



HIGHER TAXES

With all the wrangling going on in Washington, it seems it has been easy for all of us to forget that they did pass a bill in early 2013 that increased Federal income taxes. Maybe we wanted to forget. But now, it is time to wake up, study up, and deal with it. Taxes are a big expense for you and tax planning time is from NOW to December 31.

Trust rates get to the 39.6% rate at incomes above \$11,950. For this reason, Trusts need careful tax planning. It is generally better to make sure the income gets passed through to the beneficiaries so that the income can be taxed at their rates. Remember that unless the Trust contains special language, capital gains must be taxed to the Trust unless it is the final year for the Trust. That means that more than likely the 20% federal capital gains tax rate will apply. Trust rates apply to the income earned by an estate and not passed through.

HIGHER TAXABLE INCOME

For those with adjusted gross incomes over \$300,000 (\$250,000 single, \$275,000 MFS) itemized deductions start getting reduced down by as much as 20%. In addition, those individuals get their personal exemption deductions reduced by 2% for each \$2,500 (2% for each \$1,250 for MFS) of adjusted gross income over these same thresholds. This applies until the personal exemption deduction is eliminated in its entirety.

TAX RATES FOR INDIVIDUALS

Married filing jointly (MFJ):

\$0	-	\$17,850	10%	
\$17,850	-	\$72,500	15%	+ \$1,785
\$72,500	-	\$146,400	25%	+ \$9,982.50
\$146,400	-	\$223,050	28%	+ \$28,457.50
\$223,050	-	\$398,350	33%	+ \$49,919.50
\$398,350	-	\$450,000	35%	+ \$107,768.50
\$450,000	-		39.6%	+ \$125,846

Married filing separately (MFS):

\$0	-	\$12,750	10%	
\$12,750	-	\$48,600	15%	+ \$1,785
\$48,600	-	\$125,450	25%	+ \$9,982.50
\$125,450	-	\$203,150	28%	+ \$28,457.50
\$203,150	-	\$398,350	33%	+ \$49,919.50
\$398,350	-	\$425,000	35%	+ \$107,768.50
\$425,000	-		39.6%	+ \$125,846

Single:

\$0	-	\$8,925	10%	
\$8,925	-	\$36,250	15%	+ \$892.50
\$36,250	-	\$87,850	25%	+ \$4,991.25
\$87,850	-	\$183,250	28%	+ \$17,891.25
\$183,250	-	\$398,350	33%	+ \$44,603.25
\$398,350	-	\$400,000	35%	+ \$115,586.25
\$400,000	-		39.6%	+ \$116,163.75

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CAPITAL GAINS RATES

The rate remains at 15% for capital gains and dividends for most. For those in the 39.6% brackets above, the capital gains rate goes to 20%. For those in the 10% and 15% bracket, the capital gains rate can be 0%. The 28% rate continues to apply to gains on the sale of collectibles, the 25% rate to unrecaptured Code Sec 1250 gains and ordinary rates to short term (held less than one year) gains. Special provisions may apply to the sale of stock in a small business corporation.

ALTERNATIVE MINIMUM TAX

The exemption is \$80,800 for MFJ and \$51,900 for singles and MFS. However, these exemptions will continue to “disappear,” with the effect that many will continue to see the alternative minimum tax increase their tax burden. We start to worry about the AMT when adjusted gross incomes get above \$150,000.

SELF EMPLOYMENT TAX

The tax rate reverts back to 15.3% for 2013 and after. During 2011 and 2012, employees were allowed a 2% reduction on their FICA tax withholding. Self-employed individuals enjoyed the same 2% reduction. In 2013 and after, no one gets to enjoy the reduction. Employees have been having their taxes withheld all year. Self employed individuals will see it in their balance due.

0.9% ADDITIONAL MEDICARE TAX

This new tax applies to earned income above \$250,000 for married couples filing jointly (\$200,000 singles and \$125,000 MFS). In general it applies to wages and self employment income. Employers are to withhold, but a settling up will occur on your 2013 income tax return.

3.8% NET INVESTMENT INCOME TAX

This new tax applies to unearned incomes above the same thresholds as above. In general, it applies to interest, dividends, capital gains, annuities, royalties, and rental income. It does not apply to income from gain on sale of property used in an active business. It does not apply to payouts from pension plans, 401(k) plans, IRAs etc., however, these incomes are counted in determining the thresholds with the effect that they can cause other unearned incomes to be taxed. In addition, they could cause earned income to be subject to the .9% tax above. Certain expenses can be deducted such as the penalty for early withdrawal on a CD, investment interest expense and the applicable state income tax. Net capital losses are not to be deducted.

It appears that a passive shareholder (but not an active shareholder) in a Sub S Corporation will be subject to this tax on the K-1 income from the Sub S.

SOCIAL SECURITY WAGE BASE

It goes up from \$110,100 to \$113,700 for 2013. The 15.3% rate has two components, the 12.4% component that is limited to the wage base and the 2.9% component that is unlimited. Therefore the \$3,600 increase is only on the 12.4% component for a cost of \$446.40. The 2% employee rate restoration explained above on \$110,100 is a cost of \$2,202.



