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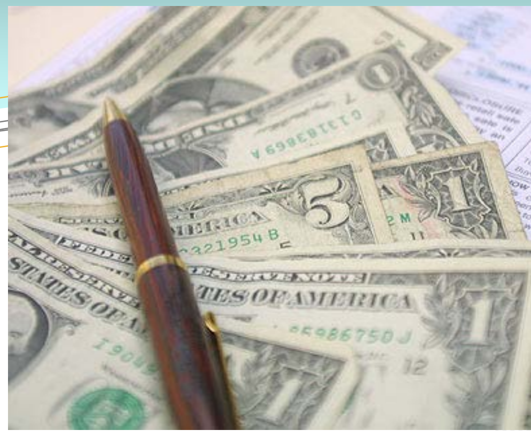
The Successful Dentist™

Dental Tax and Finance

WSDA
WASHINGTON STATE DENTAL ASSOCIATION
PREFERRED



Helping Dentists Make Smart Decisions about Money

Deadlines & Misc.

December 31st is the deadline for:

- All things salary. For incorporated dentists or for spouses working for the practice, 401k or SIMPLE-IRA deferrals must be completed by payroll paid dates ending December 31, 2018. The maximum 401k contribution for 2018 is $18,500 or $24,500 if age 50 or better by year-end. SIMPLE maximum is $12,500 or $15,500.
- December 31st is the last date to pay (or charge on your credit card) deductible expenditures for 2018. See related article on year-end planning.
- December 31st is the last date that certain retirement plans for the 2018 tax year can be initiated. If you maintain a SIMPLE plan and wish to change plans for 2019, December 31st is also the final date to initiate that change.
- December 31st is the last date that you can convert Traditional IRA dollars to a Roth IRA account for 2018.

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A DENTAL GROUP COMPANY

YEAR END TAX PLANNING UNDER THE NEW TAX LAW

Under the Tax Cuts and Jobs Act (TCJA), almost all dentists will benefit from new lower tax brackets. In addition to the savings at your marginal tax bracket you also benefit from all of the reductions in tax brackets below your marginal bracket. For example, a dentist that was in the top 39.6% tax bracket in 2017 may find themselves in the 35% or 37% marginal tax bracket in 2018. The savings is obvious. What is less obvious is that your income is also subjected to each of the tax brackets below your top "marginal" bracket as well. For example; on a joint return the first $19,050 is taxed at 10%, the next $58,350 at 12% and so on. Each of these brackets is lower than its 2017 counterpart.

Perhaps the "biggest" and most talked about new provision that will apply to many dentists is the **QUALIFIED BUSINESS INCOME DEDUCTION (QBID):**

QBID is perhaps the single biggest benefit available in the TCJA for those dentists who qualify. The QBI deduction is up to 20% of the lesser of Qualified Business Income – which includes your dental practice – or taxable income; unless you are phased out by your income level (see below).

The income level is based on your taxable income and the phase out begins at $315,000 for joint returns and $157,500 for single returns. The benefit is phased out completely at taxable income of $415,000 or more ($207,500 single).

Planning Tip: If you are a bit above the phase-out range, or in the phase-out range – your year-end tax deductions can be worth more than usual. An additional dollar of tax deduction will save tax at your marginal tax bracket (as it always has); however, you may also be generating an additional 20 cent (20% of a dollar) deduction under the QBID. If you need help determining where you stand reach out to your DG CPA-Manager or Advisor.

It is time to take action on your year-end planning

Year-end tax planning is a crucial step in managing your tax bill for 2018 and establishing your safe harbor required tax payments or withholding for 2019. Many dentists are aware that by accelerating certain expense payments in December they can lower their current tax bill; however, many dentists are not aware that ***there are two separate and diametrically opposed tax rules that come into play at year-end.***

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One of those rules is the **<u>"placed in service rule"</u>** that applies to dental equipment and other "fixed assets". In general, assets are those items expected to last longer than a year in the practice – such as dental equipment, office furniture and fixtures, etc. and cost more than $500 per unit. To be considered "placed in service" **the item must be delivered and placed into a state of readiness.** It is not required the item actually be used; **<u>rather, just usable.</u>**

Consider Equipment Order Lead Times: With less than a month left in 2018, if you plan to place equipment in service and deduct its cost this year, you will want to consider ordering as soon as possible. Documenting placement in service can be done with an installation receipt or photograph that includes the date (computer, cell phone, etc.).

