The
FINANCIAL UPDATE
DAY & ENNIS, LLC
FEE-ONLY FINANCIAL PLANNING

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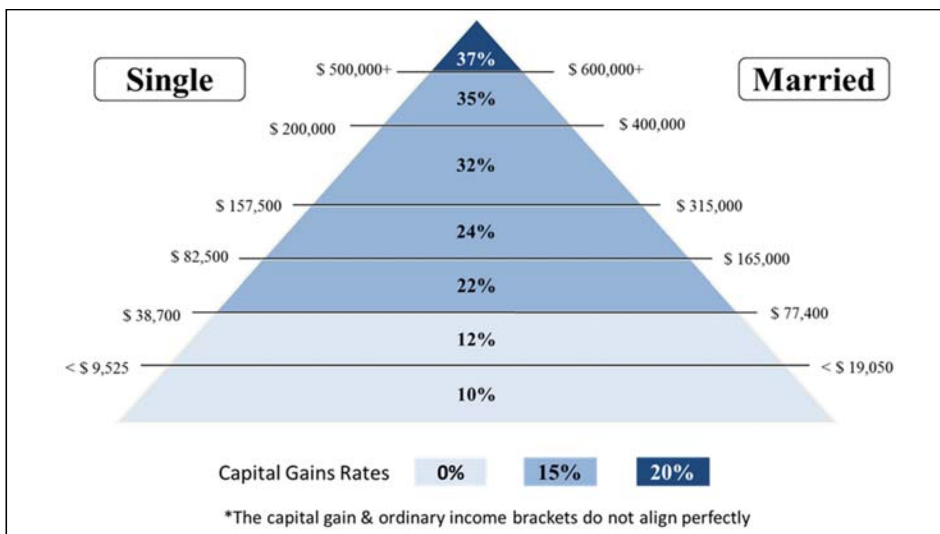
A Timely Tax Tactic For Business Owners

Dentists, doctors, and other business owners can slash their tax bill and funnel huge savings into tax-advantaged retirement vehicles with planning. This is a time-sensitive tax tactic that you might optimally want to implement before the end of this year.



To illustrate how it works, consider a dentist in her peak earnings years, with $500,000 of income. She's married and her children are out of the house. She is in the 35% federal tax bracket, biting deep into her income.

A potent antidote is establishing a federally tax advantaged defined benefit in her practice or joining with her partners in one. Money she salts away into qualified retirement plans is subtracted from her taxable income, reducing her tax bill for this year, and it enables her to manage her tax bracket to optimum advantage.

Defined benefit (DB) plans have been qualified under the federal tax code for special treatment for decades, but they are not nearly as popular as defined contribution (DC) plans.

Because your contribution is defined — but not your retirement benefit — DC plans pose less financial risk to employers and are much more popular with large companies. Guaranteeing a defined benefit on a retirement plan is riskier, so Uncle Sam imposes much higher contributions and more elaborate rules on a DB plan than on a DC plan.

In 2018, the maximum contribution to a DB plan is $220,000 versus $55,000 for a DC plan. If our dentist has a DC plan already but now adds a DB plan, she could reduce her taxable income by as much as $275,000! However, socking away so much would make it impossible to meet her current expenses, so she will need to reduce the

(Continued on page 4)

Will Your Financial Plan Pass A Risk Test?

Evaluating the risk of any financial plan is key to our process at Day & Ennis. We use the BlackRock Aladdin System to test the viability of various plans in designing client portfolios.

This system is relied upon by approximately 25,000 investment professionals around the world. It is powered by more than 1,000 developers who make continuous enhancements, which we pass along to our clients.

It provides us the answers clients need when they ask, "How will inflation affect me?", "What will happen if interest rates keep rising?", "What impact will a change in oil and gas prices have?" These are just a few of the scenarios we can test, but this system allows us to anticipate, interpret and respond to literally hundreds of them.

Managing risk in a portfolio requires proper asset allocation. If adjustments are necessary, the Aladdin System allows us to make them quickly. This gives our clients the confidence they need as we deal with the inevitable stresses that occur in day-to-day portfolio management.

Please feel free to contact us at Day & Ennis if you have any questions about evaluating risk in a changing financial environment.

Sincerely,
Day & Ennis, LLC

The Big New Tax Break For Pre-Retired Professionals

Pre-retired dentists, doctors and lawyers as well as other independent professionals may be able save tens of thousands of dollars in income taxes annually during their peak income years under the new federal tax regulations. The new rules are complex. Here are 10 things pre-retired business owners need to know about qualifying for a 20% reduction in qualified business income under Section 199(A) of the new Internal Revenue Code:

