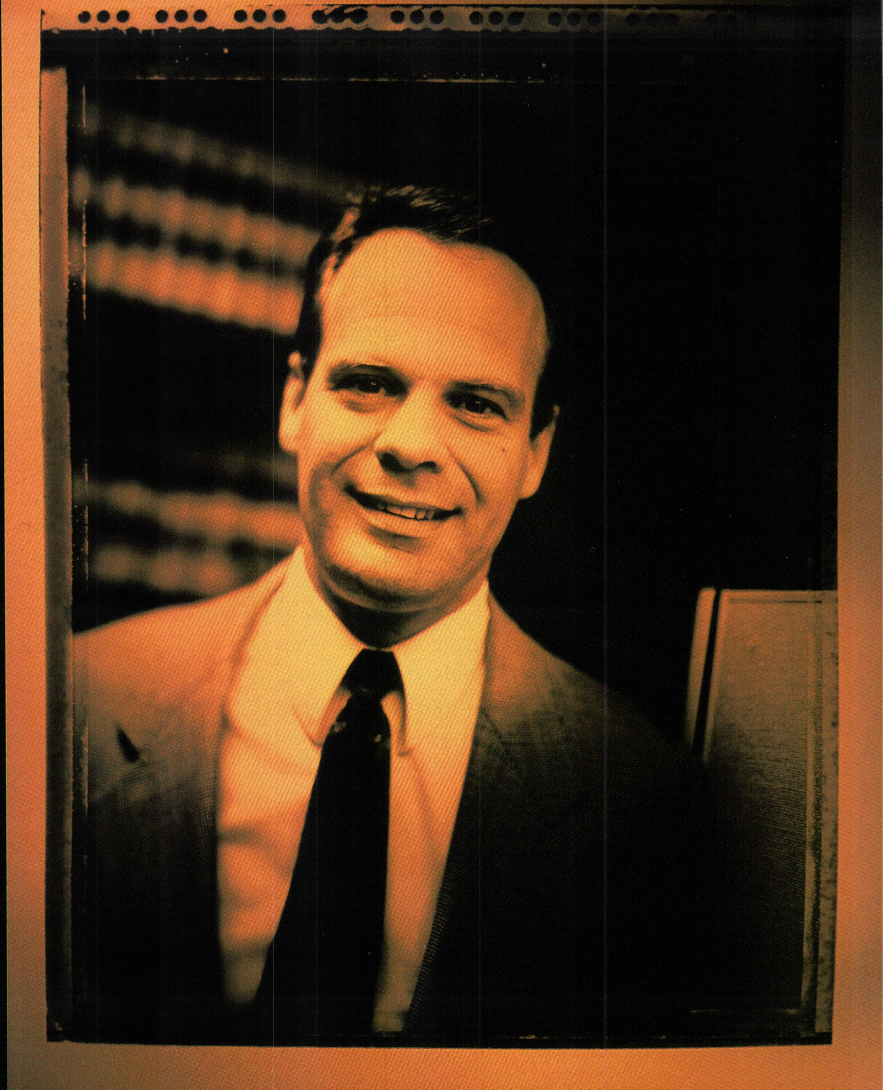
Tax Talk

Planning for April 15 should be year-long adventure

by Cynthia Scanlon
photography by Jim Marshall



Mitchell Chronister, CPA and tax partner for Toback CPAs, P.C.

Let's admit it, tax planning ranks right up there with root canal work or having to get your car emissions tested: annoying, somewhat painful, but it must be done. With a little bit of thought and planning, however, the looming tax deadline need not be all-consuming. While it may be too late to take advantage of many write-offs for the preceding year, it is not too late to get some money into your IRA or start planning for this year's taxes.

According to Allen Nahrwold, CPA and principle of Nahrwold and Company, P.C., corporate entities wanting to change their operating tax status need to think about doing so in January. For other small business owners, thinking about tax consequences should generally be done in January and then specifically done in the summer or early fall. And thinking three years out to plan for possible fluctuations in income is not a bad idea either.

Whether or not to do your own taxes is always up for debate. However, over the years, the tax laws have become so complicated that many individuals and companies no longer do their own returns and Nahrwold sees that as a savvy business move. "We see people who do their own returns and there's nothing wrong with that, but I think they could probably save more money if they paid a preparer," he says. "Plus it's good discipline for people. If they know they have to go someplace on Feb. 10 with their stuff, they are going to have it pretty well done."

He adds, "If you are selling mutual funds and · the brokerage house doesn't tell you what the basis is, it's pretty difficult for the average taxpayer to compute that. Unless they have formal training, people in business are apt to miss things when they do their own returns."

So what can you do to minimize your tax bite with only a short time away from the filing deadline? You can make a $2,000 deductible IRA contribution before April 15, according to Richard Bingaman, CPA and manager at Simek & Company, P.C. You can also extend the set up date of a Simplified Employee Pension Plan as late as September 15 of the following year to go back and take a deduction for the prior year. These plans do have income caps, so check with your accountant to see if you are eligible to contribute. Also, keep in mind, the earlier in the year the contribution is made, the better.

