Tax & Business Alert

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CONSIDER THE FLEXIBILITY OF A SELF-DIRECTED IRA

Traditional and Roth IRAs can be relatively "safe" retirement-savings vehicles, depending on what they're invested in. But a drawback is that they limit your investment choices. A self-directed IRA gives you more flexibility in your investment choices but comes with greater risk as well.

GAINING MORE CONTROL

A self-directed IRA is simply an IRA that gives you greater control over investment decisions. Traditional IRAs typically offer a selection of stocks, bonds and mutual funds. Self-directed IRAs (available at certain financial institutions) offer greater diversification and potentially higher returns by permitting you to select virtually any type of investment, including real estate, closely held stock, limited liability company and partnership interests, loans, precious metals, and commodities (such as lumber and oil and gas).

A self-directed IRA can be a traditional or Roth IRA, a Simplified Employee Pension (SEP) plan, or a Savings Incentive Match Plan for Employees (SIMPLE). It's also possible to have a self-directed individual 401(k) plan, Health Savings Account or Coverdell Education Savings Account.

Self-directed Roth IRAs are particularly powerful estate planning tools, because they offer tax-*free* investment growth. (See "IRAs and your estate plan" on page 2.)

NAVIGATING THE TAX TRAPS

To avoid pitfalls that can lead to unwanted tax consequences, caution is required when using self-directed IRAs. The most dangerous traps are the prohibited transaction rules.

These rules are designed to limit dealings between an IRA and "disqualified persons," including account holders, certain members of account holders' families, businesses controlled by account holders or their families, and certain IRA advisors or service providers. Among other things, disqualified persons may not sell property or lend money to the IRA, buy property from the IRA, provide goods or services to the IRA, guarantee a loan to the IRA, pledge IRA assets as security for a loan, receive compensation from the IRA or personally use IRA assets.

The penalty for engaging in a prohibited transaction is severe: The IRA is disqualified and all its assets are deemed to have been distributed on the first day of the year in which the transaction took place, subject to income taxes and, potentially, penalties.

IRAs AND YOUR ESTATE PLAN

IRAs are designed primarily as retirement-saving tools, but if you don't need the funds for retirement, they can provide a tax-advantaged source of wealth for your family. For example, if you name your spouse as beneficiary, your spouse can roll the funds over into his or her own IRA after you die, enabling the funds to continue growing on a tax-deferred basis (tax-free in the case of a Roth IRA).

If you name a child (or someone other than your spouse) as beneficiary, that person will have to begin taking distributions immediately. But if the funds are held in an "inherited IRA," your beneficiary can stretch the distributions over his or her own life expectancy, maximizing the IRA's tax benefits.

This makes it very difficult to manage a business, real estate or other investments held in a self-directed IRA. So, unless you're prepared to accept a purely passive role with respect to the IRA's assets, this strategy isn't for you.

CONSIDERING THE OPTION

If you have assets such as precious metals, energy or other alternative investments, a self-directed IRA may be worth your while to consider. Contact our firm to discuss further. ■

TAX DOCUMENT RETENTION GUIDELINES FOR SMALL BUSINESSES

You may have breathed a sigh of relief after filing your 2018 income tax return (or requesting an extension). But is your office strewn with reams of paper consisting of years' worth of tax returns, receipts, canceled checks and other financial records? Or perhaps your computer desktop is filled with a multitude of digital tax-related files? You'll find it easier to file next year if you cut down on the clutter. To perform a summer cleanup, follow these retention guidelines.

GENERAL RULES

Retain records that support items shown on your tax return at least until the statute of limitations runs out — generally three years from the due date of the return or the date you filed, whichever is later. That means you can now potentially throw out records for the 2015 tax year if you filed the return for that year by the regular filing deadline. But some records should be kept longer.

For example, there's no statute of limitations if you fail to file a tax return or file a fraudulent one. So, you'll generally want to keep copies of your returns themselves permanently, so you can show that you did file a legitimate return.

Also bear in mind that, if you understate your adjusted gross income by more than 25%, the statute of limitations period is six years.

SOME BUSINESS SPECIFICS

Records substantiating costs and deductions associated with business property are necessary to determine the basis and any gain or loss when the property is sold. According to IRS guidelines, you should keep these for as long as you own the property, plus seven years.

The IRS recommends keeping employee records for three years after an employee has been terminated. In addition, you should maintain records that support employee earnings for at least four years. (This timeframe generally will cover varying state and federal requirements.) Also keep employment tax records for four years from the date the tax was due or the date it was paid, whichever is longer.

For travel and transportation expenses supported by mileage logs and other receipts, keep supporting documents for the three-year statute of limitations period. Regulations for sales tax returns vary by state. Check the rules for the states where you file sales tax returns. Retention periods typically range from three to six years.

WHEN IN DOUBT, DON'T THROW IT OUT

If you're unsure whether you should retain a document, a good rule of thumb is to hold on to it for at least six years or, for property-related records, at least seven years after you dispose of the property. But, again, you should keep tax returns themselves permanently, and other rules or guidelines might apply in certain situations. We can answer any questions you might have. ■

KNOW A TEACHER? TELL 'EM ABOUT THIS TAX BREAK!

When teachers are setting up their classrooms for the new school year, it's common for them to pay for a portion of their classroom supplies out of pocket. A special tax break allows these educators to deduct some of their expenses. This educator expense deduction is especially important now due to some changes under the Tax Cuts and Jobs Act (TCJA).

OLD SCHOOL

Before 2018, employee business expenses were potentially deductible if they were unreimbursed by the employer and ordinary and necessary to the "business" of being an employee. A teacher's out-of-pocket classroom expenses could qualify.

But these expenses had to be claimed as a miscellaneous itemized deduction and were subject to a 2% of adjusted gross income (AGI) floor. This meant employees, including teachers, could enjoy a tax benefit only if they itemized deductions (rather than taking the standard deduction) and only to the extent that all their deductions subject to the floor, combined, exceeded 2% of their AGI.

Now, for 2018 through 2025, the TCJA has suspended miscellaneous itemized deductions subject to the 2% of AGI floor. Fortunately, qualifying educators can still deduct some of their unreimbursed out-of-pocket classroom costs under the educator expense deduction.

NEW SCHOOL

Back in 2002, Congress created the above-the-line educator expense deduction because, for many teachers, the 2% of AGI threshold for the miscellaneous itemized deduction was difficult to meet. An above-the-line deduction is one that's subtracted from your gross income to determine your AGI.

You don't have to itemize to claim an above-the-line deduction. This is especially significant with the

TCJA's near doubling of the standard deduction, which means fewer taxpayers will benefit from itemizing.

Qualifying elementary and secondary school teachers and other eligible educators (such as counselors and principals) can deduct above the line up to $250 of qualified expenses. If you're married filing jointly and both you and your spouse are educators, you can deduct up to $500 of unreimbursed expenses — but not more than $250 each.

Qualified expenses include amounts paid or incurred during the tax year for books, supplies, computer equipment (including related software and services), other equipment and supplementary materials that you use in the classroom. For courses in health and physical education, the costs of supplies are qualified expenses only if related to athletics.

MORE DETAILS

Some additional rules apply to the educator expense deduction. If you're an educator or know one who might be interested in this tax break, please contact us for more details. ■