Tax Tips

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Year end tax planning: Consider defined-value gifts

To take advantage of the $5.12 million gift tax exemption, many affluent taxpayers are making substantial gifts before the end of 2012. Absent new legislation, the exemption will drop to $1 million in 2013. Unfortunately, if you wish to gift illiquid assets, such as closely held business interests, you may not have time for an appraisal before year end.

A potential solution is a defined-value gift. Instead of giving heirs a fixed percentage or interest in a business, give them a specific dollar amount. Once the company is valued, interests are allocated according to the defined values you established. Defined-value gifts also protect you against unexpected gift tax liability if the IRS determines the business was undervalued.

Defined-value gifts must be drafted carefully, so consult your CBM tax professional.

Make the most of S corporation losses

Owners of S corporations and other pass-through entities can deduct their pro rata share of entity losses, but only to the extent of their basis. One way to increase basis — and maximize your deductible losses — is to make additional capital contributions.

In a recent case, the U.S. Tax Court held that the shareholders of two related S corporations could receive a distribution of assets (in this case, accounts receivable) from one corporation and then contribute those assets to the other corporation to increase their basis.

Tax Court clarifies age-55 exception to early withdrawal penalty

Ordinarily, taxpayers who receive distributions from qualified retirement plans before age 59½ must pay a 10% penalty in addition to income taxes. There are exceptions to this rule, however, including one for distributions "to an employee after separation from service after attainment of age 55."

In a recent Tax Court case, a participant who retired at age 53 but didn't start receiving distributions until age 55 argued that the 10% penalty didn't apply. The court clarified that to qualify for the exception a participant must reach age 55 on or before separation from service.

Wellness programs: Don't overlook taxes

If your company offers wellness programs, be sure to discuss the potential tax implications with your advisors. Companies that impose a health insurance premium surcharge on participants who smoke, for example, risk excise taxes for violating HIPAA's nondiscrimination provisions if the surcharge is too large.

Also, keep in mind that cash incentives and cash-equivalent rewards (such as gift cards) will likely be considered taxable compensation subject to income and payroll taxes.

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