Take Advantage of Temporary Tax Laws

Did you know that federal income tax rates are low by historical standards? The top marginal tax rate has been twice the current 35% rate or more in several tax years since the Sixteenth Amendment was ratified in 1913. The bottom marginal tax rate hasn't been lower in decades. And, for some people, capital gains taxes couldn't get any lower.

Although the rhetoric in the presidential campaign seems to indicate that several tax cuts passed since 2001 will not be extended past their scheduled expiration dates, there are some favorable provisions in effect that many taxpayers can take advantage of right now.

Low or No Capital Gains Taxes

If you are in one of the two lowest federal marginal income tax brackets (meaning your last dollar of income is taxed at the 10% or 15% rate), you're in a good position to capture some of your long–term capital gains. Long–term capital gains (for investments held for more than 12 months) realized in 2008 by taxpayers in the lowest brackets are taxed at a 0% rate.

This is great news, but the provision is most likely to benefit single taxpayers with less than $32,550 in taxable income and joint filers with less than $65,100 in taxable income. If you are not in this group, you may still be able to take advantage of the 0% rate to help family or friends.

Unfortunately, Congress wanted to prevent parents from taking advantage of the zero tax rate to transfer highly appreciated assets to their children. It expanded the so–called kiddie tax so that a child's investment income above $1,700 would be subject to his or her parents' tax rate. The law affects kids under 18 and full–time students under 24.

However, there is nothing to prevent someone from giving highly appreciated investments to family members or friends who aren't subject to the kiddie tax and whose incomes are low enough to qualify for the 0% capital gains tax rate. Just remember that gifts over $12,000 may be subject to the federal gift tax.

For taxpayers in the higher income tax brackets (25% and up), long–term capital gains are taxed at a 15% rate, which is still low by historical standards. The top capital gains rate is scheduled to increase to 20% in 2011. The 0% rate is scheduled to expire at the same time.

New IRA Heights

The contribution limit for IRAs reached an all–time high in 2008. Individuals with earned income can contribute up to $5,000, and those ages 50 and older can put in an extra $1,000 (for a total of $6,000).

Individuals have until April 15 to contribute to an IRA for the 2007 tax year, but the contributions cannot exceed the 2007 contribution limit of $4,000 ($5,000 for those ages 50 and older.)

Contributions to a traditional IRA typically are tax deductible, subject to certain income limits for individuals who also participate in an employer–sponsored retirement plan. The deduction begins to phase out for single filers with modified adjusted gross incomes above $53,000 in

2008 ($52,000 in 2007) and for joint filers with modified AGIs above $85,000 in 2008 ($83,000 in 2007).

The same contribution limits apply to the Roth IRA. Roth contributions are not tax deductible, but withdrawals of earnings are free from federal income tax provided they are made after age 59½ and the account has been in place for at least five years (except in cases of death, disability, or a first–time home purchase up to a $10,000 lifetime limit).

Early withdrawals of earnings from a Roth IRA are subject to ordinary income taxes and a 10% federal income tax penalty. Contributions to a Roth IRA can be withdrawn at any time without tax consequences. Withdrawals from traditional IRAs are taxed as ordinary income and may be subject to an additional 10% federal income tax penalty if taken prior to reaching age 59½.

Stimulus Time

Under the Economic Stimulus Act of 2008, millions of Americans will receive tax rebates after they file their 2007 tax returns. But most high–income households (as defined by Congress) will not qualify.

According to the act's provisions, single filers who report AGI of $75,000 or less on their 2007 returns will receive $600. Married taxpayers filing a joint return with AGI of $150,000 or less in 2007 will receive $1,200. Households that meet the income requirements are also eligible for an extra $300 per dependent child.

Eligibility for these tax rebates begins to phase out at a 5% rate, or $50 for every $1,000 of income over the base limit. So a single filer with $76,000 in adjusted gross income would receive a $550 rebate; $77,000 in adjusted gross income would equate to a $500 rebate, and so on.[1]

Although there are some minimum income requirements to receive a rebate, the most important rule is the requirement to file a tax return. Individuals who do not file a tax return will not receive a rebate. Therefore, people who earned income in 2007 but have no tax liability must file a return in order to receive the rebate.

Some other provisions from the Economic Stimulus Act of 2008:

- Businesses can expense up to $250,000 for tangible depreciable personal property purchased in 2008 for use in the business. The previous limit was $128,000. The property must be newly purchased and used more than 50% for the business.
- Businesses that make qualifying equipment purchases in 2008 can depreciated the equipment by an additional 50%.
- The definition of a conforming loan has been increased by 175% from its former limit. Previously, mortgage loans issued by Fannie Mae (Federal National Mortgage Association) and Freddie Mac (Federal Home Loan Mortgage Corporation) for more than $417,000 were considered “jumbo” mortgages, which carry higher interest rates. Under the new law, FHA mortgages of less than $729,750 originating between July 1, 2007, and December 31, 2008, will be considered conforming loans, making them eligible for lower interest rates.

Most of the good news for taxpayers comes with an expiration date, so it's important to act soon to take advantage of any provisions that affect you. As always, be sure to consult your tax professional before you take any specific action.

1) *The Wall Street Journal*, February 13, 2008

7000 Central Parkway NE, Suite 1340 • Atlanta, GA • 30328

Phone: 678-579-0490 • Fax: 678-579-0491

www.mdplanning.net • rlundy@mdplanning.net