MEDICAL EXPENSES

Medical expenses did count as an itemized deduction to the extent that the total exceeded 7.5% of adjusted gross income. For 2013 and after the exclusion goes to 10%.

MILEAGE RATES

The accepted rates are 56.5 cents per mile for business mileage, 24 cents for medical and moving miles and 14 cents for charitable driving.

RETIREMENT CONTRIBUTION MAXIMUMS

The maximum for 401(k), 403(b) and 457 contributions is \$17,500, with an additional \$5,500 allowable to those born before 1964. The maximum for SIMPLE plans is \$12,000 with an additional \$2,500 for those over age 50. The maximum for IRA's is \$5,500 with an additional \$1,000 for those over age 50.

STRATEGY

In general, avoiding spikes in income is best. This can be accomplished by spreading income out using techniques such as the installment sale, or by deferring income through techniques such as Sec. 1031 exchanges, or by pulling income into a low income year. Retirement plan contributions remain a favorite tax planning tool. Tax planning becomes more critical for those with incomes above \$150,000. As always, we encourage you to schedule a tax planning appointment in the fall. These generally cost around \$250 and can pay big dividends.

BUSINESS PROVISIONS

Fifty percent bonus depreciation for new equipment is in effect for 2013 and scheduled to expire. Code Sec 179 remains in effect for 2013 (new and used tangible personal property) with a \$500,000 maximum as long as the total

investment in this type of property is less than \$2,000,000. Code Sec 179 can also apply to leasehold improvements, and certain restaurant property and retail property. If Congress doesn't act to extend these provisions, we will be back to a very limited and very small Code Sec 179 deduction.

REPAIR REGULATIONS

The IRS sometimes has powers granted by Congress to make tax laws. Under these powers, the IRS has issued a new regulation governing when taxpayers must capitalize and when they must deduct their expenses for acquiring, maintaining, repairing and replacing tangible property. The effective date is January 1, 2014. We are now studying this new development, and we will be advising you regarding compliance. In general, our approach will be more to guide our clients toward compliance than jerk them there. Experience has taught us that changes of this type take a while to understand and work their way into the system. It takes ten years to really understand a law, as court cases and IRS rulings help shape the law long after it is put into place.





ESTATE AND GIFT TAXES

The limit for gifts is \$14,000 for 2013. Gifts are never deductible to the giver nor taxable to the gift recipient. A gift above \$14,000 has an effect on the estate tax exclusion, and it requires a gift tax return even though a gift tax may not be due. The annual gift tax limit can be expanded by having a husband give \$14,000 to one person, and the wife giving \$14,000 to the same person. The estate tax is a tax on the fair market value of an estate in excess of \$5,250,000 and rates quickly get to 40%. For those with potential taxable estates, careful planning needs to take place, and we should be considered as being one of the players in your estate tax planning team. Portability rules between husbands and wives can double the \$5.25M exemption if the rules are properly followed. Trusts are often recommended as a way to meet after death goals.

Those with smaller estates should still schedule a meeting after the first death of a married couple to discuss matters such as perfecting the portability rules and the benefits of stepped up basis. Even though the estate is considered small at the first death doesn't automatically mean it will be small at the time of the second death. To obtain the portability benefit, a form 706 must be filed within nine months of the first death.

ECONOMY EFFECT

The tax increases were felt by wage earners starting with the beginning of 2013. The tax increases will be felt by the self employed and the investors in the first half of 2014. If Congress doesn't act on depreciation enhancements, that will provide a further burden on the economy. While the sun will still rise in the East and set in the West, these economic effects cannot

be ignored as we all go about running our businesses and planning our futures.

SAME SEX MARRIAGE

A June 26, 2013 supreme court decision has resulted in an IRS ruling that a legally married couple is required to file income tax returns as a married couple, and not as single persons. Kansas does not allow same sex marriage. However, the way it works is that if a couple became legally married in another state, they are legally married for the purposes of the Federal Income Tax. For Kansas income tax, they will continue to file as single persons.

OTHER FEDERAL CHANGES

We have dealt with only a portion of the changes here, some others having to do with changes based on inflation or believed to have smaller impacts. We expect that Congress will be debating tax law again soon. If you have something special going on, such as plans to hire a veteran, to expend money to research a new product or plant process, or to expand a plant, be sure to include us in your plans. Ask questions and make us work for you.



KANSAS TAX LAW

For 2013, tax rates for individuals have been reduced to 3% and 4.9%. For 2014, the rates are to be 2.7% and 4.8%. For 2015 the rates are to be 2.7% and 4.7%. For 2016 the rates are to be 2.4% and 4.6%. For 2017 the rates are to be 2.3% and 4.6%. For 2018 the rates are to be 2.3% and 3.9%. After 2018, a formula which has to do with general fund receipts is to determine tax rates.

The lower bracket applies to the first \$30,000 for married persons filing jointly and \$15,000 for single persons and MFS filers.

