2014 Tax Planning Guide

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RMS Accounting was founded in 1984 to provide business consulting for small and medium-sized businesses. Over the years our firm has grown to fit the needs of our clients. Today we provide complete accounting, bookkeeping, payroll, tax, business consulting, and financial services. With our staff of 16 full-time employees we are large enough to handle all your needs, yet small enough to give you the direct personal attention you deserve. We're here to help you make the right business decisions.

The firm's principals are Steven and Theresa Weil, a husband and wife team. Steven uses his strong background in business operations, marketing, and consulting to assist clients in expanding their profitability. Theresa oversees the accounting and administrative functions of the firm while using her background in banking to assist clients in obtaining financing.

Both principals, have PhDs in Business Administration and are enrolled to practice before the Internal Revenue Service. This enrollment makes them part of a select few who can represent clients in all fifty states before all levels of the Internal Revenue. As Enrolled Agents (EAs), they are highly qualified to assist clients with all tax matters, including tax planning, estate planning, audit representation, and tax preparation.

Tax Planning Guide

Lowering your taxes starts with proper planning, and the sooner you begin, the better. Tax benefits can help you accomplish a wide range of financial goals — saving for a child's education, funding retirement, or growing your business. In order to make the most of your money, take steps to minimize your tax liabilities and take advantage of every available savings opportunity.

As you know, tax laws change often. Congress has passed historic legislation in recent years, providing valuable tax savings to individuals, families, investors, and businesses. But, many of these breaks are temporary.

This easy-to-read brochure is your guide to year-round tax planning. We look at the current tax climate and offer year-end tips for reducing your tax liabilities. Looking ahead, we also suggest tax-efficient strategies for your future. Our goal is to help you make the most of your opportunities. Let's get started.

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The Current Tax Climate

The American Taxpayer Relief Act of 2012 (ATRA), signed into law by President Obama in January 2013, permanently extended certain tax provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) and the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA). Among other changes, it provided a permanent patch for the alternative minimum tax (AMT), and increased the top marginal income tax rate and capital gains and dividends rates on households earning more than $406,750 a year for single filers and $457,600 a year for married filers in 2014. With the implementation of the Affordable Care Act (ACA), starting this year, most individuals who do not carry health insurance will face a penalty.

The 50% bonus depreciation for businesses, which was renewed through 2013, is no longer available for most types of property in 2014. In addition, Section 179 small business expensing, which had increased in 2013 to a $500,000 expensing allowance and a $2 million investment limit, has changed significantly. Pending further legislation, the 2014 limit reverts back to the original deduction amount of $25,000, with a phase-out beginning at $200,000. The Work Opportunity Tax Credit also expired at the end of 2013, and the standard mileage allowance rate has been lowered slightly.

Given the changing nature of tax law, planning is essential in order to take full advantage of the current opportunities. We can help you develop tax-efficient strategies and keep you informed of legislative action that may affect your tax situation now and in the future.

Here are the tax rates and income brackets for 2014:

2014 INDIVIDUAL INCOME TAX RATES*

Regular Tax — Married, Filing Jointly or Surviving Spouse

If Taxable Income Is Between:	Your Tax Is:	Of Amount Over:
$ 0 – $ 18,150	.... 10%	$ 0
$ 18,150 – $ 73,800	$ 1,815 + 15%	$ 18,150
$ 73,800 – $ 148,850	$ 10,162 + 25%	$ 73,800
$ 148,850 – $ 226,850	$ 28,925 + 28%	$ 148,850
$ 226,850 – $ 405,100	$ 50,765 + 33%	$ 226,850
$ 405,100 – $ 457,600	$ 109,587 + 35%	$ 405,100
$ 457,600 and above	$ 127,962 + 39.6%	$ 457,600

Married, Filing Separately

If Taxable Income Is Between:	Your Tax Is:	Of Amount Over:
$ 0 – $ 9,075	.... 10%	$ 0
$ 9,075 – $ 36,900	$ 907 + 15%	$ 9,075
$ 36,900 – $ 74,425	$ 5,081 + 25%	$ 36,900
$ 74,425 – $ 113,425	$ 14,462 + 28%	$ 74,425
$ 113,425 – $ 202,550	$ 25,382 + 33%	$ 113,425
$ 202,550 – $ 228,800	$ 54,793 + 35%	$ 202,550
$ 228,800 and above	$ 63,981 + 39.6%	$ 228,800

Single

If Taxable Income Is Between:	Your Tax Is:	Of Amount Over:
$ 0 – $ 9,075	.... 10%	$ 0
$ 9,075 – $ 36,900	$ 907 + 15%	$ 9,075
$ 36,900 – $ 89,350	$ 5,081 + 25%	$ 36,900
$ 89,350 – $ 186,350	$ 18,193 + 28%	$ 89,350
$ 186,350 – $ 405,100	$ 45,353 + 33%	$ 186,350
$ 405,100 – $ 406,750	$ 117,541 + 35%	$ 405,100
$ 406,750 and above	$ 118,118 + 39.6%	$ 406,750

Head of Household

If Taxable Income Is Between:	Your Tax Is:	Of Amount Over:
$ 0 – $ 12,950	.... 10%	$ 0
$ 12,950 – $ 49,400	$ 1,295 + 15%	$ 12,950
$ 49,400 – $ 127,550	$ 6,762 + 25%	$ 49,400
$ 127,550 – $ 206,600	$ 26,300 + 28%	$ 127,550
$ 206,600 – $ 405,100	$ 48,434 + 33%	$ 206,600
$ 405,100 – $ 432,200	$ 113,939 + 35%	$ 405,100
$ 432,200 and above	$ 123,424 + 39.6%	$ 432,200

2014 Qualified Dividend Income 15%* (0% for lower tax brackets)

*Individuals in the top tax bracket will pay 23.8% (20% plus a 3.8% Medicare surtax).

