1996

Biting into Your Tax Bill 1996: A CPA's Guide for Taxpayers

American Institute of Certified Public Accountants. PR/Communications Team

1996 Tax Rates

If taxable income is...	The tax you owe is...
Single	
$0 – $24,000	15% of taxable income
$24,000 – $58,150	$3,600 + 28% of the amount over $24,000
$58,150 – $121,300	$13,162 + 31% of the amount over $58,150
$121,300 – $263,750	$32,738.50 + 36% of the amount over $121,300
$263,750 or more	$84,020.50 + 39.6% of the amount over $263,750
Joint or Surviving Spouses	
$0 – $40,100	15% of taxable income
$40,100 – $96,900	$6,015 + 28% of the amount over $40,100
$96,900 – $147,700	$21,919 + 31% of the amount over $96,900
$147,700 – $263,750	$37,667 + 36% of the amount over $147,700
$263,750 or more	$79,445 + 39.6% of the amount over $263,750
Married, Filing Separately	
$0 – $20,050	15% of taxable income
$20,050 – $48,450	$3,007.50 + 28% of the amount over $20,050
$48,450 – $73,850	$10,959.50 + 31% of the amount over $48,450
$73,850 – $131,875	$18,833.50 + 36% of the amount over $73,850
$131,875 or more	$39,722.50 + 39.6% of the amount over $131,875
Head of Household	
$0 – $32,150	15% of taxable income
$32,150 – $83,050	$4,822.50 + 28% of the amount over $32,150
$83,050 – $134,500	$19,074.50 + 31% of the amount over $83,050
$134,500 – $263,750	$35,024 + 36% of the amount over $134,500
$263,750 or more	$81,554 + 39.6% of the amount over $263,750

AICPA

The CPA. Never Underestimate The Value.℠

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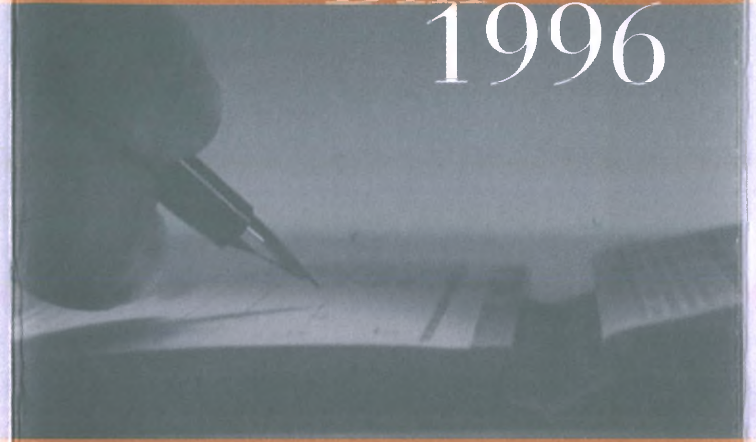

A CPA's Guide for Taxpayers

JUST THINKING ABOUT TALLYING THE YEAR'S TAX BILL IS ENOUGH TO MAKE ANYONE LOSE ONE'S APPETITE. BUT A LITTLE ADVANCE PLANNING CAN GO A LONG WAY TOWARD HELPING YOU GET A PALATABLE RESULT. PLANNING DOESN'T MEAN BITING OFF MORE THAN YOU CAN CHEW. AN APPETIZING TAX PLAN CAN BE AS SIMPLE AS **PIE**. POST INCOME IN THE YEAR IN WHICH YOUR TAX RATE IS LOWEST. INCUR EXPENSES IN THE YEAR IN WHICH YOUR TAX RATE IS HIGHEST. EXACT EVERY TAX ADVANTAGE TO WHICH YOU'RE ENTITLED – DEDUCTIONS, ALLOWANCES AND INCENTIVES. HERE ARE 21 TAX-TRIMMING TIPS AND SOME BASIC TAX INFORMATION THAT CAN HELP YOU PUT THESE THREE BASIC STRATEGIES IN MOTION. A LITTLE EFFORT CAN GO A LONG WAY TOWARD SWEETENING YOUR TAX LIFE FOR 1996.

