1990

19 Tax-Savings Tips for 1990 : A CPA's Guide

American Institute of Certified Public Accountants. Communications Division

1990 Tax Rates

If taxable income is...	The tax you owe is...
Single	
$0–$19,450	15% of taxable income
$19,450–$47,050	$2,917.50 + 28% of amount over $19,450
$47,050–$97,620	$10,645.50 + 33% of amount over $47,050
Over $97,620	$27,333.60 + 28% of amount over $97,620*
Joint/Surviving Spouses	
$0–$32,450	15% of taxable income
$32,450–$78,400	$4,867.50 + 28% of amount over $32,450
$78,400–$162,770	$17,733.50 + 33% of amount over $78,400
Over $162,770	$45,575.60 + 28% of amount over $162,770*
Married, Filing Separately	
$0–$16,225	15% of taxable income
$16,225–$39,200	$2,433.75 + 28% of amount over $16,225
$39,200–$123,570	$8,866.75 + 33% of amount over $39,200
Over $123,570	$36,708.85 + 28% of amount over $123,570*
Head of Household	
$0–$26,050	15% of taxable income
$26,050–$67,200	$3,907.50 + 28% of amount over $26,050
$67,200–$134,930	$15,429.50 + 33% of amount over $67,200
Over $134,930	$37,780.40 + 28% of amount over $134,930*

*Plus adjustments for phase-out of personal exemptions, which vary from taxpayer to taxpayer.

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A CPA'S GUIDE

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TAX SAVING TIPS FOR 1990

You *Can* Trim Your Taxes

Trying to reduce your tax bill is like trying to lose weight. It isn't easy, but it is possible. By following a careful regimen of tax planning, you can trim your taxes and improve your overall financial health at the same time.

The hardest part of tax planning is knowing where to start. That's where this brochure comes in. The guide provides you with some basic tax strategies that you can apply year after year, regardless of changes in the tax law or your personal finances. With that information under your belt, you can move on to the 19 tax tips designed to guide you to a slimmer 1990 tax bill.

The Starting Point

Effective tax planning begins with knowing how and when to *defer income and accelerate deductions*. Under this classic tax strategy, you reduce taxes by postponing income until a later year. At the same time, you try to offset current income by increasing the amount of deductions you can claim right away. This tax strategy works best when you expect federal income tax rates or your personal tax bracket to remain the same or decrease in a subsequent year. Another reason for deferring income relates to the ''time value'' of money. Basically, a dollar in hand today is worth more than a dollar in hand next year, since today's dollars can be invested to generate more wealth.

What if tax rates are rising or you expect your income to take a substantial jump and land you in a higher marginal tax bracket? In these cases, you may reap greater tax benefits by *accelerating income and deferring deductions* to a later year, when they may be more valuable.

You should also defer deductible expenses if you expect your itemized deductions to fall short of your standard deduction. In 1990, the standard deduction is $5,450 for joint filers, $3,250 for single taxpayers, and $4,750 for anyone filing as a head of household. If you can't pull enough itemized deductions into this year to beat these figures, try to push as many deductions as possible into 1990, when you may be able to take full advantage of them.

Keep these basic tax strategies in mind as you read the tax tips in this brochure. . .and you may be on your way to a trimmer tax bill.

Four Easy Ways to Defer Income

If tax rates remain the same and you decide that deferring income will work for you this year, you may want to consider the following tax actions:

- Ask your employer to delay a year-end bonus or commissions until after December 31, 1990.
- If you are self-employed, you will not have to pay taxes on bills collected after the new year.
- Defer interest income by buying short-term government securities or certificates of deposit that mature sometime after December 31, 1990.
- If you sell property for gain in December, find out if you can delay the contract signing until January 1, 1991. If you can, any capital gains you realize will have to be reported on next year's tax return.

What's New in 1990?

- The personal exemption is now $2,050, up $50.
- The maximum contribution you can make to a 401(k) plan has been increased to $7,979, up $352.
- The amount of personal interest you can deduct is 10%, down from 20% last year.
- Business-related transportation is now deductible at 26 cents per mile.
- For the first time ever, self-employed individuals will be able to deduct 50% of the self-employment taxes they paid during the year.
- For certain taxpayers, interest earned on EE Savings Bonds purchased after January 1, 1990 will be free from federal income tax if the proceeds are used to pay the costs of college or vocational school. Ask your CPA to explain the other limitations.

* Congress is considering a number of revisions to current tax law. Before acting on information provided in this brochure, contact your CPA for an update on the latest tax developments.

19 TAX-SAVING TIPS

1 Choose Less Taxing Ways to Save

Earn tax-free or tax-deferred interest by selecting the right investments. For example, municipal bonds issued in your state are generally free from federal and state income taxes. Other tax-advantaged investments include EE Savings Bonds and Treasury bills.

> **TAX-SAVINGS ALERT**
>
> If you are in the 28% tax bracket, a tax-free investment earning 7% is the equivalent of a 9.72% taxable yield.

2 Time Capital Gains

Currently, capital gains are taxed at regular income rates. However, Congress may soon elect a more favorable tax treatment of capital gains. If you think the tax will drop, you may want to delay selling appreciated assets. On the other hand, if the law doesn't change and income rates increase, you may regret not claiming gains this year. Your best bet is to consider market conditions and watch for changes in tax legislation. You should also consider offsetting any capital gains with capital losses.