GETTING STARTED

The trick to effective tax planning is taking advantage of the tax breaks that fit your particular situation. In order to maximize your savings and minimize your taxes, start by planning for both the short and long term. Here are some tips for making the most of your opportunities:

Maximize Your Exemptions — Personal and dependent exemptions are reductions in gross income, in addition to the standard deduction or itemized deductions. Every taxpayer may claim a personal exemption, unless another taxpayer is entitled to claim the exemption. In 2014, each personal exemption claimed reduces your taxable income by $3,950. However, exemptions decrease for taxpayers with adjusted gross incomes (AGIs) exceeding certain thresholds.

2014 AGI Beginning of Phaseout	
Married, Filing Jointly	$305,050
Married, Filing Separately	$152,525
Head of Household	$279,650
Single	$254,200

You may claim exemptions for relatives under the following conditions:

- You pay more than half of their support, and they earn less than $3,950 annually.
- Your children are younger than 19-years-old.
- Your children are full-time students under the age of 24.

If several family members help support a relative but no one person pays more than half, no one may claim the exemption. You may designate one member to pay the majority of support and take the exemption, or you may file a multiple support agreement.

Plan around the Kiddie Tax — While Congress has provided many favorable tax breaks to individuals in recent years, the "kiddie tax" has been expanded. With the most recent reform, unearned income over $2,000 for children under age 18 (age 19 if the child does not provide more than one half his/her own support or age 24 for full-time students) is taxed at

the parents' top rates. In 2014, children will owe no taxes on the first $1,000 of unearned income and will be taxed at their own rate on the next $1,000. Original law applied the kiddie tax to children under age 14. This permitted children 14 and older to file their own returns, allowing their taxable investment income, such as dividends and interest, to be taxed at rates most likely lower than their parents' top rates.

Even with the bump up in age, there are steps you can take to plan around the kiddie tax. Consider shifting your children's investments to tax-free securities, low-dividend growth stocks, or low-turnover mutual funds. A trust may also be an option. Be sure to consult your legal professional for specific guidance.

Health Insurance — The Patient Protection Act, as amended by the Reconciliation Act, will bring a number of changes to the health insurance landscape now and in the coming years. Starting this year, all U.S. citizens and legal residents who are uninsured will be required to obtain health care coverage or pay a tax penalty. Also, starting this year, subsidies will be provided on a sliding scale to individuals with lower to mid-level incomes.

To help raise revenue, a Hospital Insurance tax rate of 0.9% will be assessed on earned income in excess of $200,000 for individuals and $250,000 for married couples filing jointly, as well as a 3.8% Medicare contributions tax on the lesser of net investment income or the excess of modified adjusted gross income (MAGI) over the same threshold amounts. Some trusts and estates will also be liable to pay this 3.8% tax. Starting in 2018, a 40% nondeductible excise tax will be imposed on high-cost, or "Cadillac," health insurance plans.

TAX CREDITS & DEDUCTIONS

Take advantage of every tax credit and deduction available to you. Credits, in particular, are valuable because they provide a dollar-for-dollar reduction of your tax bill.

Child Tax Credit — One of the most popular credits is the child tax credit, which is worth $1,000 for each child under the age of 17. The child tax credit is refundable to the extent of 15% of an individual's earned income in excess of $3,000 in 2014. However, income limits apply; phase-outs start at $75,000 for single filers and $110,000 for joint filers. Other family-related tax credits include the adoption credit, the dependent care credit, and education credits.

ITEMIZED DEDUCTIONS

Itemize your deductions when the total of your allowable deductions exceeds the standard deduction for your filing status: $12,400 for joint filers, $6,200 for singles, $9,100 for heads of household, and $6,200 for those married and filing separately. To lower current tax bills, many taxpayers benefit from deferring income and accelerating deductions, when possible. Let's take a look at some tax-saving deduction ideas.

Bunch Deductions — Try "bunching" your expenses to ensure that you exceed the deduction "floor." Bunching two years' worth of expenses into one year enables you to increase your total deductions over the two-year period and avoid losing the tax benefit from your deductions. However, remember that the AMT may apply if you have numerous deductions.

Pay Estimated State Tax Early — You can gain a larger Federal deduction in 2014 if you pay your state 4th quarter estimated tax payment by December 31st and the AMT does not apply. If you are subject to the AMT, early payment will not be of benefit.

Donate Appreciated Property — If you donate appreciated capital gain property to charity, your deduction amount is generally equivalent to the value of the property, rather than its cost if the organization uses the property to further its exempt purpose. You are never

taxed on the amount of appreciation. For most property donations, an annual deduction limit of 30% of AGI applies.

It is important to note that, for all charitable donations, you must obtain a bank record or *written* acknowledgment from the recipient charity that specifies the amount and date of contribution, as well as the name of the charity. For property, the acknowledgment must describe the gift and indicate an estimated valuation. Be aware that special rules may apply if you donate an automobile to charity.

Optimize Investment Interest Expense — If you have capital gains or dividend income, as well as investment interest expenses, we can help you calculate the breakeven point to optimize both the lower capital gain and dividend tax rates and the investment interest deduction.

Understand the Tax Aspects of Divorce —

- Legal fees for divorce may be deductible by the party seeking taxable income, such as alimony, or property giving rise to taxable income, such as a business interest. To support the deduction, be sure to obtain these details on separate invoices.

- Divorcing couples may want to consider having child support payments reclassified as alimony. Child support is not included on the recipient's tax return, and the payer cannot deduct it. Alimony, on the other hand, is included as income on the recipient's tax return, and it is an above-the-line deduction for the payer. By splitting the difference, both parties could save money.

