

MAKING YOUR LIST, AND CHECKING IT TWICE

On January 1, 2013, various changes in the tax code took effect, so you will want to approach your tax planning with considerable care this year. The changes include those that are meant to help pay for the Affordable Care Act (ACA) and to address the fiscal cliff.

Please give a call if you need a tax advisor for the tax-specific topics or contribution limit items below. I have a couple of good resources to whom I can refer you.

RETIREMENT PLAN CONTRIBUTIONS

Seek to maximize your retirement plan contributions. As you are likely aware, contributions can reduce your overall tax burden, and allows for tax-deferred growth of these assets.

- *401(k) Contributions*

In most cases it is necessary to fully fund these accounts **by December 31**.

- The maximum salary deferral limit for 401(k), 403(b), and 457 plans in 2013 is \$17,500.
- If age 50 or older, you may contribute an additional \$5,500 per year under these plans (a total of \$23,000).

- *Self-employed Retirement Plan Options*

If you have no employees, the primary difference among various plan options is the contribution limit for each (see appendix) If you want to set up a retirement plan, I strongly recommended that you consult with a tax professional. In most circumstances you can contribute more — sometimes much more — to an individual 401(k) than you could contribute to a SEP IRA or SIMPLE IRA. However, there are other factors to consider, including reporting requirements and non-discrimination features.

IRA CONTRIBUTIONS

Contribution limits and/or tax deductibility may be limited based on various factors including income level and contributions to other retirement plans (see above.) Make sure to consult with your tax advisor.

- The maximum contribution amount for both Traditional IRAs and Roth IRAs is \$5,500 for 2013 (subject to eligibility requirements). Contributions may be made **until Monday April 15, 2014** and still be counted for the 2013 tax year.
- Individuals age 50 and over are eligible to make an additional \$1,000 catch-up contribution.

IRA REQUIRED MINIMUM DISTRIBUTIONS (RMDs)

- All of the following must complete the required withdrawals **by December 31**:
 - IRA owners who turned 70 ½ prior to 2013.
 - IRA owners receiving 72(t) distributions, and/or
 - IRA owners receiving “Inherited / Beneficiary IRA” distributions.

Failure to meet the IRS requirements may result in a significant penalty. The custodian of your accounts should contact you regarding RMDs. Contact your investment advisor if you have questions.

BENEFICIARY DESIGNATIONS

- Review beneficiary designations for IRAs, qualified plans, and life insurance policies. Life changes (birth, death, divorce) may require modifications to beneficiary designations. The beneficiary designations on these accounts should generally be living people, and not an estate or trust, and should include primary and contingent beneficiaries.
- Please note that the distribution is determined by the beneficiary form, **not by the individual's will**.

ROTH CONVERSIONS

- Taxpayers should also consider the option of converting a Traditional Individual Retirement Account (IRA) into a Roth IRA. Income limitations that had previously prohibited high-income individuals (those with an adjusted gross income over \$100,000) from converting to a Roth are now suspended.
- Advantages to a Roth IRA include no required minimum distributions during the owner's lifetime and of course, tax-free investment growth (if distributions satisfy the "five-year holding period" criterion. However, the conversion will qualify as a "taxable event" in the year it occurs.

EDUCATION FUNDING

- Contributions made to a 529 College Savings plan **by December 31**, sponsored by your state of residency, may be eligible for a state income tax deduction or credit.

CAPITAL GAINS / LOSSES

- *Tax Loss Carry Forward* - As a result of stock market volatility from October 2007 – March 2008, many investors continue have unused capital loss carry-forward. Given the increased tax rates, these capital loss carryovers should be viewed collectively as an asset. Consult with your tax advisor and investment advisor to determine how you can use this asset.
- *Long-term Capital Gains* - Congress increased the 15% long-term capital gains rate to 20% **for high-income earners** (singles with a taxable income above \$400,000 and couples above \$450,000).
- *Short-term Capital Gains* - Investment held less than a year will continue to be taxed at the ordinary income tax rate. Consult with your investment advisor to determine if you **can shift less-tax-efficient investments into tax advantaged accounts**, allowing assets to grow tax deferred.

PORTFOLIO INCOME

- While there isn't much you can do to change the timing of interest or dividend payments from bonds and equity investments, you can increase the likelihood of a greater rate of return by having a tax-efficient portfolio. Ways of doing this include realigning your personal portfolio to shifting less-tax-efficient investments into retirement accounts, where the assets will grow tax deferred.

3.8% MEDICARE SURTAX ON NET INVESTMENT INCOME

- Another aspect of healthcare reform is the **3.8% Medicare surtax that begins this year**. The calculation is dependent on 2 components – the taxpayer's modified AGI (above \$200,000; and for couples \$250,000 (\$125,000 for separate filers) and net investment income. The tax will be levied on the smaller of the filer's net investment income or the excess of modified AGI over the applicable dollar threshold. Consult your tax professional for additional information.

MUTUAL FUNDS

- Be cautious about buying mutual fund shares in a taxable account toward the end of the year. Many funds distribute their taxable gains for the year in December. It is important to avoid creating a tax liability on a year's worth of gains on an investment held for only a few days.

CHARITABLE GIFTING

- **2013 is the final year** in which IRA accounts owners over age 70 1/2 can make non-reportable direct transfers from IRA accounts to charity. Direct transfers are not included in adjusted gross income, and therefore reduce AGI and have the potential to increase deductions.
- If you are planning to make a charitable donation this year there may be options, including gifting securities, available to maximize the tax benefit to you and the non-profit organization whose cause you wish to support; donations **must be mailed by 12/31** to qualify for a 2013 deduction.
- The estate and gift tax exemption for 2013 increases to \$5.25 million during one's lifetime, however the tax rate jumps to over 40% for amounts above this threshold.
- In 2013, **up to \$14,000 in cash or securities** can be given to any other individual free of federal gift tax; the gift must be completed (i.e. deposited) by December 31st, 2013. Direct payments of tuition or medical expenses are not included in the \$14,000 limit.

APPENDIX

- *Self-employed Retirement Plan Options*

If you have no employees, the primary difference between the plan options below is the contribution limit for each. There are a number of options, which I have included in the Appendix.

- *SEP IRA* - An individual with a simplified employee pension individual retirement account (SEP-IRA) may be eligible to make a contribution up to the lesser of \$51,000 or 20% of net self-employment income after reducing for the deductible portion of the self-employment tax.
- *Simple IRA* - An employee contribution equal to 100% of your net earnings from self-employment, up to \$12,000 for 2013 (\$14,500 if you are 50 or over), plus an employer contribution equal to 3% of your business's net profit after reducing for the deductible portion of the self-employment tax.
- *Individual 401(k)* - An employee contribution of 100% of your net earnings from self-employment, up to \$17,500 (\$23,000 if you are 50 or over), plus an employer contribution of 25% of your net earnings from self-employment.

The conclusion? In most circumstances you can contribute more — sometimes much more — to an individual 401(k) than you could contribute to a SEP IRA or SIMPLE IRA.

If you have employees and you want to set up a retirement plan for your business, I strongly recommended that you consult with a tax professional. There are additional factors to consider when establishing a plan, including the reporting requirements and non-discrimination features.