CPA

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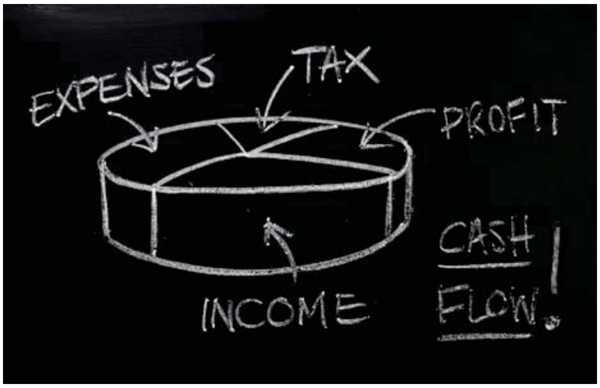
Client Bulletin

Smart Tax, Business & Planning Ideas *from your* Trusted Business Advisor℠

January 2015

What's Inside

Create a Personal Cash Flow Statement



As the year begins, this can be an excellent time to review your financial circumstances. You can look back at 2014 and see how much money came in and where it went during the year without adjusting for seasonal variations. The knowledge you'll obtain by creating a personal cash flow statement can help you make realistic financial plans for 2015. (If you're married or cohabiting, you can use this technique to create a household financial statement.)

Tabulating income

Begin the process by adding up all the spendable cash that came in during 2014. Typically, that information can be found in the monthly statements from your checking account or accounts. If you haven't kept all the monthly statements, or if you don't feel like juggling all the papers, you probably can retrieve all of last year's statements online from your bank's website.

If you are an employee, you probably have your paychecks (after various deductions) deposited directly into such an account; if you are retired, your Social Security checks (after Medicare deductions) go there, along with any pension you're receiving. Self-employment income and investment income paid by checks also will show up as deposits, as well as transfers from investment or savings accounts.

Generally, only cash income (payments in currency) won't show up in a statement from a bank or investment account. If you do receive meaningful amounts of cash regularly, you should have some idea of the total. In fact, you'll need records in case the IRS questions how much cash you've received from working during the year.

Once you've calculated all the income you've received, make any necessary adjustments. Subtract inflows not likely to occur again in 2015, such as

continued on page 2

Expensive Education

The three most expensive U.S. colleges are in New York state: Columbia ($51,008 in tuition and fees for 2014-15), Sarah Lawrence ($50,780), and Vassar ($49,570).

continued from page 1

exceptional gifts, bequests, asset sales, and so on. Altogether, you'll have an idea of how much cash flow you can expect in 2015, raising or lowering the number to keep up with current circumstances, such as a higher salary this year.

Tracking your outlays

Your checking account statements also will show how much you've spent during the year: checks you wrote, bills you paid automatically, personal checks that you cashed for spending money. Be sure to include your debit card or ATM withdrawals in the money you spent during 2014, even if they are linked to an account other than your regular checking account.

To complete the picture of what you spent during the year, request annual statements from your credit card companies. If your credit card bills are not on autopay and you've paid less than the total balance, you may have increased your outstanding debt during the year. Credit cards usually charge double digit interest rates, and the interest you pay is not tax deductible, so paying down any balances (or converting to deductible home equity debt) probably should be a top financial priority for the year.

Focus on the future

Once you have calculated your cash flow from last year and the amount you spent, you can make certain plans for 2015.

Example 1: Steve and Sue Smith had $150,000 of cash flow last year and $130,000 of expenses. The Smiths contributed a total of $2,000 a month to their 401(k) plans in 2014, or $24,000 in all. Going over their cash flow, the Smiths see they'll be able to increase their retirement savings by $20,000 in 2015 without crimping their lifestyle. They plan to boost their 401(k) salary deferrals this year.

On the other hand, this procedure can be valuable to show you that a cutback is necessary, and where to trim.

Example 2: Jim and Joan Jackson also had $150,000 of cash flow but they spent $170,000 last year, in addition to adding to their credit card balances. Going over their cancelled checks and their annual credit card summaries, the Jacksons were surprised to learn how much they spent on dining out and online merchandise purchases. They decide to rein in all their outlays, especially in those areas, and pay down their credit card balances.

Creating a personal or household cash flow statement can start your year off with a greater grasp of your finances. In addition, this exercise is an excellent way to begin gathering the data you need to prepare for your 2014 tax return. ■

Did You Know?