This Year's Basics

Standard Deductions. Standard deductions have been adjusted upward from 1995 levels to:
Single – $4,000 (up $100); $5,000 if age 65 or older on or before 1/1/97 (up $150)
Married, filing jointly – $6,700 (up $150); $7,500 if either is 65 or older, $8,300 if both are (up $200/$250)
Head of Household – $5,900 (up $150); $6,900 if 65 or older (up $200)
Married, filing separately – $3,350 (up $75); $4,150 if 65 or older (up $125)

As in '95, the standard deduction for each individual claimed as a dependent by another person may not exceed the greater of $650 or earned income up to $4,000. A dependent includes not only children, but others you support, such as elderly parents.

Exemptions. Each personal exemption in 1996 is worth $2,550, up $50 from 1995.

Exemption Phase-Out. The income levels (adjusted gross income, or AGI) at which exemptions begin to be phased out also have been increased for 1996, as follows:
Single – $117,950 (up $3,250)
Married, filing jointly – $176,950 (up $4,900)
Head of Household – $147,450 (up $4,100)
Married, filing separately – $88,475 (up $2,450)

Exemptions are cut 2 percent for each $2,500 or fraction thereof above these AGI levels. Exemptions are lost entirely at: $240,450 for singles; $299,450 for couples; $269,950 for heads of households; and $149,725 for couples filing separately.

Itemized Deduction Phase-Out. The income level at which itemized deductions start phasing out has risen to $117,950 ($58,975 for couples filing separately). Itemized deductions are reduced by 3 percent of the amount your AGI exceeds this limit. The reduction does not apply to deductions for medical expenses, non-business casualty and theft losses, gambling losses, and investment interest. However, the reduction can never be more than 80 percent of your otherwise allowable deductions. This phase-out can add as much as 1.19 percent to your marginal tax rate.

New For '96

401(k) Plans. The maximum elective salary deferral for a 401(k) for 1996 rises to $9,500 from $9,240 in 1995.

Retirement Plan Payout Tax. The 15-percent excise tax on "excessive" retirement plan payouts is triggered at $155,000 for 1996, up $5,000 from last year. For lump sum distributions not rolled over, the excise tax kicks in at $775,000.

State Taxation of Pensions. Generally, states are now prohibited from taxing former residents' retirement-plan income.

Social Security Benefits. In 1996, retirees can earn more before benefits are cut. Those under 65 can earn up to $8,280 this year before they lose

$1 for each $2 above that figure. Beneficiaries between 65 and 70 can earn $12,500 before incurring a $1 loss for each $3. As always, once you've reached 70, there is no longer a limit.

SOCIAL SECURITY NUMBER FOR NEWBORNS. For babies born before December 1, 1996, a Social Security number must be entered on your return to claim an exemption.

21 TAX-TRIMMING TIPS

MAXIMIZE A 401(k). If your employer offers a 401(k), consider making the maximum contribution, which is $9,500 for 1996. Your contribution lowers your gross income, and your earnings grow tax-deferred until retirement.

REEVALUATE IRAS. Plan to make maximum contributions to your Individual Retirement Account (IRA). Even if you cannot deduct your contributions, IRAs still may make tax sense since earnings grow tax-deferred until withdrawal.

TRANSFER LUMP SUMS. If you expect a lump-sum distribution from a pension or profit-sharing plan, and don't have an immediate need for the money, consider rolling it over to an IRA, where it will continue to grow tax-deferred. Be sure the transfer is made directly from one trustee to another. Otherwise, 20 percent must be withheld for the IRS. In addition, the distribution must be rolled over within 60 days to continue the tax deferral.

OPEN A KEOGH. Keoghs are available to individuals with any amount of self-employment income. Generally, if you qualify, you can contribute to a defined contribution plan and deduct up to 25 percent of your net self-employment income, or $30,000, whichever is less.

ADJUST WITHHOLDING. Match your withholding to your tax liability. If you've been elevated to a higher tax bracket, adjust your withholding or risk an underpayment penalty. Conversely, you may be giving the IRS more than you need to. If you received a tax refund last year, adjust your withholding, take the extra cash, and invest it.

INVEST TAX-FREE. Municipal bond interest is not taxed on your federal return and also may be tax-free in the state in which you live. Keep in mind the after-tax yield on tax-free bonds may be more than that of corporate bonds.

