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Tax Planning Letter

Dear Clients and Friends,

As a financially volatile 2008 winds down, it is important to review your tax situation with the objective of identifying moves you can make before year-end to minimize your tax bill.

Congress passed the *Emergency Economic Stabilization Act of 2008* after the initial three-page "bail-out" bill ballooned to more than 400 pages with the inclusion of provisions on energy, disaster relief, the alternative minimum tax, and expiring tax breaks. President Bush signed the bill on October 3. The tax portion of the new law increases the 2008 exemption amounts for the alternative minimum tax, extends through 2009 the deductions for state and local sales taxes, tuition expenses, and teachers' out-of-pocket expenses, and extends the provision allowing older taxpayers to make tax-free contributions of IRA funds to charity. Credits and deductions for energy-saving investments are extended, and the business credit for research and development expenses is modified and extended through 2009.

Intelligent tax planning requires a long-term strategy, with frequent reviews and adjustments along the way. For guidance that can help you keep your taxes as low as the law allows, call now for a year-end tax review.



The Griffith CPA Firm PLLC

Check the numbers for some 2008 tax savings

Do you like numbers? Do you like them better when they involve tax savings? Here are 12 numbers – and 12 tax-saving strategies – to consider as the clock starts to wind down on 2008.

19 For 2008, the kiddie tax applies to children under age 19 as well as full-time students under age 24. What's the impact? When your child has investment income, such as dividends and interest, of more than \$1,800 for the year, the income may be taxed at your highest tax rate.

>> ACTION: Consider hiring your home-for-the-holiday children in your business during the end-of-semester college break. Wages are earned income and are taxed at your child's rate.

30 Wash sale rules can limit your current-year losses on investment sales. These rules kick in when you sell an investment at a loss and buy a substantially identical investment within 30 days before or after the sale date.

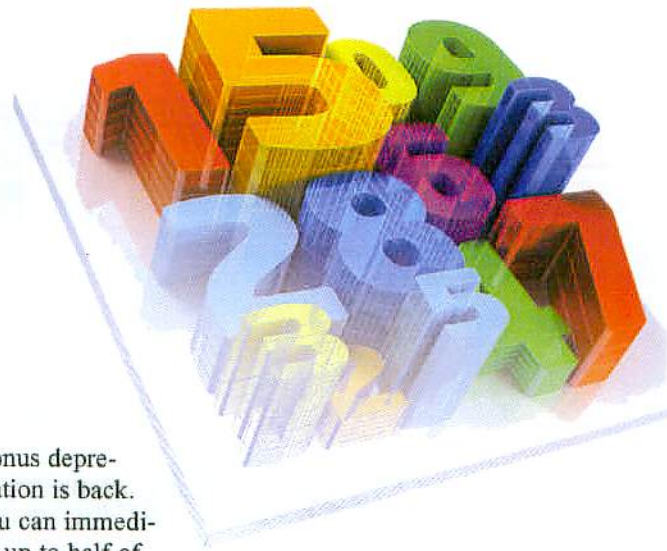
>> ACTION: Be careful to replace loss-generating securities with others that are similar, but not identical.

0% The capital gains tax rate on qualified dividends and gains from sales of stocks, bonds, and other securities you've held more than a year is zero if your 2008 taxable income is less than \$65,101 (married filing jointly) or \$32,551 (single).

>> ACTION: Assess your portfolio with an eye toward realizing gains on investments in which you have a low basis.

7.5% To take an itemized deduction for medical care, your total expenses have to equal more than 7.5% of your adjusted gross income. Not quite there? You may be able to bunch your costs. Bunching is a classic tax planning strategy that involves accelerating expenses into the current year or deferring them to the next year.

>> ACTION: Calculate your expenses to date. Include amounts you paid for family members who failed to qualify as your dependents only because they did not meet the gross income or joint return test. If you're close to the 7.5% floor, look for opportunities to increase your deduction. *Example:* Schedule deductible elective procedures before year-end.



50% Bonus depreciation is back.

For 2008 you can immediately deduct up to half of the cost of qualifying new business assets. In addition, the bonus rule increases the maximum amount of first-year depreciation on luxury passenger cars and light trucks that you use in your business by as much as \$8,000.

>> ACTION: Consider replacing worn-out business vehicles and equipment before year-end.