Among individuals age 80 and older, more than three-quarters live in their own homes. Pre-retirees also hope to "age in place." A recent survey of people 45 and older found that 73% strongly agreed that they would like to stay in their current residences as long as possible.

Source: Harvard.edu

Tax Free Roth IRA Conversions

Moving money from a tax deferred retirement account to a potentially tax-free Roth IRA usually will trigger income tax. That won't always be the case, though, thanks to recent IRS announcements. Some examples show how this can work.

Example 1: Nancy Martin has participated in her company's 401(k) plan for many years. She typically has made maximum pretax contributions to the plan. Nancy's company allows employees to make additional aftertax contributions (many employers do), which she has done. Nancy decides to leave the company at a time when she has $600,000 in the 401(k), including $100,000 from aftertax contributions.

Thanks to an IRS notice published in September (IRS Notice 2014-54), Nancy can have her plan administrator transfer $100,000 of aftertax money to a Roth IRA. Because this is aftertax money, Nancy won't owe tax on the transfer. Inside her Roth IRA, untaxed growth can continue.

Once Nancy has met the five year and age 59½ requirements, she can withdraw as much or as little from the Roth IRA as she wishes without owing any tax.

In order to qualify for this tax treatment, Nancy's Roth IRA transfer must be part of a distribution to two or more retirement accounts. Thus, she can send $100,000 to a Roth IRA and the other $500,000 to a traditional IRA. Nancy won't owe any tax on these transfers. However, her $500,000 traditional IRA (and any future earnings) will remain pretax. Nancy will owe tax on any withdrawals from that traditional IRA or any future conversion to a Roth IRA.

Beyond 401(k)s, this strategy can be executed by taxpayers with aftertax money in other types of employer sponsored qualified plans.

IRA implications

What if Nancy already had rolled her $600,000 to a traditional IRA?

In that case, any distributions from that account—including those for a Roth IRA conversion—would be considered a mix of aftertax and pretax money. If Nancy had $600,000 in a traditional IRA, with $100,000 of aftertax money, for instance, a $150,000 Roth IRA conversion would be considered $125,000 (5/6) taxable and $25,000 (1/6) untaxed.

Nevertheless, there can be a way to execute a tax-free Roth conversion in that situation.

Example 2: Assume that Nancy leaves the company and rolls her $600,000 401(k) balance to a traditional IRA. Currently, that IRA has the same balance, including $100,000 of aftertax money. Nancy has just accepted a new job with a company that sponsors a 401(k) plan for its employees.

In this situation, Nancy can roll her $500,000 of pretax money into the new company's 401(k) plan and then convert the aftertax $100,000 to a Roth IRA. Again, she'll owe no tax on either move and she'll have $100,000 in a potentially tax-free Roth IRA.

That tactic has been possible in the past but not always practical: many employer plan administrators were reluctant to accept such rollovers from IRAs into a company retirement plan because the IRS had not explained how such transactions should be handled.

That changed last year when the IRS published Revenue Ruling 2014-9, setting out the ground rules. Now, Nancy can have the custodian of her traditional IRA transfer up to $500,000 of her pretax money to the new company's plan. Nancy also has to submit a statement to the administrator of the new plan, certifying that this rollover is all pretax money. Following Rev. Rul. 2014-9, company plans are likely to accept such rollovers from traditional IRAs. ■

Trusted Advice

Roth IRA Rules

- Contributions to a Roth IRA are not tax-deductible.
- Qualified distributions are tax-free. Such distributions are made on or after the date you reach age 59½, if 5 years have passed since your first Roth IRA contribution.
- Workers and their spouses can make contributions to a Roth IRA even after reaching age 70½. There are income limits for Roth IRA contributions.
- Account owners can leave amounts in a Roth IRA as long as they live with no required distributions.

New Year's Resolutions for Business Owners

Like anyone else, business owners can begin the New Year by vowing to lose weight and revisit their insurance coverages during 2015. However, you probably should make (and implement) a separate set of resolutions to help your company prosper this year.

Here are some suggestions you can consider:

- **Turn over your paperwork.** Finish your financial statements and related supporting materials from 2014. Make hard copies of online files and store them where they'll be accessible for tax return preparation. Be sure you can locate your 2014 appointment book, in order to substantiate business meetings, and that you have recorded odometer readings of vehicles that were used for business in 2014.