1. Sole proprietors, LLCs, S corps, partnerships and other pass-through entities qualify.

2. Real estate and rental business income — including self-rentals — may qualify.

3. Some businesses are specified as ineligible and you may need a professional to determine if you qualify.

4. Service-business owners could get a deduction on 20% of their income, subject to income limitations.

5. A business owner with $315,000 in taxable income owes tax on only $252,000 — saving more than $12,000 of income tax.

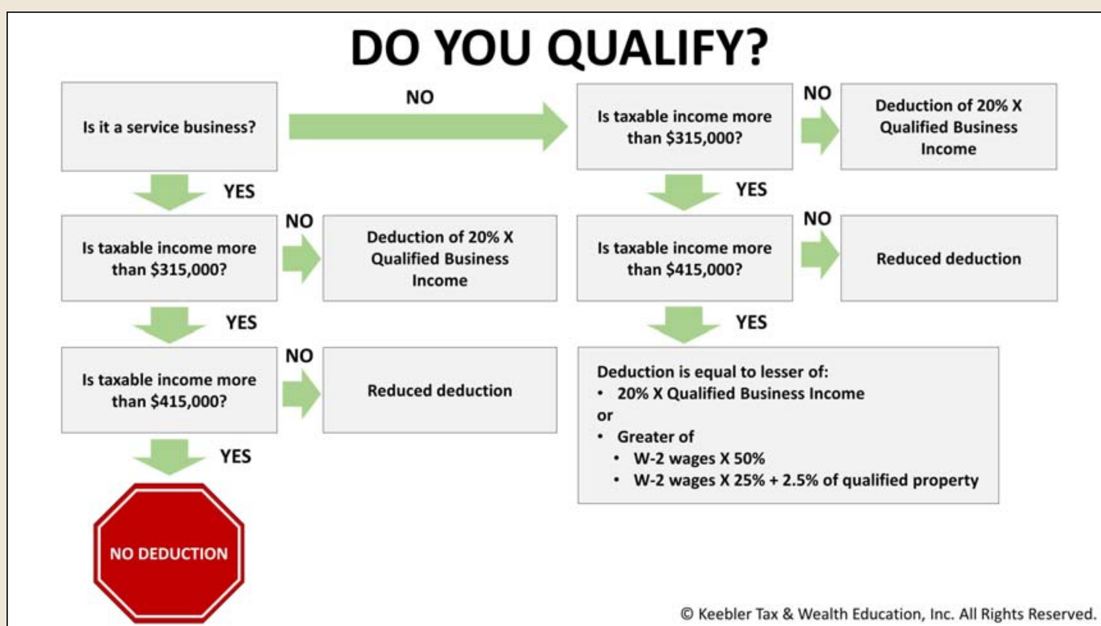
6. If you are married filing jointly and have more than $315,000 of income, the 20% deduction is subject to a phase-out. The phase-out begins at $157,500 for single filers.

7. If you have more than $415,000 of income from the service business, the 20% deduction is eliminated ($207,500 for single filers).

8. To keep your income below these thresholds, consider contributions to a defined benefit (DB) plan.

9. DB plans require you to commit to funding a defined benefit plan instead of a defined contribution plan, making them more complex.

10. A DB plan can supercharge retirement savings while minimizing your taxable income to enable you to qualify for the 20% deduction for business owners. ●



Sidestepping New Limits On Charitable Donations

If you think you're no longer allowed to deduct items like charitable donations on your income tax return, think again.

The new tax law doubled the standard deduction, slashing the number of Americans eligible to itemize deductions from 37 million to 16 million.

However, if you are among those who will lose your ability to deduct charitable donations, there is a simple strategy for managing the new limits on charitable giving, and it enables you to continue doing good while doing well for yourself by reducing your tax bill.

The strategy is simple: bunch a few years of donations into a single tax year instead of making them annually.

Rather than report charitable donations on your tax return every year, you bunch two or more years of contributions into a single tax year — enough to boost the charitable total above that year's standard deduction.

Say you're married and you give $10,000 in Year 1, $6,000 in Year 2 and $10,000 in Year 3. Your $26,000 total surmounts the $24,000 eligibility. If you deduct the total donations of $26,000 in Year 3, you

A Reminder About Harvesting 2018 Tax Losses

Once a year, investors get a chance to lower their tax bill on investments outside of tax-advantaged 401(k) and IRA accounts. It can save thousands annually and is not difficult to do, but it requires the discipline to take the time to gather your records and remember the rules. We're here to help with tax-sensitive investing, and what follows is a reminder about how tax-loss harvesting works.

This maneuver enables you to lower your taxes by realizing investment losses and applying against capital gains or ordinary income. Even though you might not have any gains right now, you can use loss-harvesting in the future for gains or income. Here's how it works:

- Sell an investment valued at less than you paid for it.
- Use that loss to lower capital gains on a profitable investment or deduct up to $3,000 of losses from your income.
- Reinvest in investments that fit into your portfolio and match your strategic goals.

The steps in tax-loss harvesting are:

Picking What to Sell. Review your portfolio and identify what no longer fits. Did that hot stock tip from your brother-in-law not work out? Sell it and use the loss to offset the gain reaped by selling a winning investment.

