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HIGHLIGHTS

* Developing Income Tax Strategies for 2014 and Beyond
* Post Mid-Term Election Consideration
* Planning For The Net Investment Income Tax
* Working With Uncertainty Over Tax Extenders
* Exploring Savings Through Repair Regs
* Planning For PPACA's Impact On Individuals and Businesses

INSIDE

Post-Election Planning……………..1
Traditional Strategies……………..2
Planning For Individuals……….…..2
Year-End Retirement Strategies.…4
Estate and Gift Taxes……………..4
Planning For Business…………….4
Business Extenders……………….5
Repair Regulations…………………5

Year-End Strategies: Creating Pathways for Tax Savings by Individuals and Businesses

Although tax planning in s a 12-month activity, year-end is traditionally the time to review tax strategies from the past and to revise them for the future. At year-end 2014, and looking ahead to 2015, individuals and businesses need to be ready for late tax legislation, prepare for a rash of new requirements and responsiblities under the Patient Protection and Affordable Care Act (PPACA); and incorporate traditional as well as innovative strategies into their year-end planning.

PLANNING NOTE. *At the time this Briefing was prepared, legislation to extend many popular but temporary tax extenders is being considered by the lame duck Congress. Late legistlation could cause a delayed start to the 2015 filing season (and possibly delay refunds to individuals) because the IRS will need additional time to reprogram its return processing systems.*

POST-ELECTION PLANNING

On November 4, Americans learned the composition of the House and Senate in the 114th Congress that will convene in January 2015. Republicans increased their majority in the House and captured a majority in the Senate. The changes could open the door for action on comprehensive tax reform in 2015 or 2016. Alternatively, lawmakers and the President may agree on smaller scale reforms.

Tax Extenders. The impact of the midterm elections on immediate year-end tax planning for 2014 principally revolves around a so-called "tax extenders" package of expired individual and business tax breaks that await retroactive reinstatement to the start of 2014. It is not year decided whether final passage will happen in mid-November or early December ...or, if negotiations break down, in January when the new Congress meets.

IMPACT. Hill sources have recently indicated that the differences remaining in House and Senate extenders bills are "easily resolvable." Making the research tax credit permanent in return for a two-year extension of the other extenders has been part of the latest buzz around how final negotiations will proceed. Although having an extenders package eventually pass Congress is "almost a sure thing" any single extender

remains subject to being jettisoned in last-minute negotiations, making year-end tax planning decisions subject to revision until final Congressional action.

Tax Reform. Comprehensive tax reform has not moved beyond the discussion stage in 2014. In the days after the November 4 elections, GOP leaders said that tax reform would be a priority in the new Congress but gave no specifics. President Obama said that tax reform could be an area where he and the GOP could cooperate. The President noted his earlier proposal to pay for a reduction in the corporate tax rate by elimininating some unspecified business tax preferances.

IMPACT. *Broad tax reform, even if put on a fas-track for passage in 2015 likely will have an effective date of 2016 (or even later with phased-in provisions). An excep-- tion, however, may be carved out for sooner action on corporate inversions.*

Health Care. Several provisions of the PPACA could be modified or repealed in the 114th Congress. Those being considered for action in the near future include rolling back the 2.3 percent medical device excise tax and the 30-hour rule for treatment as the full-time employee for purposes of the employer shared responsibility requirement. The latter change would especially impact current planning by employers on avoiding liability under the employer mandate.

IRS. The IRS operated in FY 2014 at the same rate of funding as FY 2013 and at roughly $850 million below FY 2010 levels. The lame-duck Congress is expected to approve an omnibus spending bill to fund the IRS through the end of FY 2015. The GOP-controlled 114th Congress will prepare the IRS budget for FY 2016.

