

End-of-the-Year Planning

AS THE 2006 FILING SEASON APPROACHES, IT'S TIME TO DO an annual tax check-up to see what can be done to reduce the 2006 taxes and make any necessary arrangements for 2007.

2006 Federal Tax Changes and Reminders

The 3% excise tax you have been paying on certain services on your telephone bills has been repealed effective July 31, 2006. The IRS fought this battle in the courts for some time. After losing for the fourth time, IRS has decided to give up the battle and refund the tax on billings from March 1, 2003 through July 31, 2006. This refund may be in the form of a credit on your monthly bill (if the provider applies for the refund from the government) or a credit claimed on your 2006 income tax return.

The excise tax is 3% of amounts paid for "communications services." The Courts have ruled the excise tax only applies to certain services and taxpayers are entitled to refunds. Services that are *not* subject to the excise tax include:

- **Bundled services**—These include Voice Over Internet Protocol Service, prepaid telephone cards, and plans that provide both local and long-distance service for either a flat monthly fee or a charge that varies with the elapsed transmission time for which the service is used.
- **Long distance service**—This is telephonic quality communication with persons whose telephones are outside the local telephone system of the caller.

Service that remains taxable includes "local-only service." This includes a plan that does not include long-distance telephone service or that separately states the charge for local service on its bills to customers. It also includes services and facilities provided in connection with this service such as telephone amplifiers, automatic call distributing equipment, and a special telephone.

The credit on the tax return may be a standard amount of \$30, \$40, \$50, \$60, or the actual amount paid. If you happened to have saved your old bills, you might want to find them before tax time. However, in order to claim the standard amount the taxpayer must have paid all taxes on all billings between March 1, 2003 and July 31, 2006. Therefore, the refusal to pay any taxes after this May 25, 2006 period would deny you the right to claim the standard credit and force you to calculate and claim the actual tax paid.

If you have a telephone bill in connection with your business entity, you will need to use the actual expense method. There's even a credit available for those who are not required to file a tax return. The IRS has created a special Form 1040EZ-T to receive this refund.

Those who have been affected by the 2005 hurricanes have special benefits to consider if IRA withdrawals were made. These can be returned to the IRA as if they had never been withdrawn. This unusual rollover provision is available for two years following the qualified distribution rather than the traditional sixty days.

Investors can breathe a sigh of relief with the extension of the favorable capital gain rates. The 15% capital gain rate has been extended through 2010. This includes the gains from the sale of property as well as dividends received. In 2008, the lower 5% rate for those in the 15% or lower tax bracket will drop to 0%. Originally, the rate drop was for 2008 only. The new law makes this attractive rate available for three years through 2010. If you are in a lower tax bracket, you may want to consider selling some of the appreciated property you have been hanging on to.

Client Newsletter

Paying For College

Do you have your child's college education paid for? Most of us only wish that were true. There are many alternatives available ranging from 529 plans to educational IRAs to Roth IRAs. The Hope and Lifetime Learning credits ease the pain as well. If you give money to your child or grandchild to invest for college, you may want to think about how they are investing the money. If the money is in their name in an account that generates income subject to tax, they could be paying more taxes on that money this year. Children under the age of eighteen who have unearned income in excess of \$1,700 per year are subject to tax at the parents' income tax rate rather than the child's lower rate. The new law extends the "kiddie tax" provision from those under age fourteen to those under age eighteen.

Energy Credits

You're probably well aware through advertisements that an energy credit is alive and well. The most beneficial credit is going to those who purchase new energy-efficient vehicles. Below is a list of the qualifying vehicles with the credit available.

There is a time and quantity limit for qualification for this credit. The vehicle must be

purchased in 2006 or 2007. Secondly, the full credit will be available until a manufacturer reaches a cumulative sale of qualifying vehicles of 60,000. Toyota vehicles have reached the 60,000 limit; therefore, the full credit is available for the Toyota vehicles purchased through September 2006. For those Toyotas purchased in October 06–March 07, the credit will be reduced to 50%, and then only 25% for purchases from April 2007–September 2007. No other manufacturer has reached the 60,000 sales cap, so the credits for those vehicles will be at 100% at least through the end of 2006.

