Special Edition Newsletter
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INSIGHTS

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Siegfried & Luke, Inc.

2014 Year-End Tax Planning for Individuals

There are many things a taxpayer can do at the end of year to help keep tax bills as low as possible. This is a special edition newsletter that is dedicated to helping clients of Siegfried & Luke build strategies to make smart tax planning choices now that can lead to a reduction in taxed owed later.

Basic Numbers

First, it is important for a taxpayer to know his or her adjusted gross income (AGI) because many tax benefits are tied to or limited by it. Looking at 2013 tax returns and 2014 pay stubs and other income- and deduction-related materials are a good starting point for estimating your AGI.

Another important number is the "tax bracket," the rate at which a taxpayer's last dollar of income is taxed. The tax rates for 2014 have not changed from 2013 and are 10%, 15%, 25%, 28%, 33%, 35% and 39.6%. Although tax brackets are indexed for inflation, if a taxpayer's income increases faster than the inflation adjustment, they may be pushed into a higher bracket. If so, the potential benefit from any tax-saving opportunity is increased (as is the cost of overlooking that opportunity).

Deduction Planning

The timing of deductions is complex because of factors such as AGI levels, AMT, and filling status, but it is an important element of year-end tax planning. The following are important factors to remember for any cash-method taxpayer:

- *Deduction in Year Paid*: Expenses are only deductible in the year in which they are actually paid. Therefore, if a taxpayer anticipates an increased tax rate in 2015, it is smart to postpone deductions until then.
- *Promise to Pay:* A deduction can only be taken on an amount that a taxpayer has promised to pay if money is borrowed from a third party, such as a credit card.
- *AGI Limits:* The overall limitation on itemized deductions ("Pease" limitations) applies for taxpayers whose AGI exceeds $305,050 for married couples or surviving spouse, $152,525 for married and filing single, $279,650 for head of household, and $254,200 for singles. In addition, certain deductions are only allowed if they exceed a certain percentage of AGI.
- *Standard Deduction Planning*: The standard deduction is $12,400 for married filing jointly, $6,200 for married filing separately, $6,200 for singles, and $9,100 for heads of households. In order to maximize the benefits of both standard and itemized deductions, a taxpayer should consider adjusting the timing of deductible expenses so that they stagger between higher and lower every other year.
- *Medical Expenses:* all medical expenses, including the amounts paid as premiums to health insurance are deductible only if they exceed 10% of AGI (7.5% of AGI for taxpayers who are 65+ years old).
- *State Taxes:* A taxpayer who is anticipating state income liability for 2014 should consider making the January payment before the end of 2014. Taxpayers should be cautious of calculating their own estimated payments because an excessive payment could result in being subject to AMT.
- *Charitable Contributions:* Taxpayers should consider making donations at the end of the year for the twofold benefit of being able to use that money during the year and still permitting the taxpayer to claim a deduction for the year. In 2014 it is allowable to donate money via credit, and even if the bill is not paid until 2015, the donation is deductible in 2014. Some other aspects of charitable donations to keep in mind are the following:
  - No deduction is allowed for charitable contributions of clothing and household items if such items are not in good used condition or better.
  - The IRS may deny a deduction for any item with minimal monetary value.
  - The restrictions above do not apply to a contribution that includes a qualified appraisal of any single clothing or household item for which a deduction of $500 or more is claimed.
  - Charitable contributions of money, regardless of the amount, will be denied a deduction unless the donor maintains a cancelled check, bank record, or receipt showing the name of the donee organization, and the date and amount of the contribution.

Retirement Planning

Tax-saving opportunities continue for retirement planning due to the availability of Roth IRAs, changes that make regular IRAs more attractive, and other retirement savings incentives. Keep in mind that employers generally require employees to set their 2015 retirement contribution level before the beginning of the year. Here are some tax-saving opportunities for retirement planning:

Traditional IRAs:

- For individuals who are not active participants in an employer pension plan, the annual deductible contribution limit in 2014 is $5,500 with an additional $1,000 catch-up contribution for taxpayers who are 50+ years old.
- Individuals who are active participants in an employer pension plan also may make deductible contributions to an IRA, but their contributions are limited in amount depending on their AGI. For 2014, the AGI phase-out range for deductibility of IRA contributions is between $60,000 and $70,000 of modified AGI for single persons (including heads of households), and between $96,000 and $116,000 of modified AGI for married filing jointly. Above these ranges, no deduction is allowed.
- In addition, an individual will not be considered an "active participant" in an employer plan simply because the individual's spouse is an active participant for part of a plan year. Thus, a taxpayer may be able to take the full deduction for an IRA contribution regardless of whether their spouse is covered by a plan at work, subject to a phase-out if your joint modified AGI is $181,000 to $191,000 ($0 - $10,000 if married filing separately) for 2014. Above this range, no deduction is allowed.