- During property settlement negotiations, consider the potential tax liability associated with an asset. Two assets may have the same current value but very different tax costs. If you sell property with a low tax basis, tax on the gain may reduce the available proceeds. Remember that assets are not necessarily "equal" for tax purposes, even if they have the same value.

Claim All Available Home-Related Deductions —

- If you operate a business out of your home, you may be able to take a home office deduction if the office is your principal place of business. The home office must be used regularly and exclusively for business; therefore, you cannot take the deduction if the space is used for any personal reasons. You may deduct a portion of your homeowners insurance, home repairs, and utilities, as well as all improvements to the office that relate to the conduct of business. Homeowners may claim depreciation on the portion used for business, while renters may deduct a portion of the rent.

- You may be able to deduct interest on a loan for a second home, provided your primary and secondary mortgages total less than $1 million. You can also deduct interest on home equity loans that do not exceed an aggregate of $100,000.

- If you rent out a second home, you must use it personally for more than 14 days, or more than 10% of the rental days (whichever is greater), for it to qualify as a personal residence. In addition to mortgage interest, you may be able to deduct property taxes and prorated monthly portions of your points paid over the life of the loan. If your second home qualifies as a personal residence and you rent the home out for more than 14 days a year, you can also deduct the appropriate portion of upkeep, insurance, utility, and similar costs against rental income.

BEWARE OF THE AMT

The alternative minimum tax (AMT) was originally created to prevent people with high incomes from paying little or no tax. Think of it as a separate tax system with its own set of rates and rules for deductions that tend to be less generous than the regular tax rules. If you have numerous exemptions and deductions from areas such as interest paying accounts, second mortgages, and state and local taxes, you may be subject to the AMT.

Under the AMT, individuals are taxed at rates of 26% and 28% on the amount of taxable income above the exemption amounts. The American Taxpayer Relief Act provides a permanent "patch" for the AMT. In 2014, the exemption amounts are $52,800 for single filers, $82,100 for married couples filing jointly, and $41,050 for married couples filing separately. If you think you may be subject to the AMT, it is important to take steps now to reduce expenses and plan ahead for next year's tax return.

More Tax-Saving Strategies

- ✔ Lower your taxable income by shifting income to other family members.
- ✔ Consider your plans for the near future. How could marriage, divorce, a new child, retirement, or other events affect your year-end tax planning?
- ✔ Take maximum advantage of your employer's Section 125 cafeteria plan, 401(k) plan, health savings account (HSA), and health reimbursement arrangement (HRA).
- ✔ Consider filing separately if one spouse has numerous itemized deductions subject to a floor amount.
- ✔ Repay personal debt or replace it with a home equity loan or line of credit to avoid nondeductible interest payments.
- ✔ Determine which type of IRA is best for you. Make your contribution before the due date of your tax return to obtain a current year deduction.
- ✔ Be mindful of distributions from your IRAs. Before age 59½, withdrawals are generally penalized. At age 70½, you are required to withdraw certain minimum amounts. Your withdrawal amount is generally based on your projected life expectancy and your IRA balance.

Education Strategies

Favorable tax breaks can help you optimize your education savings. However, some benefits cannot be combined. Let's explore your options.

Coverdell Education Savings Accounts (ESAs) — ESAs continue to provide a helping hand to those saving for education. Each year, you can contribute up to $2,000 to an ESA. Earnings grow tax deferred, and the funds can be used tax free for elementary and secondary education expenses, as well as for higher education costs. Contributions phase out for joint filers with AGIs between $190,000 and $220,000, and for single filers with AGIs between $95,000 and $110,000. Age restrictions apply. Contributions can be made for a beneficiary age 18 or younger, and distributions must be taken by age 30. These limits may be waived for students with special needs. Furthermore, ESA contributions for the current tax year can be made as late as the April filing deadline in the following year.

Education Credits — If you are currently paying higher education expenses, two Federal tax credits may help lessen your tax bill: the Hope Scholarship Credit (American Opportunity Tax Credit) and the Lifetime Learning Credit. For the Hope Scholarship Credit, the maximum credit amount is $2,500 for 2014. The credit is available for all four years of college and can be used to cover the cost of course materials. Income phase-out levels for the credit begin at $160,000 of modified AGI for joint filers and $80,000 of modified AGI for single filers in 2014. In addition, 40% of the credit is refundable, which could enable lower-income taxpayers to get money back from the IRS. The Lifetime Learning Credit, which applies to undergraduate study, as well as graduate and professional education, could be worth up to $2,000. For 2014, eligibility begins phasing out for joint filers with modified AGI of $108,000 ($54,000 for single filers). If a student qualifies for both credits in the same year, you may claim either credit, but not both.

Saving for Higher Education

	Coverdell Education Savings Accounts	Prepaid Tuition Plans	College Savings Plans
What is the annual contribution limit?	$2,000	Varies by plan	Varies by plan
Are there income limits?	Yes	No	No
Are K-12 expenses qualified?	Yes	No	No
Are qualified distributions tax free?	Yes	Yes	Yes
Eligible for use with tax credits?	Yes	Yes	Yes
Are there age restrictions?	Yes	No	No

529 Plans — These qualified tuition programs, offered as prepaid tuition plans or college savings plans, are valuable tools to help you finance your children's college educations. Prepaid tuition programs allow you to lock in today's tuition rates at participating private and public colleges and universities. College savings plans, on the other hand, offer a variety of investment options, and funds can be used to pay for tuition and other qualified higher education expenses at most colleges and universities.

While state tax benefits for 529 plans vary by state, all 529 plans offer Federal tax benefits: Earnings grow on a tax-deferred basis, and withdrawals to pay for qualified education expenses are tax free.