USE SERIES EE BONDS. Consider investing in Series EE bonds if you're saving for a college education. Income from bonds issued after December 31, 1989 may be totally tax-free if it is used to pay education fees. Income limits apply to this tax break, so be sure to consult a tax adviser.

INVEST FOR CAPITAL GAINS. Currently, long-term capital gains are taxed at a favorable maximum rate of only 28 percent. Congress is seeking further reductions, which means gain-producing investments may become even more attractive.

SHIFT INCOME. To reduce your family's overall tax bill, consider transferring assets to your child — the income generated will be taxed at the child's lower rate. However, watch out for the "kiddie tax." If your child under age 14 has more than $1,300 in unearned income, the excess will be taxed at your highest marginal tax rate. For children age 14 and over, unearned income is taxed at their own tax rate. (Earned income is always taxed at the child's rate.)

GIVE CASH. To minimize the tax burden for your heirs, consider a gift-giving plan. You and your spouse each can give up to $10,000 a year to as many recipients as you wish with no gift tax.

HIRE YOUR CHILDREN. If you own a business, consider hiring your child as an employee. The child earns income, and you deduct the salary. Just be sure it's a real job at a fair salary.

DONATE TO CHARITY. As long as you itemize, charitable donations are generally fully deductible up to 50 percent of your AGI. However, the rules require written documentation for any donation of $250 or more. A double tax break is available for those who donate appreciated property. If you have held the property for more than one year, you generally can deduct the property's fair market value up to 30 percent of your AGI and not pay tax on its appreciation. Certain expenses you incur for charity work also are deductible, but documentation is required.

TALLY MEDICAL BILLS. Since only medical expenses surpassing 7.5 percent of your AGI are deductible, be sure to total them before year-end to see if you are near the limit. If you are close, it may pay to accelerate your upcoming medical appointments. Otherwise, consider postponing non-essential medical procedures until next year. When making your calculation, don't forget to include expenses such as transportation to and from medical facilities and medical supplies.

BUNCH MISCELLANEOUS DEDUCTIONS. Miscellaneous expenses are deductible only above 2 percent of your AGI. Deductions generally fall into one of three categories: unreimbursed employee business expenses, investment expenses, and tax-related expenses. If your miscellaneous expenses hover around the 2-percent limit, try to bunch them into alternate years to increase your deduction.

TAKE ADVANTAGE OF YOUR HOME. You can deduct your mortgage interest, points paid to secure a mortgage on a principal residence, and property taxes. Keep in mind, however, that points paid on refinanced mortgages usually are not immediately deductible. Instead, you generally must deduct this sum ratably each year over the term of the loan.

BORROW SMART. If you have high-interest credit card debt, you might consider a home equity loan. Interest rates are generally much lower, and interest payments are generally tax deductible.

DEDUCT MOVING COSTS. For a work-related move of 50 miles or more, you generally can deduct the cost of transporting you, your family and your belongings from your former residence to your new home. However, the cost of meals incurred while traveling, temporary lodging and house-hunting expenses are no longer deductible.

BEWARE OF THE AMT. If you have an abundance of credits and deductions this year, you may be subject to the alternative minimum tax (AMT), a separate tax system designed to ensure that everyone pays a minimum amount of tax. The only way to know for sure is to calculate your taxes both ways.

TAKE THE AGE 55+ TAX EXCLUSION. If you are age 55 or older, you may be able to take a $125,000 exclusion on the gain from the sale of your principal residence. You can take the exclusion only once in a lifetime. If you're 55+ and planning to marry someone who's already used the exclusion, consider selling your house and taking the exclusion before you marry, or you will lose it forever.

CHOOSE THE RIGHT FILING STATUS. Separate returns may save you taxes when one spouse has substantial deductions in a category that is subject to AGI limitations. When filing separate returns, remember: If one spouse itemizes, the other spouse must also itemize. If single, and you qualify, you may benefit from claiming head-of-household status. To determine your best filing status, calculate taxes each way.

SEEK TAX-PLANNING ADVICE. To make sure you're not paying more in taxes than you should, talk to a CPA. CPAs are well-versed in the latest tax developments and planning strategies that can help you minimize your tax burden.