Fullerton Tax & Planning

www.fullertontax.com

30S East Avenue, Riverside, IL 60546

Ph: 708-447-5667 / Fax: 708-447-5733

E-Mail: Tfullerton@fullertontax.com

"Real People provide Real Service"

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So, keeping it simple, Valentine's Day is the beginning of Lent this year. Just a small factoid.
The markets are not caring either way. The interest is in rising interest rates and burgeoning debt limits. The combination raises inflation fears, and there goes the markets. It is a little more complex than that. But you have to admit, since we raised interest rates recently and Congress pumped $1.5 trillion debt into the market place, things have moved.

So, here is a strategy that you might want to look at regarding income tax. If you are making less than $157,000 as a single or $315,000 as married filing jointly as a small business owner you may benefit from kinder tax treatment under the new law.

The Tax Cuts and Jobs Act offer a 20 percent deduction for qualified business income from so-called pass-through entities, which include S corporations and limited liability companies.

Under the "old" tax code, income from these small businesses would "pass-through" to the owner on their own taxes and were subject to individual income tax rates as high as 39.6 percent.

Now, entrepreneurs are subject to a tax break on the income their businesses generate, but many of them face a key decision: Is it now time to incorporate — and if so, what entity should you choose?

"Everyone wants to form an LLC," said Sepi Ghiasvand, who is of counsel at Hopkins Carley in Palo Alto, California. "This is a time when an LLC can save you on taxes, but with a caveat."

Here are the things to consider before incorporating your business.

Not a free-for-all

The new tax law's 20 percent deduction on qualified business income is subject to limitations that keep it from being a free-for-all for every entrepreneur.

In general, to qualify for the full deduction, your taxable income must be below $157,500 if you're single or $315,000 if you're married and file jointly.

Filers who are below those thresholds may take the deduction no matter what business they're in, said Jeffrey Levine, a certified public accountant and director of financial planning at BluePrint Wealth Alliance in Garden City, New York.

"We've seen plaintiffs' counsel pierce the corporate veil because business owners treat the corporation as a piggy bank and don't maintain bylaws" -Rick Keller, chairman of First Foundation

However, once taxable income exceeds those thresholds, the law places limits on who can take the break. For instance, entrepreneurs with service businesses — including doctors, lawyers and financial advisors — may not be able to take advantage of the deduction if their income is too high.

Finally, partners in a business may also find themselves in a situation in which one owner gets the 20 percent deduction and the other doesn't. That's because a partner with a high-income spouse may wind up exceeding the taxable income threshold.

"What's fascinating is that you can have two people doing the same work for the same pay, but only one can take the deduction on their return because of other factors," said Levine.

How it works

The 20 percent deduction is considered a "between the lines" deduction in that it doesn't lower your adjusted gross income and you don't have to itemize on your taxes in order to take it.

Generally, if you qualify for the deduction, the 20 percent break will apply to the lesser of your qualified business income or your taxable income minus capital gains. See below for an example from Levine of BluePrint Wealth Alliance.

One Scenario:

Key Facts:
Joint filer with a Schedule C business has a standard deduction of $24,000
Business gross income of $130,000
Business expenses of $30,000
Net profit from business $100,000 (qualified business income)
Spouse works and makes $70,000
Above-the-line deductions of $7,500 for deductible portion of self-employment tax and
$20,000 for SEP IRA contribution

Analysis:
Taxable income before application of pass-through deduction = $118,500

In this case, the taxable income of $118,500 is greater than the qualified business income of $100,000. As a result, the 20 percent pass through deduction will apply to the qualified business income, resulting in a $20,000 deduction.

This couple is in the 22 percent tax bracket, so they save about $4,400 in federal taxes.

LLC formation

One big advantage in establishing an LLC is the fact that it protects owners from having their personal assets seized by the business's creditors.

Setting up your LLC may cost a couple hundred to a couple thousand dollars, and you'll be required to file your documents with the state in which your business is based.

You will have to tell the IRS how it should tax your business, using Form 8832: Is your business a corporation, a partnership or should it be on your personal tax return?