Contributions to a 529 plan on behalf of a beneficiary are considered gifts for gift tax purposes, and you may give up to $14,000 tax free in 2014 ($28,000 for joint filers). Furthermore, a special gift tax rule allows you to make a tax-free, lump-sum contribution to a 529 plan of up to $70,000 in 2014 ($140,000 for joint filers); however, you will be unable to make tax-free gifts on behalf of the same beneficiary for five years.

The American Taxpayer Relief Act raises the top tax rates on qualified capital gains and dividends to 20% from 15%. Proper planning can help you time your transactions and make tax-efficient investing decisions.

DIVIDENDS

Qualified dividends are taxed at the same rates as long-term capital gains — 15% for investors in the 25%, 28%, 33%, and 35% tax brackets. Investors in the bottom two income tax brackets, 10% and 15%, will pay zero tax on dividends. The top rate for dividends is 20%. The 20% tax rate will apply to the extent that a taxpayer's income exceeds the thresholds set for the 39.6% income tax bracket: $406,750 for single filers; $432,200 for heads of households; and $457,600 for married couples filing jointly.

CAPITAL GAINS & LOSSES

The tax rate on capital gains for assets held more than one year is 20% for taxpayers in the top income tax bracket, and 0% for those in the lowest income tax brackets. Taxpayers in the 25%, 28%, 33%, and 35% tax brackets will pay 15%.

Under the Patient Protection and Affordable Care Act (PPACA), higher-income taxpayers will pay a 3.8% Medicare surcharge on net investment income if income threshold amounts exceed $200,000 for single filers or $250,000 for joint filers. Thus, the top tax rate for these higher-income taxpayers is 23.8% for long-term capital gains and 43.4% for short-term capital gains.

It is important to keep in mind that capital gains attributable to depreciation from real estate held longer than 12 months are taxed at 25%, and the gain on collectibles and certain small business stock is taxed at 28%. In addition, short-term gains on assets held one year or less are subject to tax at regular income tax rates.

Gain on Home Sales — Married couples filing jointly can exclude up to $500,000 ($250,000 for single filers) of gain when they sell their home. The home must have been the principal residence for at least two of the last five years.

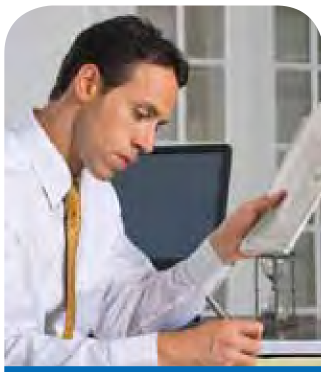
Homeowners who do not meet this requirement can still receive a portion of the exclusion based on how long they lived in the home, as long as the sale is due to a change in place of employment or in health, or because of unforeseen circumstances.

For example, if a couple lives in a home for only one year and then sells it due to unforeseen circumstances for an $80,000 profit, they may claim an exclusion of up to 50% of the $500,000 (because they lived in the home for 50% of the two years required). Thus, they can exclude every penny of their $80,000 gain.

If you have used part of your home for business, such as a home office, gain on the business portion is also eligible for the exclusion. However, depreciation taken since May 6, 1997 is still considered ordinary income. The exclusion can be used once every two years and at any age.

Timing Is Everything — When it comes to investing, timing is everything. Not only do you need to be concerned about an investment's price when you sell, but you also need to assess selling from a tax perspective.

- Unless you are holding a volatile stock and risk substantial loss, consider holding your investments for at least a year and one day Even if a stock price drops slightly, you may cut your taxes on the profit by more than half if you wait.



- If you cashed in significant gains during the year, review your portfolio for unrealized losses. Sell off any stock not likely to rebound and use the losses to offset your gains. If you end up with more losses than gains, you may use $3,000 against ordinary income and carry remaining losses over to next year.

- Reviewing gains and losses before the end of the year helps you determine if you have paid enough estimated taxes to cover any gains. A year-end review can also help you plan for the AMT, as large capital gains can trigger AMT liability.

- When selling off shares of stock purchased at different prices and at different times, inform your broker beforehand that you wish to sell the shares with the highest basis. This can minimize taxable gain or maximize deductible loss.

- An investment that increases in value while paying no income to you is not taxed until sold. By timing that sale carefully, you can enhance your tax and financial position. For instance, you can wait to sell until a year in which your tax rate is low. Or, you can give the investment to a child who is older than 19 (or 24 for full-time students) and will be taxed at a lower rate. (Be sure to consider any potential gift tax implications.)

- Mutual funds often make capital gain distributions in November or December. If you buy into a fund before the distribution date, you can be taxed on distributed gains even though they have already

been reflected in your purchase price for the shares. Consider waiting until January to buy into the fund.

- Although you cannot control the timing of sales in a mutual fund, look for mutual funds that consider certain tax-saving strategies. Some funds trade actively, while others employ tax-efficient buy-and-hold strategies.

- If you may be subject to the AMT this year, avoid investing in tax-exempt bonds that generate interest income subject to the AMT.