  Then start new files for your 2015 financials, travel, entertainment, and so on.
- **Follow through on the forms.** In January, you'll need to send W-2 forms to employees, reporting their wages, as well as Form 1099 to contractors and other recipients to whom you paid over $600 last year. If you use a payroll service, follow up to make sure it has the needed information; if you use a software program to track outside payments, pick up blank 1099 forms at an office supply store for printing the documents you must send.

  Our office can help if you run into obstacles sending these required forms on time.
- **Execute a buy-sell agreement.** If you don't already have a formal buy-sell in place, work on getting it done in 2015. Without a buy-sell, your family may not get full value for your stake in the company in case of your death or disability.
- **Update your buy-sell.** A buy-sell often will set a price for the buyout, or a method for arriving at an acceptable amount. If you

continued on page 4

continued from page 3

already have a buy-sell in place, check on the stated price and revise it, if necessary.

- **Hold meetings.** If you operate your business as a corporation, you may be required to hold directors' and shareholders' meetings at least annually. The beginning of the year can be an excellent time to hold such meetings, to set formal plans for 2015. At these meetings, you can update bylaws, cover buy-sell agreements, and generally take care of business. Make sure the meeting's discussions are well-documented and a record is entered into your corporate minutes.

  If relevant, hold your directors' meeting first, so you'll be prepared to answer questions at the shareholders' meeting. In any event, you also might want to hold a meeting for employees, to tell them your plans for the year ahead and boost their enthusiasm.
- **Review your website.** Change all 2014 references to 2015. Remove any references to year-end holidays and replace with more timely materials. Go over all the content on your site, from personnel bios to company news, to be sure everything is up to date.
- **Scrutinize your social media presence.** Savvy participation can be a key to future growth. Do you have accounts at the major networks as well as those that are gaining ground? Do your website and marketing materials reflect those connections? You might want to have young employees (or the teenage children of older ones) evaluate your efforts there and make suggestions.

  On a related topic, does your company offer products or services that are evaluated on third-party websites? If so, you might want to assign an employee or hire a contractor to monitor such sites and see what people are saying about your firm. Any negative comments can be addressed by online responses and by in-house attention to any revealed problems. ■

TAX CALENDAR

JANUARY 2015

January 15

Individuals. Make a payment of your estimated tax for 2014 if you did not pay your income tax for the year through withholding (or did not pay enough in tax that way). Use Form 1040-ES. This is the final installment date for 2014 estimated tax. However, you don't have to make this payment if you file your 2014 return and pay any tax due by February 2, 2015.

Employers. For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in December 2014 if the monthly rule applies.

FEBRUARY 2015

February 2

All businesses. Give annual information statements (Forms 1099) to recipients of certain payments you made during 2014. Payments that are covered include: (1) compensation for workers who are not considered employees; (2) dividends and other corporate distributions; (3) interest; (4) rents; (5) royalties; (6) profit-sharing distributions; (7) retirement plan distributions; (8) original issue discounts; (9) prizes and awards; (10) medical and health care payments; (11) debt cancellations (treated as payment to debtor); (12) payments of Indian gaming profits to tribal members; and (13) cash payments over $10,000. There are different forms for different types of payments.

Employers. Give your employees their copies of Form W-2 for 2014.

For nonpayroll taxes, file Form 945 to report income tax withheld for 2014 on all nonpayroll items, such as backup withholding and withholding on pensions, annuities, and IRAs.

For Social Security, Medicare, and withheld income tax, file Form 941 for the fourth quarter of 2014. Deposit or pay any undeposited tax. If your tax liability is less than $2,500, you can pay it with the return. If you deposited the tax for the quarter in full and on time, you have until February 10 to file the return.

For federal unemployment tax, file Form 940 (or 940-EZ) for 2014. If your undeposited tax is $500 or less, you can either pay it with your return or deposit it. If it is more than $500, you must deposit it. However, if you already deposited the tax for the year in full and on time, you have until February 10 to file the return.

February 17

All businesses. Give annual information statements (Forms 1099) to recipients of certain payments you made during 2014. Payments that are covered include: (1) amounts paid in real estate transactions; (2) amounts paid in broker and barter exchange transactions; and (3) payments to attorneys.

Employers. For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in January if the monthly rule applies.

Individuals. If you claimed exemption from income tax withholding last year on the Form W-4 you gave your employer, you must file a new Form W-4 to continue your exemption for another year.

February 18

Employers. Begin withholding income tax from the pay of any employee who claimed exemption from withholding in 2014, but did not give you a new Form W-4 to continue the exemption for 2015.

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