# The Numbers Game

## Personal Income-tax Considerations for Tax Year 2008

**When it comes to the bottom line — meaning the one on your tax return — proper planning is of the essence. And to plan effectively, one must know the rules and how to play them. With proper insight, such as this end-of-year primer, individuals and businesses can make smart decisions that can add up — literally and figuratively — to substantial savings.**

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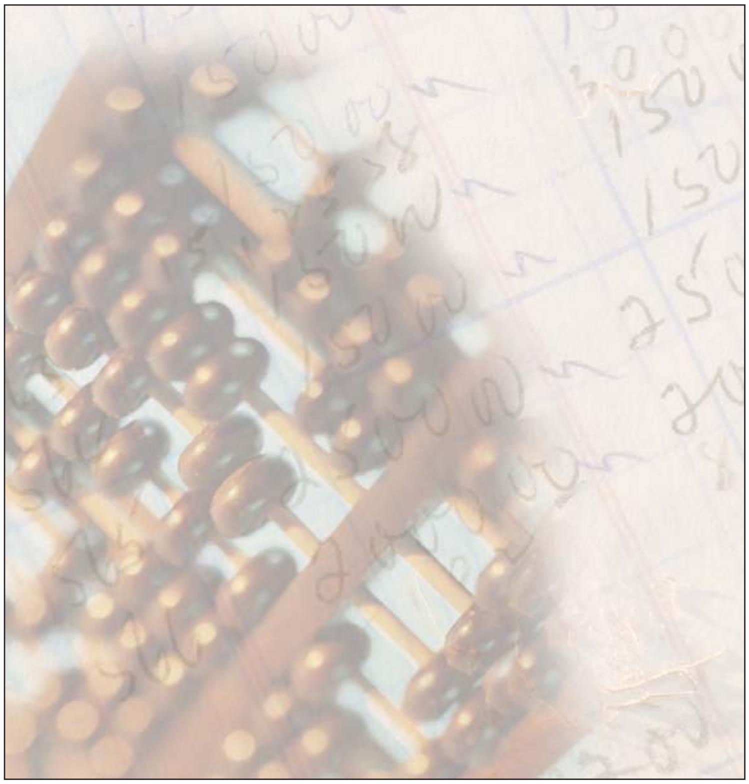

The time to do your income-tax planning and implementation of tax-wise strategies is during the tax year, not after it has ended. Part of the reason for this is that there are very few tax-planning opportunities that can be implemented after Dec. 31.

The Emergency Economic Stabilization Act, commonly referred to as the bailout bill, contained a substantial number of tax provisions and/or extensions of tax provisions that were scheduled to have expired at the end of 2007. These income-tax provisions may be a silver lining in an otherwise controversial and challenging piece of legislation.

This article is intended to provide a summary of the more generally applicable rules and provisions for use in connection with preparing and filing your 2008 income tax returns. In fact, it could be used as a checklist for your review and consideration prior to contacting your tax professional before the end of the year, to see how you might be able to maximize the benefits that apply to you during these challenging economic times.

### The 'Kiddie Tax'

In 2007, a child's unearned income beyond $1,700, such as gains and dividends, was taxed at the parents' marginal rate until the child is 18 (previously, the threshold age had been 14). Although the threshold increases to $1,800 in 2008, the applicable age is raised to 19, and 24 for full-time students, whose earned income is less than half their support. This way, families can't shift appreciated assets to their children to take advantage of the 0% rate on certain dividends and/or capital gains, as discussed below.

### Capital-gains Tax Rates

Prior to 2008, long-term capital gains from the sale of assets held longer than one year were taxed at a maximum rate of 5% to the extent the seller was in the 10% or 15% tax brackets. In 2008, the 5% maximum rate drops to 0% through 2010. However, the 15% maximum tax rate on other long-term capital gains remains the same for all other tax brackets.

### Dividend Tax Rates

Similarly, in 2008, the special 5% maximum rate on dividends of taxpayers in the 10% and 15% tax brackets drops to 0% through 2010.

### Increased IRA Contribution Limits

In 2008, the maximum IRA (traditional or Roth) contribution increases from $4,000 to $5,000. Filers who will be age 50 before the end of 2008 can contribute another $1,000.

### Higher Income Limits for Deductible IRAs and Roth IRAs

Even if you are covered by a retirement plan at work, you can still take a full IRA deduction if your modified adjusted gross income is less than $85,000 (married filing jointly) or $53,000 (single or head of household).

The allowable deduction is phased out gradually until your adjusted gross income reaches $105,000 (married filing jointly) or $73,000 (single or head of household). The opportunity to contribute to a Roth IRA is now limited once your modified adjusted gross income rises above $159,000 (married filing jointly) or above $101,000 (single or a head of household).

