MICHAEL SILVER & COMPANY
CERTIFIED PUBLIC ACCOUNTANTS

5750 Old Orchard Rd., Ste. 200, Skokie, IL 60077
Phone: 847.982.0333 **Fax:** 847.982.0219
http://www.msco.net/industries-auto.html

2017 Year-End Planning Checklist for Dealers

As another tax year comes to a close, it is time to consider your tax planning opportunities. With the new GOP tax plan recently revealed indicating potential big changes to be in effect for 2018, tax planning for this year has never been so relevant. As the year begins, it is prudent to consider opportunities that could help lower your tax bill for this year and possibly the next. Though this GOP tax plan is far from being passed, there are a few items to keep in mind as you move through your year-end planning.

Phil Kent, CPA
Audit Partner
PhilK@msco.net
847.213.2113

Judy Mason, CPA, CVA
Tax Partner
JudyM@msco.net
847.213.2075

House GOP Tax Plan Proposal Highlights:

1. Business income from Pass-Through entities such as Partnerships, LLCs, and S Corporations, would be taxed at the maximum 25% rate.
   a. 100% of passive activity income would be subject to the maximum 25% rate. For nonpassive activity income (including wages), 30% of the income would be subject to the 25% rate, and the remaining 70% would be taxed at the ordinary income rate and considered labor income. The bill also keeps the current rules for treatment of self-employment earnings in place.
   b. For certain service professionals (doctor, lawyer, accountant, consultant, financial advisor, and engineer) all income would be taxed at the ordinary income rate.
2. A flat 20% rate would replace the current four tier schedule of corporate rates for C Corporations.
3. Alternative Minimum Tax (AMT) would be repealed for both individuals and businesses.
4. State and local income tax deductions would be eliminated and property tax deductions would be limited to $10,000.

Year-End Planning:

- [ ] **Defer income until 2018.** In light of the potential change in tax brackets with the new GOP tax plan, it could be beneficial if moving into a higher bracket this year can be prevented. It is important to note many other items deductible under current law could also be reduced or eliminated under the new tax plan.

- [ ] **Section 179 expensing limit for 2017 is $500,000 with a $2 million overall investment limit (before phase-out).** Consider placing eligible assets into service before the end of 2017 to take advantage of this expensing limit.

- [ ] **If you plan to make any charitable contributions, consider making them in 2017 to receive a tax deduction.** Payments by credit card are deductible on the day they are made even if the payment to the credit card company occurs on a later date. The IRS requires written acknowledgment for each contribution of $250 or more. Don't forget to document your out-of-pocket expenses included when volunteering for a charity.

- [ ] **Confirm you have made all required personal and corporate income tax deposits for 2017**, and see that your personal income tax withholding is adequate. You should consider paying all of your personal state income tax by the end of the year in order to take a federal income tax deduction for the state tax. The new GOP tax plan has proposed eliminating the Federal deduction for state taxes for years 2018 and beyond, so this could be the last year

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for this deduction. However, you should consult with your tax advisor if you think you may be affected by the Alternative Minimum Tax as that would reduce or eliminate this deduction.

- [ ] **Consider maximizing your retirement contributions,** $54,000 for defined contribution plans. This $54,000 limit includes your employee elected deferrals ($18,000 for 2017). An additional $6,000 catch up deferral is allowed for age 50 or over.

- [ ] **If you or the dealership owns stock that has unrealized losses,** consider discussing with your tax or investment professional the benefit of selling them by year-end to offset realized gains recognized earlier in the year.

- [ ] **Confirm you have substantiation for your 2017 meal and entertainment expenses.** Travel expenses and the cost of a holiday party for employees or food ordered into the dealership for staff should not be included in this amount. This could potentially be the last year for entertainment expense as the GOP tax plan proposes eliminating the deduction for entertainment, but the 50% meals deduction will stay intact.

- [ ] **Accrued interest on loans** from shareholders and other related parties, as well as rents, must be paid in order for the dealership to deduct these amounts in the current year.

Keep the Accounting Records Open at the End of December:

- [ ] **Record December finance chargebacks** in December.

