

## TAX NEWS & TIPS

YEAR-END 2002

### Tax Time's Coming!

Year 2003 is almost upon us. You still have a little time to make sure you save as much as possible for 2002. Let's take a look at some changes and a few suggestions for trimming your tax bill. Don't wait until the night before our meeting.

### New For 2002

Here's a quick look at the key laws that differ from past years.

✓ **Tax Rates.** Most of you will pay a bit less than last year. The new 10% rate is in effect for the first few thousand dollars of taxable income. The brackets have been indexed for inflation. Each higher bracket is down by 0.5% – they are now 27%, 30%, 35%, and 38.6%. The rates will be the same for 2003.

Don't expect big savings here. A married couple with *taxable* income of \$100,000 will only save \$454 over their 2001 tax.

✓ **Savings For School.** The new Education Savings Accounts replace the older Education IRA. You may contribute up to \$2,000 for anyone under 18 years of age. There is no tax deduction, but earnings will grow tax-free. Later all your earnings are tax-free if used for education. Most types of formal education qualify. Kindergarten and all higher grades. You can even pay for tutoring and uniforms for private schools.

The law says you are not allowed to contribute if your income is too high (phase-out begins at \$95,000 of income for singles and \$190,000 for couples). **LOOPHOLE:** Since *any* person may contribute, simply give the money to the youngster and let the child open the account!

✓ **College Expenses.** We still have the Education Credits, but there is a

new *deduction* this year. Tuition and fees for classes beyond high school may reduce your taxes. The costs can be for any family member including yourself. Benefits are reduced as your income rises. The *credits* begin to disappear at income of \$40,000 (\$80,000 for a couple). The *deduction* disappears at income of \$65,000 (\$130,000 for a couple).

A tax *credit* is a direct reduction of your tax. A *deduction* reduces your income before your income tax is calculated. Getting the biggest benefit requires a little calculating. I'll take care of that for you.

✓ **Higher IRA Limits.** This year you may contribute as much as \$3,000 to your IRA. If you are age 50 or higher by the end of 2002 your limit is \$500 higher. Contributions are limited to your *earned* income – income from a job or business. If you are also active in a pension plan, you may *contribute*, but might not be able to *deduct* your contribution. For a pension participant, deductions begin to phase out at \$34,000 of income (\$54,000 for couples).

✓ **Increased Depreciation.** The law to help spur American business after the terrorist attacks in 2001 gives faster write-off for equipment. Most of the equipment used in small businesses is depreciated over 6 tax years. The old allowance for the first year was 20% – it is now 44%. This pushes more deductions into the early part of the equipment's life.

This law is retroactive to 2001 for equipment first placed in service on September 11, 2001 or later. The law will run for 3 years to include equipment placed in service by September 10, 2004. I already spoke to some of you about this, and even changed a few 2001 returns to claim the benefit. If you were affected by the change, we can still claim the benefit. We may either

amend your 2001 return or claim the additional amount on your 2002 return.

✓ **Other Changes.** A number of new rules are in effect this year.

**Pensions.** Workers were able to make larger contributions. Most pensions allowed contributions as large as \$11,000. Those who are age 50 or older this year could add up to \$1,000 more. Self-employed persons have higher limits as well.

**Adoption Credit.** The credit can be as large as \$10,000, and more parents can benefit since the income limits were raised to \$150,000.

**Earned Income Credit.** Rules are simpler. We no longer add tax-free allotments to your wages from Form W-2. More Americans will qualify for the credit.

**Savers Credit.** A special credit is given to low-income Americans who contribute to a pension or IRA. Income must be below \$15,000 (it's 430,000 for a couple), but the credit is a full 50% of the contribution.

**And More.** I've spent the year studying the new rules and will help you save as much as possible. But the information is all up to you. It's more important than ever that you keep good records!

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# December 31, 2002 – Deadline to Save Taxes!

Until December 31, 2002 you can take steps to cut your tax bill. After that it's too late.

Most of us want our tax savings as soon as possible. This is smart unless you expect a *very* large increase in income next year. You can get the largest 2002 savings by packing all the deductions you possibly can into the current year. Here are some ideas to help you cut your taxes for 2002.

**Mail That Check!** If you pay a deductible expense by check, the expense is counted when you release the check. Even if the check is not cashed until 2003, you can count the expense in 2002 if the check is released by December 31.

**Credit Cards.** You bought a deductible item with a credit card? The expense counts when you sign the credit slip, not when you pay.

**Medical Expense.** This is only deductible for expenses exceeding 7.5% of your gross income. If you pass the limit, be sure to collect all expenses. Fees to any licensed health care professional count – a doctor, dentist, counselor, chiropractor, etc. Even a weight loss program if prescribed by a physician. Also, the new laser eye surgeries. Prescription drugs qualify, but over-the-counter remedies don't. Nor do self-prescribed cures or food supplements. Look for emergency treatments, ambulance, therapy, medical supplies. If you have medical insurance, you may claim only the amounts you actually pay above your insurance coverage.

**Taxes.** Think about paying one extra installment of your property tax bill. If you will owe state income tax consider paying the balance in December.

