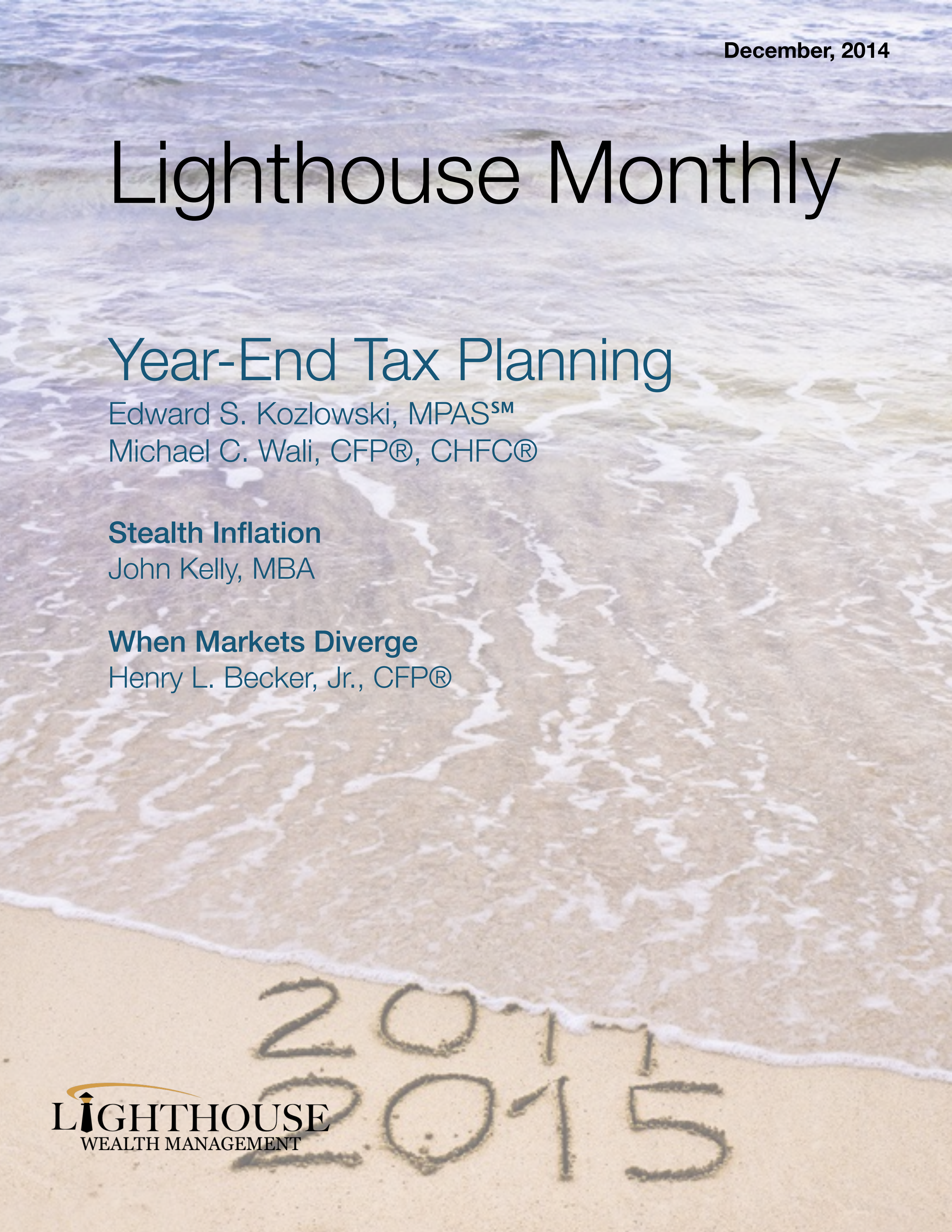

December, 2014

# Lighthouse Monthly

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LIGHTHOUSE
WEALTH MANAGEMENT

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# Year-End Tax Planning

Edward S. Kozlowski, MPAS℠ - Partner & Director of Tax Services

As we roll closer to the end of the year we also get closer to the time-honored American tradition of filing taxes.  Since we are still in 2014, there are still some ways and strategies to save a little money on taxes.

Below is a list of items to consider as we go into year end.

**Tax Loss Harvesting** - If you have investment positions in your portfolio that are showing a capital loss (not your IRA accounts) you can sell those positions to lock in the loss.  The losses can then be used to offset gains you may have or offset up to $3,000 of income.

**Postpone income until 2015 and accelerate deductions into 2014 to lower your 2014 tax bill** - This strategy may enable you to claim larger deductions, credits, and other tax breaks for 2014 that are phased out over varying levels of adjusted gross income (AGI). These include child tax credits, higher education tax credits, and deductions for student loan interest. Postponing income also is desirable for those taxpayers who anticipate being in a lower tax bracket next year due to changed financial circumstances. Note, however, that in some cases, it may pay to actually accelerate income into 2014. For example, this may be the case where a person's marginal tax rate is much lower this year than it will be next year or where lower income in 2015 will result in a higher tax credit for an individual who plans to purchase health insurance on a health exchange and is eligible for a premium assistance credit.

