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Tax $trategies for the 2008 Year End

Part 1

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Dec. 31, 2008, is right around the corner. This date is paramount to cash basis taxpayers, especially the dental profession, where 99% of you file your income tax returns using the cash basis method of accounting. We have found both locally as well as nationally through our affiliation with the Academy of Dental CPAs (www.adcpa.org), that 2008 has been a banner year in terms of profitability within the dental profession. As a result, without adequate tax planning, there will be income taxes due and payable on April 15, 2009. However, you may ask yourself, *isn't there anything I can do to lower my tax bite?* The answer, quite frankly, is *yes!*

Here are some suggestions to consider prior to Dec. 31, 2008.

"Oldies but goodies"

Since your dental practice is probably using the cash basis method of accounting, you could consider delaying your patient billings in Dec. 2008, so that the collections are received in the beginning of Jan. 2009, rather than the end of Dec. 2008. By doing so, you in effect have delayed the "tax cost" on that income for almost 16 months, that being April 15, 2010. Likewise, you can consider accelerating payment of vendor invoices that would normally be due as of Jan. 2009 into Dec. 2008. Some examples of these types of expenditures are dental supplies, lab fees, and rent. If you are on the accrual basis, this will not help you because income is recognized when earned and expenses are recognized when incurred.

There are two major exceptions to the cash basis method of accounting that could also benefit you. The first one to consider is prepaying your vendors on or before Dec. 31, 2008, by using a credit card. In order for these expenditures to be deductible in 2008, they must appear on your 2008 credit card statement, and the goods and/or services must be rendered by the vendor to you or your practice on or before Dec. 31.

The next exception would be the implementation of a retirement plan on or before Dec. 31, 2008. This liability can be accrued for a cash basis taxpayer, which does seem strange, but it is permitted within current tax law. Consider setting up a qualified retirement plan by Dec. 31, 2008, to take advantage of this tax benefit. Please consult with your third party administrator about this tax regulation. Please also see the section below explaining the retirement planning process.

Finally, if you have incurred out-of-pocket expenditures for your practice personally, please have them reimbursed to you by Dec. 31 by your practice.

Equipment

Generally speaking, equipment purchases that will last longer than one year must be capitalized and depreciated over three, five, or even seven years. However, the recent tax law that passed in Feb. 2008 ("The Economic Stimulus Act of 2008") (P.L. 110-185) allows you to immediately expense up to $250,000 in 2008. This is called the Section 179 deduction. However, should total eligible equipment purchases exceed $800,000 during 2008, the $250,000 limit is reduced dollar for dollar in the excess over $800,000. Additionally, there is available a special 50% first-year bonus depreciation available for equipment and "qualified" leasehold improvements purchased that was not subject to your Section 179 immediate expensing election. The Section 179 deduction cannot produce a loss. Any amount not used is carried forward to future years. Please see my article in the September issue of *Dental Economics* which explains this process in greater detail.

Automobiles

If you are in the market for a large sports utility vehicle (such as the Cadillac Escalade or the Ford Expedition), now may be the time to purchase it. First-year depreciation can include a Section 179 deduction up to $25,000, as well as the 50% bonus first-year depreciation and then the regular depreciation on the balance. Assume you purchase a qualifying SUV on Dec. 15, 2008, for $70,000. The potential 2008 write-off is $25,000 (Section 179), $22,500 first-year bonus depreciation, and $1,125 regular depreciation, for a total 2008 deduction of $48,625 (69.5% of the total cost). To qualify for this tax treatment, the SUV must have a gross vehicle weight rating of more than 6,000 pounds and must be built on a truck chassis. It should be noted that the Section 179 deduction claimed on the SUV counts as part of the $250,000 mentioned above. Please keep in mind you must maintain an automobile log in order to support your business use of your vehicle. The examples referred to above assume your business percentage to be 100%.