3 Capitalize on a 401(k)

In 1990, you can contribute up to $7,979 to a 401(k) plan. Whatever amount you deposit automatically reduces the amount of income on which you must pay taxes.

4 Consider a Keogh

If you are self-employed, you can contribute and deduct up to 20% of your income or $30,000 (whichever is less) to a Keogh. You must open the account before January 1, 1990 — but deposits don't have to be made until April 15, 1991.

5 Take Another Look at IRAs

If you (and your spouse) don't participate in an employer's retirement program, you can deduct up to $2,000 in IRA contributions if single and up to $4,000 if married. Participants in company plans may also qualify for the deduction, depending on their adjusted gross income.

6 Don't Stumble Over Lump Sums

To avoid a hefty tax bill on a lump-sum distribution from a pension or profit-sharing plan, consult your CPA. He or she may suggest rolling the funds into an IRA so that you will have to pay tax only on the amount you actually withdraw at a later date.

7 Capitalize on Family Ties

Hire your children in a business you own and you can deduct their salaries. What's more, your children's income will be taxed at their own rate. But your children must perform necessary duties and their salaries must be in line with what other employees earn.

8 Shift Income to Children

Another way to save taxes is by transferring assets to your children. Any interest and dividends earned by a child age 14 or older are taxed at the child's rate. For children under age 14, the first $500 of unearned income is tax-free and the next $500 is taxed at their lower rate. However, any unearned income in excess of $1,000 is taxed at the parent's highest marginal rate.

9 Offset Rental Income

If you expect your rental property to generate taxable income, you may want to accelerate some of your allowable operating expenses, such as repairs, advertising costs, fire and liability insurance, and even maid service. Keep in mind that taxpayers with an adjusted gross income of $100,000 or less can still deduct up to $25,000 in passive losses associated with a rental property that they actively participate in managing.

10 Turn a Home into Income

Rent a principal or second home for 14 days or less, and pocket the income tax-free.

11 Take Advantage of Homeowner Deductions

Your home is the key to a number of deductions. Not only can you generally deduct mortgage interest on first and second homes, but you can also deduct real estate taxes, points paid to secure a mortgage, and interest on home equity loans of up to $100,000. What's more, if you sell your home, you won't have to pay tax on the capital gains as long as you buy a new home whose price equals or exceeds the adjusted selling price of the previous home.

12 Make Your Age Work for You

Unlock the profits in your home. If you are at least age 55 and meet certain ownership and use requirements, you can exclude from taxable income up to $125,000 of the profit realized from selling your principal home. The tax break is available only once in a lifetime per person or couple.

13 Restructure Debt

Credit costs more than ever. This year, you can deduct only 10% of the interest charged on personal loans, credit card accounts, or unpaid tax bills. Next year, the deduction will disappear completely.

One way to eliminate consumer debt is by liquidating some of your investments. You can then borrow funds to finance other investments. Keep in mind that interest on investment loans is fully deductible, up to the amount of your net income. In 1990, you can also deduct up to 10% or $1,000 of the interest in excess of your net investment income. Alternately, you can use the proceeds of a home equity loan to pay off your personal debt.

> **TAX-SAVINGS ALERT**
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> If you are in the 28% tax bracket, paying off a credit card with a 19% interest rate is the equivalent of an investment earning 26% (before taxes).

14 Start a Deduction Diary

Documentation is one of the best ways to ensure your tax deductions. Keep an ongoing log of all business-related expenses, charitable deductions, and miscellaneous expenses. You will need to include the date, names of attendees or function, and purpose.

15 Reduce the Bite of Business Meals

You can generally deduct 80% of the cost of meals directly related to your trade or business—as long as they are not lavish or extravagant. If your company does not reimburse your business meal expenses, you must add the 80% to your other miscellaneous itemized deductions.

16 Bunch Miscellaneous Expenses

Miscellaneous expenses must exceed 2% of your adjusted gross income before you can deduct them. If your expenses are nowhere near the 2% floor, postpone any remaining expenses until next year. But if you are near or over the limit, draw into this year as many itemized miscellaneous expenses as possible. For example, you may be able to prepay your union dues, extend subscriptions to trade magazines, or enroll in classes related to your job. Other miscellaneous expenses include job-hunting costs and tax preparation fees.

17 Examine Your Medical Expenses

Unreimbursed medical expenses are deductible only to the extent that they exceed 7.5% of your adjusted gross income. You may be able to push your expenses into the deductible range by paying off your orthodontist's bills, purchasing new eyeglasses or contact lenses, or scheduling that long-delayed dental appointment. Other deductible expenses include transportation to and from medical facilities, insurance premiums, allergy medicines, acupuncture, and false teeth. In some cases, expensive home improvements may also be deductible as a medical expense. For example, deductions have been allowed for special bathroom facilities for handicapped individuals.

18 Charity Pays

By giving to your favorite charity before December 31, 1990, you can realize a tax savings on this year's return. And there's a bonus if you donate appreciated property: you can deduct the full value of the asset and avoid paying tax on its appreciation at the same time.

In addition to gifts of property, you can deduct expenses associated with volunteer activities, including transportation costs.

19 Check Your Withholding

Make sure you are withholding enough tax from your paychecks. If you fail to set aside at least as much tax as you owed in 1989, or at least 90% of your 1990 tax liability, you will be hit with a substantial penalty on the balance due.