Goldburd & Co. LLP
Certified Public Accountants

TAX TALK

Winter 2014

It's that time of year where we should think about preparing an estimate of your current year tax liability or calculate the expected taxable income or loss of your business and determine if there is anything we can do before the end of the year to mitigate or reduce any potential tax liability for 2014.

Individuals

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.

With respect to expiring provisions, many taxpayer-favorable provisions expired at the end of 2013. Congressional gridlock has prevented these provisions, known as the "tax extenders," from being enacted into law for 2014. Earlier this year, the Senate Finance Committee passed the Expiring Provisions Improvement Reform and Efficiency (EXPIRE) Bill of 2014, which would extend a number of these expired provisions to 2014 and 2015. Alternatively, any movement on the Bill may not come until 2015. Congress has been known to pass legislation in a tax year after the year to which the legislation applies and make that legislation retroactive. The 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 and other school professionals a $250 above-the-line tax deduction in 2014 and 2015 for expenses paid or incurred for books, supplies (other than non-athletic supplies for courses of instruction in health or physical education), computer equipment (including related software and service), other equipment, and supplementary materials used by the educator in the classroom.

(2) *Mortgage debt forgiveness* - 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 2015.

(3) *Increased exclusion from income for employer-provided mass transit and parking benefits* - This provision would increase, for 2014 and 2015, 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. The provision also modifies the definition of qualified bicycle commuting reimbursement to include expenses associated with the use of a bike sharing program.

(4) *Deduction for mortgage interest premiums* - Under this provision, for 2014 and 2015, taxpayers would be able to deduct the cost of mortgage insurance on a qualified personal residence. The deduction would be phased-out ratably by 10 percent for each $1,000 by which adjusted gross income (AGI) exceeds $100,000. Thus, the deduction would be unavailable for a taxpayer with an AGI in excess of $110,000.

(5) *Deduction for state and local general sales taxes* - This provision would extend for two years 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) *Special rules for contributions of capital gain real property made for conservation purposes* - This provision would extend for two years the increased contribution limits and carry-forward period for contributions of appreciated real property (including partial interests in real property) for conservation purposes.

(7) *Above-the-line deduction for higher education expenses* - This provision would extend an above-the-line tax deduction for qualified higher education expenses. The maximum deduction, for 2014 and 2015, 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).

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(8) *Tax-free distributions from individual retirement plan for charitable purposes* – Although this provision expired on December 31, 2013, chances are high that Congress will resurrect it retroactively before year-end. This provision would allow an individual retirement arrangement (IRA) owner who is age 70-1/2 or older generally to exclude from gross income up to $100,000 for 2014 and 2015 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 top tax rate of 39.6 percent increased from the 2013 amounts to $457,600 (married filing jointly), $406,750 (single individuals), $432,200 (head of household) and $228,800 (married filing separately).

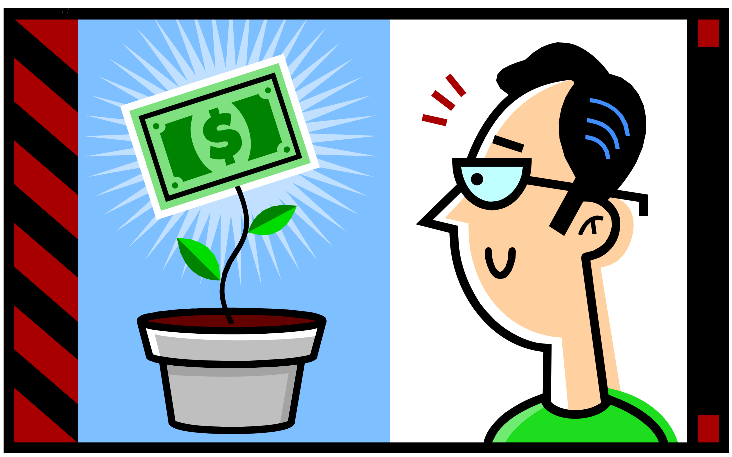
Net Investment Income Tax
The net investment income tax is a 3.8 percent tax on net investment income that took effect in 2013. Besides applying to investment income, the tax also applies to income from trades or businesses of the taxpayer that are passive activities. An activity is not generally considered passive if the taxpayer materially participates. If you are engaged in an activity which may be considered passive and thus has the potential to trigger the net investment income tax, we should evaluate the seven factors that determine material participation to see if your business can escape the net investment income tax.

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) or 1% of income, whichever is higher. In some situations, the amounts of these penalties will increase in 2015. 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 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, a 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.



Self-Employed Considerations
If you are self-employed and your business has shown losses for the past several years, there is a danger that the IRS will consider your business a hobby and disallow deductions in excess of revenue. If you are in this situation, there are certain steps we can take to mitigate this potential. For example, we can ensure there is appropriate documentation as to the business-like manner in which the business is carried on, including the adoption of new techniques or the abandonment of unprofitable methods.