What you choose matters, and here's why.

Entrepreneurs must pay self-employment taxes, which include payments toward Social Security, of 15.3 percent. However, profits that pass through from an S-corp. are subject only to income taxes.

In that case, an owner of an S-corp. would pay the self-employment tax from his salary, instead.

Compliance requirements

In order to maintain their liability protection and preferred tax status, owners of S-corps. (and C-corps.) need to have an operating agreement in place, maintain books and records, and track their minutes.

"We've seen plaintiffs' counsel pierce the corporate veil because business owners treat the corporation as a piggy bank and don't maintain bylaws," said Rick Keller, chairman of First Foundation in Irvine, California.

Consistent profits

Once your business consistently exceeds $70,000 in annual profits after expenses from 1099 income (as opposed to W-2 wages), it might be time to consider setting up an S-corp., according to Howard Samuels, a CPA and managing partner at Samuels & Associates in Florham Park, New Jersey.

That's because S-corps. are subject to bookkeeping requirements: Owners need to file returns for themselves and the business. They also need payroll services to ensure that taxes are correctly deducted.

Owners should weigh how much they will save on taxes with an S-corp. versus how much they will pay to set it up and maintain it.

On the college bound front….

Docs to Prepare for the College-Bound
By: Liz Sinner
Investment News

Even more important than the giant Bed Bath & Beyond order families will send their kids off to college with this year is that advisers make sure clients have prepared three legal documents for children who have turned 18.

Parents should have a durable power of attorney, a medical power of attorney and a HIPAA release for each adult child, advisers and estate attorneys said.

The conversations around obtaining these from 18-year-old daughters and sons can be unsettling, but they can make certain stressful situations much easier.

"It's emotionally gut-wrenching to talk about this, but the alternative is more gut-wrenching," said Ronald Stair, president of Creative Plan Designs.

He tells reluctant clients his personal experience of being unable to get any information about the conditions of his 28-year-old daughter two years ago when she had a heart attack and was in a coma for four hours. The family secured a HIPAA release and medical power of attorney shortly after she regained consciousness. Tragically, they needed to rely on those papers two weeks later when she had a catastrophic heart attack.

"At least I could sign a [do not resuscitate] order, or she might still be in a coma or in a vegetative state," Mr. Stair said.

PERMISSION TO SHARE INFO

A signed Health Insurance Portability and Accountability Act form gives medical professionals permission to share information about their patient. A medical power of attorney, also known as a health-care proxy, allows someone else to make health-care decisions when a person is incapable of doing it themselves.

While obtaining these two documents, parents might as well get the student's general power of attorney, too, Mr. Stair said. That way parents would be able to sign other papers on the student's behalf and have access to financial accounts and other information, such as grades.

Jane Wolk, an estate planning attorney, said once a child is 18, he "is legally a stranger to his parents." Troubles most often arise when students who are away at college are taken to the hospital and then, because they are sick, injured or in surgery, are unable to communicate when parents learn the news and call the hospital.

"That hospital staff is not legally allowed to share with parents or take directions over the phone if parents can't show they have authority," she said.

Ms. Wolk, who has a son heading off to college for the first time in two weeks, recommends that parents keep the original documents in a safe but quickly accessible place at home, and also keep a PDF file of the papers stored digitally for immediate access anywhere. In most cases, hospitals will accept a copy of the documents, she said.

On the market front…
How ETFs and Indexing Took Over Active Management
By: Daniel Kern
Investment Advisor

Index ETFs and mutual funds continue to gain market share at the expense of actively managed funds. According to Morningstar, more than $660 billion was added to index funds (ETFs and mutual funds) during the one-year period ending April 30. Over the same time frame, actively managed funds saw more than $300 billion of outflows. Index funds have captured more than one-third of total long-term fund assets, with an even higher market share within equity investment categories.

The appeal of index funds is understandable, given the comparatively high fees and lagging performance of actively managed funds over the past 15 years. Index funds are typically inexpensive, with annual costs ranging from 0.03% to 0.40% of assets. In comparison, many actively managed funds have annual costs of 0.85% of assets or higher.

