Reviewing Your Tax Strategies

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Minimizing your potential income taxes requires a regular review of your financial picture and the current tax strategies available to you. In fact, tax planning can be a year-round activity.

Strategies to consider
Although your tax picture is unique to you, there are common strategies to consider and discuss with your financial and tax advisors. Here are a few:

- **Minimize taxable income while saving for retirement.**
  - **If you are an employee**, you make contributions to your 401(k) plan with pretax dollars, thus reducing your current income and possibly your current-year taxes. You can also reduce current-year taxes by making tax-deductible contributions to an IRA, if you qualify.
  - **If you are self-employed**, you can use a Keogh, SEP (Simplified Employee Pension), or SIMPLE (Savings Incentive Match Plan for Employees) plan to shelter income.
- **Maximize deductions.** Some deductible items, like medical expenses, must meet a specific threshold before deductions can be taken. If you fall short of the minimum, you may be able to time discretionary expenses so that you exceed the threshold one year but not the next.

- **Consider charitable donations.** Depending on your specific tax picture, charitable donations could provide a good source of income tax deductions. One tax-saving strategy is to donate appreciated property. You can take a deduction for the fair market value and avoid capital gains tax on the sale.

- **Review interest expenses.** If you pay interest that is not tax-deductible (e.g., interest on auto loans or credit cards), consider paying off the debt or converting it to debt that allows for deductible interest (e.g., a home-equity loan, where available).

- **Review social security benefits.** If you collect social security, you may benefit from strategies to reduce or defer taxable income. If your non-social security income exceeds certain levels, it triggers taxation of a higher percentage of your social security benefits.

- **Pay attention to recordkeeping.** Keeping complete records may help you save on taxes, especially if it prevents having to locate or recreate information.

- **Review Form 1040 for missed tax opportunities.** Reviewing your 1040 could help you spot opportunities for making investments that provide greater after-tax savings. Pay special attention to the Taxable Interest, Tax-Exempt Income, and Dividend Income sections of the form.

- **Municipal bonds.** Tax-exempt municipal bonds are an excellent tax-advantaged investment, especially if you are in a high income tax bracket, or if you have moved into a higher tax bracket after a promotion or career change. Interest earned on municipal bonds is exempt from federal income taxes and, in most states, from state and local taxes for residents of the issuing states (although income on certain bonds for particular investors may be subject to the Alternative Minimum Tax).

- **Plan capital gains and/or losses.** Determining when to recognize capital gains or losses depends on whether you want to postpone tax liability (by postponing recognition of gains) or recognize capital gains or losses during the current year. If the gains will be subject to a higher rate of tax next year (because of a change in tax bracket), or if you cannot use capital losses to offset capital gains, you may recognize capital gains this year.

- **Review IRA opportunities.** If you want to maximize the timing and amount of IRA distributions as long as possible for your heirs, understanding IRA rules is critical. If you are retiring or changing jobs, consider rolling over the assets in your company's pension and 401(k) plan to an IRA. If you have a traditional IRA, evaluate whether it would be beneficial to convert it to a Roth IRA.

- **Estate planning strategies.** Review and update your estate plan to minimize potential estate and gift taxes.

- **Life insurance.** Life insurance may provide liquidity to pay estate taxes and could be an attractive solution to other liquidity problems, such as family-owned businesses, large real estate holdings, and collectibles. Life insurance proceeds can pass free of income and estate taxes when structured properly.

These are just a few of the most common tax planning strategies. Your financial advisor can work with you and your tax professional to review your current situation and determine which ideas may be beneficial to you.

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