TRADITIONAL YEAR-END STRATEGIES

Year-end 2014 presents unique challenges. At the same time, traditional year-end planning techniques nevertheless remain important both to maximize benefits in connection with what's new and to do so within the usual ebb and flow of the taxpayer's personal economy. The following traditional income and deduction acceleration techniques and their reciprocal deferral strategies should be considered:

Income Deferral/Accleration:

* Enter into/ Sell installment contracts
* Defer/ Receive bonuses before January
* Hold/ Sell appreciated assets
* Accelerate income to use available carryforward losses
* Hold/ Redeem U.S. Savings Bonds
* Postpone/ Complete Roth conversions
* Delay/ Accelerate debt forgiveness income
* Minimize/ Maximize retirement distributions
* Delay/ Accelerate billable services
* Structure/ Avoid mandatory like-kind exchange treatment

Deductions and Credits Acceleration/Deferral

* Bunch itemized deductions into 2014 and take standard deduction in 2015/ reverse steps
* Pay bills in 2014/ postpone payments until 2015
* Pay last state estimated tax installment in 2014/ delay payment until 2015
* Accelerate economic performance/ postpone performance
* Watch AGI limiitations on deduc-tions/ credits
* Watch net investment interest restrictions
* Match passive activity income and losses

"Year-end 2014 presents unique challeges."

YEAR-END INDIVIDUAL PLANNING

For individuals, the income tax rates for 2014 are unchanged from 2013: 10, 15, 25, 28, 33, 35 and 39.6 percent. The top tax rate for qualified capital gains and dividends is also unchanged from 2013: 20 percent.

STRATEGY. *Year-end planning should look to avoiding spikes in income, whether capital gains or other income, which for higher-income taxpayers may push capital gains into either the 39.6 percent bracket for short-term gains or the 20 percent capital gains bracket for long-term gains. Spreading the recognition of certain income between 2014 and 2015 may accomplish this goal.*

Net Investment Income (NII) Tax

Since 2013, taxpayers with qualifying income are liable for the 3.8 percent net investment income (NII) tax. The threshold amounts for the NII tax are:

* $250,000 in the case of joint returns or a surviving spouse,
* $125,000 in the case of a married taxpayer filing a separate return, and
* $200,000 in any other case.

STRATEGY. *All net investment in-come should be monitored for exposure to the NII tax. Net investment income is more than simply capital gains and dividends. It also includes income from a business in which the taxpayer is a passive participant. Rental income may also be considered NII unless earned by a real estate professional.*

STRATEGY. Taxpayers with potential NII liability should consider keeping income below the $250,000/$125,000/$200,000 thresholds if possible by spreading income out over a number of years or offsetting the income with both above-the-line and itemized deductions.

Additional Medicare Tax

The Additional Medicare Tax increases the employee share of Medicare tax by an additional 0.9 percent of covered wages in excess of certain threshold amounts. The tax also increases Medicare tax on self-employment income by an additional 0.9 percent of self-employment income in excess of the threshold amounts. The threshold amounts are: $200,000 for single individuals (and heads of household); $250,000 for married couples filing a joint return; and $125,000 for married individuals filing separate returns.

STRATEGY. *This is now the second year in which affected taxpayers will file returns reflecting Additional Medicare Tax. Taxpayers who only now realize that they have had insufficient income tax withholding may request that their employer(s) take out an additional amount of income tax withholding, which would be applied against taxes shown on the taxpayer's individual income tax return, including any Additional Medicare Tax liability. Taxpayers may also consider making estimated tax payments.*

Alternative Minimum Tax

The alternative minimum tax (AMT) is now permanently "patched." The patch provides for increased exemption amounts and allows taxpayers to take all of the nonrefundable personal credits against regular and AMT liability.

STRATEGY. *Even with the permanent patch, taxpayers should continue to review their AMT liability versus regular tax liability. For some taxpayers, AMT liability and regular tax liability may be roughly equal from year to year. Other taxpayers may find that they have had significant fluctuations in income or AMT-targeted tax benefits from year to year and could explore the benefit from being able to shift some AMT-triggering items from an AMT year to a non-AMT year.*

Pease Limitation/PEP

The Pease limitation reduces the total amount of a higher-income taxpayer's otherwise allowable itemized deductions by three percent of the amount by which the taxpayer's adjusted gross income exceeds an applicable threshold. However, the amount of itemized deductions is not reduced by more than 80 percent. Taxpayers who find themselves within threshold-adjusted gross income amounts that make them subject to the Pease Limitation will also need to plan for the revived personal exemption phaseout (PEP).

