

J W ENTERPRISES LLC'S

2007 Year-End Tax Planning for Individuals

Dear Client:

The end of 2007 is happening upon us faster than we think. With the year drawing to a close, now is an ideal time to review your tax situation and evaluate strategies that may help minimize your tax bill.

As is the case year after year, favorable changes to the tax laws over this past year are also accompanied by unfavorable modifications. Add to this reality the unusual number of tax incentives that are scheduled to expire at the end of this year and the need for year-end tax planning becomes even more urgent for many taxpayers as we head toward the end of 2007. Once you are filling out your 2007 return next year, it will be too late to change the result.

TRADITIONAL TAX STRATEGIES

Year-end tax planning tips typically fall into two general groups: (1) the traditional strategies that have proven themselves useful year after year, and (2) new opportunities that have arisen from recent changes to the tax laws.

Tried and true tax planning techniques can help virtually every taxpayer save money; some, of course, more than others. How much you can save depends on your individual circumstances but examination of the following general areas is worth a look in addition to considering the tax impact of any special circumstances in which you might find yourself this year.

Income shifting

One of the most fundamental year-end tax planning techniques involves accelerating deductible expenses in 2007 and deferring income, if economically feasible, into 2008. By delaying taxable income you defer taxes. Delaying taxable income may also prevent you from losing lucrative tax breaks that can be reduced or eliminated altogether as your income level rises and propels you into a higher tax bracket.

With only a few months left until the end of the year, you can probably anticipate with reasonable certainty what income and deductions you will be reporting on your 2007 tax return. You may also be able to predict with relative accuracy what your income and expenses for the first few months of 2008 will include. The ability to gauge your income and expenses for 2007 and into 2008 provides a golden opportunity to shift income or expenses into one year or the other depending on what will enable you to save the most overall taxes.

Shifting income, however, is not always a matter of simply delaying receipt of funds. Tax rules may require you to recognize certain types of income when you have earned the right to receive it, even if you arrange for its delayed payment. This office can help you recognize and navigate the differences.

Deduction management

Essential end of the year tax planning requires determining whether you will take the standard deduction or whether you will itemize your deductions. Consider "bunching" deductible expenses into one or the other year depending upon whether the standard deduction may be taken in one year or whether the adjusted gross income limits for medical (7.5 percent) or miscellaneous itemized deductions (2 percent) may be more easily met.

Even if you know you will itemize deductions, accelerating or deferring them is often a question of determining your probable tax bracket for year end and the next year to maximize their after tax value. Sometimes planning is as simple as paying your state estimated tax or real estate taxes in one year or the other; at other times, it's a question of making certain you gather the right proof and follow the proper steps in time to be entitled to a deduction in one year or the other. Again, this office can help.

Portfolio timing

The end of the year is an ideal time to examine your investments (winners and losers over the course of the year) to take the steps necessary to minimize your capital gains income and maximize the benefit of any capital losses. Long-term capital losses can be used to fully offset long-term capital gains. Losses taken in excess of gains can also be used to offset up to \$3,000 in ordinary income (or \$1,500 for a married couple filing separately). The strategy for short-term gains and losses follows a similar game plan, although coordinating the two sometimes takes special care.

Starting in 2008, traditional strategies in connection with capital gains and losses also need to accommodate a special, nontraditional opportunity -- the zero percent net capital gain rate for tax years 2008 through 2010. While this zero rate is only available for individuals in the 10 or 15 percent income tax brackets, it is well worth families, retirees, and others to manage their income tax brackets starting in 2008. That management starts at year-end 2007, as does the decision over whether to postpone a sale of a capital asset until January 2008 to take advantage of this favorable, zero rate.

Retirement planning

Year-end planning for 2007 also involves maximizing annual contributions to your retirement plan accounts, since one year's limit cannot be added to the next year's if not taken in time. While contributions to IRAs may be applied retroactively if made before the filing deadline, contributions to qualified plans must be made before the end of the calendar year.

Maximizing contributions to your retirement plan (or plans) before year end also allows you to reduce your adjusted gross income in direct proportion to those contributions. This in turn can give you the benefit of increasing the deductibility of medical and other deductions subject to adjusted gross income floors.

It is also not too early to think about a Roth IRA conversion plan if your present adjusted gross income is too high under the usual conversion rules. Although the adjusted gross income limit is not lifted until 2010 for a one-year only conversion opportunity, certain year-end maneuvers now can better set you up for maximizing conversion benefits in 2010. For example, if leaving employment, you may want to consider rolling over 401(k) balances to an IRA rather than leaving it in the plans.

Gift-giving

Take advantage of the 2007 annual and lifetime gift-giving limits to reduce your income and estate tax liabilities. For 2007 and then again in 2008, you can transfer \$12,000 per person, per year, without paying gift tax on the amounts transferred. Married couples can gift \$24,000 per person, per year without tax liability on the amounts transferred. That strategy not only avoids the possibility of paying a hefty estate tax later, but it removes earnings from those gifts from your taxable income bracket into that of the lower-bracket gift recipient.

