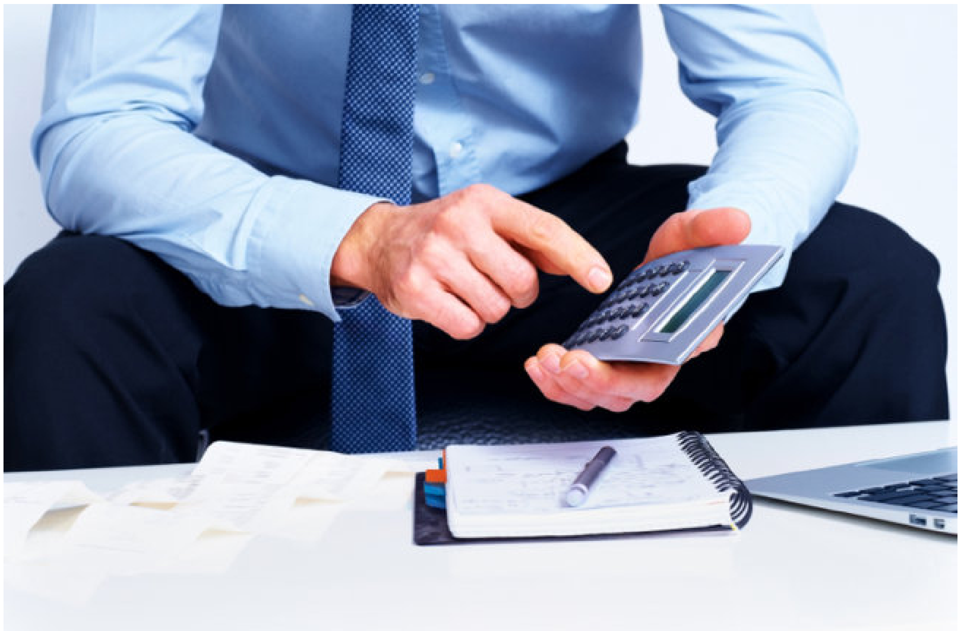
Tax Changes Coming in 2015

Taxpayers can save more in a 401(k) but will face stiffer penalties for skipping health insurance.



Some major changes are coming that will effect tax benefits, retirement accounts and the Obamacare tax penalty.

By Susan Johnston | Dec. 23, 2014 | 11:30 a.m. EST + More

Just in the nick of time, as 2014 winds down, the Senate recently extended several tax provisions – including mortgage debt forgiveness and credits for energy-efficient home improvements – that had expired at the end of last year.

Those extensions will apply retroactively, but it's unclear whether taxpayers will be able to claim them beyond 2014, which makes it challenging for taxpayers (and their accountants or tax preparers) to plan ahead. "Consumers don't know what to do," says Paul Gevertzman, a tax partner in accounting firm Anchin, Block & Anchin in New York City. "Should I make this purchase? Is it going to be deductible? Should I wait until they've changed the law? It hampers people from making these decisions."

However, the IRS has announced a few other small changes to the tax code going forward that you can plan on. Here's a look at what you need to know.

Inflation adjustments. In October, the IRS announced several tax benefits that will increase next year due to inflation. The maximum Earned Income Tax Credit amount will be $6,242 for those filing jointly who have three or more qualifying children, up from $6,143 in 2014. The personal exemption will rise to $4,000, up from the 2014 exemption of $3,950, but that exemption phases out at higher income levels (beginning at $258,250 for single taxpayers or $309,900 for married couples filing jointly and phasing out completely at $380,750 for single taxpayers or $432,400 for married couples filing jointly).

All of a child's unearned income (for instance, interest or dividends) above $2,100 will be taxed at the parent's tax rate, up from $2,000 in 2014. However, The annual gift tax exclusion remains at $14,000 per person.

Retirement. The IRS has increased the contribution limit for 401(k) and similar plans from $17,500 to $18,000 for 2015. The catch-up contribution limit for those age 50 and over will also increase $500, from $5,500 to $6,000. While the 401(k) contribution limit has been gradually rising the past few years, the catch-up contribution limit had remained at $5,500 for the past several years.

An extra $500 in a retirement account may not seem like much, but saving that amount over 25 years, assuming an 8 percent annual return, could yield an extra quarter million dollars in your retirement portfolio, points out Kimberly Foss, certified financial planner and founder and president of Empyrion Wealth Management in Roseville, California. "In one year's time, people just discard [the opportunity to save more]," she says. "But it does make a difference, especially in those critical compounding years between 40 and 65."

Starting in 2015, the IRS will also limit nontaxable IRA rollovers to one every 12 months regardless of how many individual retirement accounts you have. In the past, people with multiple IRAs would take advantage of a provision allowing them to withdraw money, and put it back within 60 days without the tax hit of an early distribution. By rolling money from one IRA to another, they could essentially give themselves a short-term loan because the money was held in separate accounts. "If you had a fair amount of IRA funds and you didn't care about the paperwork, you could set up multiple IRAs and do multiple loans per year," says Robert Zeigen, tax director at professional services company CBIZ MHM in Florida. "That was pretty common." Note that trustee-to-trustee transfers between IRAs and rollovers from traditional to Roth IRAs are not limited.

Health care. Under the Affordable Care Act, the penalty for not having health insurance increases from $95 per adult (or 1 percent of income, whichever is greater) in 2014 to $325 per adult (or 2 percent of income) in 2015. If you're enrolled in health insurance through the federal marketplace, you can renew your current plan or choose a new one through Feb. 15, 2015, although some states have different deadlines for their own marketplaces.

Other changes apply to flexible spending accounts and health savings accounts. As of 2015, employees can save $2,550 in an FSA, up from $2,500. Previously, FSAs had a "use it or lose it" rule that forced employees to use up funds for eligible medical expenses before Dec. 31 (or in some cases, during a spring grace period) or forfeit that money.

Earlier this year, the IRS announced that employers could now allow employees to carry over up to $500 from one year's FSA into the next. But if you're also using an HSA, then you can't also take advantage of the FSA carry over provision. Gevertzman says an HSA is better than an FSA for most people because it has higher contribution limits (up to $3,350 for individuals or $6,650 for a family in 2015) and greater flexibility. "It's almost like a retirement plan because you don't use it or lose it," he says. "Whatever you don't spend gets carried forward, and you can earn income that gets tax deferred."

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