TAX NEWSLETTER

2007 FALL NEWSLETTER

October 4, 2007

Dear Clients and Other Friends-

As another year end approaches, it is time to review your 2007 tax plan. And, as is becoming a regular routine, Congress is making it more difficult by waiting until the last minute to decide whether to extend certain tax breaks.

Some background – to its credit, Congress tries to make any tax change revenue neutral. So, if they give a tax break, they raise revenue somewhere else. Unfortunately, this admirable goal results in some real game playing. First, they come up with revenue raisers that would never make it in a home budget. For example, to fund a recent tax change they increased the estimated tax payments of large corporations due in July, August, and September, 2012. These payments are to be increased from 114.75% to 115% of the payment otherwise due and the next required payment is reduced accordingly. No additional revenue is raised. They robbed one year to fund the preceding year. Try that in your home budget and see how long it works.

Another “trick” they use is to approve tax breaks for just one year at a time. Then they only have to come up with revenues to fund the break for the one year. This leaves us in the position we presently are at. We are trying to plan based on changes that probably will be made, but may not be made especially since Congress and the Administration get along like the Dawgs and the Cougs. Ah, true bipartisan stupidity.

So, what tax changes are pending? One is the AMT. Will Congress extend AMT relief to avoid millions more becoming entrapped by it in 2007 and if so, how will they do it? Another big one for us in Washington is the option to deduct state and local sales tax. Since we do not have a state income tax, this is an important deduction. Other potential changes are the above-the-line deductions for qualified tuition expenses and educator expenses, the tax credit for making qualifying energy saving improvements to a home, such as insulation and energy-saving windows, and the option for individuals who have attained age 70-1/2 to exclude up to $100,000 a year for otherwise taxable distributions from an IRA (or a Roth IRA) that are paid directly to a qualifying charitable organization by the IRA trustee. For businesses, tax breaks that will expire at the end of this year unless they are extended by Congress include the research tax credit, faster write-offs for leasehold and restaurant improvements, and enhanced deductions for certain contributions to charity.

The good news with all this is I will most likely have a reason to send out another newsletter before the end of the year.

With all of the above said, I have compiled a checklist of actions that may help you to save taxes if you act before year-end. Not all actions will apply in your particular situation, but you will likely benefit from some of them. If you have any questions on whether a particular action can help you, please contact me.

•Increase the amount you set aside for next year in your employer's health flexible spending account if you set aside too little for this year. Don't forget you can set aside amounts to get tax-free reimbursements for over-the-counter drugs, such as aspirin and antacids. Tax laws – antacids: kind of go together don’t they……………

•Review the amount of your capital gains or losses from sales of stock or other capital assets to maximize the tax benefits. You may want to sell additional stock.

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•If you or a family member are thinking of selling appreciated stock or other capital assets, and your (or their) income isn't taxed at a rate higher than 15%, it may pay to hold off on the sale until 2008. That way you may pay a zero tax on the gain; if you sell this year, you will pay a 5% tax on the gain.

•If you own an interest in a partnership or S corporation you may need to increase your basis in the entity so you can deduct a loss from it for this year. Of course, most of my clients only have profits from their busnesses……

•Consider using a credit card to prepay expenses that can generate deductions for this year. Use this idea cautiously. For an individual, this might work if you have enough medical expenses in 2007 to be able to exceed the 7.5% floor, but you most likely will not in 2008. Also, cash basis business can use this method to accelerate deductions.

•If you are thinking of making energy saving improvements to your home, such as putting in extra insulation or installing energy saving windows, consider doing so before year end in order to qualify for a tax credit that may not be available after 2007.

•If you are thinking of buying a hybrid vehicle eligible for a tax credit, purchase it before year-end. Be sure to inquire how much credit the particular hybrid qualifies for.

•You may want to pay contested taxes to be able to deduct them this year while continuing to contest them next year. Of course, none of my clients would ever be in this position…..

•Business clients also should consider making expenditures that qualify for the $125,000 business property expensing option.

•You may be able to save taxes this year and next year by applying a bunching strategy to “miscellaneous” itemized deductions, medical expenses and other itemized deductions (as noted above). However, if you are subject to AMT it will not help to bunch taxes or miscellaneous itemized deductions.

•Those facing a penalty for underpayment of estimated tax may be able to eliminate or reduce it by increasing their withholding.

•Self-employed individuals should consider setting up a self-employed retirement plan.

•You can save gift and estate taxes by making gifts sheltered by the annual gift tax exclusion before the end of the year. You can give $12,000 in 2007 to an unlimited number of individuals but you can't carry over unused exclusions from one year to the next. No, your family members do not qualify as a charity so you do not get an income tax deduction………..

•This year the kiddie tax rules apply to kids under age 18; next year they will also ensnare most children age 18 and most full time students age 19 through 23. If your child holds appreciated stock, and isn't in kiddie tax territory this year but will be in 2008, consider having him or her sell the stock this year. In many cases this will result in a 5% tax on the gain, instead of 15% if the sale is postponed till next year. I don’t know about you, but when our sons were 23 I sure didn’t dare call them “kiddies”……….

•If you're thinking of donating a used auto to charity, you may want to inquire whether the charity plans to sell the car or use it in its charitable activities; the latter may yield a bigger deduction for you.

•If you are contemplating marriage or divorce consider how marriage penalties could affect you. Boy, this is real example of where taxes invade every part of our lives….

•If are age 70-1/2 or older, and own IRAs (or Roth IRAs), and are thinking of making a charitable gift before year-end, arrange for the gift to be made directly by the IRA trustee. Such a transfer can achieve important tax savings but it won't be available after 2007 under current law.

•Consider extending your subscriptions to professional journals, paying union or professional dues, enrolling in (and paying tuition for) job-related courses, etc., to bunch into 2007 miscellaneous itemized deductions subject to the 2%-of-AGI floor. Again, watch AMT……….

•Depending on your particular situation, you may also want to consider deferring a debt-cancellation event until 2008, electing to deduct investment interest against capital gains, and disposing of a passive activity to allow you to deduct suspended losses.

These are just some of the year-end steps that can be taken to save taxes. However, you need to balance the tax savings with other financial considerations before you implement a tax saving strategy. Often times the tax savings is just one of timing. You would receive it next year anyhow, but you are speeding it up to this year. The time value of money makes this worthwhile IF the benefit is not offset by other considerations such as interest on borrowed money. I would be happy to review with you the benefits of a particular strategy for your circumstances.
I will be in touch again when Congress decides what they are going to do to or for us.

Tim

Disclaimer: By nature of a newsletter, this information is in summary form and does not necessarily detail every requirement, restriction or tax planning opportunity. Prior to executing any tax strategy, you should consider non-tax implications - you may cost yourself more than you save in taxes. Please use this information with these limitations in mind. If you are considering executing a particular tax strategy, please contact me so we can discuss the specifics.

Any tax advice in this communication is not intended to be a "covered opinion." Therefore this communication cannot be used by any party to avoid penalties which may be imposed by the Internal Revenue Service.