NEW-FOR-2007 OPPORTUNITIES (AND DRAWBACKS)

Tax law changes constantly, and therefore so must individual tax planning. Tax year 2007 is no exception. While fundamental techniques should not be overlooked, attention to tax legislation -- both tax laws passed since last year and those tax laws that may be put to a vote in Congress

before year's end -- is equally important for most taxpayers. Here are the more important changes, and potential changes, directly impacting 2007 year-end tax planning.

Kiddie Tax

The Small Business and Work Opportunity Tax Act of 2007 introduced a number of tax incentives for small business, but included a few pitfalls for individuals. For 2007, a child under the age of 18 is subject to the "kiddie tax" (and thus pays tax at his or her parents' highest marginal tax rate on unearned income in excess of \$1,700). But in 2008, the applicable age rises and the kiddie tax will apply to a child under the age of 19 and full-time students under age 24. In light of this development, parents should consider selling appreciated stock and other assets belonging to their children now, especially if they will be in the 19 to 24 year-old category next year.

Expiring provisions

A variety of popular tax credits are set to sunset at the end of 2007, unless Congress extends them. However, don't wait to see what Congress does. Assess your tax situation as if Congress won't extend the tax breaks that apply to you. If this landscape changes, then fine-tuning in December is always possible: Tax breaks set to expire at the end of 2007 include:

State and local sales tax deduction. Despite being one of the more popular tax breaks, the deduction for state and local sales taxes is not permanent and is set to expire at the end of 2007. The American Jobs Creations Act of 2004 gave taxpayers who itemize deductions the option of claiming either state and local income taxes or state and local general sales taxes. Therefore, if you have been contemplating the purchase of a big-ticket item, such as a car or boat, you should consider making it sooner rather than later because the deduction for state and local general sales taxes expires at the end of 2007. However, you first need to compute what any potential state and local income tax deductions will amount to and then compare it to your potential sales tax deduction.

Mortgage insurance premiums. Premiums paid or accrued in 2007 for qualified mortgage insurance are deductible as qualified residence interest. The insurance must be carried on acquisition indebtedness for a qualified residence. A "qualified residence" is the principal residence and one other residence that is not treated as business property.

Tuition and fees deduction. Taxpayers may deduct qualifying tuition and fees paid in 2007 that are required for the student's enrollment or attendance at a post-secondary school. The tuition and fees deduction is an above-the-line write off that, depending on adjusted gross income, can reduce taxable income by as much as \$4,000. They are frequently more valuable than taking a Hope or Lifetime learning education credit. As a result, keep one eye on Congress and one on the possibility of paying next year's tuition early as year end approaches.

Classroom deduction. Full-time teachers, instructors, counselors and other educators can deduct up to \$250 worth of books, supplies, software, and other qualifying materials that they provide out of pocket expenses. The deduction is set to expire at the end of 2007, unless Congress extends it.

Qualified conservation contributions. Also set to expire in 2008 is the enhanced deduction for contributions of real property interests dedicated exclusively for conservation purposes. Easements in facades may also qualify. A 50 percent contribution base limit applies, rather than the 30 percent limit for capital gain property.

ALTERNATIVE MINIMUM TAX

Unfortunately, the alternative minimum tax (AMT) may require both traditional year-end planning techniques and new strategies to avoid or at least minimize its reach into a growing number of taxpayers' pockets. A planning technique that may save you a significant amount under the "regular tax" may be worthless if you unexpectedly fall into the AMT.

Start planning around the AMT by projecting your income for the rest of 2007 and, to the extent possible, for 2008 and even 2009. Without eleventh hour legislation from Congress, the risk of paying AMT in 2007 rises significantly over what had been the situation in 2006. In 2006, the AMT exemption amounts were \$42,500 for single individuals and \$62,550 for married couples filing jointly. For 2007, the amounts have been slashed to only \$33,750 for individuals, and \$45,000 for married couples filing jointly. While Congress may well raise the exemption amount at the last minute, planning for the worst is the safest course at this point.

Planning for the AMT typically focuses on carefully examining normal income tax deductions that become "tax preference" items and no longer deductible under the AMT. These include:

- * Personal exemptions
- * Deductions for state and local taxes;
- * Home equity loans and other mortgage interest not incurred in buying, building or improving your principal residence;
- * Incentive stock options (which may generate AMT income even when sold at a loss);
- * Interest from many tax-exempt bonds;
- * Deductions for unreimbursed business expenses; and
- * Other itemized deductions.

Give our office a call

With the complexity of the tax law, understanding what tax planning provisions to incorporate into your year-end tax planning strategy can be a daunting task. While this letter hopefully gives you a heads up on at least several strategies on which you might follow through before year end, there are many more techniques that can be used depending upon a client's individual circumstances.

For a more detailed plan that can be customized to your particular circumstances, please don't hesitate to give this office a call.

Sincerely yours,

Jake Worline