

Sauppé Tax News

Brought to you by
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Special points of interest:

- Alternative Minimum Tax and you
- IRA's Explained
- New Ohio Rates
- City Taxes
- Charitable Donations
- Basis of Assets

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Alternative Minimum Tax Looms

Will the Alternative Minimum Tax (AMT) affect you this year? It is estimated that an additional 20 million (yes, million!) taxpayers could be subject to the AMT if Congress does not adjust the rules before year end.

As mentioned in last year's newsletter, the AMT was first established to ensure that every taxpayer paid a minimum amount of tax. The AMT is a separate tax system that applies two tax rates to a broader base of income. The taxpayer must pay whichever tax is **higher**—the regular tax or the AMT.

To determine the AMT, the taxpayer must start with his or her taxable income and adjust it for various tax preference items including but not limited to

- Miscellaneous itemized deductions
- State & local taxes, including real estate taxes

- Certain mortgage interest deductions most notably home equity interest
- Tax exempt interest
- Accelerated depreciation
- Personal exemptions
- Stock options

This new income amount (called the Alternative Minimum Taxable Income or AMTI) is then reduced by a fixed dollar amount set by Congress. For 2006, the reduction amount was \$62,550 for a married couple filing jointly, \$31,275 for married couples filing separately, and \$42,500 for single taxpayers. If your AMTI exceeded these exemption amounts, the balance was then taxed at a rate of 26% on the first \$175,000 (\$87,500 for married filing separately) of income, and 28% on amounts over that threshold.

The 2006 threshold amounts were based on temporary fixes passed by Congress and expired at the end of that year. As the law presently stands, the threshold amounts are \$45,000 for married filing jointly, \$22,500 for married filing separately, and \$33,750 for single individuals.

Because Congress has not yet changed the threshold amounts, but is expected to do so before year end, your tax refund could be delayed. The IRS has announced it will take them 8 to 10 weeks to reprogram their computers to reflect the changes made by Congress. Any tax returns filed before the computers are updated may not be processed until later. If the law is not changed until the end of December, it could be the end of February or the beginning of March before the IRS computers can "catch up".

As we have done in the past, we will automatically calculate both taxes for you.

Ohio Rate Reduction

Ohio has once again reduced the state withholding rates. The rate reduction of 4.2% will be reflected in paychecks issued after

1/1/2008. This is just one of the steps in an overall plan to reduce rates by 21%. The rate reduction should be complete by 2009. If you don't see a

change in your state withholding tax in your January paycheck, contact your employer.



IRA's (Traditional and Roth) vs. 401K's

Many people are confused about Question #7 on our annual questionnaire—Did you contribute to an IRA?

This should not be confused with contributions to 401K's, 403B's, 457's or any other plan *sponsored by your employer*. You contribute to these via deductions from your paycheck (the money is never in your possession). This amount is normally reflected on your W-2 so we already know this dollar amount. Because it is deducted from your paycheck *before* your taxes are calculated (pre-tax) it is not a deduction on your tax return.

Question #7 also does *not* refer to rollover contributions where you move money from one IRA to another IRA. You will receive documentation from the withdrawn IRA. This will prompt us to ask you about any rollovers.

IRA's on the other hand represent money you had in your pocket (or checking or savings account, more likely), and then decided to contribute to an IRA. Most of the time this means you

actually wrote a check to some plan sponsor (perhaps a mutual fund company or bank) and told them to invest this money for you. Occasionally you had the money automatically deducted from your checking or savings account and invested (usually on a monthly basis). In either case, because you wrote a check, you usually do not have any documentation to show this contribution. Hence we ask Question #7. Depending on various factors, any amounts contributed to IRA's may impact your current and possibly future year tax returns.

You must indicate the total amount contributed for the current year as well as indicate whether the contribution went into a Traditional IRA or a Roth IRA.

In general, a traditional IRA may give you a deduction on your tax return. (the deduction depends on many factors including your income, filing status, and whether you are covered by a retirement plan at work). If the deduction is allowed, you get a tax benefit in the current year, but will pay tax on all the money when it is withdrawn.

