

## 2007 Federal Tax Changes and Reminders

**I**t is time to think about compiling the tax information needed to file your 2007 tax return. There are a number of items discussed below that should help you get ready and plan for the future.

### Dependency

When children graduate from high school and get jobs or go on to school, at some point they will no longer qualify as dependents. A child must meet the following conditions to be considered a dependent: the child must be under the age of nineteen or under age twenty-four and a full time student for at least five months during the year; the child must be a U.S. citizen, a resident alien, or a resident of Canada or Mexico; the child must live with the parent for more than half the year (temporary absences such as college are ignored); and the child must not provide more than half of his or her own support.

Even though a parent provides a home for the child while in college, the financial aid and loan responsibility may enter into the determination of support provided by the child.

In the year the child graduates from high school or college, it is important to look at the earnings for the entire year to determine support. Even though the child has lived at home and been a fulltime student for five months, his or her total yearly income could be high enough to have provided more than half of his or her own support.

### Kiddie Tax

This year marks a big change in the Kiddie tax rules. Kiddie tax is the name for the way of determining

the tax a child will pay when the child has unearned income (interest, dividends, capital gains, royalties, etc.) of \$1700 or more and is under the age of eighteen. Previously, Kiddie tax applied to children under the age of fourteen. In 2008, the age will rise to match the age of dependency. It will apply to children under the age of nineteen or full-time students under the age of twenty-four.

Kiddie tax rules apply the parents' tax rate to the excess unearned income of the child over \$1700. The income up to that point is subject to a standard deduction and generally a ten percent tax rate.

The importance of this change is that the child who has savings, especially through trust funds or other means, probably will be paying a larger tax than he or she would otherwise be accustomed to. Form 8615 (Tax for Children under Age 18 with Investment Income of More Than \$1,700) should be used to compute this tax. In addition, parents who want to shift income to the child through gifts of stock or other investments may need to seek advice before making the transfer.

### Expiring Tax Breaks

Congress has passed legislation during 2006 and 2007 that extended or made permanent certain tax breaks. One tax issue that has not been addressed yet is the Alternative Minimum Tax (AMT). In the year 2007, the AMT exemption will decrease to the pre-2001 tax

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act level. This could mean that you will be subject to AMT this year when you have not been subject to it in the past. If you have been subject to it in the past, it can mean you will pay more AMT. The difference between the pre-and post-exemption is about \$16,000. This could mean an additional \$4,000 in AMT in 2007.

The Energy Credit has been extended through 2008. Also, the tuition deduction and the maximum \$250 Educator's Deduction have been extended through 2007.

## Capital Gains

The capital gains rates have been very attractive since 2001. The maximum capital gains rate is normally fifteen percent unless you are in the fifteen percent income tax bracket. For those whose tax bracket is fifteen percent or lower, the maximum capital gains rate is five percent. In 2008, the five percent rate decreases to zero percent. This reduced rate will continue through 2010. If you have flexible income, this may be the time to choose to sell property to take advantage of this rate. As the tax law stands now, the lower capital gains rate of fifteen percent will be in existence through 2010. After that, rates are scheduled to return to the twenty percent/ten percent limit in effect before the 2001 change. Remember also that dividends will be taxed at ordinary income rates rather than capital gains rates after 2010. Now is the time to consider capital gains planning before it's too late.

## Nonprofit Reporting

If you are an officer or responsible person for a small tax-exempt organization such as the soccer or band booster club, your organization may need to file Form 990-N, Electronic Notice (e-postcard) beginning in 2008. This new annual notice is for tax-exempt organizations not required to file Form 990 or 990-EZ. Form 990 or 990-EZ is generally required by organizations with annual gross receipts of more than \$25,000. The IRS sent letters to the responsible parties it knew about but may have missed some or the people are no longer involved with the organization.

According to the SSA/IRS Reporter included with a taxpayer's Form 941 for the second quarter of 2007, this

postcard can only be filed electronically. IRS plans to have an option that permits free electronic submission of the e-postcard. IRS hopes people—especially those doing volunteer work—will spread the word about this upcoming requirement.

Any organization that fails to file the annual form for three consecutive years will automatically lose its tax-exempt status. Once the status is lost, the organization will have to reapply for the tax-exempt status.

## HSA

Health Savings Accounts are becoming an increasingly popular choice for individuals and companies seeking medical coverage. The savings account is available to taxpayers who have an HSA qualified high deductible medical plan. These plans generally offer health insurance at a more affordable rate. Once the insurance plan is in place, a health savings account (HSA) may be obtained. The HSA allows the taxpayer to contribute a certain dollar amount each year through which medical expenses not covered by insurance can be paid. The tax-savings feature is that the contribution is currently deductible even if it has not been spent yet. The account will grow tax free as long as the monies in the account are spent for medical expenses. If a taxpayer reaches age sixty-five, the monies may be withdrawn for nonmedical purposes, such as an IRA, without penalty. Like the IRA, the taxpayer will pay taxes at that time on the amount not used for medical care.

