Dear Clients & Friends:

There are several things to consider when doing year-end tax planning: taking advantage of expiring tax provisions, deferring income into next year, or accelerating income into the current year (and doing the opposite with expenses). The proper strategy depends on whether or not you anticipate a significant change in income or expenses next year.

On December 17, 2014, President Obama signed into law a bill retroactively extending a number of tax breaks which would have otherwise expired at the end of 2013. This extender bill includes the following items which may impact your total tax for 2014:

(1) Deduction for expenses of elementary and secondary school teachers - This provision allows teachers a $250 tax deduction in 2014 for expenses paid or incurred for classroom supplies that they buy with their own money. It is available to all teachers, whether they itemize or not.

(2) Mortgage debt forgiveness – If you sell your principal home for less than what you owe the bank or your home is foreclosed, the lending bank may agree to forgive the remaining debt you owe. The IRS typically treats forgiven debt as taxable income to you. Under this provision, up to $2 million of forgiven mortgage debt is eligible to be excluded from income ($1 million if married filing separately) through tax year 2014.

(3) Increased exclusion from income for employer-provided mass transit and parking benefits - This provision would increase the monthly exclusion from income for employer-provided transit and vanpool benefits from $130 to $250, so that it would be the same as the exclusion for employer-provided parking benefits.

(4) Deduction for mortgage insurance premiums – This provision allows you to deduct the cost of your mortgage insurance premiums if you itemize your deductions.

5) Deduction for state and local general sales taxes - This provision would allow the election to take an itemized deduction for state and local general sales taxes in lieu of the itemized deduction permitted for state and local income taxes.

(6) Deduction for higher education expenses - This provision would extend a tax deduction for qualified higher education expenses. The maximum deduction, for 2014 would be $4,000 for taxpayers with AGI of $65,000 or less ($130,000 for joint returns) or $2,000 for taxpayers with AGI of $80,000 or less ($160,000 for joint returns).

(7) Tax-free distributions from individual retirement plan for charitable purposes - This provision would allow an individual retirement arrangement (Traditional IRA) owner who is age 70-1/2 or older generally to exclude from gross income up to $100,000 for 2014 in distributions made **directly from the IRA to certain public charities.**

Income Subject to Top Tax Rate

For 2014, the amount of income subject to the highest tax rate of 39.6 percent is as follows:

Married Filing Jointly:	$457,600
Married Filing Separately:	$228,800
Single Individuals:	$406,750
Head of Household:	$432,200

Affordable Care Act ('Obamacare')

Beginning in the 2014 tax year, most individual taxpayers will be required to obtain health insurance, either through their employer or independently on a health insurance exchange marketplace, or risk facing a tax penalty. In 2014 the penalty is either $95 per adult ($47.50 per child under 18) or 1% of income, whichever is higher. For the 2015 tax year, the penalty will be the higher of 2% of income or $325 per person ($162.50 per child). If you or your family members do not have health insurance, it may make sense for us to evaluate your options by comparing the amount of the potential penalties with the cost of obtaining coverage.

Alternative Minimum Tax

If you are subject to the alternative minimum tax (AMT), your deductions may be limited. Thus, if we anticipate that you will be subject to the AMT, we need to consider the timing of deductible expenses that may be limited under the AMT.

IRA Considerations

In 2014, the waiting-period rule on IRA rollovers changed, and not to your benefit. While the rule used to be that the one-year waiting period between rollovers applied on an IRA-by-IRA basis, the courts and IRS determined that it applies on an aggregate basis instead. This means that you cannot make a tax-free IRA-to-IRA rollover if you've made such a rollover involving any of your IRAs in the preceding one-year period. This new rule applies beginning in 2015. However, the rule does not affect your ability to transfer funds from one IRA trustee directly to another, because such a "trustee-to-trustee transfer" is not a rollover and, therefore, is not subject to the one-waiting period.

Self-directed IRAs have become increasingly popular in recent years because they allow an IRA owner to have more control over the type of investments that will be held in the IRA. This higher degree of flexibility in choosing IRA investments allows the IRA owner to invest in assets with greater wealth-building potential. However, the large amount of money held in self-directed IRAs makes them attractive targets for fraud promoters. Thus, self-directed IRA can be costly if not properly managed. In addition, because of the types of investments taxpayers with self-directed IRAs are able to make, taxpayers have a greater risk of running afoul of the prohibited transaction rules. The prohibited transaction rules impose an excise tax on certain transactions - such as sales of property, the lending of money or extension of credit, or the furnishing of goods, services, or facilities - between an IRA and a disqualified person. If you have a self-directed IRA, we need to review the specifics of your arrangement.