The IRS has issued new rules on the capitalization and expensing of tangible property used in a trade or business. If tangible property is a part of your business, these rules will most likely impact your current year taxes and may require certain actions by year-end. For example, if you acquired numerous small dollar items, a de minimis safe harbor rule may apply to allow you to deduct all items below a certain threshold. Or, if you incurred significant repair and maintenance costs for heavy machinery, a routine maintenance safe harbor may be used to increase current deductions.

S Corporation Shareholders

See S Corporations below in the Businesses section.

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, you can gift up to $14,000 to each donee.

Charitable Remainder Trusts

If you are in the top tax bracket, have appreciated assets that would be subject to capital gains tax if sold, and would like to make a significant gift to a favorite charity while reducing estate or gift taxes, you may want to think about utilizing a charitable remainder trust (CRT). A CRT, which has an income interest part and a remainder interest part, can allow you to sell appreciated assets tax free, while providing you with a current income tax deduction that can offset all forms of income in addition to providing a charity with a substantial donation. Please let us know if you would like more information on this option.

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 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, we may want to accelerate deductions 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.

Businesses

This year saw numerous tax developments that affect businesses, many of which deserve special scrutiny for year-end planning in an effort to minimize your 2014 tax bill.

Perhaps the biggest development for businesses in 2014 that doesn't require guesswork, and which may require certain actions before December 31, is the IRS's overhaul of the tangible property rules. These rules affect any business that owns property and may require some modifications to your fixed asset policies so that you can take advantage of, and even comply with, the new rules. Depending on your current policies, refunds may be available for prior years.

Tangible Property Rules

Safe Harbor Election for Expensing Items
One of the more favorable rules in the tangible property regulations is the $5,000 de minimis safe harbor election for expensing an item rather than capitalizing it. In order to take advantage of this election, you must have had written accounting procedures in place at the beginning of the year and have been following those rules for book and tax accounting purposes. If such procedures were in place at the beginning of 2012 or 2013, the election can be made for these years as well but will require amended returns. If you did not have such procedures in place, it's not too late to put implement them for 2015, but it must be done by the end of this year.

In addition, you must have an applicable financial statement (AFS) to rely on the $5,000 de minimus safe harbor. If you do not have an AFS, you may rely on the de minimis safe harbor only if the amount paid for property does not exceed $500 per invoice, or per item as substantiated by the invoice. If the cost exceeds $500 per invoice (or item), then you cannot use the de minimis safe harbor. Alternatively, if you do not qualify for the $5,000 safe harbor, you may still be able to deduct amounts over $500 or even over $5,000, if you have a written policy in place, follow it for book purposes, and can prove that it meets materiality thresholds. Various types of statements qualify as an AFS so if you don't currently have an AFS, we should evaluate whether one of the available options will work for your business.

Finally, the de minimis rule also applies to amounts paid for property having a useful life less than a certain period of time.

Partial Disposition Election
Another favorable item in the final property regulations that may save you some money this year is the partial disposition election. While initially the election could only be made for tax years beginning before January 1, 2014, the IRS recently extended the time frame to any tax year beginning before January 1, 2015. Using this election, you can claim a loss on the disposition of a structural component of a building or on the disposition of a component of any other asset without needing to make a general asset account election. The partial disposition rule also minimizes circumstances in which an original part and any subsequent replacements of the same part must be simultaneously capitalized and depreciated. Thus, for example, if you replaced an engine in a truck, you would generally continue to depreciate the old engine as part of the truck while also depreciating the new engine. Under the partial disposition rule, you can now retire the old engine and recognize a loss on that disposition.

Deductions Available for Rehabilitation of Buildings and other Property
The final rules contain a routine maintenance safe harbor that allows the expensing, rather than capitalizing, of costs of performing certain routine maintenance activities for buildings or the structural components, as well as other property. If you

have done any such maintenance this year or plan to do so next year, we should discuss whether the maintenance falls under the "routine" safe harbor and review any changes to maintenance routines going forward to ensure that such costs qualify for immediate expensing.

Deductible Repair and Maintenance Expenses

Under the new tangible property rules, certain repair and maintenance expenses that were previously capitalized can now be expensed. For prior years, this will require amended returns and making certain retroactive elections. Depending on your current tax situation, we should run the numbers to see if amended returns make sense.

Bonus Depreciation

Although bonus depreciation is not currently available for 2014, there is a good possibility it will return. While the likelihood of bonus depreciation being available for 2014 depends on the "tax extenders" bill (i.e., the EXPIRE bill) being passed and signed into law, many politicians have a vested interest in seeing this bill come to fruition. The drawback is that we may not know until late 2014 or even early 2015 whether purchases in 2014 will qualify for the bonus depreciation or what amounts will qualify. On the assumption that the bill passes as written, the 50-percent additional first-year depreciation deduction in effect in 2013 will be extended to qualified property purchased and placed in service before 2016 or before 2017 for certain longer-lived and transportation assets.