More Tax-Saving Strategies

- ✔ Consider a like-kind exchange to defer gain on the sale of business or investment property. However, do not exchange loss property. Instead, sell the old property outright, deduct the loss, and then purchase the replacement property. Also, before doing a like-kind exchange, analyze whether the benefits of deferral are outweighed by the currently low capital gains rate.
- ✔ Plan around the expanded "kiddie tax." Children's unearned income over $2,000 may be taxed at the parents' generally higher marginal rate until the children reach age 18 (age 19 if the child does not provide more than one half his/her own support or age 24 for full-time students). Under the original law, the kiddie tax only applied to children under age 14.
- ✔ To avoid being taxed twice, count reinvested dividends as part of your tax basis when you sell stock.
- ✔ AMT planning is critical if you have incentive stock options (ISOs). Exercising an ISO creates an AMT adjustment, often with no corresponding cash with which to pay any resulting AMT. Selling stock to generate cash may not solve the problem if the stock has dropped in value or is sold prior to having met ISO time requirements.
- ✔ Consider your investment mix in light of the tax rates for qualifying dividends — 20% for taxpayers in the top income bracket, 15% for taxpayers in the 25%, 28%, 33%, and 35% income tax brackets, and 0% for those in the lowest income tax brackets.

Business Tax Planning

As your business grows or your personal situation changes, the business structure in which you operate may need to change, as well. Keep in mind that this decision can impact your personal liability, as well as the amount of tax you and your company will pay. Let's compare the different business structures.

Choosing a Business Structure — How Do They Compare?

	C Corporations	S Corporations	LLCs* and LLPs	General Partnerships	Sole Proprietorships
Liability of owners	Limited, even if shareholders participate in management	Limited, even if shareholders participate in management	Limited, even if members/partners participate in management	Unlimited for general partners; limited for limited partners who do not participate in management	Unlimited
Number of owners	No maximum	100 maximum	No maximum, usually a minimum of two**	No maximum, requires a minimum of two	One
Profit/loss and distributions	Special allocations permitted for separate classes of stock	No special allocations permitted	Special allocations permitted	Special allocations permitted	N/A
Transferability of interests	No restriction	No restriction, but must be to eligible shareholder or "S" status terminates	Restricted, typically requires approval of majority of members	Generally restricted unless authorized by agreement	N/A
Federal income taxes	Taxed at corporate level, plus tax on dividends to shareholders	No corporate level tax (unless previously a C corporation)	None at LLC or LLP level	None at partnership level	Taxed on individual return
Continuity of life	Unlimited	Unlimited	Limited	Limited	N/A
Avoidance of double taxation	No	Usually	Yes	Yes	Yes
Tax forms to file	Form 1120	Form 1120S	Form 1065	Form 1065	Form 1040 Schedule C

** LLCs are treated as a partnership for tax purposes. ** Single-member LLCs that do not elect to be corporations will be classified as a "disregarded entity" for tax purposes.*

CHOOSING A BUSINESS STRUCTURE

C corporations are taxed as entities separate from their shareholders. The corporation pays taxes, and you pay taxes as an employee. Investors are taxed on the dividends they receive. Salary paid to you and other shareholders must be reasonable, or a portion of it may be reclassified as a nondeductible dividend payment. If earnings are accumulated beyond the corporation's reasonable needs, an additional tax may be imposed on these earnings.

S corporations may have between 1 and 100 shareholders, which can include individuals, estates, certain trusts, and tax-exempt organizations. Income and losses are passed through to shareholders, thus avoiding the double taxation inherent in a C corporation. However, S corporations are governed by strict rules.

Partnerships also avoid corporate double taxation and usually allow more flexibility in distributions than either a C or S corporation. Family limited partnerships (FLPs) offer many benefits: You can split income with your children and realize estate tax savings, while continuing to control assets transferred to the partnership. However, it is important to ensure that the FLP is carefully structured, as the IRS monitors FLPs closely.

LLCs & LLPs offer pass-through taxation and limited liability. They have a flexible structure, which allows any entity to be an owner, including a corporation; investments in other entities are not limited. Special allocations of income and losses are possible.

Sole proprietorships report business activities on personal income tax returns. If you risk substantial liability in your business, consider some form of incorporation, LLC, or LLP to protect your personal assets.

EMPLOYER-PROVIDED BENEFITS

Even in slow economic times, it is important for businesses to offer generous benefit packages to attract and retain the best employees. But, that does not mean a company has to suffer. In fact, businesses can generally avoid payroll taxes on the portion of compensation shifted from salary to benefits. Employees who receive certain benefits in lieu of salary also win because their taxable income is lowered.

Attractive benefits include retirement plans, group term life insurance (up to $50,000), health insurance, parking, employee discounts, and noncash gifts. Consider the following options:

- Set up a flexible spending arrangement (FSA) to help employees pay for medical expenses that insurance does not reimburse, such as eye surgery, prescription drugs, orthodontia, chiropractic, and co-pays.
- Provide a health reimbursement arrangement (HRA) for employees. Medical expenses reimbursed through an HRA are not taxed to the employee and are deductible by the employer. Unused funds carry forward to later years.
- Establish a 401(k) or other qualified retirement plan, such as a Savings Incentive Match Plan for Employees (SIMPLE), Simplified Employee Pension (SEP), or profit-sharing plan. In general, employee contributions are made with pre-tax dollars, and earnings grow on a tax-deferred basis. Matching contributions, when possible, may encourage participation and enhance your employee recruitment and retention efforts. When choosing a plan, or combination of plans, consider both your business needs and your personal financial goals.

Which Is Best for Your Business? SIMPLE vs. TRADITIONAL 401(k)

	SIMPLE IRA	SIMPLE 401(k)	Standard 401(k)
Maximum Business Size	100 or fewer employees	100 or fewer employees	No limit
Individual Contribution Limit	$12,000	$12,000	$17,500
For people 50 or older, additional	$2,500	$2,500	$5,500
Discrimination Testing	No	Limited	Yes
Mandatory Employer Match	Yes, 1%–3% of salary	Yes, 3% of salary	No
Vesting	Immediate	Immediate	Up to 7 years
Administration	Least	Medium	Most

HEALTH INSURANCE REFORM

As a result of the Patient Protection and Affordable Care Act (PPACA), small businesses with fewer than 25 employees that pay at least 50% of the health care premiums for their employees qualify for a tax credit of up to 50% of their premiums (up to 35% for nonprofits), if insurance is purchased through an exchange. While employers are not required to offer health insurance plans under the law, starting in 2015, a business with 50 or more full-time employees (defined as working 30 or more hours per week) will be required to pay a penalty if a company employee qualifies for and accepts a Federal health insurance premium subsidy. Employers face an additional penalty for every full-time worker who qualifies for a health insurance coverage premium subsidy. Employers that offer health care coverage may in some cases also be required to provide “free choice vouchers” to employees.

