FOCUS ON BANKING & FINANCE

Many opportunities for tax-efficient strategies for 2015

By MICHAEL JOYCE
Special for Lehigh Valley Business

With April 15 just behind us, it's a good idea to re-evaluate your 2015 investments to ensure they are as tax-efficient as possible moving forward.

Making small adjustments can significantly reduce the amount of taxes you'll owe at this time next year.

Of particular interest are these tax-saving mechanisms: gifting stocks in lieu of cash, loss harvesting, tax exempt bonds, asset allocation and asset location, Roth conversions, deferring income, owning rental property and establishing trusts.

STOCK VS. CASH

If you are considering gifting family members this year to mitigate your tax burden, it's advisable to gift low-cost basis stock rather than cash. By gifting low-cost basis stock rather than cash, you'll potentially avoid higher capital gains brackets as well as the Medicare "surtax."

Loss harvesting against realized gains is another strategy for reducing taxes owed. Investors can lessen the amount of taxes to be paid on winning investments by selling mutual funds, stocks and bonds that have lost value over the course of the tax year.

Prudent investors who manage their investments in this way will be rewarded with a lower tax bill April 2016.

AFTER-TAX YIELDS

When it comes to bonds, it's important to analyze after-tax yield equivalents to maximize tax-efficient investment income. By choosing tax-exempt bonds over taxable bonds, investors can potentially reduce their ordinary income tax and Medicare "surtax" bills.

And it bears repeating that investors are well advised to place higher income investments into a tax-deferred retirement account such as a 401k or 403b. Your employer may even match a portion of your contribution.

Investors should make every attempt to maximize their contributions to these tax-free accounts. The annual contribution limits for 401k's and 403b's in 2015 have increased to $18,000 for investors who are under 50 and $24,000 for others.

ASSET LOCATION

Another factor for investors to consider is asset location. Investors need to decide whether to place certain investments in a taxable account such as a joint or individual account vs. a tax-deferred account such as an IRA or 401k.

The dividends on many stocks are "qualified" – meaning that they are taxed at a preferential tax rate. However, there are some equities such as real estate investment trusts and master limited partnerships whose dividends are not qualified.

All things being equal, it would be better to own these investments in an IRA or 401k.

Converting traditional IRAs to Roth IRAs is another way to reduce future taxable income – although a conversion will trigger taxable income in the current tax year. The 2015 limit on contributions to IRAs remains the same as last year; $5,500 for those under 50 and $6,500 for others.

DEFERRED INCOME

For those close to retirement age, deferring income can be a smart move. Investors would be wise to consider delaying the sale of a house or making withdrawals from their IRA until they've retired and are, therefore, in a lower tax bracket.

In so doing, their tax penalty will be less than if they sold their home or cashed out of their IRA while still working.

Investors with rental income should be aware of the many available tax deductions. Landlords can deduct mortgage interest as well as interest on credit cards used for rental activity.

Depreciation, repairs, travel for rental activity, independent contractor wages and legal and professional service fees, as well as insurance premiums, all can be deducted as operating expenses.

GIVING TO CHARITIES

Finally, trusts can be established to assist charities while simultaneously protecting assets from taxation.

Charitable Remainder Trusts serve two types of beneficiaries: income beneficiaries (typically the owner and spouse) receive income during the owner's lifetime, and charitable beneficiaries receive the residual of trust assets after the owner's death.

Charitable Lead Trusts work in the opposite way – giving income to charities during the owner's lifetime and assets to named beneficiaries at the

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PENSION AND IRA CONTRIBUTION LIMITS FOR 2015

- **The contribution limits** for employees participating in 401k, 403b, most 457 plans and the federal government's Thrift Savings Plan are:
  - $18,000 for under 50.
  - $24,000 for those 50 and older.
- **The contribution limits** on annual contributions to an individual retirement account are:
  - $5,500 for those under 50.
  - $6,500 for those 50 and older.

FUNDS

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GENERATION TO GENERATION

While the donation goes to one charity, which funds itself through fees and then distributes the money to other charities, a donor advised fund is very similar to a traditional charitable foundation, Garbutt said.

The fund can be named by the donor. It could be the John Smith Foundation, for example, even though the money is going to Fidelity Charitable.

The money also can be part of post-mortem planning with the fund left to the donor's heirs to carry on the charitable work.

"It's a good feeling to put your children in charge of your 'mini-family foundation' and to encourage your children to get involved in your benevolent activities," Volpe said.

BEST INTENTIONS, BEST USE

While the individual funds may be on the small side, the overall impact of the charity's giving is substantial, Fidelity's Judecki said.

Since Fidelity Charitable was founded in 1991, it has donated more than $19 billion from the funds it has collected, donating $2.6 billion in 2014 alone.

And the money is supporting the organizations that donors are most passionate about, she said.

It simply puts their best intentions to their best use.

STRATEGIES

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time of the owner's death. These irrevocable trusts do not have to pay any capital gains taxes – so assets can be transferred tax-free to fund the trusts.

While you may have just recently submitted your tax returns for 2014, structuring your 2015 investments in these ways will significantly reduce your future tax burden.

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5 QUESTIONS WITH ...

Chuck Hangen, senior vice president, lending services division manager, ESSA Bank & Trust

How is the Lehigh Valley economy?

We are seeing signs of improvement in the local economy. Requests to finance business and real estate purchases, as well as expansion projects, are on the rise. Center city improvements in both Allentown and Easton are creating additional lending opportunities.

Hangen

Bethlehem remains strong with its Main Street corridor of retail and restaurants. Its south side is expected to see growth as the City Revitalization and Improvement Zone program begins to implement projects.

Are business people confident? Are consumers confident? Why or why not?

Overall, it appears that there is more confidence in individuals as seen by the increase in loan applications. However, it does not seem that everyone shares the same confidence.

Individuals are ready to move on deals but are not willing to overpay just to buy something. The deal must be right.

What advice would you give to a business looking to select a bank?

The first piece of advice I would give to a business when selecting a bank is to make sure you have the ability to talk to decision-makers and gauge if they offer the products and services your business needs to expand and grow.

New technology in electronic banking and cash management can make life a whole lot easier for businesses to quickly respond to the market. These types of services can be explained by an experienced bank manager [that] businesses can confidently invest in.

Three years ago, you expanded into the Lehigh Valley. How is that going, and what are your future plans for the Lehigh Valley?

Progress has been going well in Lehigh Valley. In the future, ESSA Bank & Trust looks to expand its products and services, including investment and advisory services.

ESSA Bank & Trust is a pretty well-known name in Monroe County, our home county. We want to create the same kind of awareness in the Lehigh Valley, not only about our products and services, but also our employees.

Knowledgeable employees that help businesses reach their goals are the key to our success.

If you could change one thing about your industry, what would it be?

If I could change one thing, it would not necessarily be deregulation, but slowing down the pace at which new regulation and laws come into effect and the constant revision that comes along with those changes.

That would help free up our staff to do what they do best – serve our customers.

Editor's note: Appearing periodically, 5 Questions With spotlights a business professional's take on the economy and other industry issues. If you have a suggestion for a subject for this feature, please email Bill Kline at billk@lvb.com.