MARKET STREET TRUST COMPANY

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TAX PLANNING

New Tax Legislation Impacts 2013 Returns

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After completing another tax season, an analysis of filed returns confirms what we and other observers have been saying - that taxpayers would see increases in tax on their 2013 income tax returns. New taxes and the resurgence of deduction and exclusion phase-outs and limitations increased tax liability for many individuals. Some of the most notable changes that went into effect in 2013 included:

Net Investment Income Tax (NIIT)

As a result of the 2010 Affordable Care Act, also known as "ObamaCare", a brand new tax on taxpayers with adjusted gross income (AGI) exceeding $250,000[1] came on the scene in 2013. This new Medicare tax, called Net Investment Income Tax (NIIT), is an extra 3.8% tax on investment income and is in addition to the applicable income tax and/or Alternative Minimum Tax (AMT). For many high net worth taxpayers, investment income represents a large portion of their total income. So what types of income are subject to NIIT? Investment income includes:

- Interest;
- Dividends;
- Net capital gains;
- Rental and royalty income;
- Non-qualified annuity income;
- Income from businesses that trade financial instruments; and
- Income from passive activities such as partnerships in which the taxpayer does not actively participate.

Additional Medicare Tax

Another new tax resulting from the 2010 Affordable Care Act that took effect in 2013 was the Additional Medicare Tax. This tax is an additional 0.9% tax on earned income of taxpayers whose earned income exceeded the threshold amount for the individual's filing status. This applies to wages, compensation and/or self-employment income exceeding $250,000.[1]

Itemized Deduction Limitation

Another sizeable change for many was the return of the Itemized Deduction Limitation. Itemizing deductions is a planning strategy that might reduce overall tax liability; did you know that now when a joint filer's AGI reaches $300,000, a phase-out applies? At this income level, certain itemized deductions are reduced by the lesser of 3% of AGI in excess of the threshold or 80% of the amount of itemized deductions otherwise allowable for the taxable year, meaning that a taxpayer with an AGI of $500,000 could see a $6,000 reduction in his or her itemized deductions.[2] (The tax impact of this reduction at the 39.6% tax rate is $2,400.)

Dependency Exemption Phase-out

The Dependency Exemption Phase-out also returned in the 2013 tax year. Legislation mandates that married taxpayers filing joint returns begin to lose dependency exemptions once AGI income levels reach $300,000. The exemptions are lost at a rate of 2% for each $2,500 over $300,000 AGI and once AGI hits $422,501, the exemptions disappear entirely.[2] (The tax impact of the loss of exemptions at the 39.6% tax rate is $1,550 per exemption lost.)

At first glance, any of these changes in and of themselves may seem somewhat small. However, the combined effect of these changes can have a substantial impact on taxpayers. Take for example, a couple[1] with two children and an adjusted gross income of $500,000 (all of which is classified as investment income). The combined changes could have the following approximate tax dollar impact for this couple:

NIIT	$10,000
Itemized Deduction Limitation	$2,400
Dependency Exemption Phase-out	$6,200
Total Tax Increase	**$18,600**

Since there doesn't appear to be any relief on the horizon from Washington on income taxes, similar income tax liabilities for 2014 are expected and the addition of the shared responsibility payment in 2014 (discussed below) could increase the total bill.

What is new on your 2014 returns

The next phase of the implementation of the 2010 Affordable Care Act took effect on January 1, 2014 and will impact 2014 income tax returns. All individuals, regardless of their age, must have minimum essential health care coverage or they could be subject to a shared responsibility payment. The shared responsibility payment will be assessed on a monthly basis and ranges from a $95 minimum up to 1% of household income less a filing threshold, determined by filing status. There are exemptions from this requirement and possible credits for lower income situations, but everyone is going to have to include information on their 2014 tax return in order to calculate the payment. This payment will be due with the income tax bill.

Careful planning will be required to keep taxes to a minimum. Fortunately, the current tax environment is full of opportunities for high net worth taxpayers to utilize wealth transfer (through gift and estate planning) as a way to save not only gift, estate and Generation Skipping Transfer (GST) taxes, but also income taxes when income producing assets are gifted to individuals in lower tax brackets.

What Market Street is doing for clients

Market Street is focused on proactive tax planning and tax efficiency. Minimizing tax impact is a major driver of our planning process. From the investment managers we select, to the wealth transfer and estate planning advice we provide, we have developed a tax efficient comprehensive financial management program that pervades all we do.

Some examples of opportunities and strategies we use for our clients to take full advantage of solutions available include the following financial planning tools:

Gifts to Charity are itemized deductions. We plan to ensure maximization of those gifts in light of deduction limitations and tax impact. One example of that planning is gifting appreciated stock to maximize the charitable deduction while saving capital gains tax that would be due if the asset was sold instead.

Grantor Retained Annuity Trusts (GRATs) are trusts established and funded with assets by the grantor that pay a series of annuities to the grantor over the GRAT's term. If the assets appreciate above the applicable federal rate, the appreciation passes to the remainder beneficiaries (usually children), gift tax free.