HEALTH SAVINGS ACCOUNTS

Health savings accounts (HSAs) offer qualified individuals covered by high-deductible health plans (HDHPs) tax-favored opportunities to save for medical expenses. Employers of any size may establish HSAs, and pre-tax contributions can be made through a cafeteria plan. An employee's contributions may be tax deductible within certain limits. Distributions from an HSA for qualified medical expenses are tax free, and unused funds may be carried forward from year to year. Nonqualified distributions may be subject to income tax and a 10% penalty. If a participant changes jobs or health insurance coverage, the HSA is portable. For 2014, the maximum contribution is $3,300 for individual coverage and $6,550 for family coverage.

BUSINESS DEDUCTIONS

To keep your business' tax bill as low as possible, take advantage of every deduction available. You may be able to save by timing purchases to take advantage of temporary opportunities.

Maximize the Section 199 Deduction — In 2014, businesses may deduct 9% of the lesser of their qualified production activities income (QPAI) or their taxable income. Qualified activities include certain types of film and video, computer software, and energy production, as well as certain agricultural processing, construction, engineering, and architectural activities.

Claim Section 179 Expenses — Consider using the Section 179 expense deduction for new business equipment, furniture purchases, and off-the-shelf computer software. Through 2013, small businesses could expense up to $500,000 of Section 179 property, with a phase-out threshold of $2 million. Pending further legislation, in 2014 the limit reverts to $25,000, with a phase-out beginning at $200,000.

Bonus Depreciation — The American Taxpayer Relief Act only renewed 50% bonus depreciation through 2013. It is no longer available for most types of property.

Lower Your Taxable Income — Buy business supplies at the end of a profitable year and accelerate other expenditures, like repairs and maintenance.

Avoid Mid-Quarter Convention — Maximize your depreciation deduction by planning qualifying purchases before the end of the year. However, be sure to avoid having depreciation deductions reduced as a result of the "mid-quarter convention," which occurs when more than 40% of the total cost of all personal property placed in service during the year goes in service in the last three months of that tax year. Purchases fully deducted as Section 179 expenses are removed from the mid-quarter convention computation.

Maximize Depreciation — Consider a cost segregation study to maximize your depreciation deduction. You can accelerate depreciation by properly identifying and pricing nonstructural items and land improvements separately from your building. These items have much shorter depreciable lives than the assigned 39-year life for nonresidential real property. Landscaping, site fencing, parking lots, and security equipment are examples of assets which may need proper classification.

Depreciation

36-Month Assets (Straight-Line)
Most software

3-Year Assets (200% DB)
Dies, molds, small tools, certain horses

5-Year Assets (200% DB)
Autos, computers, typewriters, copiers, many types of equipment, private aircraft

7-Year Assets (200% DB)
Most manufacturing equipment, office furniture, printing equipment, oil and gas production equipment

7-Year Assets (150% DB)
Farm equipment

27.5-Year Assets (Straight-Line)
Rental houses, apartments, low-income housing

39-Year Assets (Straight-Line)
Nonresidential buildings

Deduct All Travel, Transportation, and Entertainment Costs —

- Many business-building expenditures are tax deductible, provided your company keeps accurate records and can substantiate that the outlays were business-related. You can deduct all business travel expenses, including travel between job sites, travel to a temporary assignment (generally one year or less) that is outside your general area of residence, travel between primary and secondary jobs, and all other cab, bus, train, airline, and automobile expenses. Any regular commuting expenses to your primary job cannot be deducted. If your home is your principal place of business, you can deduct daily transportation expenses from your home to any work location.

- You may deduct expenses for an automobile you own in one of two ways: either record and deduct your actual expenses, including depreciation, or record your mileage and deduct a standard amount per mile of travel, plus parking and toll fees.

2014 Standard Mileage Rates		
Business	56¢	per mile
Moving	23.5¢	per mile
Medical	23.5¢	per mile
Charitable	14¢	per mile

- Since annual depreciation limits apply to newly acquired automobiles, some business owners consider leasing.

- To support business travel deductions, keep supporting documents (such as canceled checks and receipts) for expenses of $75 or more. Document the following items in a travel log or on the back of receipts:
  - Date, place, amount, and business purpose of expenditures.
  - Name and business affiliation of person(s) you are entertaining, or business purpose of trip.

  In the case of meals and entertainment, all of the above, plus the activity, must directly precede or follow a substantial business discussion associated with your business. Be sure to keep personal expenses separate from business expenses.

Be Aware of Inventory Issues —

- Many businesses with $10 million or less in gross receipts can now use the cash method of accounting and not be required to account for inventory. We, as your qualified tax professionals, can help you determine if you qualify.

- In times of rising prices, using the LIFO (last-in, first-out) inventory identification method can lower income tax. It increases your cost of goods sold (thereby reducing your taxable income) by assuming that the higher priced inventory units you most recently purchased were the ones actually sold.

- In times of falling prices, the FIFO (first-in, first-out) inventory identification method may provide larger tax savings. It assumes the higher priced inventory units you purchased first are the ones you have sold.

- Inventory methods can be changed. We can help you decide what is most advantageous and advise you on the procedure for changing methods.

