Halcolm Bard
Certified Public Accountant & Consultants

TAX AND BUSINESS ADVISOR

Visit our web page at www.halcolm.com

TAX AND BUSINESS Alert™

November 2009

# Year-end Tax Planning Strategies

As we approach year-end, there is still time to take action to lower your 2009 tax bill and add to your tax-advantaged retirement accounts. Here are a few ideas to get you started before year-end. This is by no means an exhaustive list, so please contact us for additional ideas.

**Make the Standard Deduction Work for You.** If your itemized deductions are just at or below the standard deduction (currently $11,400 for joint filers and $5,700 for singles), they don't generate any tax benefit for you. However, you can bunch itemized deductions from two calendar years into a single tax year to take full advantage of them and exceed the standard deduction that year. Then you can take the standard deduction the next year. Following this two-year pattern results in greater deductions overall. Deductions that work well for this strategy include charitable contributions, property taxes, the fourth quarter estimated state income tax payment, and your January mortgage payment.

**Consider Selling Appreciated Securities.** It may be a good time to consider selling capital assets (e.g., common stock) with a low cost basis. The maximum capital gains tax rate is 15% for gains from the sale of qualifying assets held more than one year. In fact, taxpayers in the 10% and 15% ordinary tax brackets can do even better by taking advantage of the 0% capital gains rate in 2009. The 15% maximum tax rate is available for both the regular and alternative minimum tax (AMT). In addition, qualifying dividends received during 2009 will generally be taxed at the 0% or 15% capital gain rates.


Photos.com

**Contribute to Your Traditional or Roth IRA.** You can contribute up to $5,000 ($6,000 if you are age 50 or older by year-end) to your IRA in 2009 if certain conditions are met. For married couples, the combined contribution limits are $10,000 ($5,000 each) and $12,000 ($6,000 each if both are age 50 by year-end) when a joint return is filed, provided one or both spouses had at least that much earned income. In addition,

(Continued on page 3.)

# Choose I Bonds for Inflation-adjusted Earnings

The damaging effect of inflation on fixed income investments like bonds is well understood. As inflation rises, the purchasing power of your interest decreases along with the value of your bonds. Series I Bonds provide a shield from the eroding effects of inflation and allow for tax deferral on earnings until the bonds are redeemed or mature.

I Bonds are U.S. Treasury securities backed by the full faith and credit of the United States. They are sold at face value and grow with inflation-indexed earnings for up to 30 years. The earnings rate combines a fixed rate and a variable rate based on the Consumer Price Index. The minimum purchase requirements for I Bonds are $25 in electronic format and $50 in paper format. The maximum calendar year purchase is $5,000 each in electronic and paper bonds. I Bonds can be purchased from financial institutions and from the Treasury at *www.treasurydirect.gov*.

# College Financial Aid Changes

Photos.com

The "applying for college financial aid" season begins January 1—that's the first day the Free Application for Federal Student Aid (FAFSA) can be submitted for the 2010–2011 school year.

The new FAFSA includes only minor changes this year. Now, the student and parent need to report any earnings from work under a cooperative education program offered by an institution of higher learning. However, veteran's education benefits received by the student are no longer reported. Also, the Department of Education has announced regulatory changes that increase the eligibility for the Academic Competitiveness Grant and the National SMART Grant Programs. The definitions of *eligible programs* and *eligible majors* have been expanded, and the requirement for full-time enrollment has been removed.

# Substantiating Charitable Contributions

As we approach year-end, many of us may need to catch up on our charitable contributions for a number of reasons in addition to a tax break. So, let's briefly review the IRS rules on deducting charitable contributions. A donor will not be allowed any deduction for a contribution by cash or check, or any other monetary gift, regardless of the amount unless the donor retains either (1) a bank record that supports the donation or (2) a written receipt or communication from the charity showing the name of the organization, date, and amount of the contribution.

Property donations valued at less than $250 must be substantiated by a written receipt or letter from the charitable organization showing the organization's name, the date and place of the contribution, and a detailed description of the property. Donors must also obtain a written acknowledgment from the charity if the value of the contribution (in cash or other property) is $250 or more—a canceled check or other reliable records are not sufficient proof.

Please contact us if you have questions about substantiating charitable contributions.

# Tax-saving Investment Strategy

While taxes should not be the main consideration when selling investments, they certainly need to be considered since they can make a significant impact on your investment return. With that in mind, here is a tax-smart strategy to consider as you analyze your investment opportunities and decide what to do about gains. That is, should you sell now with the profit taxed at ordinary rates or wait until the stock qualifies for long-term capital gains treatment?