In the low-return world expected by most forecasters, these savings can add significantly to accumulated wealth over long time horizons. A recent report from Standard & Poor's shows that in most categories, actively managed funds have lagged their respective benchmarks over five-, 10- and 15-year periods.

ETFs DRIVE INNOVATION

Market cap-weighted index funds include the aggregate holdings in the market, investable with low turnover, high liquidity and capacity. These indexes have the longest history, and still hold the majority of index assets. However, the growth of ETFs and proliferation of smart beta investments has transformed the once-sleepy indexing industry into a major source of financial innovation.

Research is the driving force behind smart beta investments such as fundamentally weighted index and factor-based strategies. Fundamentally weighted indexes screen and weight portfolios based on company-level measure such as sales, cash flow or dividends. They provide broad-based market exposure, but differ from traditional indexes by determining portfolio weights in accordance with measures other than market capitalization.

Factor-based strategies provide a slightly different approach to smart beta investing, emphasizing factors identified in academic research that explain investment return and risk. Factor-based approaches are designed to enhance risk-adjusted returns relative to traditional indexes, most commonly using the following factors:

- Value: "Inexpensive stocks outperform expensive stocks."
- Size: "Small company stocks outperform large company stocks."
- Low volatility: "Less volatile stocks outperform the most highly volatile stocks."
- Quality: "Stocks with high earnings quality outperform stocks with low earnings quality."
- Momentum: "Winning stocks keep winning, losing stocks keep losing."
- High dividend: "Higher income stocks provide superior returns."

BlackRock, the world's largest asset manager and a leading provider of traditional and smart beta funds, projects that smart beta ETF assets will reach $1 trillion by 2020 and $2.4 trillion by 2025.

Index funds may not always be the best solution. Actively managed funds may be compelling in market segments where indexes are more fluid, and today's index may not fully represent tomorrow's opportunities. For example, most emerging markets indexes reflect the past, but some of the most promising opportunities may be in companies benefiting from the growth of the emerging markets consumer. Actively managed funds may also offer risk management benefits, as most fixed income indexes are concentrated in companies or countries that have issued the most debt, potentially creating unintended risks.

Understand the portfolio turnover and tax implications. Traditional index strategies may offer a dramatically different tax experience than certain smart beta strategies, with momentum strategies meriting particular attention. Momentum strategies typically turn over at a rapid rate, potentially creating high tax bills if held in taxable accounts.

Index investments should have a role in investor portfolios, providing a simple, cost-effective and tax sensitive means for gaining exposure to broad segments of the global economy. A diversified portfolio of index funds, selectively supplemented by active funds, is an optimal portfolio approach.

The January Markets did…

The Monthly Index Report for January, 2018

Index	January	QTD	YTD	Description
S&P 500 Index	0.44	0.44	0.44	Large Cap Stocks
Dow Jones Industrial Average	0.81	0.81	0.81	Large Cap Stocks
NASDAQ Composite	2.15	2.15	2.15	Large Cap Tech Stocks
Russell 2000 Growth	-1.74	-1.74	-1.74	Small Cap Growth Stocks
MSCI EAFE	-.35	-.35	-.35	Europe, Australia Emerging Stocks
Barclays Capital U S Aggregate	-1.82	-1.82	-1.82	U S Government Bonds
Barclays Capital High Yield	-.08	-.08	-.08	High Yield Corporate Bonds
3 Month U S Treasury Bills	0.12	0.12	0.12	U S Government Short Term Bonds

Returns as published or estimated through January 31, 2018. Returns reflect reinvestment of distribution.

On the Medicare front…

<u>Medicare Advantage Network</u>

As an alternative to the fee-for-service Original Medicare (with stand-alone Part D for drug coverage and a Medigap plan), one-third of Medicare recipients have chosen Medicare Advantage plans, which have surged in popularity over the past decade.