Individual Tax Extenders

Under current law - the individual extenders (as well as the business extenders discussed below) - are unavailable for 2014 and subsequent years, unless extended by Congress. For individuals, they include the state and local sales tax deduction, special mortgage debt forgiveness provisions, transit benefits parity, higher education tuition deduction, IRA distributions to charities, and teachers' classroom expense deduction.

PLANNING NOTE. *While some "extenders" legislation is eventually expected, the extent of what will be covered remains uncertain at press time. Some temporary individual incentives are available for 2014 and 2015 because they carry different expiration dates. They include the American Opportunity Tax Credit (AOTC) and the Code Sec. 25D residential efficient credit.*

Affordable Care Act

Effective January 1, 2014, the PPACA requires individuals, unless exempt, to carry minimum essential health insurance coverage for each

LIFE CYCLE CHANGES IMPORTANT TO YEAR-END STRATEGIES

In addition to changes in the tax law, year-end tax strategies should also consider personal circumstances that changed during 2014 as well as what may change in 2015. These "life cycle" events include:

* Change in filing status; marriage, divorce, death or head of household changes
* Birth of a child
* Child no longer young enough for child credit
* Child who has outgrown the "kiddie" tax
* Casualty losses
* Change in medical expenses
* Moving/relocation
* College and other tuition expenses
* Employment changes
* Retirement
* Personal backruptcy
* Large inheritance
* Business successes or failures

month or make an individual shared responsibility payment. Individuals liable for a shared responsibility payment during 2014 will make their payment when they file their 2014 returns. Individuals who obtain health insurance coverage through the PPACA Marketplace may be eligible for the Code Sec. 36B premium assistance tax credit to help offset the cost of coverage. 2014 was the first year that the Code Sec. 36B credit was available.

PLANNING NOTE. *Taxpayers who elect to receive advance payments of the Code Sec. 36B credit must reconcile on their returns the amount forwarded to insurers with the credit they may claim.*

Year-End Retirement Strategies

Gennerally, all types of qualified plans (as well as traditional retirement accounts) must satisfy a required minimum distribution (RMD) in which distribution of an employee's or IRA owner's interest in the plan or ITA must begin by the "required beginning date."

PLANNING NOTE. *Two year-end deadlines should be kept in mind: (1) The RMD for any given year is based on the retirement account balance on December 31 of the calendar year immediately before the year of distribution; and (2) The RMD for any year generally must take place by December 31 of that year. The interplay of these two deadlines will reach increaing importance as baby boomers begin to retire, and to do so with fewer pensions and a greater number of retirement account balances to manage..*

In *Bobrow, TC Memo. 2014-21,* the Tax Court held that a taxpayer could make only one nontaxable rollover contribution within each one-year period regardless of how many IRAs the taxpayer maintained. The one-year limitation under Code Sec. 408(d)(3)(B) is not specific to any single IRA maintained by an individual but instead applies to all IRAs maintained by a taxpayer, the court found.

PLANNING NOTE. *The Bobrow decision affects only IRA to IRA rollovers managed by the account holders, and does not limit trustee-to-trustree transfers. For planning purposes, the pre-Bobrow rule will continue to apply to IRA distributions occurring before January 1, 2015.*

Estate and Gift Taxes

The maximum federal unified estate and gift tax rate is 40 percent with an inflation-adjusted $5 million exclusion for gifts made and estates of decedents dying after December 31, 2012. The gift tax exclusion allows taxpayers to give up to an inflation-adjusted $14,000 to any individual, gift-tax free and without counting the amount of the gift toward the lifetime $5 million exclusion, adjusted for inflation.

PLANNING NOTE. *The applicable exclusion amount, as adjusted for inflation, is $5,340,000 for gifts made and estates of decedents dying in 2014 and rises to $5,430,000 in 2015.*

PLANNING NOTE. *There is no limit on the number of individual donees to w hom gifts may be made under the $14,000 exclusion. Spouses may "split" their gifts to each donee, effectively raising the per donee annual maximum exclusion to $28,000. Spouses may give an unlimited amount of gift to one another without any gift tax imposed.*

YEAR-END BUSINESS PLANNING

Businesses seeking to maximize tax benefits through 2014 year-end tax planning may want to consider three general strategies: (1) Use of traditional timing techniques for income and deductions; (2) Special consideration of significant tax incentives that expired at the end of 2013 but may be extended through 2014; and (3) Reaction to certain recent tax developments from IRS and the courts that may present either new opportunities or pitfalls.

