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THE STRAUSS REPORT

Fall 2013

FALL 2013: Fall is Tax Planning Time.....

While no new tax bills were passed since The American Taxpayer Relief Act of 2012 (at the start of 2013), the many changes from this new law as well as those from the Patient Protection and Affordable Care Act (AKA Obamacare) could (and have already had) a **major** impact on your 2013 taxes. Many taxpayers (given summer vacations, the start of the school year and just generally busy times for all of us) may not be aware of the steps they should take between now and the end of the year to lower 2013 taxes and collect tax data needed for next year's returns.

In this issue of **The Strauss Report**, we will review the tax changes in effect for 2013 and suggest year end tax saving strategies to save you money. In addition, we will review several important tax issues: rolling over an IRA to a Roth, medical expenses, cost basis for sales of capital assets as well as inheritances, what happens after a loved one passes on and as well as the increased likelihood of an IRS or IL notice with their stepped up compliance measures.

What we know right now:

1. **Rate Shock** has hit all of us in some way. Here is the comparison:

	2012	2013
Top Income Tax Rate	35%	39.6%
Top LT Capital Gains Rate	15%	20%
Top Rate on Qual. Dividends	15%	20%
Social Security Tax Rate	4.2%	6.2%
Top Estate/Gift Tax Rate	35%	40%

The "increase" in **Social Security** withholding back to 6.2% has impacted everyone who works, with a lot less take home pay since January 1. That, combined with the IL tax at 5% - and as we will discuss later - the increases in medical insurance - keeps taking a bigger chunk of our income, with little, if any of a raise in wages.

2. **Other Tax Provisions - new for 2013 -** mostly for higher income taxpayers:
   - a. **3.8% Medicare tax surtax** on **investment** income for MJ Adjusted Gross income over $250,000 and Single over $200,000
   - b. **.09% Medicare tax surtax** on **Wage** income for MJ over $250,000 and Single over $200,000
   - c. **3% phase out of itemized deductions** - begins at Adjusted Gross Income of $300,000/Married and $250,000/Single
   - d. **Phase out of Personal exemptions** - begins at same income levels above- and can phase out all exemptions at higher income levels
3. **Tax Provisions which could "hit" all of us:**
   - **Medical expense** deductions - now over 10% of AGI if under 65; stays at 7 1/2% for those older than 65 until 2017.
   - **Energy Credits** are mostly gone- only 10% of the amount spent on windows, doors, water heaters, furnaces and air conditions - but only with high energy efficiency (check out www.energystar.gov) - and with a lifetime maximum of $500 - and only if you have not used more than that amount in prior years.
   - Paying in to **flexible spending accounts** at your employer has been capped at $2,500 per

year.

- **Limitations** (based on Adjusted Gross Income) for the Child Credit, child care credit, and all education credits.

4. So is there any good news? Yes.

- The tax rates for ordinary income (wages, interest, IRAs and pensions) remained the same for most of us as in prior years.
- The tax rates for qualified dividends and Long term capital gains (0% and 15%) remain the same for most of us as in prior years.
- The formula for taxable Social Security (50% and 85% taxable for "higher" incomes) did not change.
- Most of us will not pay more tax unless our incomes increase.

So What can I/we still do this fall?

- **Make Your Deductions Count.** Many more taxpayers are itemizing their deductions due to substantially increased **medical costs** coupled with lower adjusted gross income. Medical costs include: out of pocket insurance costs (Medicare, COBRA, long term care insurance and retiree medical withheld from your pension); deductibles; doctor and increasingly major dental bills; lab fees; all eye care costs, prescription and doctor ordered drugs; medical travel, parking and lodging; hearing aids and batteries; and nursing home fees that **qualify as medical expenses**. If you pay an in-home caregiver and have a physician's letter stating the care is medically necessary, you may deduct these costs, so long as you are paying an agency or the caregiver will receive a 1099MISC from you (so their income is reported to the IRS) and is not paid in cash.

  In addition, with the cap of $2,500 on pretax medical Section 125 plans at your employer, you may pay a lot more out of pocket. These **pre-tax accounts**, which previously had no federal limit, are used to purchase everything from contact lenses to children's braces. With the cost of braces being as high as $7,200, this tax provision will play an unwelcome role in everyday kitchen-table health care decisions. Your employer's insurance may also now have a much higher deductible and co-pay and you should review your out of pocket medical expenses now to see whether you might prepay big ticket items or schedule elective medical before the end of the year. **Open Enrollment Season is in the fall for most employers** – so now is a good time to review your 2013 (and possibly 2014) medical and dental costs - so you can put money away **pretax** during the upcoming enrollment period.

Other provisions of the Affordable Health Care Act in place now or coming soon are:

1. More young adults with insurance. All health plans must allow young adults to remain as dependents on their parent's health plan until they turn 26, whether or not they live at home or can be declared as dependents on the parent's income tax return. An estimated 6.6 million young adults who would otherwise be uninsured have gained coverage during the first year of eligibility, according to a recent analysis by the Commonwealth Fund, a nonprofit health policy research organization.

2. Cheaper drugs for people on Medicare. Seniors who reach the "donut hole" – the point when they have to start paying prescription drug expenses themselves – now get a 52.5 percent discount when buying brand-name drugs and a 21 percent discount on generic drugs covered by Medicare Part D. As of March 2013, more than 6.3 million older adults and people with disabilities had saved $6.1 billion in prescription costs since the law was passed. The donut hole will continue to shrink until it disappears completely by 2020. Also, prescriptions drug premiums may drop a bit next year, depending on your plan.