- Corporations with excess inventory may donate that property to charitable organizations and receive a tax deduction. For example, if you contribute food or medical supplies to a charity that provides for the homeless, you may deduct the cost of the goods and half of the lost profit (not to exceed twice the cost).

Put Your Kids to Work — Your child's wages are fully deductible as a business expense. If you are a sole proprietor, or you and your spouse are the only owners of an entity taxed as a partnership, you do not have to pay FICA on those wages if the child is under age 18, nor do you have to pay unemployment insurance if the child is under age 21. Your child's wages may be subject to a lower tax rate than if you were to retain the money as business earnings.

Go into Business with Your Kids — Children may be partners in partnerships or shareholders in S corporations, which may reduce the overall family tax burden in certain situations.

Deduct Business Losses —

- Net operating losses (NOLs) are generated when a company's deductions for the tax year are more than its income. NOLs may be carried back 2 years to obtain a current refund and then carried forward for up to 20 years, or you may elect out of the carryback. Foregoing the carryback period could be beneficial if your marginal tax rate in the carryback years is unusually low.
- Corporate capital losses are currently deductible, but only to the extent of capital gains. A three-year carryback and a five-year carryforward period apply.
- If your business is not incorporated or operates as an S corporation, partnership, or LLC, you may deduct business losses on your personal tax return. However, NOL deductions may be limited by at-risk or passive activity loss rules.
- Bad business debts are deductible in full or in part as ordinary losses when good faith collection efforts fail. Inventory losses, casualty and theft losses (to the extent they are not covered by insurance), and losses on the sale of business assets may also be deductible.

More Tax-Saving Strategies

- ✔ To the extent possible, shift income into next year.
- ✔ Set up a nonqualified deferred compensation plan for your highest paid employees.
- ✔ Consider a compensation and benefit study to see what makes sense for your company from a tax perspective.

We can help you evaluate your retirement plan options, as well as advise you on how tax reform may impact plans you currently have in place.

INDIVIDUAL RETIREMENT ACCOUNTS (IRAs)

IRAs remain an attractive option for retirement savings. You can contribute up to $5,500 to an IRA or combination of IRAs in 2014. If you are age 50 or older, you can contribute an additional $1,000. Earnings grow tax deferred, and contributions to a traditional IRA may be deductible.

When you take traditional IRA distributions, certain rules apply. Distributions before the age of 59½ may be subject to a 10% Federal income tax penalty in addition to the income tax that will be due. There are exceptions. For example, if you tap your IRA early to pay for qualified higher education expenses or to fund up to $10,000 of your first home, the 10% penalty does not apply.

ROTH IRAs

Roth IRA contributions are not deductible, but qualified distributions are tax free, provided you have held the account for five years and are at least 59½ years old. Roth IRAs may be a good fit if you are fairly young, expect to be in a similar tax bracket when you retire, or are concerned about cash flow during retirement. Income limits may apply.

In 2010, the adjusted gross income (AGI) ceiling on converting traditional IRAs to Roth IRAs was eliminated, allowing more taxpayers to take advantage of the Roth IRA through direct contributions or conversions. When converting, the distribution from your traditional IRA is taxed, but you are generally not penalized for the early withdrawal.

IRAs for Children Make Tax Sense — If your child has earned income from outside the household, consider contributing it to an IRA.

Suppose your son saves $800 from lawn mowing when he is 15-years-old and invests in a Roth IRA. If he makes no additional contributions and the funds grow at 8% annually, he may have more than $37,000 at age 65. Or, suppose your daughter opens a Roth IRA with $2,000 when she is 15-years-old, and then she contributes $2,000 annually for the next 10 years. The estimated value of her tax-free fund balance at age 65 will exceed $700,000, if the annual growth rate is 8%.

Note: The hypothetical examples are for illustrative purposes only. They are not intended to reflect an actual security's performance. Investments involve risk and may result in a profit or a loss. Seeking higher rates of return involves higher risks.

401(k) PLANS

401(k) plans are qualified retirement plans offered by thousands of employers. As a participating employee, you can contribute the maximum dollar amount allowed by law ($17,500 in 2014) or a maximum percentage of salary, as defined by the plan. Those age 50 or older can contribute an additional $5,500. You do not pay taxes on your contributions until you receive money from the plan, which is usually when you retire and may be paying taxes at a lower rate.

ROTH 401(k)s

The Roth 401(k) allows participants in a sponsoring employer's traditional 401(k) plan to designate all or part of their elective salary deferrals to a Roth account. Although contributions are made with after-tax dollars (unlike traditional 401(k) contributions), earnings are tax free, provided you have held the account for five years and are at least 59½ years old.

Participants in traditional 401(k), 403(b), and 457(b) plans are permitted to roll over funds into Roth accounts within their plans, if available. Because contributions to traditional 401(k)s are made on a pre-tax basis, any funds transferred from traditional to Roth 401(k) accounts are taxed in the year of conversion.

2014 Contribution Limits

	Regular	Additional Age 50	Maximum
401(k)s	$17,500	$5,500	$23,000
IRAs	$5,500	$1,000	$6,500

Estate Planning

If it has been a while since you dusted off your estate plan, now is the time to do so. Failing to plan your estate may increase your potential tax liability; it also forces the state courts to split up your assets, assign guardians for your children, and dictate all other details in handling your estate. Your involvement *now* is essential to your loved ones' futures.