### Indexed Tax Brackets

One of the few benefits of inflation is that, due to indexing, the 15%, 25%, 28%, 33%, and 35% tax brackets for 2008 will all kick in at a bit more than 2% higher levels of taxable income than they did in 2007.

### Larger Personal Exemptions

Under the theme 'every little bit helps,'in 2008, each personal exemption you can claim is increased by $100 to $3,500.

### Higher Standard Deductions

Along that same theme, in 2008, the standard deduction for those taxpayers married and filing a joint return increases by $250 to $10,950.

For single filers, the amount increases by $100 to $5,450; and for heads of household, the amount increases by $200 to $8,050.

### Itemized Deductions and Personal Exemptions

For years, itemized deductions and personal exemptions have been phased out (reduced) as income rose. In 2008 and 2009, these reductions are a bit less painful. This limitation in itemized deductions happens when your adjusted gross income (AGI) exceeds $159,950, regardless of your filing status. Your itemized deductions are reduced by 1% (formerly 3%) of the amount by which your AGI exceeds $159,950, but you can never lose more than 80% of your itemized deductions.

Also, your medical expenses, investment-interest deduction, deductible gambling losses, and any casualty and theft losses are not subject to the cut. Personal exemptions are reduced by 2% for each $2,500 of AGI over $239,950 for married filing jointly, $199,950 for heads of households, and $159,950 for singles, but the reduction cannot exceed $1,167 per exemption.

### Increased Section 179 Expense Deduction

The maximum amount of equipment placed in service in 2008 that businesses can expense (deduct in full rather than depreciate over a period of time) increases by $3000 to $128,000. The annual investment limit increases to $510,000 for 2008. Thus, you won't lose the benefit of expensing until you place more than $510,000 of assets in service in 2008.

### Tax-free Parking for Employees

In 2008, employees are not taxed on up to $220 a month of employer-paid parking. The cap on the tax-free transit passes their employers can give rises to $115 a month.

### State and Local Sales-tax Deduction

The opportunity for itemizers to choose to deduct their state sales-tax payments instead of deducting their state and local income taxes has been extended through the end of 2009.

### Educators' Deduction

Also extended through the end of 2009 is the deduction for up to $250 of teachers' classroom supplies.

### Tuition and Fees Deduction

Appropriately, in the face of the ever-increasing costs for higher education, the deduction for up to $4,000 of college tuition and fees is also extended through the end of 2009.

### Direct Donations of IRAs to Charity

Another example of a positive extension provided in the bailout bill is that IRA owners age 70 or older are allowed, for years 2008 and 2009, to continue to make tax-free contributions up to $100,000 from their IRAs to qualified charitable organizations without having to report the withdrawal as income and then deduct the donation as a charitable contribution.

### Additional Standard Deduction for Real Property Taxes

A new tax provision enacted as part of the Housing Assistance Tax Act of 2008 allows homeowners to claim an additional standard deduction for real property tax if the taxpayer does not itemize. The additional amount is limited to $500 or $1,000 for joint filers. Homeowners can still deduct real property taxes and mortgage interest as an itemized deduction. However, now homeowners who don't have enough itemized deductions to exceed their standard deduction by the otherwise deductible amount noted above for real property taxes could be better off using their standard deduction.

### Alternative Minimum Tax Patch

In what is one of the more important components of the bailout bill not relating to the economic stabilization efforts, the patch to the Alternative Minimum Tax (AMT) was extended through 2008. The AMT is a supplemental tax calculation established by the Internal Revenue Code many years ago as part of an effort to try to make sure that higher-income individuals would pay an income tax in spite of their best efforts to use tax-avoidance strategies. When the legislation was written, it did not provide for an increase in the personal exemptions applicable to the tax calculation. The unintended result was that, as more, so-called middle-class taxpayers have seen their earnings increase, more and more of them have been ensnared by this well-intentioned but flawed legislation. Approximately 22 million taxpayers could have seen their 2008 income tax bills rise by anywhere from $2,000 to $7,500.

Generally speaking, it is good strategy for people not to think of their tax return as a destination. Don't measure the 'wonderfulness' of the tax return in question by the size of your refund or balance due. That figure is only a function of how accurately you had your taxes withheld and/or set up your estimated tax payments. Instead, the best result from any tax return is the one that leaves the greatest number dollars in your pocket after having gone through the income-tax tollbooth.

In closing, while all of these issues may not apply to all of you, there are likely to be some that could put you in a position to achieve some tax savings for you or other members of your family. Whether those savings are for one year only or continue for many years to come, it is money that will be left in your pocket for you to elect how to spend and use it.❖

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