Favor Short-Term Gains and Losses. Securities bought and sold for a year or less are subject to ordinary income tax rates, which can range as high as 37%, depending on your bracket. But long-term gains (investments held for more than a year) are taxed as capital gains and at a lower rate: 15% for most people and 20% for high-income joint-filers — $425,801 or more for singles, $479,001 or more for couples. IRS rules require you first apply all your short-term losses to offset short-term gains, but any additional short-term can offset long-term gains realized in 2018.

Watch Out for the Wash Sale Rule. This IRS dictum forbids you from taking a tax write-off if you buy the same security, or one "substantially identical," as you sold within 30 days before or after the transaction. One way around that is to substitute a mutual fund or ETF that tracks the industry your stock is in.

Be Aware of Cost Basis. When evaluating what to sell, knowing the cost basis of taxable security is critical. Cost-basis is the price you paid for a security, plus brokerage costs or commissions. If you bought XYZ for a $10 share and sell it for $25, your gain is $15. Monthly and annual brokerage statements show the cost basis.

Choose Your Method. One final complication: You must choose one of two methods for accounting for your security. The "average-cost" method is easiest if you added to a position over time. Then, you cost-basis is determined by averaging the cost per-share of all your purchases. The other method uses the actual cost of each lot of shares purchased, and lets you pick specific, higher-cost lots to sell, which can boost the amount of the loss and can most efficient.

With the longest bull market for stocks in post-War America continuing in 2018, and volatility higher — and outsized gains in large technology stocks — opportunities to harvest losses may be more common than usual this year. This is a reminder of what can be a highly technical and important subject best handled with guidance from a tax and financial planning professional. We are here to answer any questions and help you implement tax-efficient investing strategies. ●

without losing the tax benefits.

And if you can plan to make the larger donations in a year when you expect higher income, bunching charitable donations can be even more effective in lowering your tax bill.

We'll be speaking with clients about this in the months ahead because this tactic does take some planning in advance.

If you have any questions about your personal situation, please do not hesitate to give us a call. ●

can take the standard deduction in Years 1 and 2 and itemize in Year 3.

Instead of giving in dribs and drabs, you will need to plan your giving strategy, but this will allow you to give as much as you used to before the limits

Paying Off A Mortgage And The New Tax Code

Among the most prized tax deductions to get trimmed by the Tax Cut And Jobs Act was the monthly mortgage interest. Should you pay off your mortgage, if your mortgage interest deduction is gone? The answer more often now is "Yes," providing you can afford to retire the debt. If you can't afford that now, aim to do it as soon you can.

Due to a large increase in the standard deduction, fewer taxpayers qualify for the mortgage interest deduction. The standard deduction under the new tax law almost doubled to $12,000 for single filers and $24,000 for married couples. Only people with deductions of more than those amounts can itemize and deduct their mortgage interest.

Piling up that much to itemize, especially for couples, will be difficult. As a result, the Tax Policy Center estimates that only 20 million Americans will itemize in 2018, as opposed to 46 million, had the tax law not changed.

Other changes in the law lessen the benefit of carrying the burden of a mortgage. There's now a $10,000 cap on deductions for state, local and property taxes. Before the law changed, the amount you could deduct was unlimited.

In addition, you are restricted from deducting interest on home equity loans if you use the debt for anything other than buying, building or upgrading a home. If you want to use the home equity loan for a tuition payment or to purchase a boat, Uncle Sam won't allow it anymore.

If you have deductions totaling more than the $12,000 and $24,000 thresholds, you can still itemize. In many cases, you can save more money by erasing your mortgage than you could earn in "risk-free" investments.

Here's the math. Say you have a $300,000 mortgage, which is about the average amount nationally, at a 4% yearly interest rate, and are in the 30% percent marginal tax bracket - 24% federal and 6% state levies combined. If you pay off the mortgage, you no longer have to pay roughly $12,000 annually in interest. When you did pay it, you received a tax deduction worth $3,600 - 30% of the mortgage interest. So that means, after the loan is retired, you saved $8,400. That beats the risk-free Treasury bond return. ●

A Timely Tax Tactic

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amount she contributes while optimizing it for maximum income tax savings.

Our dentist could put $185,000 into the retirement accounts, for instance, just enough to reduce her taxable income to $315,000 and putting her in the 24% tax bracket instead of the 35%.

And because the dentist is a partner in the business, she also qualifies for a 20% deduction under the Sec. 199 (A) of the new tax code for owners of small business that are S corps, LLCs, sole proprietorships, or other pass-through entities. To get this extra tax break, her taxable income must not exceed $315,000 for a married couple ($157,500 for a single).

Twenty percent of $315,000 works out to a deduction of $63,000, placing her taxable income at $252,000, firmly in the middle of the 24% bracket. The taxes are a lot lighter than if she hadn't taken steps to whittle down that half a million in income, and she has socked away a large defined benefit for retirement.

Setting up a defined benefit plan requires expert help and careful planning but is a great tactic to consider this year, especially because of 20% tax deduction. ●

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