If your deduction is not allowed on your current tax return, you have contributed to a non-deductible IRA. You need to report this amount on the current year tax return on a special form (8606). When you take out money from this IRA, a portion of the proceeds will not be taxed based on the ratio of non-deductible contributions to the investment balance. For example, say you contribute \$4,000 to a non-deductible IRA. It grows to \$10,000. You withdraw \$5,000 of the money at age 60. The non-deductible portion is 40% (\$4,000/\$10,000) of the total, therefore 40%, or \$2,000, of the distribution is non-taxable. Your plan sponsor is NOT required to keep this information in their records. It is your responsibility to do so. Not keeping accurate records can result in large tax bills that could have been avoided.

A Roth IRA, on the other hand, never gives you an immediate tax deduction, though it may entitle you to the retirement saver's credit. The advantage to a Roth IRA is when you withdraw the money—**ALL** of the money withdrawn is tax free if certain requirements are met.

Another important difference between a traditional IRA and a Roth IRA is the fact that you can withdraw your contributions from a Roth IRA after 5 years. For example, say you contribute \$4,000 to a Roth IRA in December, 2007. This Roth grows to \$10,000. In January, 2012 you need some ready cash and withdraw \$3,500 from this account. NONE of the distribution is taxable to you because it is less than your contribution. The interest portion, however, must remain in the account until you reach at least 59 1/2 or you will be subject to a penalty on the withdrawal.

The amount that can be contributed in 2007 is \$4,000 per person. If you are over age 50, you can make an additional contribution of \$1,000 for a total of \$5,000. For 2008, the base amount increases to \$5,000 while persons over age 50 can contribute \$6,000.

Many factors should be considered when deciding whether to contribute to an IRA and what kind. This discussion only covered a small portion of the complex IRA rules. If you would like to discuss this further, please feel free to call our office.

City Taxes Explained

City taxes can be more complicated than federal taxes, depending on various factors. Be aware that everyone has the potential to owe city taxes where they work AND where they live. Whether you are one of those affected depends on many factors. In order for us to accurately

prepare both the federal and city tax returns, it is imperative that you provide us with correct and complete information on the amounts and timing of all your payments to any city. Therefore, please be sure to include copies of all city tax bills you received during 2007 and the first few months of 2008 with the tax

paperwork you send us. Be sure to note on the last bill any payments you made showing the amount AND date paid.

You can also complete the city estimated tax payment section on the questionnaire. We thank you in advance for your help.

**Please include all
city tax bills with
your paperwork.**

Charitable Donation Rules Tightened

As we mentioned in last year's newsletter, the IRS is cracking down on charitable contributions.

ALL monetary donations must now have proper documentation in order to be deducted on your tax return. You must have either a cancelled check, credit card statement, or a receipt from the charity in order to take a deduction on your tax return. Any money "dropped" into a collection box without documentation cannot be included on the tax return. If you regularly put cash into the

Sunday collection plate and don't get proof from the church, you will NOT be able to claim this on your tax return. Be sure to include all required paperwork for your charitable contributions in your tax paperwork.

All non-monetary donations (clothing, household items., etc), must now be in good or better condition for a deduction to be taken. The IRS has not provided guidance on how to prove the condition of an item after it has been donated, but has stated that it will not accept donations of used socks or underwear.

If you wish to claim a deduction for non-monetary donations, regardless of the amount, you must have a detailed list of the items donated, their fair market value, and a receipt from the charity that received the goods. The charity does not usually place the value on the item—that is your responsibility. A possible source for determining valuation can be found at <http://www.goodwill.org/page/guest/about/howweoperate/donations/>

Please do not ask our office to determine a value for your donations—we are not allowed



to do that.

Also be aware that with the

new charitable donation rules, the IRS is more than likely going to be looking closely at all donation deductions, especially non-monetary donations.

By all means claim any charitable donations you make, but just be sure to have all paperwork in order in case of audit. More information on charitable donations can be found in IRS Pub. 561

Asset Sales and Cost Basis

Sales of stocks, mutual fund holdings, or other assets will often trigger a taxable event. Most of these types of sales are reported to you via Forms 1099-B or 1099-S. These tax forms should be included with your 2007 paperwork.

The hard part comes when the cost, or basis, of the item or items sold needs to be determined. At present, your brokerage or mutual fund company does not have to keep track of your cost, though Congress is considering requiring them to report

this in the future. Many companies, as a courtesy, do provide an average cost basis which can often be used for tax purposes.

If your company does not provide this information, it is your responsibility to keep accurate records to calculate the basis.