**Interest Expense.** You can't pre-pay interest, but IRS generally lets you deduct the January payment if made early, as long as it is due by January 15. Paying several months' interest in advance won't work. Warning: Note carefully the amount reported by your bank – we may need to make the proper adjustment next year.

**Contributions.** Look for both cash and merchandise gifts.

Dig out your canceled checks, and try to recall cash gifts at work or the front door. When you buy cookies or candy from youth groups your contribution is usually about 50% of what you spent – the other 50% is the value of the merchandise.

**Needed Receipts.** For a single gift of \$250 or more, a receipt from the charity is a must. If you are audited later, your canceled check alone WILL NOT be enough!

**Noncash.** Is it time to clean out the garage? Don't wait until January to give away those discards, or you won't see the tax savings for over a year. When you give merchandise instead of cash, you need a list of the items given, plus your reasonable estimate of the value. A snapshot of the items can be most helpful.

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Tip: Check prices at thrift stores for guidelines on household discards. For gifts totaling \$250 or more, a receipt is a must. If your gift reaches \$5,000 or more you'll need an appraisal as well.

**Job Expenses.** Expenses for your job or investments are called "miscellaneous." You may deduct these to the extent they exceed 2% of your gross income. Once you pass this "floor" everything helps. Look for union or professional dues, special books and publications, job search and employment agency fees, job-related education, job supplies and materials, business meals and entertainment expenses, and business gifts. Be sure to include any mileage associated with the costs.

**Investment Expense.** This includes investment books and publications, and account fees on your investments. Investment counseling, tax preparation or planning fees are also deductible.

**Special Transactions.** Be sure to gather all records for any special sales, purchases, or investments. And don't forget the refinance! I'll need to see all the paperwork – loan documents, sale contract, settlement statement, broker statement, whatever.

**Businesses.** Why not buy those supplies you need now. Check your stock of business cards, stationery, and office supplies. Don't wait until January to buy them! Are all your bills paid? Need equipment soon? If you buy in December (and actually *use* the equipment) you get the tax savings right now. Look at employee bonuses, advertising, repairs you need done. If you have a separate credit card for business purchases, you can deduct the finance charges as a business expense. We can still deduct part of your health insurance costs. Find the premiums.

**Landlords.** Are there any last-minute repairs you should make? Is the place in need of a paint job? Are property taxes and insurance paid up? Have you been keeping track of your driving in connection with the property? Don't try to ignore income, though – a rent check you receive in December is counted as income this year even if you don't cash it until January.

**Mileage Deductions.** When you deduct business expenses, you are also entitled to deduct the related driving expense. We have a choice – claim 36.5¢ per mile, or a pro-rata share of all vehicle expenses. Every 274 miles you claim is a \$100 deduction.

**Parking, Tolls, Taxes.** These may be claimed in addition to the amounts above. Interest on a car loan may be claimed by those who are self-employed, but not by employees.

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# January, 2003 – Getting Your Records Together

## January Alert

Many tax records show up in your January mail. Usually IRS gets a copy too. Don't miss any of these!



**W-2s.** Read them carefully.

Contact your employer if there is a problem. If one is missing after January, contact your employer. If you can't locate the employer, you'll need to collect your pay stubs.



**1099s.** There should be a 1099-INT or 1099-DIV for each account which pays interest or dividends. Even tax-exempt interest must be listed on your return.

**Other 1099s.** If you sold real estate, look for 1099-S. For stock sales, it's 1099-B. Pensions show up on 1099-R. There are several others. If you sell or transfer mutual funds and reinvest dividends, I need a *complete* history of your activity. Bring all year-end statements.



**Form 1098.** This is your mortgage interest. Commercial lenders use this form. If you have a private loan, you need your payment book, or a statement from the lender to verify the amount.



**Other Income.** Look for other reports of income. You may see forms for state tax refunds, unemployment income, prizes, gambling wins, or rents you collect. Read each of these carefully.



**Your Records.** Check your own records carefully for both income and deductions. Review your calendar and your check register. Look back over the year in your mind. I'd prefer that you have receipts for all expenses, but if you recall paying a deductible expense it should be claimed.

Start compiling the information right away. Don't wait until the day before you give the information to me. Make careful lists of missing items. Write down any questions you might have for me.

Take a few minutes each week to review your information. Short reviews will help you remember items you might miss. It's your money – protect it!

## Will You Send 1099s?

You may need to send Form 1099 to someone else. There are two cases:

- **Business/Rental.** You must report payments for services.
- **"Nominee" amounts.** If you are named as receiving income, but part of the income belongs to another, you are a nominee.

You must issue form 1099 to the other party by January 31. IRS wants a copy by February 29. There are penalties for not sending them!

**Business/Rental.** If you paid \$600 or more to anyone during 2002 you may need to issue the form. Look at "business" expenses only. Expenses in your personal life are not reported. Nor are payments to a corporation.

If *any* part of the payment was for services, report the *total* amount on Form 1099. Paying for merchandise

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alone doesn't count. Rent you pay to an agent instead of to a landlord are excepted. Look for repairs, painters, consultants, builders and the like.

