

Holiday Tax Planning

by James E. Davis, Jr.

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With the holidays upon us, thoughts of year-end tax planning often plague our celebrations of the Christmas and New Year's season. We often know the benefits of tax planning discipline, but tend to procrastinate. The checklist below provides us an opportunity to review potential savings situations, prioritize them according to potential benefit, and customize and apply them to your personal situation. The top ten year-end tax planning potentates, in inverse order, are



- 10. Defer income and pre-pay deductible expense items:** Look at earning and spending patterns in previous months for potential year-end opportunities. Examine moving manageable income items forward by invoicing later in the month or prepaying things like insurance, mortgage interest, or taxes. Consider inventory and equipment levels with future needs for opportunities to stock up before year-end.
- 9. Review asset portfolios for opportunity to manage capital gains or losses:** Up to \$3,000 *net* capital losses may be written off annually against earned income. If you have taxable capital gains, you may have potential capital losses to offset these or if you have capital losses in excess of the \$3,000 limit, you may have capital gains that could be realized without being taxed.
- 8. Spend the flex spending plan balance:** The flexible spending plan many employers provide allows you have put aside tax-free earnings to cover un-reimbursed health care and dependent expenses, but most do not allow balances to be carried over year-end. Consider physical examinations, medical supplies, dental, and eye care covered in the plan before year-end.

7. **Make charitable donations:** Consider donations of cash to charity to meet present or future commitments to churches and charities of your choice. These are usually directly deductible from income, thereby reducing taxes and potentially moving you into a lower tax bracket. Be sure to document deductions with cancelled checks, receipts, and any correspondence or memorandums of transmittal.
6. **Determine whether you're subject to AMT:** The alternative minimum tax, which was designed to make sure that high-income earners with multiple deductions pay at least some tax, now captures many upper-middle-class workers because it is not indexed to inflation.
5. **Making a gift:** The 2001 estate law's annual gift exclusion allows taxpayers to transfer gifts up to \$12,000, or \$24,000 for a married couple filing jointly, to any number of individuals without tax to the transferor or transferee. Also, there is no cap on the exclusion on gifts for educational and medical expenses if the payments are made directly to the educational or medical service provider. But remember, you cannot carry over unused annual exclusions from one year to the next, they are not cumulative.
4. **Environmental investment tax credits:** Potential tax credits are available for installing solar panels, fuel cells, or wind turbines to provide electricity at home and for buying alternative-fuel vehicles, like hybrid or electric cars. More specific information is available at the Internal Revenue Service's website: <http://www.irs.gov/>.
3. **Consider converting your traditional IRA to a Roth IRA:** Keeping your traditional IRA will let you defer taxes until retirement while the conversion forces you to pay tax immediately on the amount you convert. The advantage is Roth IRAs, unlike traditional IRAs, do not force you to take minimum annual distributions after you turn 70. Roth IRAs give you control of distribution throughout your lifetime and at death, all tax free. You must have gross income of less than \$100,000 to qualify now, but, under current law, that cap is eliminated in 2010 and you will be able to spread the tax due on conversion over two years.
2. **Beware of the Alternative Minimum Tax:** If you have significant personal exemptions, state and local income and

property tax deductions, interest deductions on non-purchase or non-improvement mortgage or home equity loans, or other significant deductions and your income is above the \$75,000 range, you need to be aware of the potential for “additional tax” imposed by the AMT. You and your accountant can use IRS Form 6251, Alternative Minimum Tax – Individuals, to determine the impact and plan accordingly.

- 1. Clean-up your act:** There are benefits to working hard, spending less, saving more, eating right, getting more exercise and appropriate rest, tending to your own business, keeping your mouth shut, and being thankful for your blessings. You will not get a tax deduction, a tax credit, nor an estate tax deduction, but you will be the beneficiary of more happiness, less stress, and a more peaceful and satisfying relationship with your self, family, co-workers, and God. And who knows, after the promises made in the last election, these may be worth more in the long-run!