The maximum that may be contributed in 2007 for a family plan is \$5,650 and \$2,850 for a single plan. In addition, the year the plan begins, the maximum contribution may be made regardless of the time of the year the account is opened.

## Retirement Decisions

As the end of the year approaches, you are asked to make pension contribution decisions as well as flex spending, cafeteria, dependent care, and other deferral decisions. Congress has made permanent the increases in pension and IRA amounts. This year, you may con-

## TAX APPOINTMENT WORKSHEET

	√	EVENT	DOCUMENTS OR INFORMATION NEEDED
1		Married or divorced in 2007	Married – prior year return of both spouses Divorced – copy of the divorce decree
2		Birth or Adoption	Social Security cards and adoption papers
3		Death of child or spouse	Date of death -
4		Additional members of household	Date of occupancy and relationship
5		Job change	Start date; Name of new employer; W-2s from new and old employers
6		Unemployment	Unemployment Form
7		Retirement contribution	Type of plan; Amount of contribution
8		Retirement distributions	Form 1099-R
9		Social Security Benefits	Form 1099-SSA
10		Sale of stocks, bonds, etc.	Form 1099-B or other sale documents; basis or original costs
11		Purchase of stocks, bonds, etc., personal residence, or other real estate	Purchase documents; closing papers
12		Inheritance	Will; K-1 from the estate
13		Trade any property	Date of trade, property given up and property received, basis and FMV; Qualified intermediary sales agreements or closing papers
14		Start or end a small business	Formation or termination dates; Property contributions or distributions
15		Lawsuit settlements	Date received; reason for the settlement; 1099-MISC
16		Rental property	Income; expenses; new property purchased
17		Prizes	Form 1099-MISC; value of prizes not included on Form 1099-MISC
18		Lottery or gambling winnings	Total amount won whether on W-2Gs or not; total amount of losses
19		Health insurance, medical, dental, or drug expenses	Health insurance premiums; post-taxed payments; totals of other medical, dental, and drug expenses. If the health insurance is pre-taxed (ie. cafeteria plan, §125, POP), premiums have already been deducted from the wage.
		Medical Miles (18 cents per mile)	Total miles driven
20		State income or property taxes paid	Prior year's income tax return; property tax bills; closing papers from the purchase or sale of property; letter from the state regarding any change in a prior filed return
21		Purchase or refinance a home	Closing papers from purchase; Forms 1098
22		Charitable contributions of money, property, or out of pocket expenses	Date and type of contributions, knowledge that receipts from the organizations have been received; mileage log for charitable work
		Charitable Miles (14 cents per mile)	Total miles driven
		Transfer of IRA to charity	Brokerage statement showing transfer
23		Job related expenses	Meals, lodging, and miscellaneous expense amounts for items related to employment
		Business miles (48.5 cents per mile)	Total miles driven, business miles driven per vehicle
24		Educational or student loan interest expenses	Form 1098-T for parents or children; Interest record for student loans; If the child is a student, the form will come to the child.
25		Child or disabled spouse care	The name, address, and ID number of the day care provider; the amount paid to the provider; if the provider comes into your home a W-2 may be required.
26		Energy credit	Information regarding the purchase of qualifying vehicle, windows, doors, furnace, solar, or other energy upgrades.

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tribute up to \$4,000 into a regular or a Roth IRA. The maximum amount that can be contributed to a 401k for 2007 is \$15,500. If you are age fifty or over, you may qualify for catch-up contributions. This could be up to an additional \$5,000 depending on the type of plan.

The Saver's Credit has been made permanent as well. That means that taxpayers with income not more than the following amount may qualify for up to a fifty percent credit on the amount placed in IRAs or qualified pension plans: single individuals, \$26,000; head of household, \$39,500; and married couples, \$52,000 (as indexed for 2007).

## Information Disclosure

IRS rules are pretty specific. The rules prohibit disclosure of your tax return information to anyone other than you *unless* you have authorized the release. This includes

sharing your tax return information with one of your children, your lawyer, a mortgage company, etc.

This is the law and was passed to protect your privacy and prohibit any unauthorized disclosures. If you want your tax return information shared with anyone, you will need to provide written authorization. The authorization should specifically authorize the disclosure of *tax* information, the applicable years, who it is to be disclosed to, who is disclosing the information, and contain your signature. A general authorization to disclose financial information may not be sufficient, so please specify *tax* information. Caution: Once the requested information is disclosed to the person or company you authorized to receive it, there is no control over what the person or company does with the information. Again these IRS restrictions on disclosure are for your protection. **EA**



Your Business Card Here