The Financial Navigator - December Newsletter

Happy holidays to all. Since we are nearing the end of the year this newsletter focuses on tax planning moves that can be made in December to reduce your 2009 tax bill. Bottom line; review your tax situation now before the end of the year! Too often over the years I have received calls from clients on December 31rst to discuss potential tax saving strategies, which is about 30 days too late. So look below for some ideas that might apply to your situation. If you have any questions on the information below please feel free to give me a call.

Sincerely,

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2009 Tax Planning

Year-end tax planning always makes sense, but this year it's especially critical as the economic crisis and the turbulent markets have created opportunities to cut your tax bill through 'crisis legislation' passed this year. In addition, there are potential tax traps looming as tax rates may change in the next year as lawmakers confront record deficits, so read on.

Investment Tax Loss Harvesting

Even after the run-up following the lows of last March, many investors still have long-term capital losses on investments held longer than one year. Taxpayers may deduct up to $3,000 of these losses per year against ordinary income, with the excess losses carried forward for use in future years. The assets must be actually sold, and held in taxable accounts, as opposed to IRAs and other tax-sheltered retirement plans.

Capital losses also may be matched dollar-for-dollar against capital gains. For example, if you have $15,000 of long-term losses on some investments, theses losses could be used to eliminate up to $12,000 of gains on others, after taking the $3,000 deduction against your ordinary income. Beware of the tax code's 'wash sale' rules which applies to investment loses; the Internal Revenue Service says a 'wash sale' occurs when you sell or trade a stock or securities at a loss and buy the same stock, or something 'substantially identical' within 30 days of the sale. (That means within 30 days before or after the sale.) If you violate the rule, you can't deduct your loss.

Lock in 15% Capital Gains Tax Rate

If you are bullish on an investment with gains, it may make sense to sell it to soak up losses, or to just lock in the 15% capital gains tax rate. Then you can always purchase the identical investment right back as the 'wash sale' rule only applies to losses. This may be a wise strategy since the current top capital-gains tax rate of 15% is the lowest in decades. As the law stands today, this capital-gains rate will increase for upper-income tax payers in 2011; however, with the record deficit there is some thought that rate increases may apply to 2010. It should be noted that there is a history of tax increases passed in mid-year, or later, being made retroactive to the beginning of the year, see the 'kiddie-tax' changes two years ago and the estate tax increases during the Clinton years. So if you are in the upper income tax brackets, consider locking in the

15% tax rate now by selling the investment in 2009. As mentioned above you can always buy the investment back which resets the basis in the investment. The only capital at risk would be the commissions you pay on the sell and buy orders, which would be minimal in comparison to potential hundreds or thousands of dollars in tax savings.

For more details, see IRS publications 17 and 550, available at www.irs.gov.

First-Time Home-Buyer Tax Credit

Congress has just extended and altered this benefit, making it more generous for many; the new rules took effect on Nov. 6. The provision is a true dollar-for-dollar tax credit of up to $8,000 for 10% of the cost of a home. The credit is also refundable, meaning that even if a buyer doesn't owe $8,000 of tax, she can claim the full benefit and receive a refund check. In addition, the new law has more generous phase-outs. The credit now begins to disappear for single taxpayers with modified adjusted gross incomes of $125,000 and married couples with incomes of $225,000. It is available for purchases through July 1, 2010 if the buyer has a contract in place before May 1, 2010. It also authorizes a similar $6,500 credit for buyers who already own a home. It too is a refundable credit for 10% of the purchase price of a house costing no more than $800,000. To qualify the buyer has to have owned and lived in the same home for five of the eight years preceding the new home purchase, and the new home must become the buyer's principal residence.

Medical Expenses

Check your medical expenses as you may be able to deduct some of your out-of-pocket expenses. This has long been one of the least useful deductions in the tax code, because the taxpayer must spend more than 7.5% of adjusted gross income to claim any deduction. However, rising insurance costs and diminishing coverage plus this year's economic turmoil may qualify more people for this deduction. In general, taxpayers may deduct all un-reimbursed medical expenses recognized by the IRS. This category includes after-tax dollars spent on insurance premiums, Medicare Part B and D premiums, and co-payments for drugs and treatments. It also extends to costs that insurance almost never covers such as medical travel (24 cents per mile) and acupuncture to name just a few.

American Opportunity Credit

It is a tax credit for as much as $2,500, generated by spending on tuition and other education expenses (books, possibly a computer) up to $4,000. Currently this credit is available for 2009 and 2010 to single taxpayers with less than $80,000 of modified adjusted gross income and married couples earning less than $160,000. Amounts paid in 2009 for the spring of 2010 are eligible for a 2009 credit.

New Car Purchases

Taxpayers who buy a new car before Jan. 1, 2010, may deduct sales and excise taxes and other fees on as much as $49,500 of the purchase price. This provision has generous phase-outs: It disappears between $250,000 and $260,000 of modified adjust gross income for married couples and $125,000 and $135,000 for singles.

Charitable Gifts

Unless Congress acts, this will be the last year for taxpayers over 70 1/2 to make a charitable contribution directly from an IRA. This provision is useful: without it, the donation would have to be withdrawn from the IRA, claimed as income and then deducted as a donation. That, in turn, can trigger deduction limits or jack up Medicare premiums in the future.

If you have any questions on this topics, or need some help with other financial issues you are facing give me a call at (603) 373-8793.