The opposing rule is related to expenses paid by cash-basis taxpayers; the rule that applies to 99% of dental practices. **Under this rule, the key <u>is</u> when you pay for the item versus when you receive the item or service.**

Tax Deduction – Generally Yes	Tax Deduction – Generally No
▪ Rent (limited to one month)	▪ Fixed Assets (See above)
▪ Supplies (clinical and office)	▪ Debt Principal
▪ Services	▪ Interest Expense (beyond December 31st.)
▪ Small Equip (< $500)	
▪ Laboratory	
▪ Wages	
▪ Utilities	
▪ Other periodic expenditures	

The tax law is not precise in regard to how much and/or how far in advance you can prepay qualified expenses and still take the deduction. It appears that prepaying for a year or less will usually qualify. That said; the Internal Revenue Service does have the potential ability to overturn an overly aggressive prepayment under certain general principals within federal tax law, so there is some unstated tipping point at which your prepayment might be successfully challenged.

In most cases, it is unlikely to make practical sense to prepay more than one to two months' worth of any particular expense. This is due to the cash required to make the prepayment and it may not be financially prudent to prepay a vendor too far in advance since from time to time vendors do go out of business (for example, there is still a caterer running around loose with a $1,000 deposit we made for our 1990 new office open-house). Nonetheless, it is not uncommon for our clients to prepay perhaps $25,000 to $100,000 in December depending on the size of practice, its profit and the degree to which there is fear and loathing regarding payment of federal taxes.

S Corporations and Prepayments: To the extent that you prepay expenses and create a negative cash balance you may or may not be able to utilize the deduction depending on your "tax basis" in the S Corporation. This is a complex topic and you should consult your DG Advisor in advance of year end. If S Corporation basis is a problem, it can be overcome by contributing personal dollars (permanently or temporarily) to the corporation (even if you use a **<u>personal</u>** line of credit to do so). **Note: A line of credit in the name of the corporation will not count toward "basis" but a personal one will.**

Credit Cards and Other Financing of Year-end Expenditures: One way to "finance" year-end prepayments is by utilizing your credit card. The law allows you to charge in December and take the deduction even if you do not pay the credit card bill until January or later. You can also utilize your practice line of credit for this short-term requirement (but see S Corporation above). Borrow the funds in December, write and mail checks by December 31 and then repay the line of credit over the next month or two as the practice cash flow rebounds due to the prepayments made in December. For credit cards, **document the charge as a 2018 expense by using your QuickBooks credit card register to record the charge in 2018** (versus recording a "split transaction" when you pay in 2019). DG

Dentists Who Should Not Defer

Despite the foregoing, there are situations where deferral (acceleration of expenses) is contraindicated. The most common situation might be in the year of purchasing or starting a practice. In these cases the combination of large deductions combined perhaps with low revenue may leave you in a low income tax bracket, whereas future years are expected to bring significantly higher income tax brackets. With current liberal tax incentives available, often an "optimization study" is required to determine just how much deduction to take in the current year versus how much to "save" for future high-bracket years. Planning before the end of the year and then using 20/20 hindsight after the end of the year to engineer the optimum deductions are key tools to optimizing your tax results. DG

Other Year-End Planning for You and Your Practice

QuickBooks: If you are utilizing a version of QuickBooks older than the 2018 version, it is time to update to 2019 (i.e. you should now be running either the 2018 or 2019 version). **Or consider migrating to QuickBooks Online.** Despite an initial learning curve, QBO has many advantages. Three significant ones are: you do not have to worry about updating; you can give your accountant online access (avoiding the sometimes-cumbersome process of uploading and downloading files) and you can access and work on QBO from any location.

You can acquire QuickBooks Pro 2019 at local or online retailers or at www.intuit.com. ($179.95 to $189.95 plus tax and shipping at Amazon). You may find certain retailers with a slightly lower price. DG

MEALS AND ENTERTAINMENT – CHANGES UNDER TCJA:

Entertainment expenditures, which previously were 50% deductible if documented and tied to legitimate business activities. This deduction is now entirely gone – no deduction for entertainment. Maintain an "Entertainment" (only) category in your QuickBooks or other chart of accounts to record any non-deductible entertainment expenses – to make sure these expenses are not mixed-in with partially or fully deductible meals expenses.

Business Meals: The Internal Revenue Service has corrected congress's mistake of eliminating the Business Meal deduction along with Entertainment Expenses. **The "Business Meal" has been reinstated retroactively as 50% deductible** as we thought might happen.