Bonus Depreciation

For tax years after 2013, bonus depreciation has officially expired (except for certain noncommercial aircraft and longer production period property which may be eligible for 50 percent bonus depreciation through 2014).

STRATEGY. *Although the pos-sibility of retroactive reinstatement of the bonus-depreciation election shuld be factored into a year-end strategy, a final decision on making it is not required until a return is filed. Further, bonus depreciation is not mandatory. Certain taxpayers should consider electing out of bonus depreciation to spread depreciation deductions more evenly over future years.*

"Business incentives that officially expired after 2013 include enhanced Code Sec. 179 expensing, the Work Opportunity Tax Credit (WOTC)…and many more."

Research Tax Credit

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to the employer mandate starting in

Research Tax Credit

The research tax credit also officially expired after 2013, but it may be retroactively revived by Congress. The research credit may be claimed for increases in business-related qualified research expenditures and for increases in payments to universities and other qualified organizations for basic research. The credit applies to the excess of qualified research expenditures for the tax year over the average annual qualified research expenditures measured over the four preceeding years.

Small Business Stock

A full 100-percent gain exclusion applies to qualified small business stock that is acquired after September 27, 2010, and before January 1, 2014, and held for more than five years. Under current law, the percentage that is excluded is 50-percent (60-percent for empowerment zone stock) for qualifying stock acquired after December 31, 2013.

STRATEGY. *Even with the reduced exclusion, the provision is a worth-while strategy. Taxpayers should consider making investments before year-end 2014 so that the required five-year holding period begins to run. Also to keep in mind is that being even a single day short of the five-year period - measured fromt he acquisition date - eliminates any benefit, with no proration allowed. Certain ex- changes of similar stock before the five year period, however, are permitted.*

Code Sec. 199 Deduction

The Code Sec. 199 deduction allows taxpayers to deduct an amount equal to the lesser of a phased-in percentage of taxable income (adjusted gross income for indivi-tivities income. The deduction is calculated as a percentage (gen-erally nine percent under current law, subject to some exceptions) of qualified production activities income.

PLANNING NOTE. *The Code Sec. 199 deduction is often viewed as being underutilized. Taxpayers should not let the complexity of the calculations deter potential savings under the deductions.*

Business Extenders

Business incentives that have officially expired after 2013, unless revived by Congress, include, in addition to bonus depreciation and the enhanced Code Sec. 179 expensing, the Work Opportunity Tax Credit (WOTC), Indian employment credit, special expensing rules for film and television productions, and many other temporary provisions.

Affordable Care Act

Effective January 1, 2015, the PPACA's employer shared respons-ibility requirements ("employer mandate") take effect for applicable large employers. However, there is a carve-out for mid-size employers for 2015. Some related standards for larger employers also are available in 2015.

PLANNING NOTE. *Employers with fewer than 50 full-time employees (including full-time equivalent employees) are completely exempt from the employer mandate for any year. Employers with at least 50 but fewer than 100 full-time em- ployees (including full-time equiva- lent employees) are exempt from the employer mandate until 2016; and employers with 100 or more full-time employees (including full-time equivilent employees) are subject 2015, with certain relaxed standards.*

Repair Regulations

Final regulations for treating costs related to tangible property (the so-called "repair regulations") may open significant tax planning opportunities. For acquisitions of tangible property, a de minimus safe harbor allows taxpayers to deduct certain items. The safe harbor applies to items that cost $5,000 or less (per item or invoice) and that are deducted on the company's applicable financial statement (AFS) in accordance with a written accounting procedure.

STRATEGY. *Under the $5,000 de minimis safe harbor in the final regulations, taxpayers must have a written policy in place at the beginning of the tax year that specifies a dollar amount for following book treatment. The de minimis safe harbor is an annual election and not an accounting method, so it can be made and changed every year. Calendar-year taxpayers need to have a written policy in place by year-end 2014 to qualify for 2015. The annual election is made by filing a statement with the taxpayer's income tax return.*

PLANNING NOTE. *The de minimis limit is $500 per item or invoice for companies without an AFS. A written policy while not required here, is nevertheless recom-mended.*