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THE STRAUSS REPORT

Summer 2015

Summer has finally arrived but taxes are as uncertain as ever!

The 2015 filing season was extremely stressful and complicated – thanks to the drastic reductions in the IRS budget (by $1.2 billion since 2010), the expense of more than $1.2 billion to implement the new health care law and the total reduction of IRS customer service. The IRS overloaded phone system hung up on more than eight million taxpayers this filing season - and only 40% actually got through to a person. (On our special Professional Line, waits of over 1-2 hours were not uncommon!) In addition, the continued headache of identity theft - stealing your Social Security number and filing bogus tax returns - and scammers pretending to be the IRS and calling to demand immediate tax payments continues to worry both you - and us. And finally, many of us owed both the IRS and IL in 2015 due to the unexpected large capital gains distributions from mutual funds at the end of 2014. Now you (and we) are facing the sad fact that the "extenders" passed by Congress at the very end of 2014 have indeed expired once again and while Congress talks of reforming and stabilizing - and hopefully simplifying the tax code, our tax policies have not been significantly overhauled since the Reagan Administration in 1986 - before many of us were born!

In this issue of **The Strauss Report**, we will review what we know now: on changes and tax saving measures in place for 2015, the tax laws that that are in limbo once again, on the cost basis requirements when you sell a stock or mutual fund, on required IRA distributions and the Medicare and investment surtaxes. We will also answer questions we get on identity theft, home sales, Required Minimum Distributions, gift and estate taxes, inheritances and medical expenses. And, we will begin to address the big questions in IL with our budget crisis and the divided government: will the new 3.75% lower rate become permanent; will IL tax rates become graduated; will services like haircuts (and pet grooming and lawn care) be subject to sales tax, or will we be taxed on retirement income.

2015: What's in...

- The **low income tax rates** both for ordinary income and for qualified dividends and long term capital gains are now permanent for most of us. This includes the 0% rate on investment income for taxpayers in the 15% bracket and the 15% rate for those with taxable income below $413,200 Single and $464,850 Married Joint. For those taxpayers, the marginal rate increases on ordinary income to 39.6% and to 20% on dividends and long term capital gains. For Trusts and estates, the higher rate begins at $13,150.
- The **new 3.8% tax on investment income** from the health care bill is on dividends, interest and capital gains (but not tax-free municipal bond interest) - on income over $250,000 for Married joint and $200,000 for Singles - and the same $12,150 for trusts and estates.
- **An additional .009 Medicare tax** will be levied on those taxpayers with greater than $200,000 earned income - Single and $250,000 Married joint (combined income),
- The **Marriage Penalty Relief** (so the brackets are double that for singles) has been made permanent.
- **Education Credits - American Opportunity and Lifetime Learning** (up to $2,500) and the deduction for student loan interest. There are income limitations for both of these.
- The $**1000 per child credit** until age 17 (phased out at higher incomes) is made permanent.
- **Limitations on Itemized Deductions and Personal Exemption**s are back, with those messy worksheets - when Adjusted Gross Income exceeds $258,250 Singles and $309,900 for Married Joint. This is huge and can wipe out exemptions completely for higher income taxpayers.
- The **floor for the Medical expense deduction** is now 10% if you are under 65; it stays at 7 1/2% for those older than 65 until 2017.

<u>What's Expired as of December 31, 2014 - and Uncertain Once Again for 2015</u>....

- Deduction for State and local Sales taxes - if you itemize
- Classroom teacher expense deduction ($250)
- Tuition deduction - on Page 1 of the 1040
- Tax-free distributions from IRAs donated to charities
- Energy credits
- Deductions for mortgage insurance premiums deductible as qualified interest

The 5% rate for IL expired on December 31, 2014. The 2015 personal tax rate is 3.75%. It is projected that this decrease will result in $2 billion less revenue for the Fiscal year 2014-5 and an additional $3 billion less in the Fiscal year 2015-6 when the full effect of this reduced rate will be felt. This is more than the sum of all General Fund appropriations for Human Services scheduled for the FY 2015 which is $4.8 billion. Governor Rauner's new state budget includes the above extending of sales taxes to consumer (but not professional) services as well as draconian cuts in services that benefit the middle class and the poor, including:

1. 31.5% cut to higher education/universities
2. Slashing funding for the Department of Children and Family Services.
3. Eliminating all Department of Children and Family services for youths 18-21.
4. $27.5 million in reductions to community substance abuse programs.
5. $82 million reduction to community mental health programs
6. Moving state employees - most of whom make middle class salaries or less - into pension plans with lower benefits

The "Madigan-Cullerton" Budget passed by the IL legislature and which begins on July 1 for FY 2016 is $4 Billion in the "hole" according to the Governor and these and other budget cuts will begin soon. Given our Republican Governor and Democratic legislature, we see no solution in the near future.