100% Subject to certain restrictions, you can claim self-employed health insurance premiums "above the line" – meaning you can subtract them from your gross income. However, at the beginning of 2008, the IRS issued a notice spelling out the procedures you'll need to follow to keep this deduction from being disallowed if your business is set up as an S corporation.

>> ACTION: Have your business write an additional compensation check before year-end to reimburse you for premiums you paid personally.

58.5¢ Use this standard mileage rate to calculate the amount you can deduct for each business mile you or your mobile employees drive from July 1, 2008, through year-end. (For business miles driven from January 1 through June 30, 2008, the deductible rate remains at 50.5¢.) Remember, estimates are not enough to support a deduction. The IRS requires adequate records, either written or electronic.

>> ACTION: Maintain a mileage log, recording the date, destination, purpose, and total miles of business trips.

\$1,800 The maximum Hope Scholarship credit for 2008 is \$1,800, up from \$1,650 last year. (A higher credit is available for students in certain disaster areas.) The credit reduces your tax bill dollar for dollar and is available for the first two years of college or vocational expenses you pay for yourself, your spouse, or your dependents. Two cautions: Income phase-outs apply, and taking the Hope credit may limit other educational tax breaks, such as the lifetime learning credit.

>> ACTION: Add up your 2008 tuition expenses to determine whether it makes sense to pre-pay first semester 2009 costs.

\$3,000 You can use up to \$3,000 of capital losses to reduce other taxable income. Is your income too high to benefit from the zero percent capital gains rate in effect this year? "Harvesting" tax losses to offset gains can generate tax savings.

>> ACTION: Total your realized gains and losses from your 2008 transactions; then consider weeding out poorly performing investments.

\$3,500 Each dependency exemption you're eligible to claim reduces your taxable income by \$3,500.

In addition to your children, dependency exemptions are available for others, including parents that you support. There's no age requirement for a qualifying relative, and in some cases your loved one does not need to live with you. However, your relative's gross taxable income must be less than \$3,500, and you need to provide over half of his or her support during the calendar year.

>> ACTION: Review food, housing, and medical care support you provide to dependents. If more than one family member contributes, consider whether a multiple support agreement would benefit you.

\$5,000 Make a deductible contribution of up to \$5,000 to a traditional IRA and save tax dollars now. Contributions to a Roth IRA are not deductible, but provide tax-free withdrawals later. In both cases, growth within the accounts is generally tax-free. If you're over 50, you can contribute up to \$6,000 to an IRA for 2008.

>> ACTION: Maximize your savings by contributing as much as you can to all retirement plans for which you qualify.

\$250,000 The Section 179 depreciation deduction lets you treat up to \$250,000 of the cost of business assets you purchase and place in service during 2008 as a current-year expense. The deduction phases out when you buy more than \$800,000 of assets during the year.

>> ACTION: Schedule purchases of business equipment and machinery so you'll have time to make sure the assets are up and running before December 31.

Effective tax planning requires a comprehensive assessment of current-year transactions, as well as your intentions for 2009 and beyond. Other factors, including financial aid for education and cash flow and liquidity needs, can also affect strategy decisions. Please call us to schedule an analysis of the tax-saving opportunities that are available in your particular personal or business situation. ┘



Several new laws enacted during 2008 offer year-end tax planning opportunities. Here's an overview.

■ **Prepay real estate taxes.** Normally, this planning suggestion has the goal of increasing your itemized deductions. But this year, thanks to a break included in the *Housing Assistance Tax Act*, you can deduct state and local real property taxes even if you don't itemize deductions on your 2008 tax return. Pay your property taxes by December 31, and you'll be able to increase your standard deduction by up to \$500 (single) or \$1,000 (joint).

■ **Buy a first home.** There's a new tax credit of as much as \$7,500 for first-time homebuyers. To qualify, the home must be the first you've owned in the past three years, and the home must be purchased after April 8, 2008, and before July 1, 2009. Phase-out of the credit begins when your adjusted gross income exceeds \$150,000 (\$75,000 for singles). The credit must be repaid over 15 years, starting two years after you claim it.

