

ClientLine®

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MINIMIZING THE TAX BITE on Your Investments

When you invest, your main focus should be achieving your financial goals, not avoiding taxes. That said, if an investment decision causes your tax bill to go up, it will take you longer to achieve your goal. So what should you do? Be aware of the impact taxes can have.

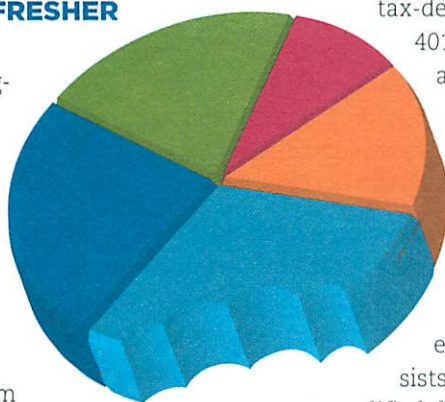
CAPITAL GAINS REFRESHER COURSE

For most taxpayers, long-term capital gains and qualified dividends are generally taxed at 15%. Those in the 39.6% ordinary tax bracket pay 20% (the highest rate). For taxpayers in the 10% or 15% bracket, the rate is 0%. Short-term gains* and interest are taxed as ordinary income. Note that high-income investors may be subject to an additional 3.8% net investment income tax.

From a tax standpoint, it may make sense to hold investments that are taxed at relatively low rates, such as stocks you intend to hold for more than one year, in a taxable investment portfolio. That way, taxes wouldn't be due until you sell shares and realize a capital gain.

THE TAX DEFERRAL ADVANTAGE

Alternatively, you might consider holding investments that generate ordinary income (e.g., bonds that pay taxable interest) in



tax-deferred accounts, such as a 401(k) or individual retirement account (IRA). You'd avoid having to pay income tax until funds are withdrawn. Keep in mind, however, that withdrawals from tax-deferred accounts are generally taxed at ordinary income-tax rates, even if the withdrawal consists of long-term capital gains or qualified dividends.

TAX-WISE REBALANCING

Over time, performance can change the makeup of any investment portfolio, and the way you originally allocated investments in the portfolio can shift, along with your exposure to investment risk. Since selling investments in a taxable portfolio can have tax consequences, if you are going to rebalance, you may want to direct your new investments to the underweighted categories until your portfolio is back in balance. In a tax-deferred portfolio, selling assets in the overweighted categories could be part of your rebalancing strategy.

* Gains on investments held for one year or less

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A Healthier Outlook for Retirees

Estimates from the Employee Benefit Research Institute of the savings retirees need to cover their health care costs (including insurance premiums) declined between 2012 and 2013 and again between 2013 and 2014.*

Example: A 65-year-old man retiring in 2014 needs a projected \$64,000 in savings to have a 50% chance of covering his health care expenses during retirement. That's down from an estimated \$70,000 in 2012. A 65-year-old woman needs \$83,000 in 2014, down from \$93,000 in 2012. Figures are based on individuals with median prescription drug expenses. Higher drug expenses would require more savings.

What's the reason for the good news? Lower projected growth rates for Medicare and Medigap insurance premiums and health care costs. Note: These projections do not include long-term care expenses.

* ebri.org Notes, October 2014, Vol. 35, No. 10

Improving **CASH FLOW**

Slow paying customers, seasonal revenue variations, an unexpected downturn in sales, higher expenses — any number of business conditions can contribute to a cash flow crunch. If you own a small business, you may find the suggestions that follow helpful in minimizing cash flow problems.

Billing and collections. Your employees need to work with clear guidelines. If you don't have a standardized process for billing and collections, make it a priority to develop one. Consider sending invoices electronically instead of by mail. And encourage customers to pay via electronic funds transfer rather than by check. If you don't offer a discount for timely payment, consider adding one to your payment terms.

Expense management. Know when bills are due. As often as possible, pay suppliers within the period that allows you to take advantage of any prompt-payment incentives. Remember that foregoing a discount in order to pay later is essentially financing your purchase.

Take another look at your costs for ongoing goods and services, including telecommunications, shipping and delivery, utilities, etc. If you or your employees travel frequently for in-person meetings, consider holding more web conferences to reduce costs.

Inventory. Focus on inventory management, if applicable, to avoid tying up cash unnecessarily. Determine the minimum quantities you need to keep on hand to promptly serve customers. Systematically track inventory levels to avoid overbuying.

Debt management. Consider how you use credit. Before you commit to financing, compare terms from more than one

lender and keep the amount to a manageable level. For flexibility, consider establishing a line of credit if you do not already have one. You will be charged interest only on the amount drawn from the credit line.

Control taxes.

Make sure you are taking advantage of available tax breaks, such as the Section 179 deduction for equipment purchases, to limit taxes.

Develop a cash flow budget. Projecting monthly or weekly cash inflows and outflows gives you a critical snapshot of your business's cash position and shows whether you'll have enough cash on hand to meet your company's needs.



Client PROFILE.....

Val's business is in need of some new equipment. Instead of buying equipment as he usually does, Val wonders if leasing the equipment would be a better option.

The first factor Val needs to consider is cost. If cash flow is a concern, leasing might be a better choice since he generally won't need as much money up front to lease equipment as he would to purchase it.

Another factor he should look at is time frame. Val might want to consider leasing if the equipment will fill only a short-term need. But if he knows he'll be able to resell the equipment for a good price, then purchasing the equipment may be a better decision.