The same is true in Congress, with competing "visions" of tax reform. With a Democratic President and a Republican Congress, we do not expect any broad based tax legislation this year.

However, our lives do not stop! Many of us have changed jobs, gotten married, retired, sold our principal residences or vacation/rental properties or have had a loved one pass away. Mid year and end of year tax planning is ongoing - and we are here to help you plan for 2015.

<u>HERE ARE SOME OF THE QUESTIONS WE GET:</u>

- **How do I know what to withdraw for my minimum distribution (RMD) at age 70 ½?**

First, if you are still employed, you do not have to withdraw from your 401K at **your current employer**. However, you have to withdraw from any other IRA and from any other 401K. You must take a minimum amount out of each IRA/401K **or take it all** from one pretax investment. The IRS has a Uniform Lifetime Table (life expectancy) to compute this RMD; the amount is computed based on the 12/31/14 value of each IRA or the Fair Market value total of all investments. Many of us have more than one IRA – in banks, in mutual funds and often in annuities as well. The companies holding your IRAs will send you a notice reminding you of the required withdrawal, but ultimately it is **your responsibility.**

You can choose not to withdraw in the year you are 70 1/2 but you **must** withdraw your first RMD before April 1 of the following year. In addition, you **must** withdraw the age 71 year RMD in that same year - or before December 31, or two distributions in the same year. We usually do not recommend postponing, but check with us if you have a question.

There are tax consequences when you withdraw. You will pay tax on the total withdrawal at ordinary income rates. The IRA withdrawal may make more of your Social Security taxable. You may have some nondeductible IRAs and we need to determine the nontaxable amount – on a form 8606. You may need to pay Estimated Tax or have tax withheld from your withdrawal so you are in good shape at tax time.

You may also want to check the beneficiary designations on your IRAs. There are important tax rules for inherited IRAs. Check with your bank, investment advisor or us to make sure you are withdrawing the correct amount, are protected at income tax time, and also that there are no surprises after you pass on.

- **I/we sold a stock. How do I compute the Basis?**

When you sell a stock, mutual fund, land, second home etc., the IRS gets a 1099B showing the gross sales price and the cost basis supplied by the broker or mutual fund company if the purchase was after January 1, 2011 (called covered sales). If you bought a stock or mutual fund or a home or land prior to that date (uncovered sales), it is up to you to determine the cost basis – and thus the profit on the sale. Only the profit is taxed – and only at 0% or 15% (and now 20% for higher income taxpayers) if you held it more than one year! In addition, with the new Form 8949, the IRS is planning to match cost basis shown on the 1099B with what you/we put on your tax return - and we expect letters in a year or so if there are discrepancies.

However, you may have inherited an asset, bought it over many years and reinvested the dividends, or transferred it from another investment company - and the cost basis may either be unknown or not correct on your broker's records. If you sell an asset in 2015, it is a good idea to call us for an appointment and make sure you (and we) have the cost basis correctly computed prior to tax season next year.

- **Home Sales - your principal residence and other homes too.....**

The "old" law on rolling over tax profit from home sales and only excluding up to $125,000 changed a long time ago. The current tax law says you can exclude up to $500,000 of gain if Married and up to $250,000 of gain if Single if you owned the property and lived in it as your primary residence for two out of the last five years. Losses on either primary homes or second homes not used as rentals or for business purposes cannot be taken. There are exceptions if you are in a nursing home and if you are recently widowed. In addition, if a former primary residence becomes part of a trust or estate after the owner passes away, there are different rules for the sale on a form 1041 and losses can be taken. Call to get our home sale information worksheet.

