KAKENMASTER REPORT

A Newsletter from Kakenmaster & Associates and Libertyville Insurance Agency

Tax Issue 2014 *Volume XVII Issue II*

Social Security & Medicare

2015 Social Security (S.S.): The S.S. wage is $118,500, and the FICA rate is 6.2%. The Medicare tax continues at 1.45% for both the employee and employer's portion, but the .09% Medicare surtax is in effect for couples earning more than $250,000 and $200,000 for single filers.

The self-employed taxpayer will pay 15.3% on the first $118,500 and 2.9% after this point.

S.S. benefits are increasing 1.7%. For those taxpayers turning 66 years of age in 2015, Social Security will not decrease their benefits if they earn $41,800 or less in the year they reach age 66.

Medicare Part B Premiums: For 2015 the basic Medicare Part B premium will stay at $104.90 a month. Seniors with modified adjusted gross incomes for 2013 that exceeded $170,000 for couples and $85,000 for singles will pay a surcharge for Part B and D premiums. The total surcharges may be as high as $301.60 per month.

Social Security Reminder: New dependents in your family are required to have a S.S. number to file as a dependent.

Retirement Plans: Changes and Updates

Planning for retirement is a top priority, and this issue of the *Kakenmaster Report* highlights some new guidance for 401(k) plans, as well as the 2015 contribution limits. In addition, this issue provides important information regarding inherited IRAs and how to avoid unnecessary penalties, as well as a recent court decision on how IRAs are treated in an unfortunate bankruptcy.

IRS Provides Guidance for 401(k) Plans with Pretax and After-tax Contributions

New Guidance for Company 401(k) Plans

Employees who have been contributing to their company's 401(k) for many years are likely to have a portion of their contributions from after-tax dollars. In the past it was not clear how to roll over accounts that included both pretax and after-tax contributions. However, new guidance from the IRS this past September now allows the distribution of after-tax contributions made to a company 401(k) to roll over to a Roth IRA and grow tax free. The entire account (pretax and after-tax contributions) must be transferred simultaneously to take advantage of this change. For example, if you want to roll over your company 401(k) worth $100,000, with $80,000 of it consisting of pretax money and $20,000 of after-tax money, you could transfer the pretax $80,000 directly to a traditional IRA and the after-tax $20,000 to a Roth IRA and not incur any taxes for this move.

Inherited IRAs

Inherited IRAs need to be handled properly to avoid an unnecessary tax bill and allow it to continue to grow tax-deferred. Here are a few things to keep in mind regarding an inherited IRA:

1) Required Minimum Distributions (RMDs)—Non-spouse beneficiaries of inherited IRAs must begin taking RMDs the year following the year the owner died and will have to pay tax on the distribution of deductible contributions and earnings from a

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Retirement Plans cont'd...

traditional IRA. Regarding Roth IRAs, although spouses never have to take RMDs, non-spouse beneficiaries must make withdrawals, but they will be tax free. Not taking RMDs could result in a 50% penalty on the amount that should have been withdrawn for that year.
2) Dividing the IRA Among Heirs—Be sure to divide the IRA between the beneficiaries. This is particularly important if there is a wide gap in ages because the RMDs are based on life expectancy, so a younger beneficiary will have a much lower RMD than an older beneficiary.
3) Non-person Beneficiaries—If an inherited IRA includes a non-person or charity as one of the beneficiaries, the entity's share must be paid out by September 30 of the year following the owner's death. If this does not occur, the rest of the beneficiaries will not be able to take withdrawals over their life expectancies.

If you have inherited an IRA and have questions, please feel free to contact Kakenmaster and Associates.

Protection in Bankruptcy
A recent court decision set a new precedence for inherited IRAs, ruling that inherited IRAs are not "retirement funds" within the meaning of the Federal bankruptcy laws. Therefore, they are available to satisfy creditors' claims. The Court differentiated between an inherited IRA from a participant owned IRA with three factors, the first being that the beneficiary of an inherited IRA cannot make additional contributions, unlike the owner of the IRA. Secondly, beneficiaries of an inherited IRA must begin taking required minimum distributions, regardless of their age. Finally, the beneficiary of an inherited IRA can withdraw all the funds anytime, for any purpose, unlike the owner of an IRA, who must wait until they reach 59 1/2 or incur penalties for early withdrawals. This ruling has also raised questions regarding inherited 401(k) and 403(b) accounts, as well as IRAs inherited by spouses.