In 2015 AGI thresholds increase to $61,000-71,000 for singles and heads of households, $98,000-$118,000 for married couples filing jointly where the spouse making the IRA contribution is covered by workplace retirement plans, and $183,000-$193,000 for married couples filing jointly, but the spouse making the contribution is not covered by a workplace retirement plan.

Spousal IRA

- If an individual files a joint return and has less compensation than his or her spouse, the IRA contribution is limited to the lesser of $5,500 for 2014 plus age 50 catch-up contributions, or the total compensation of both spouses reduced by the other spouse's IRA contributions (traditional and Roth).

Roth IRA

- A nondeductible contribution of up to $5,500 is allowed in 2014. The maximum contribution is phased out in 2014 for persons with an AGI above certain amounts: $181,000 to $191,000 for married filing jointly, and $114,000 to $129,000 for single taxpayers (including heads of households); and between $0 and $10,000 for married filing separately who lived with the spouse during the year.
- *Roth IRA Conversion Rule:* Funds in a traditional IRA (including SEP and SIMPLE), §401(a) qualified retirement plan, §403(b) tax-sheltered annuity or §457 government plan may be rolled over into a Roth IRA, however, the amount converted is taxable. In addition, if a taxpayer already made a conversion he or she can undo it, which would be useful if the investment has decreased in value because the taxes would be lower to convert back.

401(k) Contribution:

- The 2014 401(k) elective deferral limit is $17,500. Taxpayers who are 50+years old may contribute an additional $5,500 in catch-up contributions, totaling and maximum contribution of $23,000.

SIMPLE Plan Contribution:

- The 2014 SIMPLE plan deferral limit is $12,000 and catch-up contributors may contribute an additional $2,500.

Catch-Up Contributions for Other Plans:

- Those who are 50+ years old by December 31, 2014 may contribute an additional $5,500 to any §403(b), SEP, or eligible §457 government plan.

In 2015, these amounts increase to $183,000-$193,000 for married couples filing jointly and $116,000-$131,000 for singles and head of household.

Required Minimum Distributions:

- For 2014, taxpayers who reach age 70 ½ must take their required minimum distribution from IRAs or defined contribution plans (§401(k) plans, §403(a) and §403(b) annuity plans, and §457(b) plans that are maintained by a governmental employer).

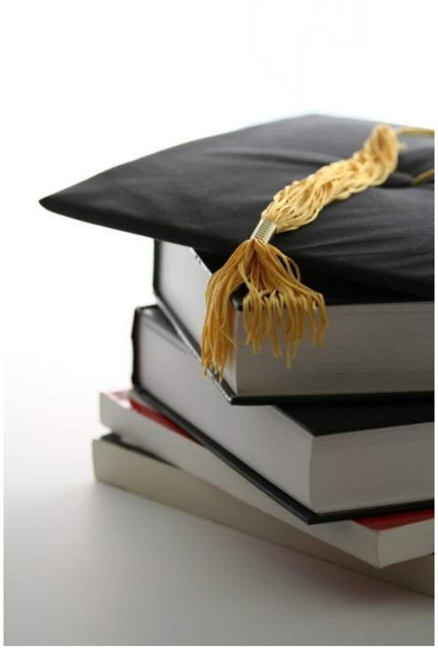
Maximize Retirement Savings:

- In many cases, employers will require employees to set their 2015 retirement contribution levels before January 2015. If you did not elect the maximum 401(k) contribution for 2014, you can increase your amount for the remainder of 2014 to lower your AGI in order to take advantage of some of the tax breaks described above. In addition, maximizing your contribution is generally a good tax-saving move.

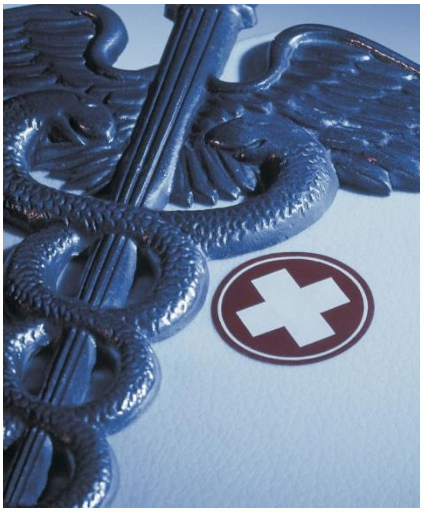
Gift Giving

- *Annual Gift Tax Exclusion*: This is one of the most commonly used methods for tax-free giving. An individual can give up to $14,000 to an unlimited number of donees (family and non-family alike) without reducing his or her estate and lifetime gift exclusion amount. Married donors are able to double that amount of the exclusion to $28,000 per donee. A person may not carry over his or her annual gift tax exclusion amount to the next calendar year. Qualifying tuition payments and medical payments do not count against this limit.