- **What is going on with the Estate and Gift Tax?**

The Federal Estate Tax now has a top rate of 40% and an exemption of $5.43 million for estate taxes for 2015. 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 IL exclusion is now $4 million. The annual exclusion for tax-free gifts is still $14,000 per donor. A person may make an unlimited number of $14,000 gifts, so long as they are to different individuals, without filing a 709 or Gift Tax return.

- **What is important for medical expenses this year?**

It is no surprise that medical insurance premiums are going up - and up! You should review your insurance costs and deductibles (often $1000 - $2000 + now) to see which spouse's insurance has the best coverage and is the most cost effective. Just because they are "pre-tax" does not mean they are good. This is also true for retirees on their prior company plans vs. Blue Cross or other supplementary plans. Also, the Patient Protection and Affordable Care Act of 2010 allows parents to keep their children (even if not dependents) on their insurance until age 26; depending on the child's plan, this may be a better "deal."

In addition, more taxpayers (and our clients) are itemizing their deductions due to substantially increased **medical costs.** Medical costs include: out of pocket insurance costs (Medicare, COBRA, long term care insurance and retiree medical withheld from your pension); deductibles; doctor and dental bills; lab fees; all eye care costs, prescription and doctor ordered drugs; medical travel, parking and lodging; hearing aids and batteries; in home care required by the doctor and nursing home fees that **qualify as medical expenses**. If you are thinking about a retirement or nursing home, they provide information about deductible fees and upfront buy-in costs; we can review these with you to determine the tax impact.

JUDI STRAUSS IN PRINT, ON MEDIA

Our Website - **www.strausstax.com** continues to offer tax tips and tax update alerts when new legislation is passed - as well as workshop dates. Our **Facebook** page also offers tax tips as well as links to many interesting and timely articles - you can "like" Strauss Tax Service and tell your friends as well. In the fall, Judi will be offering a workshop on September 29, 2015 7:00 p.m. on "Estates and Trusts: What You need to Know Now" at the Downers Grove Public Library. Check for other dates at your local library and on our website.

TAX and FINANCIAL TIDBITS …..

- One of the IRS's highest priorities is prosecuting people who use **stolen identities** to steal money from the United States Treasury by filing fake tax returns that claim tax refunds. Working to stop Stolen Identity Refund Fraud, the IRS has stopped more than 19 million cases since 2011 and protected over $63 billion dollars of fraudulent refunds. Call us if you think your identity is stolen; we can help you report it to the IRS. Waiting until tax time may be too late to avoid a phony return using your Social Security number.
- **Many people are asking about retiring at age 62** - and indeed starting to collect SSA early. You get 75% of the full SSA if you retire early. However, you can get Medicare at age 65, but you must sign up and pay for it yourself. Call SSA 1.800.772-1213 or Medicare 1.800.633-4227 or for retirement/tax projections, call for an appointment.
- **Contributions are good** - but make sure your charity uses your money wisely. Check out **www.charitywatch.org** - they rate charities from A to F based on funds used for program services as opposed to overhead. You can also make sure you are giving to a 501 (c) 3 true charity.
- **The IRS and IL are busy sending out notices this summer**. IL will not let us figure underpayment penalties on your IL 1040 and many clients have recently received these unwelcome letters. Call us if you receive one. In many cases, the IRS problem can be solved with a phone call on our practitioner priority line or with a letter. For the IL notices, usually you just have to pay!
- **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 after death and help you successfully complete the required tax filings and communication with beneficiaries, asset companies, and the IRS. We work with you and your attorney to answer questions and prepare required tax returns so as to minimize future problems. Call for our **Estate Check-off list** and our **Questions/ Answers about Estates and Trusts.**

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NEW NUMBERS TO NOTE	2015
Maximum Social Security payroll tax limit	$118,500
Age for full SSA	66
Maximum Earnings to collect full SSA - under full retirement age	$15,720 ($1,310/month)
Business miles	57.5 cents/mile
Medical miles	23 cents/mile
Charitable miles	14 cents/mile
Gift Tax exclusion	$14,000/per donee/ year
Estate Tax exclusion	$5.34 million
IRA maximum (over 50 catch up)	$5,500 + $1,000
401K maximum (over 50 catch up)	$18,000 + $6,000