Estate/Gift Tax Considerations

Annual Exclusion

There is still time to reduce your estate by gifting amounts to relatives or friends, free of the gift tax that normally applies. For 2014, the annual gift tax exclusion amount is $14,000 per individual. You may give this amount to as many individuals as you would like without the giver incurring a tax penalty or having to report the gift.

Other Steps to Consider Before the End of the Year

The following are some of the additional actions we should review before year end to see if they make sense in your situation. The focus should not be entirely on tax savings. These strategies should be adopted only if they make sense in the context of your total financial picture.

Accelerating Income into 2014

Depending on your projected income for 2015, it may make sense to accelerate income into 2014 if you expect 2015 income to be significantly higher. Options for accelerating income include:

(1) harvesting gains from your investment portfolio;

(2) if you own a traditional IRA or a SEP IRA, converting it into a Roth IRA and recognizing the conversion income this year;

(3) taking IRA distributions this year rather than next year;

(4) selling stocks or other assets with taxable gains this year;

(5) if you are self-employed with receivables on hand, trying to get clients or customers to pay before year end; and

(6) settling lawsuits or insurance claims that will generate income this year.

Deferring Income into 2015

There are also scenarios (for example, if you think that your income will decrease substantially next year) in which it might make sense to defer income into the 2015 tax year or later years. Some options for deferring income include:

(1) if you are due a year-end bonus, asking your employer to pay the bonus in January 2015;

(2) if you are considering selling assets that will generate a gain, postponing the sale until 2015;

(3) delaying the exercise of any stock options you may have;

(4) if you are selling property, considering an installment sale;

(5) consider parking investments in deferred annuities;

(6) establishing an IRA, if you are within certain income requirements; and

(7) if your employer has a 401(k) plan, consider putting the maximum salary allowed into it before year end.

Deferring Deductions into 2015

If you anticipate a substantial increase in taxable income, we may want to explore deferring deductions into 2015 by looking at the following:

(1) postponing year-end charitable contributions, property tax payments, and medical and dental expense payments, to the extent you might get a deduction for such payments, until next year; and

(2) postponing the sale of any loss-generating property.

Accelerating Deductions into 2014

If you expect your income to decrease next year, accelerating deductions into the current we can into the current year to offset the higher income this year. Some options include:

(1) consider prepaying your property taxes in December;

(2) consider making your January mortgage payment in December;

(3) if you owe state income taxes, consider making up any shortfall in December rather than waiting until your return is due;

(4) since medical expenses are deductible only to the extent they exceed 10 percent (7.5 percent if you or your spouse are 65 before the end of the year) of your adjusted gross income (AGI), if you have large medical bills not covered by insurance, bunching them into one year may help overcome this threshold;

(5) making any large charitable contributions in 2014, rather than 2015;

(6) selling some or all of your loss stocks; and

(7) if you qualify for a health savings account, consider setting one up and making the maximum contribution allowable.

Life Events

Certain life events can also affect your tax situation. If you've gotten married or divorced, had a birth or death in the family, lost or changed jobs, retired during the year, we need to discuss

the tax implications of these events.

Miscellaneous Items

Finally, these are some additional miscellaneous items to consider:

(1) If you have a health flexible spending account with a balance, remember to spend it before year end (unless your employer allows you to go until March 15, 2015, in which case you'll have until then).

(2) If you own a vacation home that you rented out, we need to look at the number of days it was used for business versus pleasure to see if there is anything we can do to maximize tax savings with respect to that property. For example, if you spent less than 14 days at the home, it may make sense to spend a few more days and have the house qualify as a second residence, with the interest being deductible. For a rental home, rental expenses, including interest, are limited to rental income.

(3) We should also consider if there is any income that could be shifted to a child so that the income is paid at the child's rate.

(4) If you have any foreign assets, there are reporting and filing requirements with respect to those assets. Noncompliance carries stiff penalties.

Please call me or email me if you have any questions concerning this memo.

Regards,

Charles A. Kerner