



In This Issue

Reminder: Second estimated tax payment due June 16

Don't overlook FBAR filing requirement

Prepare for the Medicare surtax in your 2014 planning

Court case changes rules on IRA rollovers

Schedule a midyear tax review soon

Tax Planning Guide



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June 2014

Reminder: Second estimated tax payment due June 16

June 16, 2014, is the due date for making your second installment of 2014 individual estimated tax. Your check to the United States Treasury should be accompanied by Form 1040-ES. June 16 is also the due date for calendar-year corporations to make their second quarter 2014 estimated tax payment.

Don't overlook FBAR filing requirement

If you hold foreign bank or financial accounts and the total value of your account exceeds \$10,000 at any time during the calendar year, you may be required to file a Treasury Department report known as the FBAR. It's easy to overlook this requirement because it's separate from your federal income tax filing, with a different deadline and strict rules.

FBAR refers to "Form 114, Report of Foreign Bank and Financial Accounts." That form is new this year, replacing the prior Form 90-22.1.

Your 2013 Form 114 must be filed electronically with the Treasury Department no later than June 30, 2014. No filing extension is available. Contact us if you need details or filing assistance.

Prepare for the Medicare surtax in your 2014 planning

The new 3.8% Medicare surtax on net investment income (NII) appears to be here to stay. If this tax caught you by surprise when you filed your 2013 tax return, you should be better prepared this year.

- **Here's how the tax works.**

If your investment income exceeds certain thresholds, you may owe a 3.8% Medicare tax on the excess. The taxable amount would be the lesser of (a) your net investment income (NII), or (b) the excess of your "modified adjusted gross income" (MAGI) above \$200,000 for singles, \$250,000 for spouses filing jointly, or \$125,000 for spouses filing separately. MAGI is adjusted gross income increased by certain deductions and exclusions.



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Net investment income includes items from most taxable income sources, such as interest, dividends, capital gains, passive activity income, and the like. However, certain other items – including income from an active trade or business, tax-exempt interest and distributions from qualified plans and IRAs – are specifically exempt.

Note that items exempted from the definition of NII could still cause problems because of the way the surtax is calculated. For instance, if you're over age 70½ and you take a required minimum distribution (RMD) from your IRA, the payout increases your MAGI. This could push you over the threshold for the 3.8% surtax or add to the amount you already owe.

• What can you do now to reduce your exposure to the surtax? Consider these five potential strategies.

1. Time income to stay below the threshold. For example, you might delay the sale of securities until next year or sell real estate property on the installment sale basis to reduce current capital gains.
2. Include municipal bonds ("munis") in your investment portfolio. Income from munis doesn't count as NII or increase your MAGI for this purpose.
3. Avoid the passive activity rules. By meeting the tax law test for "material participation," you might be able to turn a passive activity into a regular business activity. But be aware that special rules affect rental real estate activities.
4. Convert traditional IRA funds into a Roth. Because qualified Roth distributions are generally tax-free, this may avoid future problems. Calculate the optimal amount to convert for your personal situation.
5. Maximize deductible contributions to traditional IRAs, 401(k) plans, or similar sheltered investments. Earnings in these accounts are not included in NII, and the contributions will reduce your MAGI.

At the very least, you can't simply ignore the surtax and hope it will go away. Develop a tax plan for 2014 that takes the relevant factors into account.

Court case changes rules on IRA rollovers

A recent Tax Court decision will change the way the IRS applies the law on IRA rollovers.

For years, the IRS has interpreted the IRA rollover rules to mean that a taxpayer could do one rollover per year for each IRA he or she owned. In doing a rollover, the taxpayer is not taxed on the funds taken from the IRA so long as the funds are redeposited into an IRA within 60 days of the withdrawal.

The recent court decision changed the way the tax rule is applied, ruling that the limit on rollovers should be applied on an aggregate basis – that is, only one rollover per year is allowed for all the IRAs a taxpayer owns. If a taxpayer takes funds from one IRA and rolls the money back into an IRA within 60 days, he or she can't do any other tax-free rollovers within the following 365 days.

This change goes into effect January 1, 2015; therefore, the aggregate rule won't apply for rollovers done during the remainder of 2014. Note, also, that trustee-to-trustee transfers can still be done as often as the taxpayer likes; the limit doesn't apply to these transfers because the taxpayer never has possession of any of the IRA funds.

Schedule a midyear tax review soon

As summertime approaches, tax planning is probably the last thing on your mind. The problem is that if you wait until December, there's little time for changes to take effect. But if you take the time to plan now, you still have six months for your actions to make a difference on your 2014 tax return.

Making time for 2014 tax planning now not only helps reduce your taxes, but also helps to put you in control of your entire financial situation. Tax planning should be a year-round process, but it's especially effective at midyear. Give us a call for guidance in implementing the best moves for your particular situation.

This newsletter provides business, financial, and tax information to clients and friends of our firm. This general information should not be acted upon without first determining its application to your specific situation. For further details on any article, please contact us.

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