Other Tax Information

Expensing Business Assets:
Although 55 tax provisions expired at the end of 2013, many expect that some of the more popular ones will be reinstated and become retroactive to the beginning of 2014. This makes it difficult for year-end planning, particularly with the provision to expense business assets. Small and mid-sized business owners were allowed to immediately deduct an amount up to $500,000 of qualifying equipment, rather than having to depreciate the expense. If this provision is not reinstated, the limit drops to $25,000.

Healthcare Reform Tax Implications:
Due to healthcare reform laws, 2014 tax returns will be more complex for taxpayers who purchased health coverage through an exchange in 2014 and were allowed a health premium tax credit in advance. This credit will need to be reconciled against the actual credit allowed depending on the coverage purchased and the taxpayer's income. Also, taxpayers who do not have health insurance may have to pay a penalty unless they fall under one of the exemptions not requiring them to purchase a policy.

Deduction for Service Animals:
For those who own animals to assist them because they are visually impaired or have other physical disabilities, the IRS allows veterinary costs as deductible medical expenses (to the extent total medical expenses exceed 10% of the adjusted gross income, 7.5% if 65 or older) along with the amounts needed to purchase and care for the animal.

IRS 2015 Per Diem Rates:
The IRS has increased the simplified per diem amounts for lodging, meals and incidentals. The per diem amount allowed per day increases to $259, up from $251 in high-cost areas, and to $172 in other areas, up $2. For 2015 the per diem for meals and incidentals per day remains unchanged, $65 in high-cost areas, $52 in other areas. The per diem rate for incidental expenses remains at $5 per day. Self-employed taxpayers can use the daily meal and incidental rates without receipts but must have receipts for lodging expenses.

Worker Classification:
Almost 20 states have received federal funding to conduct worker classification audits to help identify businesses that are misclassifying workers as contractors, lowering their state income tax bills. These results are shared with both the IRS and the Labor Department. See the fall issue of the *Kakenmaster Report* for more information about the 20-factor test.

Taxpayer IP Pin:
If you have ever contacted the IRS regarding identity theft, you may have received a notice from the IRS containing a six-digit identity protection personal identification number (IP PIN). This is needed on your tax return to avoid a processing delay.

The IRS Does Not Make Phone Calls or Send Emails

The IRS recently released a Tax Scams video in response to reported incidents across the country of an aggressive telephone scam with impostors posing as tax agency representatives. The IRS warns taxpayers not to be fooled by these callers. You can view the video at http://www.youtube.com/user/irsvideos.

Keep in mind that the IRS will never call to demand immediate payment, nor will the IRS call about taxes owed, without first having mailed you a bill. Secondly, the IRS will never call and demand that you pay taxes without giving you the opportunity to question or appeal the amount they say you owe. They also will not require you to use a specific payment method for your taxes, such as a prepaid debit card or ask for credit or debit card numbers over the phone. In addition, the IRS will never threaten to bring in local police or other law-enforcement groups to have you arrested for not paying.

The IRS is asking that if you get a phone call from someone claiming to be from the IRS and asking for money, hang up and call the IRS at 1-800-829-1040 to inquire about any owed taxes, and they will be able to assist with a payment issue. If you do not owe taxes or have no reason to believe that you do, report the incident to the Treasury Inspector General for Tax Administration (TIGTA) at 1-800-366-4484 or at www.tigta.gov. If you have been targeted by this scam, also contact the Federal Trade Commission and use their "FTC Complaint Assistant" at FTC.gov. Please add "IRS Telephone Scam" to the comments of your complaint.

In addition, the IRS does not send emails, text messages or use social media to discuss tax matters. For more information on reporting tax scams, go to www.irs.gov and type "scam" in the search box.

Is It a Business or Hobby?

The IRS has guidelines to help taxpayers determine whether the activities they are engaged in are considered a business or a hobby. A key feature of a business is that you do it to make a profit. Hobbies are often engaged in for sport or recreation, not to make a profit.