If the stock sale qualifies for long-term capital gains treatment, it will generally be taxed at a maximum tax rate of 15%. Otherwise it will be taxed at your ordinary income tax rate, which can be as high as 35%. Generally, you'll pay less in taxes (and keep more of your gains) if the stock sale qualifies for long-term capital gains treatment. The amount of taxes you'll save depends on your ordinary income tax bracket.

To qualify for the preferential long-term capital gains rates, you must hold the stock for more than 12 months. The holding period generally begins the day after you purchase the stock and runs through (and includes) the date you sell it. These rules must be followed exactly, because missing the required holding period by even one day prevents you from using the preferential rates.

The question then becomes: Are the tax savings that would be realized by holding the asset for the long-term period worth the investment risk that the asset's value will fall during the same time period? If you think the value will fall significantly, liquidating quickly, regardless of tax consequences, may be the better option. Otherwise, the potential risk of holding an asset should be weighed against the tax benefit of qualifying for a reduced tax rate.

Comparing the risk of a price decline to the potential tax benefit of holding an investment for a certain time is not an exact science. However, the following should be considered:

1. Your expected ordinary income tax rate relative to the anticipated capital gains rate.
2. The amount of appreciation that will eventually be taxed.
3. How much longer the asset must be held to qualify for favorable capital gains rates.
4. Whether any existing capital losses could offset the gain (and the benefit of the lower rate).

Photos.com

We would like to help you develop a personal strategy for maximizing the benefit of this tax break. Please call us to discuss this issue or any personal or business tax-saving idea.

## Year-end Tax Planning Strategies

*(Continued from page 1.)*

contributions to traditional IRAs may be tax-deductible, subject to specific conditions and limitations.

**Contribute to Your Employer-Sponsored Retirement Plan.** The 2009 annual deferral limit for qualified retirement plans is $16,500. If you are at least age 50 by year-end, you can contribute an additional $5,500 to 401(k), 403(b), and 457 plans. These contributions normally decrease your taxable income and thereby lower your tax bill.

**50% Bonus Depreciation.** Qualifying equipment, which includes most tangible personal property and software and certain leasehold improvements acquired and placed in use during 2009, is eligible for an immediate 50% bonus depreciation deduction. This is in addition to the normal depreciation deduction on the remaining balance.

Once again, please call us for additional year-end tax planning ideas or to discuss any tax compliance or planning issue.

# Increase or Create a 2009 NOL Using Bonus Depreciation

The Section 179 deduction privilege allows taxpayers to immediately expense the cost of most new and used depreciable personal property, including software. For tax years beginning in 2009, the maximum Section 179 deduction is a relatively generous $250,000. As indicated in the page one article, 50% first-year bonus depreciation is available for qualifying new (not used) assets, including most software, placed in service by December 31, 2009. But, for many businesses in today's struggling economy, the bonus depreciation has more value. Here's what you need to know.

Photos.com

While the Section 179 deduction privilege is generally a great deal, it's not so great if you have low or negative income. This is because the Section 179 deduction is limited to taxable income for 2009. This is the so-called *taxable income limitation*. In essence, the practical impact of the limitation is that the Section 179 deduction cannot create or increase a net operating loss (NOL). This can be a pretty big disadvantage in today's lousy economy, when even healthy businesses may be much more interested in making moves that will create or increase current-year NOLs to carry them back and recover taxes paid in prior years as a means to increase cash flow.

Unlike the Section 179 deduction, 50% first-year bonus depreciation write-offs can create or increase your 2009 NOL, which can then be carried back to prior years with the resulting recovery of taxes paid in those years. If necessary, those tax recoveries can be used to pay part of the cost of the very assets that gave rise to the bonus depreciation deductions in the first place.

If you are interested in creating or increasing a 2009 NOL by using bonus depreciation, you should be prepared to act soon. Unless Congress takes further action, which could certainly happen, the bonus depreciation privilege for most assets will expire at the end of the year. That is, to qualify for bonus depreciation, qualified assets must be placed-in-service before January 1, 2010.

Please contact us to discuss this or any other personal or business tax-saving strategy.





◇ Corporations ◇ LLCs ◇ Proprietorships ◇ Bookkeeping & Payroll ◇ Taxes ◇ Businesses & Individuals ◇ Financial Statements ◇
Halcolm Bard CPA • 38 Fraley Street • Kane, Pennsylvania 16735 • (814) 837-9150 • Tax and Business Advisor