■ **Take advantage of extended tax breaks.** Nearly three dozen expired or about-to-expire tax breaks were extended in the massive bailout legislation that was signed into law on October 3. Among the tax breaks that were extended through 2009 were the following:

- The optional itemized deduction for state and local sales taxes.
- The deduction for qualified higher education expenses.
- The above-the-line deduction for teachers who purchase classroom supplies.
- The additional standard deduction for property taxes paid by those who don't itemize.
- Tax-free contributions from IRAs to charities by older taxpayers.
- The business research and development credit.
- 15-year straight-line cost recovery for qualified leasehold, restaurant, and retail improvements.

The law also increased the 2008 alternative minimum tax exemption amounts to \$46,200 for singles and \$69,950 for couples.

The 2008 laws contain other changes that can affect your tax planning, including disaster relief and energy provisions, additional breaks for farmers, ranchers, and military personnel, as well as changes to expatriation tax rules and the home-sale exclusion rules. Please contact us for more details on changes that could apply to you. ┘

Tax relief may ease a financial loss

Looking for a little upside to a recent financial downturn?

In a year noted for mortgage failures, investment losses, and natural disasters, you may be surprised to learn that help is available from an unlikely source – the IRS. Knowing what tax breaks are available, and how you may qualify, can be a good first step toward recovery.

■ Home mortgage debt

With falling home values, foreclosures, and floods, homeowners have had little to cheer about in 2008. Fortunately, new tax laws were passed to address some of these problems. For instance, the *Mortgage Forgiveness Debt Relief Act of 2007* excludes from taxable income up to \$2 million of certain home mortgage debt that has been absolved. Forgiven debt is normally treated as taxable income. The new rule was extended in the recent economic stabilization law and now applies to debt forgiven in 2007 through 2012. It only covers loans incurred to purchase a principal residence. Home-equity debt used to consolidate bills or buy other items does not qualify for this exclusion.

■ Natural disasters

Natural disasters pose another threat to homeowners, and the IRS provides a little reprieve for that as well. The amount of casualty loss incurred as a result of a sudden, unexpected event and not reimbursed by insurance is deductible on your tax return to the extent that the loss exceeds \$100 and 10% of your adjusted gross income. When the casualty loss occurs in a declared federal disaster area, the rules are less restrictive, allowing more disaster victims to claim losses.

Also, if your loss is in a federal disaster area, you have the option to apply the loss to your prior year's return, thus providing a more immediate deduction and possible tax refund. Other

benefits of federal disaster declaration may include extended tax return filing due dates, the abatement of interest and penalties during the extension period, and special tax breaks for businesses.

As strange as it may sound, a natural disaster can in fact generate taxable gain under certain conditions. If the proceeds from an insurance settlement exceed your property's cost basis, you could owe tax on the difference. However, the tax on any such gain may be deferred by reinvesting the funds in replacement property within a fixed time period. The replacement period varies depending on the type of property involved.

■ Investment losses

Investment losses can also generate tax breaks. The losses are known as capital losses and can be categorized as either unrealized or realized. An unrealized loss occurs whenever the market value of an unsold security falls below its cost basis. While hard to swallow, such losses do not qualify for a tax deduction. Only realized capital losses – those that happen when a security is actually sold – can result in a write-off.

Generally, capital losses are used to offset capital gains within the same holding period, i.e. short-term (owned for 12 months or less) or long-term (owned for more than 12 months). When capital losses exceed capital gains, up to \$3,000 can be deducted from ordinary taxable income, such as wages. Capital losses in excess of capital gains and the \$3,000 deduction limit are carried forward to the next year.

■ Business operating losses

In this struggling economy, many businesses are facing operating losses. Those which operate as pass-through entities, such as partnerships or S corporations, can pass those losses down to their owners. A net operating loss (NOL) deduction not only provides business owners with an offset against ordinary income, it can be applied to previous years' tax returns through the filing of amended returns for prior profitable years. This can potentially lower taxable income, increase itemized deductions, and provide a quicker tax refund.

When going through a financial loss, taxes may be one of the last things on your mind. But through proper planning, you may be able to squeeze a little lemonade from a fiscal lemon. For details on how your loss can be a tax gain, give our office a call today. □



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NOTE: This newsletter is issued annually to provide you with information about minimizing your taxes. Do not apply this general information to your specific situation without additional details. Be aware that the tax laws contain varying effective dates and numerous limitations and exceptions that cannot be summarized easily. For details and guidance in applying the tax rules to your individual circumstances, please contact us.