Available from private insurers, MA plans are simpler to buy and use the Original Medicare premium to cover the entire plan and usually end up costing less, even though their premiums come in addition to Part B premiums instead of replacing them. Most are sold with Part D prescription-drug coverage built in, and many include dental, hearing, and vision coverage, which aren't covered by Original Medicare or Medigap. Although Original Medicare has no cap on annual out-of-pocket expenses (unless you have Medigap), MA plans do limit your maximum exposure. What's not to like?

Here's the catch: If you're on Original Medicare, you can use any care provider that accepts Medicare patients--and most do. MA plans, by contrast, usually require members to use only the providers within a plan's network. The plan picks the doctors, hospitals, and other key health care providers you can see. If your doctor and preferred hospitals are in the network, terrific. If not, you'll pay higher out-of-network fees or full price.

About two-thirds of MA plans are health maintenance organizations, most of which make you get all your services in their networks (except for emergency care and out-of-area urgent care). Your primary physician coordinates your treatment and is the gatekeeper for any referrals you might need. This is generally the cheapest type of MA plan.

Most other MA plans are preferred provider organizations.

The next Republican target: Social Security and Medicare

Trimming entitlements has been a longtime goal

By
Paul Brandus
Columnist

Republicans haven't cared about deficits and the debt for years. When he was vice president, Dick Cheney famously said deficits didn't matter, and for all the criticism about the debt soaring on President Obama's watch, it's important to remember that 1) Congress, not the president, controls the purse strings, and 2) Republicans controlled Congress for the last six of Obama's eight years in office. Their hands are stained in red ink just as much, if not more, than his.

The tax deal that landed on President Trump's desk is more of the same: another $1.5 trillion, probably more, for our kids and grandkids to pay off.

But the GOP's spendthrift ways are about to change and the target for their soon-to-be frugality will be your Social Security and Medicare.

Just ask House Speaker Paul Ryan, who has been salivating at the prospect of whacking entitlements for years. "I think it's important that you do comprehensive health care entitlement reform, other kinds of entitlement reform," he said back in 2011. Nothing was done about it, he claimed, because of then-President Obama. He made a vow: "We plan to step in the breach and provide that kind of leadership by showing the country how we would do things different."

But isn't there another president now, Donald Trump, who also promises to preserve entitlements? "I was the first & only potential GOP candidate to state there will be no cuts to Social Security, Medicare & Medicaid," he tweeted in 2015.

So that's where we are. What happens next?

The three big ways that Social Security can be preserved are 1) raising the retirement age, 2) raising payroll taxes, 3) raising—or eliminating—the cap on taxable wages. The first is a de facto benefit cut because it delays payments; options two and three are outright tax hikes. All three mean pain for voters, so Trump, Ryan, and Senate Majority Leader Mitch McConnell must calculate politically how much they can inflict.

As for Medicare, cuts are looming, thanks to the Senate and House tax reform bills. Here's where it gets a bit complicated. Estimates vary, but there's no question we're talking billions in Medicare cuts, perhaps tens of billions. Both Ryan and McConnell vowed last week to prevent these cuts, saying there are legislative gimmicks (my word, not theirs), they can deploy if necessary. But again, Republicans like Ryan have made no secret of their long-term desire to trim entitlements. Tax bill hints at new GOP tack: Actually it's OK to add to deficits

If Republicans want to move on Social Security, Medicare (and Medicaid), they've got a year to do so; after that, all bets are off.

Meanwhile, Marketwatch posted the stocks for the quarter to watch. The tickers are VIG, VYM, DIA, SPY.
Proceed with caution, but proceed.
See you in a month.

 Timothy T Fullerton, Sr.

Note: The securities listed are subject to market change. The above information is compiled with information from Research Departments of Investors Business Daily, Standard & Poor's, Zacks.com, The Motley Fool, Marketwatch and Bankrate.com. It is not reflective of Fullerton Tax & Planning or FTP Services as a solicitation to buy or sell a specific security. The report is for information purposes only. For further details on any specific listed securities, visit the websites of the research companies listed. Securities offered through Fidelity, UBS, Wayne Hummer, Scottrade, Schwab and ETrade.