If the activity is considered a business, the taxpayer may deduct ordinary and necessary expenses for conducting a trade or business or for the production of income. According to the IRS, the following factors, although not all inclusive, may help you to determine whether your activity is an activity engaged in for profit or a hobby:

Does the time and effort put into the activity indicate an intention to make a profit?
Do you depend on income from the activity?
If there are losses, are they due to circumstances beyond your control or did they occur in the start-up phase of the business?
Have you changed methods of operation to improve profitability?
Do you have the knowledge needed to carry on the activity as a successful business?
Have you made a profit in similar activities in the past?
Does the activity make a profit in some years?
Do you expect to make a profit in the future from the appreciation of assets used in the activity?

It is also presumed that an activity is for profit if it makes a profit in at least three of the last five tax years, including the current year (or at least two of the last seven years for activities that consist primarily of breeding, showing, training or racing horses). If an activity is not-for-profit, losses from that activity may not be used to offset other income. An activity produces a loss when related expenses exceed income. The limit on not-for-profit losses applies to individuals, partnerships, estates, trusts, and S corporations. It does not apply to corporations other than S corporations.

The IRS is also gearing up for the 1099-K Matching Program, which will compare payments from credit and debit card companies and payment services such as PayPal with the reported taxpayer's income. It is important to determine if your activities would be considered a hobby or a business by the IRS and plan accordingly before the 1099-K Matching Program begins.

2015 Retirement Plan Contributions

401(k), 403(b) and 457 Plans - Contributions increase to $18,000, previously $17,500 (individuals born before 1966 may contribute up to $24,000).
SIMPLE Plans - The contribution level increases to $12,500 (50 or older in 2015 can contribute up to $15,000).
Roth IRAs - Contribution levels remain at $5,500 ($6,500 for those 50 years or older). The phase out range is between $183,000 to $193,000 (AGI) for couples, and between $116,000 to $131,000 (AGI) for singles.
Traditional IRAs - Contributions remain the same as the Roth IRAs, but the phase out level increases to $118,000 (AGI) from $98,000 for couples, and to $71,000 (AGI) from $61,000 for single filers. If only one spouse is covered by a plan, the phase out range for the uncovered spouse is $183,000 to $193,000 of AGI.

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Season's Greetings to You and Yours!

Financial, Insurance, and Real Estate Services for Businesses and Individuals

Planning for Your 2014 Tax Return

Watch for the ***Kakenmaster Report Data Sheet*** issue to arrive in your mailbox in the beginning of January. This issue provides a simple way to compile your 2014 tax data.

Tax Appointments:
Schedule your tax appointment soon to help assure that you will receive the appointment time that is best for you. We also offer convenient drop-off service.

New Online Portal:
Kakenmaster's new secure client portal will allow you to upload your confidential tax documents securely and conveniently. It will allow us to send you files such as your completed tax return and other documents. The client portal is password protected, allowing your tax information to be transmitted safely and securely. Visit our website at www.kakenmaster.com for more information.

Online Gambling

If you gamble online using Internet accounts, there is a very good chance that these accounts are located outside the United States. If so, you may have to file a Report of Foreign Bank and Financial Accounts (FBAR). According to the IRS, you are required to file an FBAR if: 1) the United States person had a financial interest in or signature authority over at least one financial account located outside of the United States; and 2) the aggregate value of all foreign financial accounts exceeded \$10,000 at any time during the calendar year reported. Taxpayers who hold a foreign financial account may also have a reporting obligation even when the account produces no taxable income.

The IRS continues to get cooperation from foreign banks to report U.S. owned accounts. A recent court ruling found that even though the money used to gamble was wired from the U.S. and that the computer used to gamble with was in the U.S., the "accounts" were located in foreign countries and fell under the FBAR requirements. The Court ruled that the online accounts held money, made disbursements, and accepted deposits and therefore was considered "other financial accounts." If you are unsure if you need to file an FBAR, please feel free to contact Kakenmaster and Associates.

Thank You!

We would like to say thank you once again for trusting us as your tax preparer. We would also like the opportunity to serve your friends and family. This referral coupon is good for \$30.00 off tax consultation services to any new tax client. As a thank you for your referral, we will also send you a \$30.00 thank you check. Thank you for choosing and recommending Kakenmaster and Associates to your family and friends.

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