Inherited assets often obtain a "stepped-up" basis. This is the fair market value of the item on the date of the donor's death. If an estate tax return was prepared, this would provide the starting

cost basis for your sale.

If the item was a gift, the rules are a bit trickier. You must know the donor's adjusted basis, the fair market value on the date the item was given to you, and any gift tax paid on the transaction. All of this information can be obtained from the donor.

The holding period (the time between your purchase and your sale) are very important to determine whether you have a long term gain (with lower tax rates) or a short term gain. One sale may

actually consist of two holding periods (for example, when you reinvest in additional dividends) and requires the sale price and cost to be broken down into both long and short term.

This office does not provide cost basis calculations included in the low price of our tax preparation. If you require assistance in calculating cost basis, we would be happy to do so for an additional fee.

More information is available in IRS Pub 544 and Pub 551.

New Drop Box

To better serve you, we have installed a new, locking drop box (see picture). This box will allow you to leave your sensitive tax information in a secure location with no fear that unauthorized people will have access to it.

We have never had a problem with security in this area, but decided to be proactive.

Of course, if you prefer, you may continue to leave items in the round tube or mail it direct via USPS. Anything left for you to pick up will always be placed in the tube.



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*Specializing in personal
and small business taxes*

TAX TIDBITS

Energy Credits Still Available—Tax credits (which reduce your tax liability dollar for dollar) for energy efficient investment in your main home are still available thru 12/31/2007 so act now. The following items are eligible

- Insulation systems that reduce heat loss
- Exterior windows (excluding skylights)
- Exterior doors
- Metal roofs (meeting applicable energy star requirements).

In addition, the law provides a credit for costs relating to residential energy property expenses. To qualify as residential energy property, the property must meet certification requirements prescribed by the Secretary of the Treasury and must be installed in the taxpayer's main home in the United States.

The following items are eligible:

- \$50 each for advanced main circulating fan
- \$150 for each qualified natural gas, propane, or oil furnace or hot water boiler
- \$300 for each item of qualified energy efficient property

The maximum credit for all taxable years is \$500 – no more than \$200 of the credit can be attributable to expenses for windows.

Tuition and Fees Deduction –As of this writing, the tuition and fees deduction allowed against income is only available thru 12/31/2007. So if you have a student in college, and can't take the Education credits, you may want to pay the January 2008 tuition bill in December.

IRA Funds Direct to Charity -Taxpayers age 70 1/2 or older can now direct their IRA sponsor to send their IRA distribution directly to a recognized 501 c 3 organization. The distribution will be tax free, and the taxpayer may not claim a charitable donation for the amount. Having the distribution sent to the charity may benefit the taxpayer indirectly because it will reduce adjusted gross income. A reduction in adjusted gross income may allow the taxpayer to claim more of his medical and/or miscellaneous itemized deductions, and may decrease the tax on social security benefits. This provision is scheduled to expire at the end of 2007, but it is expected Congress will extend it

Hybrid Car Credit –Tax credits are still available for some hybrid car purchases. The car must be bought new (used hybrids do not qualify) and the credit is based on the model purchased. Check out www.irs.gov for a complete list of dollars available.

Kiddie Tax Expanded Again! -Last year the "Kiddie Tax" was expanded to cover children up to age 18 (prior law was age 14) with unearned income over \$1,700. These children had to pay tax at their parent's tax rate. Effective 1/1/2008, the tax has been expanded to include children under age 19 or full-time students under age 24 if their earned income is less than half their support.

Take your Required Minimum Distribution -If you are age 70 1/2 or older, or a beneficiary of an IRA you inherited from someone other than your spouse, be sure to take your required minimum distribution (RMD) from your traditional IRA before 12/31/07. Failure to do so may result in a penalty of 50% of the amount that should have been withdrawn. If you need help determining your RMD, contact your plan sponsor. Be sure to give them sufficient time to complete the withdrawal before the end of the year.

IRS E-Mail Scam -Have you received an e-mail from the IRS? Have you responded to this e-mail? Hopefully the answer to both questions is NO. These e-mails are more than likely scams. The IRS does NOT communicate with taxpayers via e-mail and they certainly do not ask for sensitive tax information that way. Please do not respond to any "IRS" e-mails. Instead forward the e-mail to the IRS at phishing@irs.gov