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# Client Update

## Table of Contents

Minimum Tax Warning	Page 1
Ideas Concerning Deductions	Page 1
Giving to Charity Without Giving it All Away	Page 1
Plan Before It's Too Late!	Page 1

## Minimum Tax Warning

Watch out for the bite of the alternative minimum tax. The AMT has two tax rates: 26% on the first \$175,000 of AMT income and 28% above that. It is owed to the extent it exceeds your regular tax. It can hit you if you exercise incentive stock options, have a big family, take large capital gains or pay high state income, sales or real estate taxes. If you owe it, you can't use many of the strategies we normally suggest. For example, don't pay your January 2007 state income tax estimate this year. Don't buy a car in December to deduct sales taxes. Home equity loan interest isn't deductible unless you buy, build or fix your home with the proceeds. And if you exercised an incentive option in 2006, the discount you got is not subject to the AMT if you sell the acquired shares by December 31.

*The Kiplinger Tax Letter, November 2006*

## Ideas Concerning Deductions

Several itemized deductions can be shifted between years:

State and local income tax. If you mail your January 2007 estimate in late December, you can write off the payment this year instead of in 2007.

Interest. Making the January 2007 mortgage payment on your residence before the end of December enables you to deduct the interest portion in 2006.

Gifts to charity. You deduct them in the year you mail the check or hand over the money, not the year you make a pledge or give a note.

Medicals. Consider getting and paying for elective procedures in 2006 if you have exceeded the 7½% of AGI limit or are close to it.

*The Kiplinger Tax Letter, November 2006*

## Give to Charity Without Giving it All Away

A charitable gift annuity allows you to make a sizable contribution to your favorite cause while also generating a stream of income for yourself. That comes in handy if you want to savor the results of your good deed but don't have the endless resources of, say, Warren Buffett. The annuity works much like a regular immediate annuity: You make a single, lump-sum gift, and in return receive regular checks for as long as you live. Payouts are smaller than those for regular annuities, however. Most charities use standard rates to determine the payouts: Currently, they pay 6% a year for life if you purchase at age 65. You can claim a healthy tax deduction for the estimated amount the charity will eventually keep – usually about half your original donation, although the percentage varies based on how long you're expected to live.

*Kiplinger's Personal Finance Adviser, November 2006*

## Plan Before It's Too Late!

If you're like us, you're stunned to find that the Thanksgiving holiday is right around the corner. Christmas songs will soon be in the air, and before you know it, we'll be celebrating another new year. The time has come to take one final look at your financial situation and make your last minute moves to minimize your tax bill for the year. Here is a very brief overview of some steps you might want to consider before the ball drops in Times Square.

### Individuals

- **Be energy efficient:** You can claim a credit of up to \$2,000 for installing solar water heating equipment in your home. You can also claim a credit of up to \$500 for making various energy-saving improvements such as energy-efficient heat pumps, air

conditioning, insulation materials, and exterior windows and doors. Additionally, the purchase of a qualifying alternative-fuel vehicle could provide you with a tax credit of up to \$3,400.

- **Flexible spending account (FSA):** Maximizing your employer's FSA will generally allow you to decrease your taxable income while simultaneously paying for otherwise nondeductible expenses. And with the new grace rules, an FSA is much less of a use it or lose it proposition.

- **Beware of the new kiddie tax rules:** The age limit for the imposition of kiddie taxes on a child's unearned income has been recently increased from 14 to 18. Take time to review these rules and make changes to allow for the reduced payment of the kiddie tax now and in future years.

- **Retirement contributions:** Maximize the contributions to your employer's tax-deferred savings plan, thereby saving taxes immediately and deferring taxes on earnings in your account. Also, don't overlook your IRA contributions (either Roth or Traditional).

- **Charitable contributions:** If you've held appreciated stock for more than one year, consider donating those shares, rather than making similar cash donations. You'll avoid paying taxes on the stock appreciation but can claim the full fair market value of the stock as a charitable deduction.

#### Business

- **Purchase business assets:** If your business will soon require additional computers, furnishings, or even transportation equipment, make those purchases before the end of the year to take maximum advantage of the Section 179 expensing election.

- **Plan for retirement:** If you don't have a retirement plan, consider setting one up before the end of 2006, even if you don't have to actually fund the plan until 2007. In fact, there are federal tax credits for some of the costs of setting up a new retirement plan. And don't overlook a simplified Employee Pension (SEP) plan, which does not have to be established or funded until 2007.

- **Use your credit card:** Even a cash-basis business (as most are) can deduct expenses purchased with a credit card on the date of the charge, not necessarily when the credit card payment is made. So if you find that you need business supplies or equipment before the end of the year, and you're short of cash,

don't be afraid to charge and deduct it this year.

- **Defer income and accelerate deductions:** For cash-basis taxpayers, consider sending out your invoices late in December, so that the payment isn't received until the following year, thereby deferring current taxes. You should also stock up and pay for office supplies and other office items before year's end, including paying any outstanding bills or prepaying business expenses.

#### Investments

- **Lower taxes on dividends:** You might find that the more favorable tax rates now in place on dividends (15% or 5%, depending on the circumstances) might make dividend-paying stocks more attractive than ever. You'll want to be careful, though, since there are holding-period restrictions on those dividend payers, and not all dividends are given the favorable rates.

- **Offset gains and losses:** If you decide to rebalance your portfolio before the end of the year, or if you simply decide to sell some shares at a profit, don't forget the pent-up power of your capital losses. If you find that you have more losses than gains, you can deduct as much as \$3,000 of those losses in one year. You'll have to carry forward any losses in excess of \$3,000 against future gains or future ordinary income. But don't overlook the wash sale rule, which requires you to defer your loss if you purchase a "substantially identical" security within the period beginning 30 days before and ending 30 days after the date of the loss sale.

- **Long-term capital gains:** To be eligible for the lower (again, 15% or 5%) capital gains tax rates, you must hold the capital asset being sold for more than one year. So when selling or otherwise disposing of your stocks, bonds, investment property, rental property or other capital assets, pay close attention to your holding period. If you find that your holding period is less than one year, consider putting off the sale until later.

These are only a few of the many moves you can make to reduce your taxes before the end of the year. Don't overlook them. For more information on any of these strategies or to tailor a strategy that fits your tax situation, please call us today for a tax and financial planning consultation.

[www.fool.com/taxes/2006](http://www.fool.com/taxes/2006)

