and to remit such without being assessed interest or penalties.

Visit <http://www.NCCash.com/Reporting> or contact us for more information to ensure compliance.

**Action item.** Review on an annual basis outstanding checks over a reasonable number of days and attempt to follow up with the payee. Consider remitting and reporting the payments to the State Treasurer if due diligence was not successful. Consider filing a negative report to run the statute of limitations on that reporting period.

## **SOCIAL SECURITY LIMIT FOR 2019**

The Social Security wage maximum for 2019 increased to \$132,900; thus, you will need to make sure that your payroll software settings are adjusted for this limit in 2019.

## **PENSION LIMITS FOR 2019**

Be sure that your payroll systems reflect these amounts; there are some changes from 2018. The 2019 amounts include –

- 401(k) or 403(b) maximum deferral - \$19,000 (an increase of \$500 from 2018, plus additional catch-up of \$6,000 for those who turn age 50 or higher in 2018 and 2019).
- 401(k) maximum contributions from all sources in 2019 is \$56,000 (\$62,000 for those 50 or older). This is an increase of \$1,000 from 2018.
- SIMPLE plans maximum deferral - \$13,000 (an increase of \$500 from 2018, plus additional catch-up of \$3,000 for those age 50 or older).

Consider whether your 401(k) plan should offer a Roth deferral option. For those who defer at the maximum amount, a Roth option allows the individual (economically speaking) to defer an additional amount represented by the tax on their deferral contribution.

Also, a new comparability profit sharing allocation plan can benefit small businesses by allowing owners to reach or approach the \$56,000 total contribution limit (\$62,000 with catch-up) for 2019 with less total required funding than a profit sharing plan that is integrated with social security or uses another allocation formula.

To make this change effective for 2018, your plan document would need to be amended by December 31, 2018. **DMJ Wealth Advisors' Qualified Plan Specialist, W. Brad Mann, JD, QPFC** ([bmann@dmjwa.com](mailto:bmann@dmjwa.com) or **336.275.9886**) can help you analyze whether this makes sense for you.

### **FOREIGN BANK OR INVESTMENT ACCOUNTS**



If you and/or any of your officers have any interest or signatory authority over any non-U.S. bank or investment accounts, please note that certain Treasury Department disclosures are probably required. The IRS has been aggressively auditing taxpayers in this area and penalties for non-compliance are significant. Foreign accounts include bank accounts, hedge funds, brokerage accounts, and other investments. Talk with us if you think that this requirement may apply to you. Please note that the due date is April 15, 2019, with a six-month extension available.

### **TRAVEL PER DIEM RATES FOR 2019**

The standard business mileage rate for 2019 is not available at the time of this letter's publication, to compare to 54.5 cents for 2018. Follow us on twitter, visit our website at [www.dmj.com](http://www.dmj.com), or check with your DMJ tax professional for the latest information on this.

The per diem travel rates for hotels, and meals and incidentals are as follows. These rates actually took effect on October 1, 2018.

The reimbursement rates are:

<b>High Cost Areas</b>	
Lodging	\$216 (unchanged)
• Meals and incidental expenses	\$71 (previously \$68)
• Low cost areas	
Lodging	\$135 (previously \$134)
• Meals and incidental expenses	\$60 (previously \$57)

For NC and adjoining states, the only designated high cost areas are the following:

NC	None
VA	Washington DC metro area (year-round) Virginia Beach (from June 1 to August 31) Wallops Island (from July 1 to August 31)
SC	Charleston (March 1 to October 31)
TN	None

### **REDUCTION IN NC TAX RATES FOR “C” CORPORATIONS**

The State of NC’s corporate tax rate is 3 percent effective for tax years beginning on or after January 1, 2017. The rate drops to 2.5 percent for tax years beginning after January 1, 2019.

### **COMPENSATION PAID TO AN ITIN CONTRACTOR IN NORTH CAROLINA**



If you pay non-wage compensation of more than \$1,500 during the calendar year to an ITIN contractor, you must withhold North Carolina income tax at the rate of 4% from non-wage compensation. An ITIN contractor is a contractor who performs services in North Carolina for compensation other than wages and whose taxpayer identification number is an ITIN number instead of a social security number. An ITIN is issued by the IRS to a person who is required to have a taxpayer identification number, but does not have one and is not eligible to obtain a social security number. The ITIN is a nine-digit number that always begins with the number 9.

### **IDENTITY THEFT**



We also want to ask you to please be careful and protect yourself and your business against the continuing identity theft problem. Identity theft occurs when someone uses your identification information, like your name, Social Security Number, or credit card number without your permission to commit fraud or other crimes. They may acquire this information via entry of your data on unsecure websites, getting insider information from businesses or organizations that may have your personal information, or by tricking you into releasing the information. We are also seeing fraudulent tax filings in the name of legitimate taxpayers in order to seize their tax refunds.

The United States Federal Trade Commission estimates that millions of Americans have their identities stolen each year. Please refer to the FTC web page to learn more on how to protect yourself from identity theft - <http://www.ftc.gov>.

One of the best ways to protect yourself is to use a credit monitoring service. Also consider freezing your credit report.

There are several good credit monitoring services available online that cost about \$200 per year. We think this is a small investment for highly needed protection.

### **DMJ PORTAL IS AVAILABLE & TAX UPDATES**

DMJ has a secure portal available for you to upload the electronic files that you need to send to us. Speak to your DMJ representative if you want to gain access to the portal.

In closing, DMJ is committed to improving our connection with each client. We encourage you to stay in contact and learn more about our services and relevant news by following us at:



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Receive monthly email updates and relevant tax news by joining our mailing list by contacting [contact@dmj.com](mailto:contact@dmj.com)

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Learn more at [www.dmj.com](http://www.dmj.com).

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Sincerely,

*DMJ & Co., PLLC*

Certified Public Accountants

#### **DMJ TRIAD**

Greensboro

703 Green Valley Road, Suite  
201

Greensboro, NC 27408

Phone: 336.275.9886

#### **DMJ SANDHILLS**

Sanford

509 West Main Street  
Sanford, NC 27332

Phone: 919.774.4535

#### **DMJ TRIANGLE**

Durham

3620 Shannon Road, Suite 200  
Durham, NC 27707

Phone: 919.489.3393



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