**Defer Bonuses** - It may be advantageous to try to arrange with your employer to defer a bonus that may be coming your way until 2015.

**Use credit wisely** - Consider using a credit card to pay deductible expenses before the end of the year. Doing so will increase your 2014 deductions even if you don't pay your credit card bill until after the end of the year.

**Adjust tax withholding** - If you expect to owe state and local income taxes when you file your return next year, consider asking your employer to increase withholding of state and local taxes (or pay estimated tax payments of state and local taxes) before year-end to pull the deduction of those taxes into 2014 if doing so won't create an alternative minimum tax (AMT) problem. » **More**

**AMT planning** - Estimate the effect of any year-end planning moves on the alternative minimum tax (AMT) for 2014, keeping in mind that many tax breaks allowed for purposes of calculating regular taxes are disallowed for AMT purposes. These include the deduction for state property taxes on your residence, state income taxes, miscellaneous itemized deductions, and personal exemption deductions. Other deductions, such as for medical expenses, are calculated in a more restrictive way for AMT purposes than for regular tax purposes in the case of a taxpayer who is over age 65 or whose spouse is over age 65 as of the close of the tax year. As a result, in some cases, deductions should not be accelerated.

**Bunching deductions** - You may be able to save taxes this year and next by applying a bunching strategy to "miscellaneous" itemized deductions (i.e., certain deductions that are allowed only to the extent they exceed 2% of adjusted gross income), medical expenses and other itemized deductions.

**Required Distributions** - Take required minimum distributions (RMDs) from your IRA or 401(k) plan (or other employer-sponsored retirement plan) if you have reached age 70-1/2 . Failure to take a required withdrawal can result in a penalty of 50% of the amount of the RMD not withdrawn. If you turned age 70-1/2 in 2014, you can delay the first required distribution to 2015, but if you do, you will have to take a double distribution in 2015-the amount required for 2014 plus the amount required for 2015. Think twice before delaying 2014 required distributions to 2015 as it might might push you into a higher tax bracket or have a detrimental impact on various income tax deductions that are reduced at higher income levels. However, it could be beneficial to take both distributions in 2015 if you will be in a substantially lower bracket that year.

**Health Care** - Increase the amount you set aside for next year in your employer's health flexible spending account (FSA) if you set aside too little for this year.

**Maxing out HSA** - If you are eligible to make health savings account (HSA) contributions in December of this year, you can make a full year's worth of deductible HSA contributions for 2014. This is so even if you first became eligible on Dec. 1, 2014.

**Gifting** - Make gifts sheltered by the annual gift tax exclusion before the end of the year and thereby save gift and estate taxes. You can give $14,000 in 2014 to each of an unlimited number of individuals but you can't carry over unused exclusions from one year to the next. The transfers also may save family income taxes where income-earning property is given to family members in lower income tax brackets who are not subject to the kiddie tax.

*- The above is provided to stimulate thought and should not be construed as tax advice. Be sure to check with your tax professional regarding your particular situation.*

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# Stealth Inflation

John Kelly, MBA - Support Paraplanner

Frequent business television patrons or mainstream print media readers are bombarded with reports that there is little inflation in the economy. Those that pay even a modest amount of attention to their spending know otherwise. We all know that the cost of certain, obvious things such as healthcare and college have rocketed upward. Those that pay attention in the grocery store most likely have noticed that certain food costs move periodically.

However, there is a more insidious inflation that we do not see and that is 'stealth inflation.'

My personal example has to do with a pair of khaki pants I bought a few years back that had a coin pocket feature. I recently had to replace the pants. After about a week of owning the new pants, I went to put some parking change in the coin pocket and to my surprise there was no coin pocket. Now, keep in mind that these were the same pants from the same online retailer.

To satisfy my curiosity, I laid both pair of pants on the floor side by side and analyzed the differences. I started by looking at cost which was the same even after three years. For most, the fact that cost is the same may prove that there is not inflation. Yet, if we look at the pants we find some differences that are surely not accidental. First, as we already know, there was no coin pocket on the new pants. Second, there were two fewer belt loops. Third, the heft of the material was not quite the same. I am sure you get the point here.

From manufacturers to food makers there has been a stealth reduction in quality and/or quantity yet prices remain flat. If you put yourself in the shoes of manufacturers of finished goods or food makers, a first step in trying to retain profitability when input costs rise is to hold prices steady and lower quality or quantity.

Over the last few years there have been a number of articles in the media pointing stealth inflation in boxes of tissues, bacon, candy bars, orange juice and peanut butter. The issue is the same over time and that is prices hold and quantity drops. So, the next time you hear that there is no inflation consider that stealth inflation is often not considered in the mix.

