YEAR-END PLANNING: WHEN C CORPORATIONS SHOULD DEFER OR ACCELERATE INCOME

As the year end approaches, calendar year C corporations, like individuals, should decide when and how to shift income and deductions between 2015 and 2016. Although C corporations will generally benefit from the deferral of income and the acceleration of deductions in the same way as individuals, there are a number of special rules which should be taken into account.

Take, for example, a corporation subject to the 39% "bubble". Corporate taxable income between $100,000 and $335,000 is taxed at the rate of 39% to phase out the benefits of the 15% and 25% brackets which apply to a corporation's first $75,000 of taxable income.

Taxable income between $75,000 and $100,000, and between $335,000 and $10 million, is taxed at 34%. Taxable income over $10 million is taxed at 35%, except there is also a 38% "bubble" which applies to corporate taxable income between $15 million and $18,333,333 to eliminate the benefit of the 34% rate.

> Illustration. Assume a C corporation expects taxable income of about $90,000 for 2015, but expects its income to go well over $100,000 in 2016. Accelerating $10,000 in income from 2016 to 2015 will save about $500 in taxes since the $10,000 will be taxed at only 34% instead of 39% ($10,000 × 5% = $500). This represents a return of 14.7% on the $3,400 used to make the early tax payment ($500 divided by $3,400).
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> Observation: Similar considerations apply to situations where the acceleration of income from 2016 into 2015 will prevent the corporation from moving into other higher tax brackets next year, say from the 15% bracket into the 25% bracket, or from the 35% bracket into the 38% "bubble" which applies to corporate taxable income between $15 million and $18,333,333.

Qualifying for the small corporation AMT exception. The tentative minimum tax of a corporation is zero for any tax year it qualifies as a small corporation meeting a "gross receipts test." To qualify: (i) the corporation's average annual gross receipts for *all* three-tax-year periods beginning after December 31, 1993, and ending before the tax year do not exceed $7.5 million; and (ii) the corporation's average gross receipts do not exceed $5 million for the corporation's *first* three-tax-year period taken into account in (I).

> Illustration. A calendar-year corporation was created on January 1, 2008. To qualify as a small corporation for 2015, (1) the corporation's average gross receipts for the three-tax-year period 2008 through 2010 must be $5 million or less, and (2) the corporation's average gross receipts for the 2009 through 2011 period, the 2010 through 2012 period, the 2011 through 2013 period, and the 2012 through 2014 period must be $7.5 million or less. If the corporation qualifies for 2015, the corporation will qualify for 2016 if its

average gross receipts for the three-tax-year period 2013 through 2015 is also $7.5 million or less. If the corporation does not qualify for 2015, it can't qualify for 2016 or any later year.

Thus, a corporation such as the one in the illustration should consider deferring income to 2016, if necessary, to keep average annual gross receipts for the three-tax-year period 2013 through 2015 at $7.5 million or less. This will preserve the AMT exemption for 2016.

Accelerating or deferring income can save estimated tax break. Corporations (other than certain "large" corporations, see below) can avoid being penalized for underpaying estimated taxes if they pay installments based on 100% of the tax shown on the return for the preceding year. Otherwise, they must pay estimated taxes based on 100% of the *current* year's tax. However, this 100%-of-last-year's-tax safe harbor isn't available unless the corporation filed a return for the preceding year which showed a liability for tax (i.e., a return showing a zero tax liability doesn't satisfy this requirement). Only a return showing a positive tax liability for the preceding year makes the safe harbor available.

Recommendation: A corporation (other than a "large" corporation) anticipating a small net operating loss (NOL) for 2015 and substantial net income in 2016 may find it worthwhile to accelerate just enough of its 2016 income (or to defer just enough of its 2015 deductions) to create a small amount of net income, and thus a small positive tax liability, for 2015. This will permit the corporation to base its 2016 estimated tax installments on the relatively small amount of tax shown on its 2015 return, rather than having to pay estimated taxes based on 100% of its much larger 2016 taxable income. Also, by accelerating a small amount of income from 2016 to 2015, the corporation might be able to take advantage of the lower rates - e.g., 15% instead of 25% or 34%. However, where a 2015 NOL would result in a carryback which would eliminate tax in an earlier year, the value of the carryback should be compared to the cost of having to pay only a small amount of estimated tax for 2016.

Recommendation: Generally speaking, a taxpayer will be treated as a "large" corporation (and won't be eligible for the safe harbor) only if it had taxable income of $1 million or more in any one of the three preceding tax years. As a result, a corporation which didn't reach that threshold in 2013 or 2014 but expects net income of $1 million or more in 2016 and later tax years will have an additional incentive for deferring income into (or accelerating deductions from) 2016. If such a shifting of income or deductions lets the corporation avoid reaching the $1 million threshold in 2015, it will be able to use the 100%-of-last-year's-tax safe harbor in 2016.