Education & Child Tax Benefits



- *Child Tax Credit*: A tax credit of $1,000 is available for qualifying children under the age of 17. The credit is phased out at a rate of $50 for each $1,000 (or fraction of $1,000) of modified AGI exceeding these amounts: $110,000 for married filing jointly, $55,000 for married filing separately, and $75,000 for all other taxpayers. These amounts are not adjusted for inflation and a portion of the credit may be refundable.
- *Education Credits*: The maximum credit is $2,500 (100% on the first $2,000, plus 25% of the next $2,000) for qualified tuition and fees paid on behalf of a student who is enrolled at least on a half-time basis and in the first four years of post-graduate education. The credit is phased out at modified AGI levels between $160,000-$180,000 for joint filers and $80,000-$90,000 for other taxpayers. 40% of the credit is refundable, which means a taxpayer can receive up to $1,000 even if no taxes are owed.
- *Lifetime Learning Credit*: The 2014 credit maximum is $2,000 (20% of qualified tuition and fees up to $10,000) for any student taking post-secondary classes to acquire or improve job skills. This credit is phased out at modified AGI levels of $108,000-$128,000 for joint filers and $54,000-$64,000 for single filers.
- *Student Loan Interest*: There is an above-the-line deduction for student loan interested paid on qualified education loan at a maximum deduction of $2,500. The deduction is phased out at modified AGI levels of $130,000-$160,000 for joint filers and $65,000-$80,000 for single filers.
- *Kiddie Tax*: For 2014, the kiddie tax applies to qualifying children who have $2,000 of unearned income or more.



Health Care Planning

- *Individual mandate*: Individuals and their dependents must have health insurance that is minimum essential coverage or pay a penalty.
- *Self-Employed Health Insurance Premiums*: Self-employed individuals are allowed to claim 100% of the amount paid during the taxable year for insurance that constitutes medical care for themselves, their spouses and dependents as an above-the-line deduction, without regard to the general 10% of AGI floor.
- *Health Savings Accounts*: A health savings account (HSA) is a trust or custodial account exclusively created for the benefit of the account holder and their spouse and dependents, and is subject to rules similar to those applicable to individual retirement arrangements (IRAs). Contributions to an HSA are deductible, within limits. For 2014, the annual limitation on deductions for an individual with self-only coverage under a high deductible health plan is $3,300; for an individual with family coverage under a high deductible health plan is $6,550. For 2014, a "high deductible health plan" is a health plan with an annual deductible that is not less than $1,250 for self-only coverage or $2,500 for family coverage, and the annual out-of-pocket expenses (deductibles, co-payments, and other amounts, but not premiums) do not exceed $6,350 for self-only coverage or $12,700 for family coverage.

Deferring & Accelerating Income

For taxpayers who expect their AGI to be higher in 2014 than 2015, the tax-saving strategy of deferring income may be a beneficial tactic. However, if the deferred income is subject to §409(a), a nonqualified deferred compensation plan, the amount will be included in gross income and therefore subject to additional tax. Preferred methods to defer income include the following:

- *Delayed billing*: those who are self-employed and use cash-basis should delay year-end billing to clients to ensure that payments are not received until 2015.
- *Interest and Dividends*: taxpayers may consider purchasing short-term bonds or certificates that will not mature until the following year. Interest income that is earned from Treasury securities and bank certificates of deposit with a maturity period of one year or less are not includable as income until received.

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On the other hand, some taxpayer may benefit from accelerating income into 2014 to lower his or her tax bracket in 2015 or to take advantage of an offsetting deduction or credit that will not be available in future tax years. Ways to accomplish accelerating income are the following:

- *Accelerate collection of Accounts Relievable*: Those who are self-employed and use cash-basis should issue bills to clients and attempt to collect money owed before the end of the year. Offering to allow clients to pay for services in advance may also bring more money in before the end of the year.
- *Year-End Bonuses*: A taxpayer may ask his or her employer to receive a bonus before the end of the year.
- *Retirement Plan Contributions*: Taxpayer over the age of 59½ who participate in an employer retirement plan could make a taxable withdrawal before the end of the year. Making a ROTH IRA Conversion as previously mentioned could also potentially increase a taxpayer's current year income.

Alternative Minimum Tax

- For 2014, the alternative minimum tax exemption amounts are: $82,100 for married individuals filing jointly and for surviving spouses; $52,800 for unmarried individuals other than surviving spouses; and $41,050 for married individuals filing a separate return. Also, for 2014, nonrefundable personal credits can offset an individual's regular and alternative minimum tax, and capital gains will be taxed at lower favorable rates for AMT.