You need name, address, and Tax I.D. Number for these people. Call them or send Form W-9 to request the information. If someone uses their own name, they should give you their Social Security Number (like 555-55-5555). If they give a business name, you should see an Employer I.D. Number (like 55-555555).

**Nominees.** Limits are lower. If you pay \$10 or more to another, you may be liable for the form. You file the same type of 1099 as you received, but you are filing as a "middle man."  
**Getting the Forms.** I can help, or you can get forms from IRS. If you need my help, please call early! My tax season is hectic and the deadline comes quickly. Get forms from IRS at 1-800-829-3676. Or download them at [www.irs.gov](http://www.irs.gov). You need Form 1099-MISC and form 1096.

## Got it All?

Here's a list of items frequently missed. Check it against your list.

- Refinances.** I need to see the settlement statement. Maybe it's best to bring all the paperwork.
- Child Care Expenses.** I need full name, address, telephone and I.D. number of care providers.
- Estimated Tax Payments.** If you paid estimates, I need dates and amounts for all payments. Look in your check register near April 15, June 15, and September 15 of 2002, and January 15 of 2003. The January 2002 payment was claimed on your last return.
- Sale of Property.** The most important thing is the settlement statement. Bring all the paperwork.
- Student Loans.** Form 1098-E reports your interest. I need this plus information about the nature of the loan.
- College Tuition.** Form 1098-T lists college tuition paid. I need the form and full details on who took the courses. This may help you get valuable tax credits or deductions.
- Sales of Stock.** Brokers send Form 1099-B to show sale price. I need the original purchase price and date. Can you find the "buy" slip?
- Business Records.** Please separate purchases of major equipment from other supplies.
- Contributions.** Review the article on the facing page to be sure you have the proper receipts. We don't attach them to the return, but you must keep them.
- Employer Reimbursements.** If your employer reimburses any of your expenses we need records to insure we claim only the excess.
- Partnership Information.** Schedule K-1 from a partnership will likely be the last piece of tax data you receive. They always seem to be late. Don't worry. We can do everything else, then be ready to go when the K-1 shows up.
- Social Security Benefits.** Be sure you have the actual Form 1099-SSA. We must declare the GROSS amount you were paid, not your net monthly benefit.

## Tips For You

**Mileage Rate Declines.** You can claim a deduction of 36.5¢ for each business mile driven in 2002. For 2003 IRS has announced the rate will decline to 36¢. IRS says the decline is a result of a drop in the price of gasoline.

**IRA Distribution – Age 70½.** New rules began in 2002 for your annual mandatory distribution. It is now a simple matter to calculate your minimum distribution for any year. We simply divide the account balance as of December 31 of the prior year by a factor determined by your age in a simple table. This is true no matter what your age, who your beneficiary is, or what you did in prior years.

**Donating Your Car?** IRS has reviewed several cases of cars contributed to a charity. You must be sure the vehicle is going to the charity, rather than to an agent. If the car's value is \$250 or more, you must retain the receipt (often a "thank you" letter) from the charity. Most charities will list the vehicle's "blue book" value, but IRS says this may need to be modified to reflect the car's condition. If the value is \$5,000 or more, you will need a qualified appraisal. You should pay for this appraisal rather than the charity. The cost of the appraisal is deductible.

**Hybrid Car Deduction.** There is a new \$2,000 deduction allowed for anyone who purchases a "hybrid" car. These cars combine a gasoline engine and an electric motor. To date IRS has certified the Toyota Prius for 2001-2003, the Honda Civic Hybrid for 2003, and the Honda Insight for 2000-2002. The reduction does not require the car to be used for business, and the deduction is allowed whether you itemize your deductions or not.

**Audit Activity Increases.** IRS stepped up their audits in October. The most feared audit, a grueling line-by-line review of the return will be used on only about 2,000 returns selected at random. IRS was barred from doing these special audits a few years back. Now they are using a scaled-down version to gather fresh data on taxpayer activity. IRS will also conduct about 30,000 face-to-face (traditional) audits on 2 or 3 areas of returns. Their key targets:

- Abusive tax shelters
- High-income taxpayers with complex returns who invest via pass-through entities, such as partnerships, S-corporations, and trusts
- High-income nonfilers
- Unreported income of business owners

As always, if you should hear from IRS, don't respond. Call me first. I am familiar with procedures and can help avoid costly errors.

## Happy New Year!

To all of you I wish peace, health, and contentment as 2002 draws to a close. I hope the coming year brings you and your family good health, joy, prosperity and all the finest things in life.

Happy 2003!

## Your Tax Calendar

Dec. 31	A check mailed today counts for 2002. Last chance for deductions! Last chance for IRA withdrawals. State estimated tax paid today is deductible on 2002 Federal return.
Jan. 15	4 <sup>th</sup> quarter estimated tax payments due.
Jan. 31	Employers – Quarterly payroll & FUTA due. W-2's and 1099's due to recipients.
Feb. 28	W-2's and 1099's due to IRS.
April 15	2002 tax returns due. Last day for 2002 IRA contributions.