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Financial Briefs

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Tax Planning Through Your Life

Tax planning is perhaps one of the most misunderstood aspects of financial planning. Most people only think seriously about taxes when they file their annual state and federal tax returns. While there are things you can do to reduce your taxes when filing, like making sure you're taking advantage of all possible tax credits and deductions, by that point, it's really too late to do any serious tax planning.

True tax planning involves making strategic decisions throughout the year that will help you minimize taxes both in the coming April and perhaps many years in the future. And, contrary to many people's assumptions, tax planning isn't something that's just for the ultrawealthy. If you earn money and file taxes, you can probably benefit from some level of tax planning. Today, we'll walk you through some key tax planning issues you may face throughout your life.

In Your 20s

You're just getting started building your life and career, and there's a good chance your taxes are a bit more complicated than they were when you were a high school or college student. Consider sitting down with an accountant to make sure you understand where things stand with your finances and that you are doing all you can to reduce the taxes you owe. Specific tax planning steps you may want to take in your 20s include:

- Contribute money to a tax-deferred retirement account, like

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Watch Out for These Tax Mistakes

Many taxpayers avoid the entire income tax process until the last minute and then rush through it as quickly as possible. But if your objective is to pay the least amount of income tax, you should spend some time planning for that result. Some common mistakes to avoid include:

- **Maintaining poor tax records** — Don't rely on memory to keep track of deductions. During the year, accumulate any tax receipts or notes concerning deductions in one place.
- **Withholding too much in taxes** — When you receive a refund, you've given the government an interest-free loan for the year. Consider reducing your withholding and investing the additional sums.
- **Ignoring the alternative minimum tax (AMT)** — A variety of items must be added to your taxable income when calculating the AMT, including personal exemption deductions; standard deductions; state, local, and property tax deductions; miscellaneous itemized deductions; medical expenses under a certain percentage of your adjusted gross income (AGI); municipal interest from certain private-activity bonds; certain business-related items; and the difference between the market price and exercise price of incentive stock options. If you are subject to the AMT, conventional tax planning does not apply, and you need to consider your tax situation carefully.
- **Not contributing to your company's 401(k) plan** — Not only will the plan help you save for retirement, but it can help you reduce your current year taxable income. For instance, in 2015, you can contribute a maximum of $18,000, plus individuals over age 50 can contribute an additional $6,000 catch-up contribution, if permitted by the plan. If you are in the 35% tax bracket,

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Tax Planning

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a 401(k) plan or IRA.

- Keep track of your student loan payments, if you have them. If your income falls below certain limits, you may be able to deduct the interest you pay on that debt, even if you don't itemize.
- Save receipts and other records if you move for a new job, since expenses related to a move you make for work can be deducted even if you don't itemize.
- Check your withholding. If you're getting a big refund at tax time, you may need to tweak how much is being withheld from your paycheck, so that you're not giving an interest-free loan to the government.

Finally, make sure you're keeping all your key financial documents organized. Find a secure place to store everything, and get essential documents from your parents if they still have them, like your Social Security card, birth certificate, and information about any accounts they may have opened for you when you were a minor.

In Your 30s

Your finances are probably getting more complicated as you increase your savings and complete major financial goals like buying a house. These tips will help you keep things on track:

- Getting married or having children? Set up a meeting with a tax advisor or financial advisor (or both together) to make sure you're making tax-smart financial decisions, like itemizing or not itemizing your return. An advisor can also talk to you about setting up a 529 plan to help pay for your children's future college educations.
- The government has plenty of credits and deductions for people with children, like the child tax credit, the child and dependent care credit, and the adoption credit. Know what you do — and don't — qualify for.
- Take advantage of flexible spending plans and reimbursement accounts. Between you, your spouse, and your children, you may be spending a lot of money on co-pays, prescription drugs, dental appointments, and more. Save a bit of cash by using money in a tax-free flexible spending account for these costs.

In Your 40s

You're hitting your financial stride. Don't let any bumps in the road derail your financial plans:

- Incomes tend to hit their peak when people hit their 40s. That's good news, but it also means that you may find yourself in a higher tax bracket. If that happens, look for ways to reduce your taxable income, like maximizing deductible retirement contributions.
- You may be making more money than in past years, which could mean that you're ready to upgrade your charitable giving. Make sure you're keeping track of any gifts you make to eligible charities, whether they are in cash, stock, or in-kind gifts, since you'll need that documentation if you plan to deduct them on your tax return.
- If your children are headed off to college, don't neglect tax credits for education, like the lifetime learning credit and the American opportunity tax credit.
- Some parents may draw money from taxable investment accounts to pay for college or other expenses. If you're tapping that cash, be aware of the tax implications of selling appreciated securities. It may be well worth it to meet with an advisor before you make any big moves.