Itemized deductions (other than for charity) are to be reduced by 30% in 2013, 35% in 2014, 40% in 2015, 45% in 2016. And 50% in 2017. Starting in 2014 no deduction will be allowed for gambling losses. In 2013 the standard deduction for married couples is increased from \$6,000 to \$7,500, for head of household filers from \$4,500 to \$5,500. The standard deduction for single taxpayers remains at \$3,000. A food sales tax rebate provision will remain for eligible households who may claim a nonrefundable \$125 for every exemption claimed for those persons under the age of 17.

For 2013 and after, income reported on schedule C (business income), schedule F (farming income), business income reported by limited liability companies, business income reported by Subchapter S corporations, and rental and royalty income is exempt from Kansas income tax.

Net operating loss carryovers are disallowed. Retirement contributions and self employed health insurance are no longer deductible. Most credits have been repealed and the subtraction for long term care insurance has been eliminated. Renters will no longer be able to claim the homestead property tax refund.

The Kansas legislature amended the law so that partners and Subchapter S shareholders will continue to use Federal basis calculations, which is important when computing gain or loss on disposition.

In general, C Corporations remain taxed as before.





PATIENT PROTECTION AND AFFORDABLE CARE ACT (PPACA)

The Act imposes requirements on insurers, employers, medical device manufacturers and individuals. The following deals only with employers and individuals. Employers with over 50 full time equivalent employees must file an information return that reports the terms and conditions of health insurance coverage provided to full time equivalent employees for the year. A failure to file penalty applies. This has been delayed to January 1, 2015. These “large” employers are required to furnish affordable health insurance or pay a “shared responsibility payment.” The coverage must be offered to at least 95% of their full time employees.

All employers were supposed to have notified employees by 10-1-13 of the availability of coverage through individual marketplaces or the Small Business Health Options Program (SHOP). Examples of the notification form are available from the U S Department of Labor. Small employers (less than 50) may keep their current coverage or offer coverage through a SHOP exchange. Enrollment in the SHOP exchange was to have begun 10-1-2013, but some functions have been delayed. If an application is completed by 12-15-2013, coverage could begin as early as 1-1-14. Beginning in 2016, SHOP exchanges will be open to employers with up to 100 employees.

Self employed persons with no employees will not use the SHOP exchange. They will use the marketplace for individuals. The marketplace is also referred to as Affordable Insurance Exchanges. These are insurance plans offered by private companies for a core set of benefits including emergency services, hospitalization,

maternity and newborn care, mental health services, preventive and wellness services and rehabilitative care.

Prior to 2013 there has been a small employer health care credit that provided a help to employers who offered health insurance, had fewer than 25 employees and paid less than an average annual wage of less than \$50,000. The credit worked in such a way that it started phasing out if the number of employees was over 10, and/or the average annual wage exceeded \$25,000. The phase out severely limited the credit. Starting in 2014 the credit will remain, but, the credit will only be available to those employers that obtain coverage through the SHOP program. The credit will increase from 35% to 50% of health insurance premiums paid by the employer, if the employer pays over 50% of the total cost of the policy. The thresholds are to be adjusted for inflation.

Beginning in 2014 eligible individuals who obtain coverage under a qualified health plan through a marketplace may qualify for a premium assistance tax credit. They will not qualify if they receive employer sponsored coverage that is affordable. Eligibility for the credit is determined by the relationship of the taxpayer’s household income to the Federal poverty level. Some credit may be available to those with household incomes up to 400% of the poverty level. Employees who do not acquire the minimum essential coverage may pay an additional amount called a shared responsibility payment. This payment is computed monthly and would be paid with their 2014 Federal income tax return. At the time of tax preparation, we



will go through calculations to determine the amount of payment, or if the employee is exempt due to household incomes under the threshold amount or one of the other exemptions provided for.

The law provides a way for the premium assistance tax credit to be applied against the premium paid for health insurance. At this point, we advise against that. There will be a “squaring up” calculation on the 2014 income tax return,

and there can be no assurance that the premium tax credit will be available until that calculation is completed.

Those employers who offer a self insured health insurance policy will pay a PCORI fee by using form 720 to report and pay the fee. Form 720 is due on July 31 of the year following the last day of the policy or plan year. The PCORI fee is deductible for income tax purposes.

TO DO LIST

- Review your income, expenses, withholding, and estimates paid. Do you need to schedule a tax planning meeting?
- Plan your cash to meet any April 15 tax due and first quarter estimates.
- Review capital gains and losses, then review your portfolio to determine whether you have gains/losses to recognize before year end.
- Consider additional contributions to a retirement plan or IRA.
- Does a 529 college savings plan fit your goals?
- Consider “bunching” of itemized deductions such as paying three halves of real estate tax, two years of contributions etc.
- Make plans now if you need to defer income or accelerate business expenses.
- Consider the timing of equipment purchases. Liberal expensing provisions are still in place for 2013.
- Consider the timing of sale of no longer needed assets.
- Make inventory plans. Consider a sale of slow moving items.
- Consider gift giving if appropriate.
- Review your estate plan. Review beneficiaries on insurance policies and retirement plans. Consider whether wills and trusts need to be updated.