Val should also consider whether the equipment will have to be upgraded or replaced in the near future. If it will, then leasing may give him more options. Maintenance is often included in lease agreements, and he could have the choice at the

end of his lease to either buy the equipment he has or lease newer equipment.

Owning the equipment and using it in his trade or business will generally entitle Val to tax deductions for regular depreciation (or a first-year write-off under Internal Revenue Code Section 179). If he leases, his payments generally will be tax deductible unless the transaction is characterized as a sale instead of a lease.

Business owners should consider the pros and cons of buying versus leasing equipment before making a decision.

Client Profile is based on a hypothetical situation. The solutions we discuss may or may not be appropriate for you.

THE HIRING Game

If compensation is the only consideration, you may not be able to compete with the “big guys” for top talent. But money isn’t everything. There are highly qualified candidates who are looking at more than pay — and that’s where you might have the edge.

Responsibility. Bert was offered a supervisory position at Mega Corp, a Fortune 500 company. But he accepted a job with Small Biz instead. Although the pay is less, the scope of the job is considerably greater and more interesting.

Culture. Another thing Bert likes about Small Biz is the way the employees all work together. Large companies often strive to create a

culture of teamwork, but it can be an elusive goal.

Advancement. Bert thinks Small Biz is a better choice in this category, too. Large companies are generally slow growing. Small companies are more nimble and can expand rapidly, creating opportunities for employees to advance.

Sometimes, Small Biz is the way to go. Just ask Bert.

New Tax-advantaged Accounts FOR THE DISABLED

The Tax Increase Prevention Act of 2014 introduced a new type of state-run tax-advantaged savings program. It is designed to help meet the financial needs of disabled individuals without impacting their eligibility for certain governmental benefits.

THE ABLE ACCOUNT

From a tax standpoint, the new “Achieving a Better Life Experience” (ABLE) accounts are similar to Section 529 college savings plans. Like contributions to Section 529 plans, contributions to ABLE accounts are not deductible. Investment earnings are tax deferred and withdrawals are tax free when used to pay qualified disability expenses.



account beneficiary) include housing, education and employment training, transportation, and personal support services, to name just a few. Note that

for Supplemental Security Income (SSI) purposes, ABLE account distributions for housing expenses are considered income and amounts in the account in excess of \$100,000 are considered a resource of the designated beneficiary.

SOME DETAILS

A designated beneficiary may have only one ABLE account, and the aggregate amount donors may contribute in any year is generally equal to the federal gift-tax annual exclusion for that year (\$14,000 for 2015).

Qualified disability expenses (i.e., expenses that benefit the ABLE

POTENTIAL DRAWBACKS

To be eligible for an ABLE account, individuals must become disabled prior to age 26. When a beneficiary dies, the state administering the account can claim an amount equal to the Medicaid benefits the beneficiary received after the account was established.

... Q&A

Q I recently filed my 2014 federal income-tax return and expect to receive a refund from the IRS. Is there a way I can check on the status of my return and refund?

A The IRS has an online tool called “Where’s My Refund?” at www.irs.gov or you can use the IRS2Go mobile app, which is available for free download from the iTunes App Store (iOS devices) or the Google Play Store (Android devices). The IRS says that electronic filers can start checking on the status of their returns within 24 hours after they are received by the IRS. Taxpayers filing paper returns should wait four weeks after mailing. The tool allows you to follow your return through three stages: Return Received, Refund Approved, and Refund Sent.

Q What’s the difference between a tax deduction and a tax credit?

A A tax deduction reduces the amount of income subject to tax, while a tax credit is a dollar-for-dollar reduction in tax liability. A tax credit is generally more valuable than a tax deduction of the same amount. For example, a \$1,000 tax deduction claimed by a taxpayer whose marginal tax bracket is 25% saves the taxpayer \$250 ($\$1,000 \times 25\%$) of tax. On the other hand, a \$1,000 credit would shave \$1,000 off the same taxpayer’s tax liability. Note that certain credits are “refundable” to taxpayers whose tax liabilities are not high enough to absorb the credit.

ClientLine ITEMS.....

> WHAT ARE THE CHANCES OF GETTING AN INCOME-TAX REFUND?

Pretty good. The IRS reports that every year, nearly eight out of 10 U.S. individual tax filers get a federal tax refund. The average refund in 2014 was \$2,792.

> **SECTION 529 COLLEGE SAVINGS PLANS** may be a little more flexible after the Tax Increase Prevention Act of 2014. Plans can now allow account contributors and designated beneficiaries

to direct investments up to two times per year. Previous IRS guidance had restricted investment changes to once per calendar year.

> CHARITIES ARE HAVING TROUBLE RETAINING AND MOTIVATING DONORS.

A study by the Urban Institute found that for every \$100 in new donations a nonprofit organization received in 2013, it lost \$92 from supporters who didn't contribute again and others who gave less than

they had previously. Only 43% of 2012 donors made repeat gifts to charities in 2013.

> **EMPLOYER CONTRIBUTIONS TO 401(K) AND PROFIT SHARING PLANS** increased to 4.7% of pay in 2013, as compared to 4.5% in 2012 and 4.1% in 2011, according to a survey by the Plan Sponsor Council of America. The majority (98.1%) of plans that have a match provision made matching contributions in 2013.

The general information provided in this publication is not intended to be nor should it be treated as tax, legal, investment, accounting, or other professional advice. Before making any decision or taking any action, you should consult a qualified professional advisor who has been provided with all pertinent facts relevant to your particular situation.

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