- If a taxpayer has a stock holding due to the exercise of an incentive stock option during this year that is now below the value at the exercise date (underwater), consider selling the shares before the end of the year to avoid the AMT tax due on the original exercise of the option.

- Some of the standard year-end planning ideas will not reduce tax liability if a taxpayer is subject to the alternative minimum tax (AMT) because different rules apply. Because of the complexity of the AMT, it would be wise for us to analyze your AMT exposure.

- If you have any questions, please do not hesitate to call. We would be happy to meet with you at your convenience to discuss the strategies outlined in this newsletter. While we are getting very close to the end of the year, there is still time to implement these strategies to minimize your 2014 tax liability. ■

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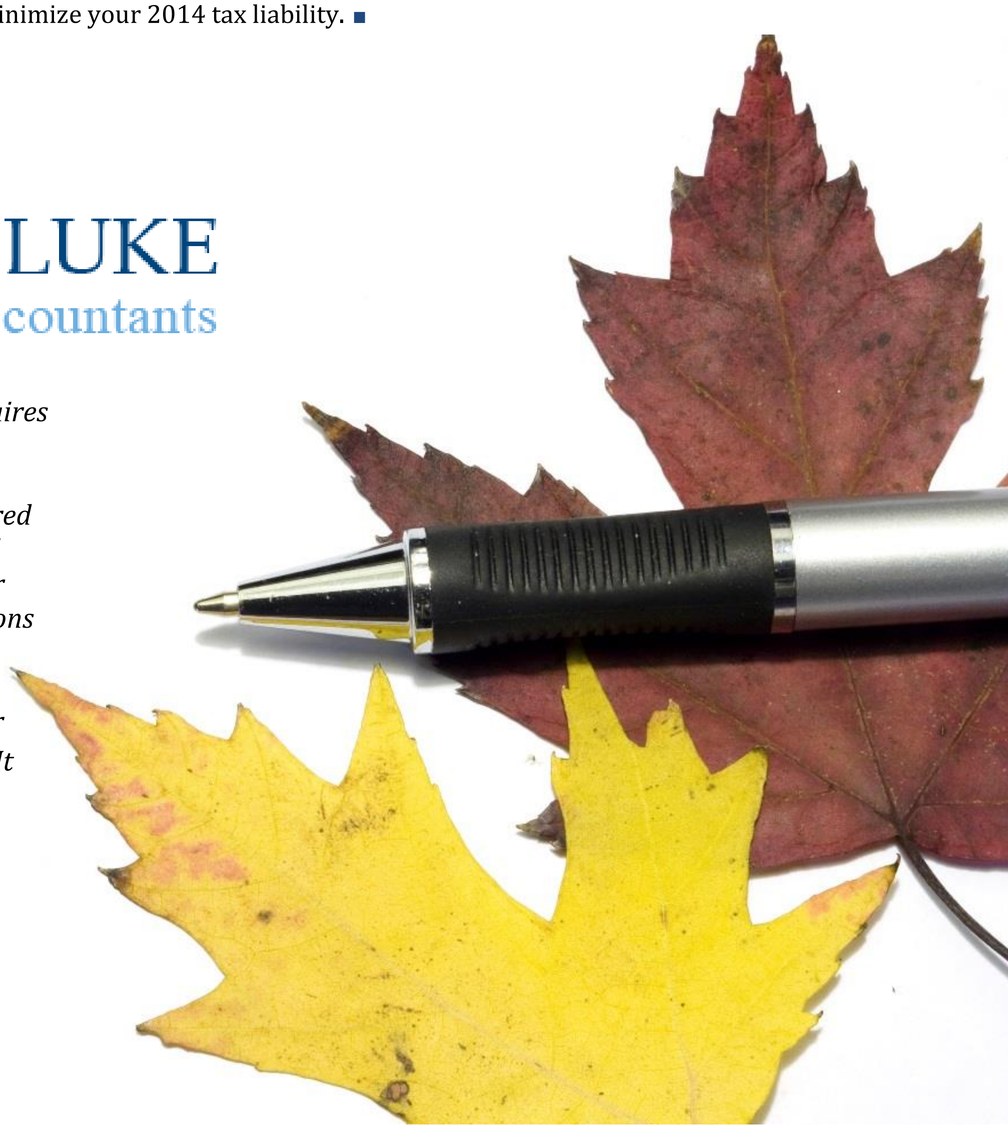
Certified Public Accountants

Every taxpayer's situation is different and requires careful review and analysis.

If you have any questions about any item covered in this newsletter or items that you have heard about but were not covered, please contact our office to schedule a time to discuss your questions in greater detail.



Please contact Siegfried & Luke, Inc. with any questions.