Benefits of Estate Planning

	With an Estate Plan	Without an Estate Plan
Your Assets	You decide who gets what	Inheritance is determined by state law
Your Children	You choose the guardian	The court appoints a guardian
Your Inheritance	You decide how and when beneficiaries receive their inheritance	Terms and timing are set by law
Your Business	You decide how the family business is to continue	Forced sale or liquidation may cause financial loss and family hardship
Your Executor	You decide who will manage your estate	The court appoints an executor
Your Final Expenses	You can reduce estate settlement costs	Costs may add up due to administrative expenses and unnecessary taxes

Watch for Changes in Estate Tax Laws —

The estate planning landscape has been marked by change and uncertainty over the past several years. Under 2001 tax reform, the Federal estate tax became progressively generous in the run-up to 2010, when it was phased out completely for a single year. Under the 2010 Tax Relief Act, the Federal estate tax was reinstated in 2011. In 2014, there is a top tax rate of 40% and an exemption amount of $5.34 million, or $10.68 million for married couples.

Early preparation is key to developing appropriate strategies to minimize potential estate taxes and ultimately maximize the amount transferred to your heirs. The estate tax exemption allows you to transfer $5.34 million to your children or other heirs tax free at death. (Bear in mind that an unlimited amount may be passed tax free to a spouse.) If you are married and your combined assets (including life insurance) surpasses $10.68 million, consider implementing advanced planning tools, such as trusts, to help minimize taxes.

You may also want to consider a gifting strategy to gradually transfer assets to loved ones. However, it's important to consider gift taxes. Under the 2010 Tax Relief Act, starting in 2011, the Federal gift tax was reunified with the estate tax. In 2014, there is a top tax rate of 40% and an exemption of $5.34 million. A gifting program can play a valuable role in your estate plan.

Estate and Gift Tax Exemptions

Year	Estate Tax Exemption	Gift Tax Exemption
2013	$5,250,000	$5,250,000
2014	$5,340,000	$5,340,000

ESTATE PLANNING STRATEGIES

- "Gifting" is a great way to gradually transfer your estate and ultimately minimize your estate tax burden. Each year, you may make gifts of $14,000 to as many recipients as you wish, tax free. If you and your spouse "split" gifts, then as much as $28,000 may be given to an unlimited number of recipients tax free.

Gifting Benefits

- Post-gift appreciation escapes the estate tax.
- To the extent of the $14,000/$28,000 per donee, per year annual exclusion, no transfer tax is ever imposed.
- Gift tax paid reduces your taxable estate. (Limited exceptions apply.)
- Income or appreciation is taxed to lower tax bracket donees.

- If you own stock temporarily depressed in value but with high appreciation potential, consider giving it to your children now. The gift tax impact (determined by the fair market value on the date of gift) may be reduced. When the stock price recovers, you can enjoy a second benefit — the increase in value does not increase your estate tax base.

2014 Lifetime Gift Tax Exemption	$5,340,000
2014 Annual Gift Tax Exclusion	Gifts per person $14,000 Joint gifts by spouses $28,000

- If you would like to make a gift to a grandchild (or anyone else) and not be limited by the annual exclusion amount, you can make a direct payment to the providers for education (tuition only) and medical expenses. Gifts of this nature do not count toward the annual limit. You can also exclude gifts of tuition or medical payments made now for future services.

- If you wish to make gifts of more than $1 million, consider transferring funds in exchange for an installment note. Proceeds from the note can be distributed to the obligors at death and be sheltered by the estate tax exemption.

- If you are married, be sure to understand the portability provision under the 2010 Tax Relief Act, which was made permanent for 2013 and beyond by the American Taxpayer Relief Act. It allows the estate tax exemption to be transferred between spouses.

In other words, if one spouse dies and does not use the full exemption amount, the remainder can be used by the surviving husband or wife. For estate planning purposes, this means that husbands and wives do not have to split assets between them, or be concerned about who holds the title on various assets.

Yet, these changes to the estate tax do not eliminate the need for planning. Wealthy taxpayers who currently fall within the exemption limits may still want to consider setting up a bypass trust in anticipation of future changes in the rules. In addition, couples with different sets of final beneficiaries, such as children from previous marriages, may wish to set up a bypass trust in order to clarify the beneficiaries of their separate assets.

- In light of changing tax laws, it is important to review your estate conservation strategies. We can help you develop appropriate strategies for your situation.

More Tax-Saving Strategies

Set up a trust to own life insurance so that the value of the policy can be excluded from your taxable estate.

SUCCESSION PLANNING

If you have spent the greater part of your life building a profitable business, implement a business succession plan. At a minimum, a good plan can help you accomplish the following:

- Transfer control according to your wishes.
- Carry out the succession of your business in an orderly fashion.
- Minimize the tax liability for you and your heirs.
- Provide economic well-being for you and your family when you retire.

Here are some ideas for succession planning:

- Gift stock to family members now so ownership can be transferred without incurring unnecessary transfer taxes.
- Employ a buy-sell agreement that values your business for estate tax purposes. An effective agreement provides estate tax liquidity and provides your successors with the means to acquire your stock.
- Create an employee stock ownership plan (ESOP) and sell your stock to the plan. You can "roll over" the sale proceeds into other investments tax free, ownership can be transferred to your employees over time, and your business can obtain income tax deductions for the plan contributions.
- Take advantage of the estate tax installment payment option. It allows you to pay the portion of your estate tax attributable to inclusion of your closely held business interest over a period of up to 14 years. Artificially low interest rates apply during the tax-deferral period. Other special rules may apply.

ACT NOW

Early planning is key to making the most of your opportunities, especially considering the changing tax laws. We are here to help you reduce your current tax bill and plan for the future. Contact us when planning transactions and before year-end. We will keep you up-to-date.

Be advised that this information was not intended or written to be used, and cannot be used, for the purposes of avoiding tax-related penalties or for promoting, marketing, or recommending to another party any tax-related matters addressed herein.

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Notes & Questions:

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