Here is a run-down on how tax-deductible meals are now handled under the TCJA:

Overview of Meals & Entertainment 2018:

	Deductible for 2018 and Forward		
Type of Expense	**100%**	**50%**	**0%**
Meals with clients, prospects, referral sources		X	
Entertain clients, prospects, referral sources			X
Employee meals for the convenience of employer (on site)		X	
Year-end outing/party for employees & spouses	X		
Golf outing for all employees & spouses	X		
Meals for General Public at Marketing Presentation	X		
Team-building event for all employees	X		
Year-end party for customers, clients, referral sources			X
Football game with top referral sources or clients			X

This new "regime" of expense percentages will require an update to your chart of accounts. Employee outings and events should have their own category – and be a sub-category of Staff Expenses and are 100% deductible. On site meals "for the convenience of the employer" should likewise have its own category and are 50% deductible. "Business Meals" should have their own category and are 50% deductible. Finally, Entertainment should have its own category to capture this now, non-deductible expense.

In order for a business meal or other meal expense to be deductible, the expenditure must either be "directly related to" and/or "associated with" the active conduct of your trade or business which includes staff related activities. Simplified, this means that an actual and meaningful business discussion is held during the course of the meal or substantial business was conducted immediately preceding or following. This activity must be clearly associated with the active conduct of your trade or business.

If the meal expense is incurred when traveling away from home **on business** overnight, it is 50% deductible regardless of fitting either of the "directly related to" and/or "associated with" tests.

Optimizing Your Meals and Entertainment Deductions:

- Keep required documentation for all expenditures. In addition to a receipt, you need to note or log the individuals involved, the business purpose and topic in order to sustain your deduction. This can be written right on to the credit card receipt. We recommend that you then scan these documents into an annual archive folder as the physical receipts tend to fade over time. Train your admin staff to help you with this by making sure you have entered the description (who, what and why) and do the scanning for you. Enter the scans chronologically and the receipts will line up nicely with your monthly credit card statements – handy if audited.
- Track fully deductible meals separately from those only 50% deductible (as described above).
- Capture legitimate meals with colleagues, referral sources and advisors.
- Capture 50% of meals brought in to the practice that allow you personally to prepare paperwork or allow you to meet weekly with your office manager or for a staff meeting.

- Capture 100% of meals and entertainment related to staff activities. These can be working activities, such as a retreat or they can be simply celebrations of a job well done. These include for example, holiday events for staff and spouses and/or a summer outing to generate team building and morale.
- Capture legitimate meals with your spouse. For example, document a quarterly meeting to assess the health and progress of the practice **(always better over fine dining and perhaps a nice Merlot)**. With related parties it is always best to document with more detail – for example a short agenda with notes.

Planning Point: Go through your personal receipts that may apply to business, document the meeting (see above) and have your practice reimburse you before December 31 in order to capture this expense.

S Corporation – Auto Expense Reimbursement before January 1st

If you practice in an S Corporation or a C Corporation you must deduct your business use of automobile(s) at the corporate level. If you **have not** run any significant amount of automobile expense through your corporation to date you should be sure to reimburse yourself for business auto miles driven this year. The rate of reimbursement for 2018 is 54.5 cents per mile.

Contact us ASAP for a copy of our "Auto Worksheet Resource" to help you estimate your miles and document your reimbursement. **Note: The reimbursement must be made by December 31st!**

EQUIPMENT & OTHER FIXED ASSET INCENTIVES

There are three limits to be aware of when assessing the Section 179 expensing election: The first is the maximum expense amount (maximum amount you can elect to expense in a given tax year). The second is the maximum amount of Section 179 qualified asset purchases you are allowed in a given year. Over that threshold, the maximum expense amount is phased-out.

The third limitation is the taxable income limitation – you must have business income, including related salary to deduct the expense against. This applies at both the individual level and the entity level. So those practicing in a Partnership or S Corporation may have extra planning to consider.

Item	2018	2019
Section 179 Max Deduction	$1,000,000	$1,000,000+
Threshold (Phase-out start)	$2,000,000	$2,000,000+
Complete Phase Out (no deduction)	$2,500,000	$2,500,000+

Under the TCJA, the Section 179 Expense can be as much as $1,000,000 and is indexed for inflation after 2018. The TCJA also embellished the "First Year Bonus Depreciation" deduction to now cover 100% of new and used equipment costs. Besides being unlimited, Bonus Depreciation is not limited to income as is the Section 179 Expense. DG

HEADS UP: Important "Stuff" Headed to Your Mailbox: During the last two months of the year we will mail a number of very crucial items to you that require your immediate attention. These items will be mailed to you and posted to your secure Dental Group portal.

Help Us Help You!