In Your 50s

As you hit the mid-century mark, keep doing what you can to reduce the taxes you owe and save as much as you can for retirement.

- Don't forget about catch-up contributions to IRAs and 401(k) plans. In 2015, you can contribute an extra \$6,000 to a 401(k) plan and an extra \$1,000 to an IRA once you hit age 50.
- Start thinking about health care expenses in retirement, if you haven't already. Putting some money into a tax-free health savings account is a way to reduce your taxable income today and have a tax-free fund to draw on for health expenses later in life.
- Selling the family home? Don't neglect to consider the potential tax implications.
- If you've earned stock options or other perks through your employer, make sure you understand the tax implications of a cash-out.

In Your 60s

Retirement is on the horizon. The tax planning decisions you make in this decade will be crucial to your overall retirement success.

- Understand how your Social Security benefits will be taxed. Up to 85% of your total benefit may be taxed, depending on how much other income you have.
- Check your options before retiring. The choices you make regarding distributions from your pension plans and IRAs will have a significant impact on your tax situation after retirement. Make sure you review all your options before deciding how to withdraw those funds.

Please call if you would like to discuss your tax situation in more detail.

Tax Mistakes

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contributing $18,000 will reduce your current year tax bill by $6,300.

- **Failing to bunch deductions** — It only makes sense to itemize deductions if your total deductions exceed the standard deduction amount, which for 2015 is $12,600 for married taxpayers filing jointly and $6,300 for single taxpayers. In addition, some deductions must exceed certain thresholds. Many expenditures can be bunched in one year or another to take advantage of these limits. For instance, if your total itemized deductions are slightly below the limit, you might consider prepaying property taxes or estimated state taxes.
- **Using the wrong basis for investments** — When calculating gains and losses on investment sales, your basis includes your original cost plus any reinvested dividends and capital gains. If you are only selling a portion of the investment, specifically identifying which portion you are selling can affect the amount of gain or loss.
- **Overlooking charitable contributions** — In addition to cash and property donations, you can deduct mileage, parking fees, postage, and long-distance phone calls made while performing charitable work.
- **Not considering filing separate returns** — In some situations, it may be more beneficial for a married couple to file separately. Once you file jointly, your return can't be amended to file separately, so calculate your tax both ways before filing.
- **Forgetting deductions carried over from prior years** — Don't forget about items you carried forward because you exceeded annual limits, such as capital and/or passive losses, charitable contributions, and alternative minimum tax credits.

Why Tax Planning Matters

Tax planning is an essential and yet often overlooked aspect of financial planning. By engaging in tax planning, you can have more control over your financial future. Here's why.

Tax Planning Matters for Your Income Today

At this level, tax planning involves shielding as much of your income from taxes as reasonably possible while always keeping your overall financial goals in mind. For example, you might contribute money tax free to a flexible spending account that you can use for out-of-pocket medical expenses or deduct the expenses you incurred from searching for or moving for a job. Homeowners will make a point to deduct the mortgage interest deduction, while people with high medical expenses can save money by deducting those costs.

Because taxes can be complicated, many people choose to work in partnership with an accountant to make sure that they are taking advantage of all credits, deductions, and other tax minimization strategies.

Tax Planning Matters for Your Long-Term Financial Goals

Being strategic about taxes can also make it easier for you to achieve your long-term financial goals. For example, if you want to set aside money to help your children pay for college, a tax-advantaged 529 account could be a way to do so. The money you put in this type of account grows tax free and can be withdrawn tax free to pay for educational expenses. Cash placed in a health savings account can protect you from the sting of high medical bills in the future.

Consistent tax planning can also free up additional income you can use to reach your long-term financial goals. Money saved on taxes can later be allocated to savings for a down payment on a house, used to pay down student loan debt, save for other major purchases, or fund your retirement.

Tax Planning Matters for Your Retirement

Tax planning and retirement are closely linked. Money contributed to a traditional IRA or 401(k) plan can be deducted from your taxes in the year you make the contribution. But that's just the tip of the iceberg when it comes to tax planning for retirement. While there are many advantages to avoiding taxes today, you may also want to put some money into a Roth IRA. While you won't get a current-year tax deduction for money contributed to these accounts, you will get tax-free income in retirement. Many retirees appreciate the option of having both taxable and tax-free income streams in retirement. Some people even set aside some money for retirement in taxable investment accounts, since this income will be taxed at lower capital gains rates.