Automobiles costing at least $14,800 and nonqualifying SUVs purchased in 2008 are limited to first-year depreciation of $10,960, which is made up of first-year depreciation of $2,960 plus bonus depreciation of up to $8,000. If a hybrid vehicle interests you, there may be an income tax credit available depending on how many units the automobile manufacturer has sold. The amount of the credit available varies depending upon the vehicle you choose. It could be as much as $3,000.

Cost segregation

Consider having a cost segregation study performed on your office for the leasehold improvements you have incurred. It analyzes the various components of your office space. As a result of the study, you may be able to depreciate the components classified as personal property much faster than the components classified as real property.

Retirement plans

There are many different types of retirement plans available to choose from. Your particular form of practice may rule out certain choices or make others more desirable. Each type has its own set of advantages and disadvantages. If you are over 50 years old, you should consider a defined benefit plan, because it will allow you to make much greater contributions than a defined contribution plan. Consultation with a competent professional advisor is greatly advised as not all plans are proper in all situations.

If you have a 401(k) plan, consider adding a profit sharing plan or, better yet, a cash balance plan. This plan can greatly increase your retirement plan contributions (see the accompanying chart in the Download Center at **www.dentaleconomics.com**).

If you have a SIMPLE-IRA for 2008, you can contribute up to $10,500 (with an additional $2,500 if you are age 50 or over). If you have not contributed to your SIMPLE-IRA in 2008, consider opening a qualified plan (as mentioned above) instead. If you have contributed to it in 2008, you will need to wait until 2009 to open a qualified plan. Contributions to qualified plans are usually significantly higher than the amount possible with a SIMPLE-IRA.

Contributions to Roth IRAs or Roth 401(k)s are not tax deductible. However, distributions are not taxable once requirements are met — generally, the contributions have been in the plan for at least five years and you are at least 59.5 years of age. The ability to contribute to Roth IRAs begins to phase out when modified adjusted gross income exceeds $160,000 for married filing joint. Traditional IRAs can be converted to Roth IRAs if your income is below $100,000 and you pay tax on the amount being converted.

Employ your family members

If you are self-employed, consider employing your children who are under age 18. Their salary will not be subject to Social Security, Medicare, or federal unemployment taxes. Additionally, many states will classify them as exempt from state unemployment tax. If you employ your spouse, there will be Social Security and Medicare taxes, but not federal unemployment tax. As with your children, your spouse may be exempt from state unemployment tax.

If your practice is a partnership, both parents must be partners to avoid Social Security and Medicare taxation on the children. If your practice is incorporated, there is no exemption from Social Security, Medicare, and federal unemployment taxes and most state unemployment taxes.

Even if payments to your children will be subject to Social Security, Medicare, and federal unemployment taxes, you should still consider employing them. It is very likely that your children will be in a lower tax bracket than you are. Additionally, they can invest their pay in an IRA or college savings plan.

You must be able to substantiate that your children actually provided services to your practice and that the compensation was reasonable should the Internal Revenue Service make an issue of it. Please be sure to set up personnel files on all family members along with a detail of their job responsibilities.

Medical insurance

If you are self-employed, a partner in a partnership, or a more than 2% shareholder in an S Corporation, health insurance paid by the practice is deducted as "self-employed health insurance" and is an adjustment for adjusted gross income on your individual income tax return. If your practice is a regular C Corporation, these expenses are deducted on the corporation's income tax return instead.

If you are considering long-term-care insurance, it may be deductible as well. You may want to consider bringing this type of policy into your practice and making it a fringe benefit for all employees. Consider having your practice purchase a policy for your spouse-employee who elects employee/spouse or family coverage.

You should also consider replacing costly medical insurance with either a Health Savings Account (HSA) or Health Reimbursement Arrangement (HRA). You will probably have a significant savings in medical insurance costs utilizing one of these plans. Please consult with your insurance advisor.

Please be sure to see next month's issue of *Dental Economics* for the completion of this article. DE

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