We have been getting lots of calls on how the provisions of the Affordable Health Care Act and the new health exchanges will work. First, if you are on Medicare, you can ignore the fuss. Second, if you have questions, call us for your copy of an excellent article on A Guide to the New Health Care Exchanges published by The New York Times recently.

Finally, you should also review your company medical plan (if any) with other supplemental insurance plans. Many companies have or will stop offering group health insurance by 2014 to retirees (citing health care reform changes), replacing them with new "pre tax health insurance arrangements" that can be used to buy supplemental medical insurance. In addition, many companies have substantially increased your share of medical insurance premiums so comparing your and your spouse's plan to see which is better for your family is a good idea.

- **Check your 401K contributions and your allocations**. The maximum contribution for 2013 is $17,500 and $23,000 for those of us over 50. Many employers still have some sort of matching program so if you are not at least contributing pre–tax the amount up to the employer contribution, you are losing free money. In addition, for many of us our 401K will be our major source of retirement income, so if you don't save systematically and invest carefully, you may wind up working way longer than you planned, just to have enough money for daily living and increased medical expenses.

- **Review Capital gains and Stock or Mutual Fund sales**. Many taxpayers sell stocks or mutual funds and wait until tax time to determine gain or loss. This can create a problem since we need the **basis** as well as the selling price to determine if you made a profit. Determination of basis can be tricky since it often includes one or more purchases, splits, spin offs, reinvested dividends, date of death values and records which are incomplete. You may need year-end statements and/or prior tax returns – or we may have to do research. The broker sends a 1099B reporting the gross sale (and basis if bought after January 1, 2011 - before that it is still your responsibility) to the IRS. Sometimes, mutual fund companies or brokers provide complete information with your year-end or tax reporting statement, but it is best not to wait to find out.

  We suggest that if you have sold a capital asset that we work with you to compute gain or loss now. This can assist you in tax planning - selling other assets at a loss to balance a gain or determining the tax consequences of a gain or loss.

- **Check your Will or Trust - or have one made now!**
  The Federal system has been overhauled, with a top rate of 40% and an exemption of $5.25 million for estate taxes. In addition, any applicable exclusion amount that remains unused as of the death of a spouse who dies after December 31, 2010, generally is available for use by the surviving spouse, as an addition to such surviving spouse's applicable exclusion amount. The annual exclusion for tax-free gifts is $14,000 per donor. A person may make an unlimited number of $14,000 gifts, so long as they are to different individuals. Gifts of tuition and payments for medical care are exempt from these limits. In IL, the Estate Tax exclusion is now $4 million for 2013 and thereafter.

JUDI STRAUSS IN PRINT, ON MEDIA

Our Website - www.strausstax.com continues to offer tax tips and immediate tax update alerts when new legislation is passed - as well as workshop dates. **We also have a Facebook page** and are posting updates and links to important articles on taxes and investing and retirement planning real time. You can both find us online and "like " us (and suggest it to your Facebook contacts - and even your adult children - as well). Judi is now the tax and financial expert for Life Matters Media (www.lifemattersmedia.org), discussing important end of life tax and financial issues.

In January 2014, Judi will be offering her annual "Tax Update" workshop on the following Tuesdays: January 14 at the Downers Grove Public Library, January 21 at the Woodridge Public Library and January 28 at the Lisle Public Library - all at 7PM.

TAX and FINANCIAL TIDBITS...

1. **Don't forget your Required Minimum IRA Distribution (MRD) for 2013.** You can donate directly from your IRA to a charity this year - generally a good tax saving strategy. You should also review your IRA beneficiaries - we are finding that there can be problems after death if the beneficiary is your trust or one or more of the beneficiaries cannot be located.
2. **Continue to be very careful about identity theft.** The IRS is paying out billions of dollars in fraudulent tax refunds to identity thieves who steal identities of taxpayers, file bogus returns and collect fraudulent refunds. The inspector general estimates that the IRS could issue as much as $21 billion in fraudulent tax refunds over the next five years. Strauss Tax Service assures you that your identity is protected; your personal information is secure in our office and is never released to others without your permission.
3. **You - and - we are seeing many more letters from both the IRS and IL** - whether asking for penalties or checking unreported income or auditing deductions. Call or email us if you get a letter or notice and we will review, explain and tell you what to do - or what we can do.

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4. **Roth rollovers** (from your IRA or 401K) are available to all of us in 2013- but you must pay all the tax on your 2013 tax return. You can also change your mind at tax time - and "recharacterize" – up until the tax deadline. Call us to review if this is a good idea for you.
5. Many people are asking if their **home sale** - principal residence or vacation home is tax free. Call us for our home sale question and answer worksheet.
6. **When someone passes on**, there is a lot of tax work to do. We recommend that if you are the Executor or Trustee, we review the steps that need to be taken immediately after death and help you carefully and successfully complete the required tax filings and communication with beneficiaries, asset companies, employers and the IRS. We work with you and your attorney to answer questions, prepare required tax filings and complete paperwork so as to minimize future problems. Call for our **Estate Check-off list** or our **Questions and Answers about Estates and Trusts.**
7. Mileage rates are: 24 cents/mile for medical; 56.5 cents/mile for business and still 14 cents/mile for charity.

Judi Strauss