Tax Planning Matters for Your Heirs

Many people hope to leave some of their wealth to their children, other relatives, and favorite charities. If that's part of your long-term financial plan, you'd be wise to consider taxes as you draw up your plan for your estate. For example, if you want to leave money to your children, you might want to put money in a Roth IRA, since your children will be able to draw tax-free income from the account. Or, you might start transferring some money to your heirs while you are still alive, taking advantage of the annual gift-tax exclusion. Other tax planning strategies you might look into include using life insurance, charitable remainder trusts, charitable lead trusts, or donor-advised funds.

Please call to discuss the pros and cons of these different strategies and whether they make sense for your situation.

News and Announcements

From the Alexander Household

I'm grateful to have arrived at a point in my life that I experience many facets of abundance. Some people think of abundance in terms of money, but I believe that it refers to much more than that. I enjoy abundance in relationships with family, friends, and clients: all of these deeply enrich my life. I am blessed with a healthy body. I enjoy meaningful work and have the opportunity to help people utilize their resources to achieve their dreams.

To evolve from a mindset of scarcity, you have to realize when you have enough. Unless you approach this thoughtfully, "enough" monetarily tends to be a moving target. For most people, if you ask how much they need to be financially secure, it will be a number they have not yet attained, no matter how much they have. Looking back, I now realize I could have experienced abundance much earlier in my life, but I didn't know how much, for me, was enough.

That being said, I had always thought of abundance as what I possess or am experiencing. Then I read this quote by Brother David Steindl-Rice. He said, "We measure abundance not by what flows in, but what flows out." As Barbara Stanny says in *Sacred Success*, when we focus on what we can contribute, "We not only help (and inspire) others, but imbue our own life with meaning and purpose."

Carol Ringrose Alexander, CFP®, AIF®, CDFA™

From the Flinton Household

"To be what we are, and to become what we are capable of becoming, is the only end of life."

~ Robert Louis Stevenson

My wife and I are mindful of steering clear of labels for our kids. I fervently believe that your belief about someone or something can manifest into reality. Samantha is our firstborn and exhibits all of the qualities and attributes one would normally associate with a firstborn.

Her younger sister, Emerson, is something else. Emerson is a pistol. She has never asked a question she wasn't willing to repeat a few dozen times. She has only one volume — loud. She has only one speed — fast. I'm not sure that her behavior is in line with the youngest sibling, as I am the youngest of four, and I am fairly certain I never behaved this way (Mom and Dad, please stop laughing).

Recently, I asked her to clean up her toys, to which she responded with a resounding, "I don't want to." She clearly thinks she is in charge at times, so I crouched down and looked her in the eyes. "Emerson, you are not in charge of this family. Look at me. Look at me. Who's in charge here?" With a slight pause, giving her answer careful consideration, she said "Jesus." Well played, kid. "After Jesus, who's in charge in this family?" Without hesitation she smiled and said, "Mom!" Here's to keeping the correct hierarchy in order.

Make it a great month,

Andrew Flinton, CFP®

From the Rudy Household

My local Rotary group provides a lot of local community service, but we also extend our club's service internationally. Two years ago, I was part of an eight-person team to complete a water well for a Honduran village and orphanage. During this trip, we also identified future projects that included desks for the village school and long-term medical support for the village.

I just returned from my second trip to Honduras where we delivered 40 new classroom desks to the village's school. Many of the desks we replaced were hazardous and barely usable. The surfaces were very splintered and many weren't even attached. After the new desks were installed, all 40 of the children hugged or shook hands with all seven members of our Rotary team and were greatly touched.

The second part of the trip was to identify requirements and initial plans for a medical clinic for the village and orphanage. After meetings with the villagers, it was determined that their top priorities were dental, optometry, pregnancy support, and basic medical needs. Our team had the opportunity to meet with local Rotary groups to help with clinic design and local permitting.

Our initial clinic design has been submitted to architects for final design. Over the next 18 months, our club will continue to raise the necessary funds and return to Honduras to assist with the construction. I look forward to the clinic dedication, and I am confident it will be as rewarding as delivering the 40 school desks.

Best wishes,

Chad Rudy, CFP®