MONEY MATTERS

SMART TAX MOVES

By Jacob Ansel

LAST YEAR WAS A GOOD ONE FOR taxpayers who own stock and mutual funds outside of their retirement accounts. But come April you might have to share some of that bounty with the IRS. Smart tax planning now can help reduce your taxes. Here are a few suggestions.

Set up a 529 plan for children or grandchildren which is tax deductible in most states. If you live in New York, for example, where the tax rate is almost 11%, you can deduct up to $10,000 per child per year, thus saving $1,000.

How often do you look at your investment account? Most folks review it every month when the statement comes in, but year-end tax planning requires a thorough review. Harvesting tax losses against gains is a smart tax move. Some of our clients have their investment advisors call us to review losses in their portfolio to determine how we can help offset gains.

Review your paycheck to make sure you're withholding the right amount of taxes. It's not smart to have more withheld and receive a refund at the end of the year which amounts to an interest free loan to the government. Use extra money from each paycheck to invest in stocks or bonds on a consistent basis. Owing too much isn't a smart move either. The best scenario is to break even at filing time.

Max out your 401(k) at the start of the year instead of doing what most folks do, waiting until the end of the year to fund it. The idea behind a 401(k) plan is that you get to deduct contributions against ordinary income which grows tax deferred. If you invest at the start of the year, the earnings will be greater than if funded at year's end.

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Tax day is just around the corner and to ensure you pay the IRS the least possible amount you need to make some tax moves before the tax year ends. Some moves will take a little planning; others are easy to accomplish.

Use an HSA or FSA. An HSA is a health savings account which you can fund with pretax contributions. The account can be used for qualified medical expenses incurred that plans don't recognize. An FSA is a flexible spending account also known as a reimbursement account for medical expenses. These accounts are sponsored plans by employers. There are two types of FSA plans: one for medical expenses and one for dependent care expenses. Both are good tools in reducing a tax bill.

If you think your tax rate is going to rise, converting to a Roth IRA makes sense. Withdrawals from traditional IRAs are taxed at your ordinary income tax rate, while all withdrawals from Roths are tax-free and penalty-free as long as you're at least 59½ and the converted account has been open at least five years.

You can give up to $14,000 to as many individuals as you like before Dec. 31 without filing a gift-tax return. If you're married, you and your spouse can give up to $28,000 per recipient.

If your adult children or parents are in the 10% or 15% tax bracket, they qualify for the 0% tax rate on long-term capital gains. When they sell securities, profit that would have been taxed at a rate as high as 23.8% on your return will be tax-free on theirs. Children under 18 and full-time students under age 24 are subject to the kiddie tax. Investment income that exceeds $2,000 will be taxed at the parent's higher rate. To qualify for the special rate for capital gains, the securities must have been held for at least 12 months. For securities given as gifts, though, the holding period includes the time you owned them.

Captive insurance companies are becoming more popular with the onset of higher tax rates. A captive insurance company is created by the parent organization to underwrite the insurance needs of its operating affiliates. A manufacturer may create and form a captive insurance company to provide insurance to its own manufacturing company against environmental issues. The goal of the captive is to reduce insurance costs by having the captive retain the underwriting profits that would be lost from a standard carrier. It's basically self-insurance. The balance left comes back to the organization in the form of capital gains; a powerful and smart tax move if it works for you.

There are plenty of ways to reduce a tax burden. Make sure you speak to your tax professional to make sure your money works for you, not against you. ❑