- [ ] **Maximize LIFO deductions.** Record all new vehicles that were <u>built and invoiced</u> in 2017 as vehicle purchases in 2017 by keeping the new vehicle purchase journal open the first few days of 2018.

- [ ] **Keep your accounts payable journal open** to record all 2017 expenses in 2018, including advertising, interest, utilities, telephone, gasoline, data processing, insurance, etc.

- [ ] **Adjust your property tax payable account** to equal at least the total you actually paid in 2017.

- [ ] **If any vehicle deal is not a 100% completed deal** in 2017 (all paperwork and funding in 2017), then treat it as a 2018 vehicle sale.

- [ ] **Make sure all miscellaneous inventories are adjusted to actual,** including labor inventory, sublet, gas-oil-grease, body shop materials, etc.

- [ ] **Distributions paid to S corporation shareholders should be equalized** in accordance to their ownership percentage before year-end.

- [ ] **You must include a reasonable estimate of your LIFO adjustment** for the year on <u>all</u> versions of your December financial statements. <u>**There are no exceptions.**</u> If there is not a separate LIFO cost of sales account, charge the LIFO estimate to cost of sales in a cost account that has no other activity.

- [ ] **Compare your actual parts inventory to the accounting parts inventory** and make adjustments where appropriate. Have your parts manager determine which parts should be considered worthless. Subject to your review, dispose of these parts by year-end.

- [ ] **All wages and commissions paid in 2018 for 2017 services should be accrued in 2017.** Make sure the first payroll in 2018 (even though some portion of the payroll was for 2017 services) is **not** included on your W-2s for 2017, but will instead be on the W-2s for 2018.

    a. All accrued payroll for non-shareholders must be paid no later than March 15, 2018 for it to be deductible in 2017.

    b. If you are a C corporation, make sure you pay any salaries, commissions, or bonuses to stockholders and related parties in December (if their ownership exceeds 50% including related party interests) in order to take a 2017 tax deduction.

    c. If you are an S corporation, wages to a shareholder cannot be accrued and deducted for

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tax purposes. You must pay them in 2017 and include the wages on the 2017 W-2.

- [ ] **Reconcile, where possible, all balance sheet accounts** before closing the year.

Additional Year-End TO DOs:

- [ ] **If you are not on LIFO for used vehicles,** adjust all of your used vehicles to current wholesale market value at year-end. On an annual basis, used vehicle LIFO should be discussed with your tax advisor.

- [ ] **Businesses should consider the "de minimis safe harbor election"** to expense the costs of lower value capital assets, materials, and supplies. Regulations allow businesses to write-off small asset purchases. The safe harbor amount that can be written off is up to $5,000 per item or invoice if you have an audited financial statement and $2,500 if you do not. However, you can set a write-off policy at any level that is material to you. The policy must be in writing.

- [ ] **Review all past due accounts receivables,** including employee receivables. Write-off those receivables that are not collectible.

- [ ] **Review prepaid assets and expense all items** in this account that are not valid as prepaid at year-end.

- [ ] **All payroll tax and sales tax payable accounts must equal the actual amount of the applicable taxes paid** in 2018 for the 2017 fourth quarter and year-end filings. Investigate variances. The year-end payroll tax accrual can only include taxes owed on wages actually paid in 2017.

- [ ] **Compute the December 31, 2017 accrued vacation wages** payable and adjust the books accordingly. Accrued Vacation wages paid January 1, 2018 through March 15, 2018 are deductible in 2017 for tax purposes. No vacation accrual is allowed for any shareholders.

- [ ] **Review bank reconciliations for checks** (including payroll checks over 60 days old) not expected to clear. These checks should be voided and reissued. Funds owed to payees who cannot be located may be considered unclaimed property, which would require you to remit the funds to the appropriate state agency. Before reissuing a check to a vendor, be sure that it has not been paid with a subsequent billing.