Annual Exclusion Gifts can be made to any individual (and as many individuals as you like) without any impact on your lifetime exemption. The annual exclusion amount for 2014 and 2015 is $14,000 for individuals. Married couples can combine their annual exclusion amounts and gift $28,000 to individuals even if the gift comes from one person. Special favorable rules apply to § 529 plans (tuition programs).

Direct payment of medical and tuition bills are gifts that can be made in addition to annual and lifetime exclusion gifts. These gifts can be made without limit but are subject to certain rules including that the expenses not be reimbursed and that these gifts be paid directly to the provider.

Lifetime Gift Tax Exclusion is the total amount a person can give away in their lifetime without incurring current taxes on the gift. This is in addition to annual exclusion gifts and direct payment gifts. The lifetime exclusion amount for 2014 is $5.34 million and will increase to $5.43 million for 2015.

It is paramount to pay close attention to your tax situation. Be sure to keep your records up to date whenever something changes in your life, including changes in employment, charitable gifting plans, a contemplated change to your state of residence and other similar life changes.

[1] Married filing jointly. Any foreign earned income exclusion is added back to adjusted gross income for the NIIT.

[2] Taxpayers subject to AMT may not be impacted

HOLIDAY SHOPPING:

How each generation will do their holiday shopping this year

By: Kim Lear, BridgeWorks Generational Expert

It's the most wonderful time of the year…for shopping! Yes, we're in the thick of the holiday shopping season…from Black Friday to Cyber Monday to Green Monday. And each of the generations has something to say about how they are spending their hard-earned cash this winter.

Folks were out in full force on Black Friday, some even starting on the actual Thanksgiving holiday. According to a recent Time Magazine article, Millennials were behind the early start, even if that meant leaving the turkey dinner behind a little earlier than usual.

So what can we expect from each generation during this holiday season?

Millennials

Millennials crave experiences. Many Millennials would rather spend money on a concert or a trendy restaurant than a car. They treated Black Friday as an experience…enjoying the freedom to head out after the family Thanksgiving to stand in line with their friends and snap selfies.

They will continue to search for "retail-tainment" during the remaining holiday shopping season. For example, Cabela's will put a large aquarium in the store, while Victoria's Secret will invite customers to a free private party with DJs. For Millennials, holiday shopping isn't going to be just a chore; it's going to be a shareable experience.

Gen X

Many Gen Xers are the parents out on the front lines of the shopping wars looking for that affordable big name toy

or game for their kids. Skeptical Xers will be the ones scouring prices online and making sure they are getting the best deals. While the Millennials were shopping online since they were teenagers, the Xers can still be a little apprehensive when making purchases online. Some Xers like to touch and see a product before they pass over their credit card. Even though Gen Xers do a lot of research, they are still nervous that they might get a lemon; therefore, they're going to read the fine print to make sure the return policy is a good one.

Baby Boomers

Baby Boomers may have the longest holiday shopping list of all. Some Baby Boomers are looking for gifts for parents, children AND grandchildren! Let's just say that the Sandwich Generation is now becoming a three-decker club! With so many folks to buy gifts for, the Boomers are just asking for a little simplification when it comes to the buying experience. They work hard to get everyone's gift lists, and just want to check them off as quickly and easily as possible. So keep it simple—a "one-stop shop" would be just the way to go. Millennials and Gen Xers usually get all the attention for online shopping habits, but this year we may see Boomers flocking online in order to get gifts for all the loved ones in their life.

Each generation may go about holiday shopping differently but at the end of the day, each generation is simply trying to put a smile on a face of a loved one. Enjoy the holidays and happy shopping!

Unclaimed Funds

By: Caroline Larson, Business Development Associate

Want a little extra spending money this holiday season? You are in luck! Someone might owe you money of which you are completely unaware. This is the case today for millions of Americans who have unclaimed property. The good news is that there is a simple process to search for and retrieve your unclaimed funds.

According to the National Association of Unclaimed Property Administrators (NAUPA), there is approximately $41.7 billion in unclaimed property in the United States and the average claim amount is $892. In 2014 alone, the state of New York has returned over $360 million worth of unclaimed property to its rightful owners.

NAUPA defines unclaimed property as "accounts in financial institutions and companies that have had no activity generated or contact with the owner for one year or a longer period." There are various types of unclaimed property, a few examples being dormant checking or savings accounts, unredeemed gift certificates, security deposits, or contents of a safe deposit box.

As a result of the Uniform Unclaimed Property Act, and to help better protect consumers, each state is required to have an unclaimed property fund where all abandoned assets are held until claimed by its owner. Some states hold this money in perpetuity and other states will hold it for a designated time period before it is turned over to the state.

Would you like to see if you have unclaimed property under your name? Just go to www.unclaimed.org, select the state you currently reside in (or states you used to live in), and type in your name. A list will generate with all the unclaimed funds in your name, if any. You can claim it either online or via a mail claim form. Going on a treasure hunt for your unclaimed property is easy. Happy hunting!

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