Other Energy Credits

As a home or property owner you may be able to make some energy changes to your home or your rental property and qualify for a 10% credit or a 100% credit. There is a lifetime maximum of \$500 for this credit. There are various limitations, but the credit is available for storm doors and windows; insulation; electric heat pump water heaters; electric heat pumps; certain air conditioners and water heaters using other forms of energy; and certain fans inside gas, oil, or propane furnaces.

Solar heating panels, qualified fuel cells, and solar water heaters are among the items that may qualify for the credit. The maximum

GM Saturn Vue Green Line (2007)	\$650	Model Years 2005–2006	
Model Years 2006–2007		Honda Civic GX (compressed natural)	\$4,000
GM Sierra (4WD) hybrid pickup truck	\$650	Honda Insight CVT	\$1,450
GM Sierra (2WD) hybrid pickup truck	\$250	Toyota Prius	\$3,150
GM Silverado (4WD) hybrid pickup truck	\$650	Honda Civic Hybrid CVT (2006)	\$2,100
GM Silverado (2WD) hybrid pickup truck	\$250	Honda Civic Hybrid SULEV MT (2005)	\$1,700
Ford Escape Hybrid Front wheel drive	\$2,600	Honda Civic Hybrid SULEV CVT (2005)	\$1,700
Ford Escape Hybrid 4 WD	\$1,950	Honda Accord Hybrid AT (2005)	\$650
Mercury Mariner Hybrid 4 WD	\$1,950	Honda Accord Hybrid AT (2006)	\$1,300 (\$650 without control calibration)
		Lexus GS 450h (2007)	\$1,550
		Lexus RX400h 2WD (2006)	\$2,200
		Lexus RX400h 4WD (2006)	\$2,200
		Toyota Camry Hybrid (2007).....	\$2,600
		Toyota Highlander 2WD Hybrid (2006)	\$2,600
		Toyota Highlander 4WD Hybrid (2006)	\$2,600

Tax Appointment Worksheet

√	EVENT	DOCUMENTS OR INFORMATION NEEDED
1	<input type="checkbox"/> Married or divorced in 2006	Married – prior year return of both spouses Divorced – copy of the divorce decree
2	<input type="checkbox"/> Birth or Adoption	Social Security cards and adoption papers
3	<input type="checkbox"/> Death of child or spouse	Date of death –
4	<input type="checkbox"/> Additional members of household	Date of occupancy and relationship –
5	<input type="checkbox"/> Job change	Start date – Name of new employer – W-2s from new and old employers
6	<input type="checkbox"/> Unemployment	Unemployment Form
7	<input type="checkbox"/> Retirement contribution	Type of plan – Amount of contribution –
8	<input type="checkbox"/> Retirement distributions	Form 1099-R
9	<input type="checkbox"/> Social Security Benefits	Form 1099-SSA
10	<input type="checkbox"/> Sale of stocks, bonds, etc.	Form 1099-B or other sale documents; basis or original costs
11	<input type="checkbox"/> Purchase of stocks, bonds, etc., personal residence, or other real estate	Purchase documents; closing papers
12	<input type="checkbox"/> Inheritance	Will; K-1 from the estate
13	<input type="checkbox"/> Trade any property	Date of trade, property given up and property received, basis and FMV; qualified intermediary sales agreements or closing papers
14	<input type="checkbox"/> Start or end a small business	Formation or termination dates; Property contributions or distributions
15	<input type="checkbox"/> Lawsuit settlements	Date received; reason for the settlement; 1099-MISC
16	<input type="checkbox"/> Rental property	Income, expenses, new property purchased
17	<input type="checkbox"/> Prizes	Form 1099-MISC; value of prizes not included on Form 1099-MISC
18	<input type="checkbox"/> Lottery or gambling winnings	Total amount won whether on W-2Gs or not; total amount of losses
19a	<input type="checkbox"/> Health insurance, medical, dental, or drug expenses	Health insurance premiums; if it is an employer- sponsored plan, know whether it is paid with pretax dollars; totals of other medical, dental, and drug expenses.
19b	<input type="checkbox"/> Health insurance	Pre-taxed (i.e. cafeteria plan, §125, POP)
19c	<input type="checkbox"/> Medical miles (18 cents per mile)	
20	<input type="checkbox"/> State income or property taxes paid	Prior year's income tax return; property tax bills; closing papers from the purchase or sale of property; letter from the state regarding any change in a prior filed return
21	<input type="checkbox"/> Purchase or refinance a home	Closing papers from purchase; Forms 1098
22a	<input type="checkbox"/> Charitable contributions of money, property, or out-of-pocket expenses	Date and type of contributions, knowledge that receipts from the organizations have been received; mileage log for charitable work
22b	<input type="checkbox"/> Charitable miles (14 cents per mile)	During 2006 –
23a	<input type="checkbox"/> Job-related expenses	Mileage log, travel, or miscellaneous expense amounts for items related to employment
23b	<input type="checkbox"/> Business miles (44.5 cents per mile)	
24	<input type="checkbox"/> Educational or student loan interest expenses	Form 1098-T for parents or children; interest record for student loans
25	<input type="checkbox"/> Child or disabled spouse care	The name, address, and ID number of the day care provider; the amount paid to the provider; if the provider comes into your home a W-2 may be required