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# Market Review

## When Markets Diverge

Henry L. Becker, Jr., CFP® - Partner & Director of Investment Research

This past year has been one of the more pronounced divergent markets many have ever seen. The US stock market as a whole has diverged amongst its market cap weighted indexes. In addition, we have seen developed western markets diverge greatly. Lastly, the gap between economic fundamentals and investing markets has grown ever wider.

It is one thing for different segments of the stock market to outperform, it is another to have such a wide disconnect between the markets and the economy. Consider chart one that outlines the percent change in US population, US GDP and the S&P 500 index since March 2009. You will note that the S&P has grown nine times more than US GDP and dwarfs the population growth rate.

In chart two, we see the divergence between the S&P 500 (black) and the US 10-year Treasury Yield (red). Historically, the two have moved together but now are diverging from one another thanks to the ongoing economic intervention of global central banks such as the Fed. ➳ **More**

**Chart one**

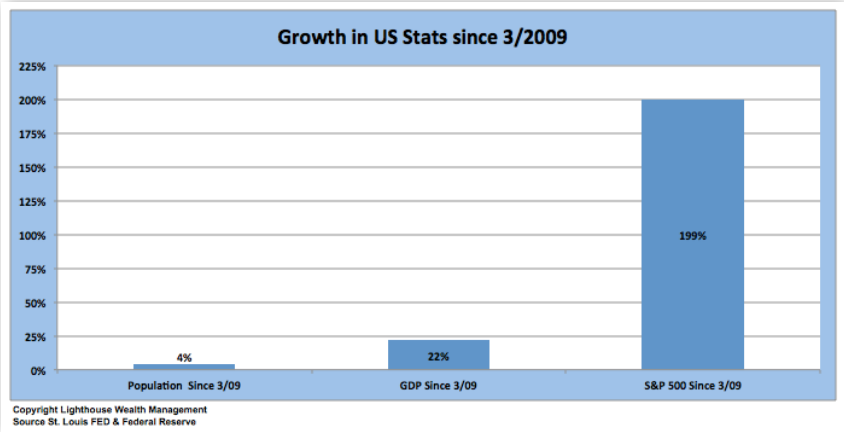
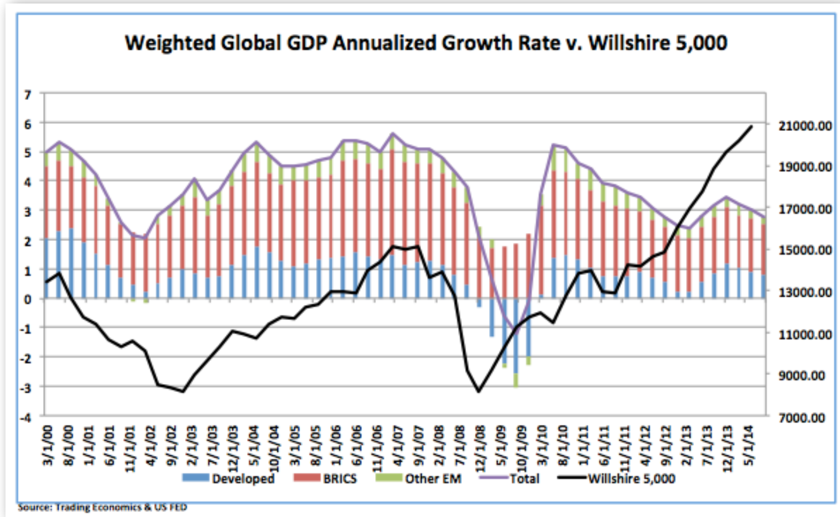



**Chart two**

Chart three graphs weighted global GDP annual growth rates versus the Wiltshire 5,000 US stock index. The Wiltshire 5,000 is considered the total US stock market index. As you can see, since 2010 global GDP growth has been sliding while the total US stock market has risen.

Chart three




Lastly, in chart four we have the S&P 500 (black) versus the Dow Jones Commodity Index (red). You can see that historically these two have tracked each other very closely. But, since 2011 this relationship appears to be broken.

Chart four


## Bottom line

The common thread through all of the charts is that US stocks are moving in one direction and the other data points in the other direction. Obviously, this has been going on for a few years. And, it could go on a bit longer. In the end, stock values must be predicated or underpinned by economic fundamentals.

As the gap between stocks and fundamentals grow we maintain our cautious stance on stocks. Logic alone tells us that stocks will have to catch down to the economy, meet the economy in the middle or the economy will have to roar higher. Two out of three scenarios call for lower stock prices ahead. A wise investor will not just look at the market but also the context that it operates within. The context is what gives the investor clues about what lies ahead. The tricky part is timing. Just because something looks eventual it may not be imminent. Therefore, investing in such unique times will require either a blind eye toward risk or plans to protect capital. We choose to keep the risks in focus and remain prepared to protect client capital when necessary.

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