Year-End Tax Reporting:

- [ ] **IRS Form 1099-MISC must be issued to all businesses that are not incorporated** (including LLCs) and received $600 or more during 2017 for payment of services, awards, commissions, or fees for services. A Form 1099-MISC must be issued for payments to an attorney even if they are incorporated. When preparing the 1099, for those vendors from whom you purchased parts in conjunction with a service, you must report the total payment made to them on the 1099. Also, Form 1099-MISC must be issued for all rents paid to non-corporate taxpayers, including shareholders, and Form 1099-INT must be issued for interest paid to shareholders and any other individuals. The deadline for filing 1099s is January 31, 2018, for both paper and electronically filed Box 7 non-employee compensation. All other 1099s are due February 28, 2018, if paper filed and April 2, 2018, if electronically filed.

- [ ] **W-2s for S corporation shareholders must include in wages health insurance premiums paid by the corporation.** This amount is not subject to social security or Medicare tax. If the dealership pays the insurance premiums on behalf of the shareholders' children who are employees of the dealership, the children's W-2 must include the insurance premiums.

- [ ] **Under the Affordable Care Act, if you have 50 or more full-time or full-time equivalent employees, you are considered an Applicable Large Employer ("ALE").** ALEs are required to complete Form 1095-C, Employer-Provided Health Insurance Offer and Coverage for all full-time employees. This form details by month the employer health insurance offered to individual employees. The deadline for providing the forms to employees is January 31, 2018. Paper filed

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forms are due to the IRS on February 28, 2018 and electronic forms on April 2, 2018. There are extensions available if requested.

- [ ] **Determine if you are receiving services from individuals who should be considered employees.** The IRS provides a voluntary program that will allow you to convert these individuals prospectively from independent contractors to employees with partial relief from penalties and interest including protection from prior year audits of the converted class of workers. Consult your tax advisor for details.

Review Procedures for the Use of Demonstrators to Ensure You Comply With the Current IRS Regulations:

- [ ] **All individuals who are provided a demo to drive** should sign a written demonstrator agreement.
- [ ] **There are two IRS approved methods that can be used for full-time salespersons.** The first method provides them with tax-free use of the demo. This method is fairly complicated and restrictive. The second method, used by most dealers, is the partial exclusion method. Under this method, an amount is added to wages on a monthly basis. The IRS has provided daily income amounts based on the value of the vehicle. For example, for a vehicle valued at $25,000, the daily inclusion is $6.00. Under this method, employees are not required to maintain logs.
- [ ] **For employees who are not full-time salespersons** and any other individuals who drive demos, the annual lease value method is used. The amount included in income is based on personal-use mileage and the IRS annual lease table. The IRS requires that logs be maintained in order to verify business versus personal use of the vehicle.
- [ ] **The amount included in income is to be added to each employee's W-2.** Non-employee family member income amounts must also be included in the employee's W-2. This income is subject to social security and Medicare tax. Shareholders not on the payroll and any other non-employees must be issued a Form 1099-MISC for the income.
- [ ] **You can obtain more information about the personal use of autos** including sample demonstration agreements by requesting our Dealer Demonstration Guidelines.

Other:

- [ ] **Form 8300 must be filed if you receive cash in excess of $10,000 from a customer.** This includes cashier checks, money orders and traveler's checks except those issued by financial institutions requiring a lien on the vehicle.
- [ ] **If the dealership has a Section 125 plan** (cafeteria plan), make sure eligible employees complete the 2018 election forms before the first 2018 payroll. Remember that stockholders owning more than 2% in S corporations (LLCs, etc.) are not eligible to participate.
- [ ] **If you offer a health care Flexible Spending Arrangement (FSA) as part of your cafeteria plan,** in order for it to be a qualified benefit under a cafeteria plan, the maximum salary reduction contribution to the health care FSA for 2018 is limited to $2,650. Stockholders owning more than 2% in an S corporation or an LLC are not eligible to participate. If your company offers a qualified high deductible health insurance plan, you and employees might be able to contribute to individual Health Savings Accounts (HSAs). Contribution limits for 2018 are $3,450 for an individual and $6,900 for a family with a $1,000 additional contribution for those who are age 55 and over.
- [ ] **If you make gifts to individuals each year for estate tax purposes,** the payments must be made by year-end. You may also be required to file a gift tax return depending on the size of the gift, please consult your tax advisors on further guidance on this.

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