credit available is \$2,000 for solar water heating property and an additional \$2,000 for photovoltaic property (electricity from light). The credit for qualified fuel cells is limited to \$500 for each 0.5 kilowatt of capacity but has no overall maximum. The enhancements must be certified to qualify for the credit. Before you buy, ask your dealer what certification measures have been taken.

The energy legislation provided more incentives to businesses than to the individual. These incentives may be passed on to you from the manufacturers. One such program was the credit for manufacturers of energy efficient home appliances such as washers and dryers. There is no personal tax credit but watch for manufacturer rebates.

The Saver's Credit has been made permanent. This credit can be as much as 50% of your pension or IRA contribution up to a maximum of \$2,000. The credit decreases as income approaches the maximum level. This credit was established to encourage savings among lower income taxpayers. If your income is within the qualifying limits, now is the time to make arrangements for the deferral options through your employer for the coming tax year. You can make qualifying IRA contributions up to the due date of your return.

The Status of Expiring Incentives

Congress is still considering the extension of the tuition deduction, the deduction for supplies for teachers, and the deduction for state and local sales tax. These provisions will not exist this year unless they are renewed.

The estate tax issue is still on the table. The estate tax exemption for 2006 is \$2 million. In 2010, there will be no estate tax. However, the estate tax will be reinstated in 2011 under current rules. Congress is struggling with the decision to make the estate tax permanently exempt or to modify the current rules. The proposal currently in front of the Senate has a \$5 million dollar exemption. This will be an important issue to follow.

Charitable Contribution Alert

Charitable contributions will require more backup. You will need to keep receipts of all cash contributions regardless of their size for contributions made in years beginning after August 17, 2006 (i.e. starting January 1, 2007 for calendar-year taxpayers). This means bank information such as cancelled checks or written acknowledgement from the organization including the name of the organization, the date, and the amount given. Effective for contributions after August 17, 2006, household items and clothing donated in kind must be in good condition. The IRS can deny any contribution which is not in good condition. Having photographs of the items before they are contributed may be the best way to substantiate the deduction. Put your digital camera to use. Other contributions of single items with values in excess of \$500 will not be questioned although they will need appraisals. This new legislation adds to the already existing rules regarding cash contributions of \$250 or more or contributions of vehicles. Take time to follow the rules so you get your justly deserved deduction.

Planning with New Legislation

Pension planning begins before the end of the year. If you wish to participate in tax deferred arrangements such as 401k or SIMPLE plans, you must notify your employer before the beginning of the coming year.

There may be another decision to make. The Roth 401k became available in 2006 for

the first time. If your company has amended its 401k plan to accommodate Roth contributions, you may want to make after tax Roth contributions rather than pre-tax 401k contributions. The Roth 401k allows taxpayers who have income too high to contribute to a Roth IRA to make those contributions. In addition, the allowable contribution to the Roth 401k exceeds the \$4,000 Roth IRA limit and can be as much as the regular 401k limit of \$15,000 (plus \$5,000 catch-up contribution for those over fifty years of age). The benefit of this choice comes when distributions are made tax free.

Other deferral decisions must be made before the end of the year as well. Participation in cafeteria plans, flex spending accounts, HSAs, and dependent care arrangements must be announced before 2007 begins. Many of these plans allow you to allocate dollars to be used to purchase these services or investments. Income tax and payroll tax savings result from the use of these plans. If your employer has these plans, you may want to examine their benefit in your particular circumstance.

Look at the tax appointment worksheet to get you ready for tax season. Check the applicable entries and gather the necessary documents to make the most of your tax appointment.



Your Business Card Here