Included in these mailers are items that, with proper attention, may save you a little or even a lot of money. These include:

1. Self-Employed Health Insurance (S corporations)
2. Fixed Asset Schedules **(update to keep these clean and lower your personal property tax bill)**
3. Automobile use for S Corporations
4. Small Business Health Insurance Credit

By taking the short amount of time to address these mailers you <u>help us to help you</u> save on various taxes – and your prompt reply helps keep our costs down which in turn helps us keep our fees lower than otherwise! *DG*

Other Planning

Credit Balances: Review all credit balances and identify those where the patient does not have scheduled treatment. If the patient has diagnosed but unscheduled treatment – make a phone call to discuss the credit balance and attempt to appoint the patient for treatment "your credit balance overpayment will help you to cover the treatment necessary…" If the patient is not willing to schedule, issue a tax-deductible refund check prior to the end of the year.

Charitable Donations: All cash donations must be evidenced by a "bank receipt" meaning a cleared check or credit card receipt regardless of amount. This means that actual cash can no longer be effectively utilized for donations. Check or credit card donations in excess of $250 **require a contemporaneous written acknowledgment from the charitable organization** containing certain required information <u>including whether or not there was anything of value provided in exchange</u>. A canceled check or credit card receipt alone is not sufficient unless the amount of contribution is less than $250. Be sure to obtain a written receipt from the charitable organization. This rule also applies to non-cash donations.

Non-Cash Donations: As noted above, individual donations of $250 or more will require a contemporaneous written receipt and if aggregate annual non-cash donations exceed $500 you must provide details on the items donated and the registered charitable organizations. Donations of automobiles and other vehicles are now subject to strict valuation rules. **Non-cash donations in excess of $5,000,** other than publicly traded securities require a **<u>formal appraisal</u>**. The $5,000 rule applies to all items of similar nature donated during the year even if donated at different times and/or to different organizations. **Contact us for assistance with significant donations before you make the donation!**

Corporate Use of Personal Residence: Internal Revenue Code Section 280A(g) allows you to rent a primary or secondary (vacation) residence for up to 14 days in a year and not report the income. This provision was established to set a de minimis short-term rental period that would require no recordkeeping or reporting of income.

If your dental practice is incorporated and if you have a valid business purpose for "renting" your home or vacation home – say for a staff retreat or holiday dinner, you may be able to have your corporation pay you personally at the highest justifiable rate – such as equivalent to a fine restaurant or country club. The result would be a tax-deductible expenditure by your corporation and a non-taxable receipt of income by you individually. As with all such "self-dealing", the business purposes must be clear and supportable and you will want solid documentation to this effect and in support of the rental amount.

Cost Segregation: If you are contemplating a remodel or build-out in the near future a proper Cost Segregation Study could save you tens of thousands of dollars. Estimated tax savings (acceleration) on a $250,000 project can be in excess of $50,000. In short, a Cost Segregation Study carves up your contractor's bill into categories that can qualify for 5 or 7-year depreciation deductions versus the default 39-year or 15-year schedule that applies to commercial buildings and their structural components. DG

Mortgage Interest Personal Residence

The TCJA has placed heavier restrictions and limits on mortgage interest deductions; however, if you acquired your mortgage(s) prior to December 15, 2017, you are and will remain "grandfathered" with one exception as follows. Under prior law, a taxpayer could deduct the interest on home acquisition or construction mortgage up to $1,000,000. In addition, the taxpayer could deduct the interest on an additional $100,000 of home mortgage indebtedness – the proceeds of which could be used for any purpose.

The $100,000 of home mortgage indebtedness will also be "grandfathered" and the interest will continue to be deductible if it was used as home acquisition or for building costs. If the funds were used for any other activity, they become non-deductible starting in 2018. Nonetheless, the $1,000,000 rule continues and even applies to refinancing to the extent additional dollars are not extracted.

The new rule effective in 2018 for any home mortgage taken on or after December 15, 2017 limits the tax deduction to the interest on up to $750,000 of home mortgage acquisition or building costs. Consequently, a grandfathered taxpayer will be faced with this lower threshold in the event of selling an existing residence and purchasing a new one. DG

Qualified Charitable Distribution from Individual Retirement Account (IRA) For Those Age 70 ½

Congress has made it fully tax free for a taxpayer age 70 ½ or greater to distribute funds to qualified charities and this distribution still counts toward your annual Required Minimum Distribution (RMD) in the year of the distribution. For those who routinely make gifts to qualified charities and must also take RMD's, this may be a most tax-efficient way to accomplish both goals. Note, the charitable distribution need not be for the full RMD – partial is just fine. DG