



Year-End Tax Planning

Some Thoughts on Year-End Tax Planning

by Matthew Deutsch

"It's the most wonderful time of the year." As the holidays approach, now is a good time to think about that other important year end subject: Tax Planning. Now, I know that you are all thinking, "yuck, please let me get through the holidays first." But, there is a reason why the IRS sends out your tax return forms to arrive right after Christmas. It's a last opportunity to structure your affairs before December 31st to pay the appropriate tax on your income.

Automobiles: In order to obtain a deduction for business, medical or charitable use of your automobile, you must maintain a "contemporaneous record of the miles driven and the purpose." Prior to year end is a good time to make sure that you can go back to your annual calendar and note the miles driven for business appointments, trips to the doctor's office and deliveries of non cash charitable contributions to the local food pantry or other tax exempt entity. While the rates per mile change almost every year and are available on the IRS's website at www.irs.gov, the rates (in cents per mile), for 2004 (and 2005) are as follows: business 37.5 (40.5), medical 14(15) and charitable 14(14). Also make sure to note the ending mileage on your odometer on December 31st so that you can calculate the annual miles driven in case the IRS audits your return.

All taxpayers are permitted a standard deduction in addition to the personal exemption based upon filing status. For 2004, the amount of the standard deduction for married taxpayers filing a joint return is \$9,700 and the deduction for single or married filing separately taxpayers is \$4,850 while the deduction for head of household filers is \$7,150.

In order to benefit from the advice below, your itemized deductions need to exceed these amounts. Itemized deductions include: medical expenses in excess of 7.5% of your adjusted gross income, mortgage interest, investment interest, property taxes, state income taxes, and charitable contributions as well as miscellaneous itemized deductions (the total of unreimbursed employee business expenses, safe deposit box and investment advisory fees and tax preparation fees.) In some cases you can benefit from the standard deduction in one year while claiming deductions for actual expenses in another. Thus, deferring or accelerating deductions should be considered on a two year basis.



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Contributions: Charitable contributions make a great way to lower your tax bill if you itemize. If you are planning on giving a charitable contribution near the beginning of 2005, you can accelerate the deduction (assuming that you are already over the standard deduction) and receive a tax benefit at the filing of your 2004 return. Please note the tax benefit of a \$1 deduction is based upon the marginal tax bracket, i.e. (10%, 15%, 25%, 28%, 33%, 35%).

Non cash contributions: Year end closet cleaning is another good way to gain a tax benefit. Deductions are available for contributions of non cash items such as stocks, clothes, household goods and automobiles given to charitable organizations. Claiming a deduction in excess of \$500 requires preparation of Form 8283 with the tax return. A deduction for a single item in excess of \$5,000 requires a qualified appraisal or valuation with acknowledgement by the charitable organization.

There are no "hard and fast" rules for the value of non cash items given to charity. However, use of a "thrift shop value" should provide a reasonable safe harbor for most donations. This means that based upon the quality and utility of the materials donated, sales of comparable items at a local re-sale shop should suffice. Ideally, you should keep copies of the pick up or drop off receipts from the charity, with your own itemization of the value of each item donated on the receipt or an attached sheet kept with your tax records.

You should also beware of advertisements of large tax deductions for donating your car to charity. The IRS is taking a hard look at the values claimed for such donations and has also determined that very little of the proceeds ended up in the hands of the charity. Therefore, Congress authorized more stringent reporting rules and a limitation on the benefits claimed on these transactions. If you are planning on making such a deduction, be sure that you are working with a well-respected widely known organization which will be able to help you assist you in complying with the newly complicated rules.

Estimated State Taxes: If you are required to make estimated state tax payments to cover your state tax liability, you may benefit by accelerating and making the payment otherwise due on January 15th 2005 prior to December 31. Since state tax payments are not deductible for alternative minimum tax (AMT) purposes, in addition to exceeding the standard deduction amount, an additional level of analysis is required to determine whether or not to accelerate the payment. An increasing number of



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taxpayers are falling prey to the AMT, and it is "dirty little tax increase secret." If you are close to the AMT, you should prepare your tax estimate based upon a draft of Form 6251 available on the IRS's website or at your post office.

Self Employed Retirement Planning: Most business owners can take advantage of many different self funded retirement planning options. These plans typically permit a self employed business person to fund retirement with "pre-tax" dollars, (i.e., tax deductible contributions and tax deferred growth.) What most of these plans require is that the plan is "in place", that is, "set up" prior to year end, even though contributions can be funded up to the filing date of the tax return. If you are a first time business owner or are considering self employed retirement planning, contact your investment advisor with enough time prior to December 31st to discuss your options.

Employees only: Finally, if your employer offers a "pre-tax" medical expense account, you should review the amount you have recovered during 2004 to make sure you are not leaving any funds in an account that is a "use it or lose it" account. Any amounts in these plans must be spent before December 31. If you have questions on the type of plan that you have, you should contact your company's human resources department.

"Render unto Caesar those things that are Caesar and unto God those things that are God's". This rejoinder which Jesus gave to the Pharisees also serves as a reminder to us that we are responsible to make sure that we don't give something to Caesar that really belongs to God. Year end tax planning can help manage our tax liabilities in a way to make sure we pay the appropriate amount, but not any more, and also can help manage cash flow to meet our other obligations as well.