Section 179 Deduction

The Section 179 deduction, which allows current expensing of items normally capitalized and depreciated, is also in limbo until the fate of the tax extenders bill is known. Unlike the bonus depreciation, however, there is a limit on the amount that may be expensed and the business must have taxable income to take advantage of this deduction. If the bonus depreciation and Section 179 deduction are passed, we need to evaluate whether it may make more sense to spread these deductions over the life of the property by electing out of these provisions. Currently, for taxable years beginning in 2014 and thereafter, your business may immediately expense up to $25,000 of Section 179 property annually, with a dollar for dollar phase-out of the maximum deductible amount for purchases in excess of $200,000. If the EXPIRE bill becomes law, it would increase the maximum amount and phase-out threshold in 2014 and 2015 to the levels in effect in 2010 through 2013 ($500,000 and $2 million respectively). The law would also extend the definition of Section 179 property to include computer software and $250,000 of the cost of qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property.

Research Tax Credit

Perhaps one of the most popular provisions in the tax extenders bill on both sides of the aisle is the extension of the research tax credit through 2015. It is almost a given that if any provision gets extended, this one will. Additionally, the EXPIRE bill would allow qualifying startup businesses to claim unused credits against their payroll tax after applying the credit to income tax liability. And, it is worth noting that, in 2014, two taxpayer-favorable court cases rejected IRS attempts to rein in taxpayers' ability to take full advantage of this credit. If you've taken research tax credits in the past couple of years, it may be worthwhile to review the calculation of those credits in light of these cases to see if additional expenses can be claimed based on the court holdings.

S Corporations

In 2014, the IRS loosened the rules relating to S corporation shareholder debt. Under the new rules, it is easier for such debt to give the shareholder basis against which to deduct losses coming from the S corporation. The rules generally eliminated the "actual economic outlay" doctrine replacing it with a clearer "bona fide debt" requirement, and made the changes retroactive. Thus, if a shareholder previously could not deduct losses because the actual economic outlay doctrine wasn't met, amended returns may be in order.

Real Estate Developers

For real estate developers, two court cases this year drew a bright line between the type of contracts that will qualify as home construction contracts eligible for the completed contract method and those that will not. As a result of the decisions in these cases, one pro-taxpayer and one pro-IRS, it is worth taking a second look at whether the method being used to account for income from such contracts can be reported under the completed contract method.

Affordable Care Act ('Obamacare')

The Affordable Care Act includes several provisions that may affect you as an employer, including the shared responsibility provisions, also known as the "employer mandate." Under the employer mandate, which is effective January 1, 2015, a penalty is imposed on certain large employers that do not offer health insurance coverage, offer health insurance coverage that is unaffordable, or offer health insurance coverage that consists of a plan under which the plan's share of the total allowed cost of benefits is less than 60 percent.

It is important to note that this provision only applies to an employer who employed an average of at least 50 full-time employees on business days in the preceding calendar year.

Additionally, subject to certain requirements, no employer shared responsibility payments will apply during 2015 for employers with fewer than 100 full-time employees.

The penalty is assessed for any month in which a full-time employee is certified to the employer as having purchased health insurance through an Exchange with respect to which a premium tax credit or cost-sharing reduction is allowed or paid to the employee. However, it is worth noting that currently there are multiple ongoing court battles over whether insurance purchased on a federally established Exchange qualifies for the subsidies, which then triggers the tax on the employer. The issue will most likely not be resolved until sometime later next year.

Small Employer Credit

With respect to health insurance, your business may be eligible for a credit for contributions to purchase health insurance for employees. The amount of the credit increased this year to 50 percent (35 percent for tax-exempt organizations) of premiums paid. The tax credit is subject to a reduction if you have more than 10 full-time employees or if average annual full-time employee wages exceed $25,000.

Mass Transit Benefits

If you subsidize your employee's commuting expenses, there is an item in the EXPIRE Bill which could affect your business. The provision would increase, for 2014 and 2015, 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. In order for the extension to be effective retroactive to January 1, 2014, employers may reimburse expenses incurred by employees before enactment for vanpool and transit benefits on a tax-free basis to the extent the expenses exceed $130 per month and are not more than $250. The Bill also modifies the definition of qualified bicycle commuting reimbursement to include expenses associated with the use of a bike sharing program for two years. Thus, the benefits that are excludible from income will not be includible in the employee's income on Form W-2 and are deductible by employers as fringe benefits.

Give us a call

All of the tax opportunities and considerations at this time of year can be a lot to remember, and the details of all these provisions can make it even more complicated. Fortunately, you won't have to remember all of them by yourself – that is why you hired us. The two most important pieces of tax advice for any year are to keep good records and ask questions. We look forward to hearing from you.

If you are projected to owe additional income tax, a tax projection can help determine which tax-minimizing strategies should be used before the end of the year to reduce or eliminate any tax due. If you are due a refund, we can ensure your tax return is filed as early as possible to allow you to receive your refund and enjoy your money more quickly.

If you need additional information on any of the above items or wish to speak with us directly about your tax picture for 2014, please do not hesitate to contact us at (212) 302-8970.

In addition, if you feel that your friends or business associates could benefit from this newsletter, please feel free to pass it on to them.

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