"The sooner you get it in, the more tax-deferred return you earn on that account, so make those contributions early," says Bingaman.

For those still confused about traditional versus Roth IRA, Bingaman clarifies the confusion fairly simply. In a traditional IRA, the investment return on that IRA account is tax-deferred, meaning when you take distributions from the IRA, you will pay tax on the distributions from that account. For the Roth IRA, your account grows tax-free. When you take distributions out of that account, it will be tax-free. "When you make a contribution to a traditional IRA, you get a deduction for it; you get a tax benefit," says Bingaman. "But you have to weigh that current tax benefit against the benefit you're going to receive with a tax-free Roth IRA contribution. You get no current deduction against your taxes, but it grows tax-free."

In deciding to convert a traditional IRA to a Roth IRA, Bingaman says you have to run the numbers to figure out the tax consequences. Asking questions like: "When are you going to retire? How long are you going to have income below the income limitation to facilitate you being able to contribute to a Roth IRA?" is a good place to start. These are questions a qualified certified public accountant can help you answer.

Bingaman adds, "If you're putting contributions into a IRA account and those contributions are going to be in that account for more than 10 years, the benefits of a tax-free Roth are going to far outweigh a traditional IRA."

Allen Nahrwold, CPA and principle of Nahrwold and Company, P.C.

Richard Bingaman, CPA and manager at Simek & Company, P.C.

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As far as deductions go, there are the old stand-bys and a few newcomers to the list. As usual, any individual can gift up to $10,000 in value to any person they chose with no tax impact, says Mitchell Chronister, CPA and tax partner for Toback CPAs, P.C. "If you're going to give cash, have the check clear before the 31st [of December]."

Bingaman also recommends paying your January mortgage payment early, time enough for the draft to clear the bank, and send those charitable contributions in by the end of the year, as well. If you are expecting an end-of-the-year bonus from your employer, see if you can defer receiving it until the following January.

While the home-based business is becoming more predominant, Bingaman says the IRS has fairly stringent rules on what people can deduct for their home business and they keep an eye on how people are reporting those deductions. Complete and accurate records are vital and a good way to avoid many headaches down the road.

Something that is new is school contributions. If you make a $200 contribution to any public school in Arizona, you will get a $200 tax credit on your state tax return and the money will go to the school's extra curricular activity pot. You will also get a $200 deduction on your federal return. At a 32 percent tax rate, you would get back $64. So you get all $200 back on your state tax return, plus $64 back on your federal return.

You can do the same thing for private schools in Arizona if you contribute up to $500 for their scholarship program. You will get $500 credit on your Arizona return and $500 deduction on federal return for a total of up to $660 back on a $500 donation.

"If you have a business and you use your car in your business, there are certain makes that you can expend up to $19,500 in the year of purchase that you place in service," says Chronister. The vehicles must have an unloaded gross vehicle weight of greater than 6,000 pounds. These are usually Suburbans, Ford Expeditions, and big sport utility vehicles. Chronister says you can also expense office furniture and computers before year-end.

Again, you can deduct up to $19,500 and not depreciate it. If you donate a vehicle to a charitable organization, Bingaman says your charitable amount will be the fair-market value of that vehicle based on an appraisal. "The Blue Book won't do it," he says, referring to the book that gives wholesale and retail values of automobiles. "You'll need someone at a dealership or someone that regularly appraises vehicles to do it."

He adds, "The IRS has stated that the Blue Book isn't going to do it because there are different values given in the book and that doesn't take into consideration the true condition of the vehicle."

As far as audits go, Bingaman says the IRS looks for things that might raise an eyebrow, such as significant fluctuations of income. Hobby losses are also a flag. Many people start a small, side business at home based on their hobby and tend to take losses on it for the first year or two. But if your expenses far outweigh your income for the business, you might be hearing from Uncle Sam. To help make your case that the business is legitimate, Bingaman recommends having a business plan, separate checking account, and solid record keeping in place. "You want to hold yourself out as a business and look like you are truly trying to create business income and profit," he says. "Consistently creating losses will not be allowed on your return, and it's easy for the IRS to spot it on your schedule C return."

So what exactly is the news on the IRS' desire to become "kinder and gentler?" According to Bingaman, the IRS has made strides in becoming more customer service-oriented. "The IRS has been updating their Web site (www.irs.gov) on a consistent basis recognizing the fact that many more people are using the Internet to gain information," he says.

The IRS is also willing to "offer and compromise" if you have outstanding liabilities that you haven't paid. They are a little kinder and gentler with regard to accepting offers in compromise, says Bingaman, which translates to making a deal on amount and method of payment. "That's a significant change."

Bingaman says the IRS is also being kinder in divorce situations where one spouse was truly unaware of what another spouse was doing financially, such as a husband owning a business and keeping his wife in the dark about the financial dealings of that business. "There are innocent spouse rules that protect one spouse from being subject to the joint liability if they really didn't have knowledge of what the other spouse was doing," says Bingaman. "The IRS is very favorable in that area now."

But as Nahrwold reminds us, "The IRS is somewhat kinder and gentler, but they still have a job to do."

And if you haven't filed your returns yet, so do you. **AB**

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