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2009 Year-End Tax Planning Tips

The window of opportunity for many tax-saving moves closes on December 31. Set aside time to evaluate your tax situation now, while there's still time to affect your bottom line for the 2009 tax year.

The basics: timing is everything

Year-end tax planning is as much about the 2010 tax year as it is about the 2009 tax year. There's a real opportunity for tax savings when you can predict that your income tax rate will be lower in one year than in the other. If that's the case, some simple year-end moves can pay off in a big way.

If you think your tax bracket next year will be the same or lower than your tax bracket this year, look for opportunities to defer income to 2010. For example, you may be able to defer a year-end bonus, or delay the collection of business debts, rents, and payments for services. Similarly, you may be able to accelerate deductions into 2009 by paying some deductible expenses such as medical expenses, interest, and state and local taxes before year-end.

Delay income	Accelerate deductions
• Delay collection of business debts, rents, and payments for services (if you use the cash method of accounting) • Defer compensation/year-end bonus if possible • Defer sale of capital gain property or take installment payments instead of lump-sum payment • Postpone retirement plan distributions that aren't required	• Make next year's charitable contribution this year instead • Pay medical expenses that are due in January before the end of the year • Prepay deductible interest and property tax • Make first quarter installment payment of state estimated tax in December • Accelerate alimony payments

AMT: what you don't know could hurt you

If you're subject to the alternative minimum tax (AMT), traditional year-end maneuvers, like deferring income and accelerating deductions, can actually hurt you. The AMT--essentially a separate federal income tax system with its own rates and rules--effectively disallows a number of itemized deductions, making it a significant consideration when it comes to year-end moves. For example, if you're subject to the AMT in 2009, prepaying 2010 state and local taxes won't help your 2009 tax situation, but could hurt your 2010 bottom line.

Legislation earlier this year included the latest in a long series of temporary "fixes" for AMT, but this patch (which includes increased AMT exemption amounts) expires at the end of the year. While it's likely that additional legislation will be passed to address 2010, right now AMT exemption amounts for 2010 are scheduled to return to pre-2001 levels.

AMT triggers

You're more likely to be subject to the AMT if you claim a large number of personal exemptions, deductible medical expenses, state and local taxes, and miscellaneous itemized deductions. Other common triggers include home equity loan interest when proceeds aren't used to buy, build, or improve your home, and the exercise of incentive stock options.

AMT exemption amounts	2009	2010
Married filing jointly	$70,950	$45,000
Single or head of household	$46,700	$33,750
Married filing separately	$35,475	$22,500

IRA and retirement plan contributions

Traditional IRAs (assuming that you qualify to make deductible contributions) and employer-sponsored retirement plans such as 401(k) plans allow you to contribute funds pretax, reducing your 2009 income. Contributions you make to a Roth IRA (assuming that you meet the income requirements) or a Roth 401(k) aren't deductible, so there's no tax benefit for 2009, but qualified Roth distributions are completely free from federal income tax--making these retirement savings vehicles very appealing.

For 2009, the maximum amount that you can contribute to a 401(k) plan is $16,500, and you can contribute up to $5,000 to an IRA. If you're age 50 or older, you can contribute up to $22,000 to a 401(k) and up to $6,000 to an IRA. The window to make 2009 contributions to your 401(k) closes at the end of

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the year, while you can generally make 2009 contributions to your IRA until April 15, 2010.

RMDs suspended for 2009

When you reach age 70½, you're generally required to start taking required minimum distributions (RMDs) from any traditional IRAs or employer-sponsored retirement plans you own. RMD requirements, however, were suspended for 2009. This presents an opportunity for those normally required to take RMDs to postpone the receipt of taxable income. If you already took an RMD for 2009, you may be able to roll over the RMD to the same (or to a different) IRA or eligible retirement plan--you generally have until the later of 60 days from the time you took the distribution or November 30, 2009.

Roth IRA 2010 conversions

It's worth looking ahead to 2010, when special rules will apply to Roth conversions. Current limitations based on income and filing status that prevent many individuals from converting a traditional IRA to a Roth IRA will be eliminated in 2010. Additionally, if you convert in 2010, half the income that results from the conversion can be reported on your 2011 federal income tax return and half on your 2012 return (you can choose to report the full conversion tax on your 2010 return, if you want).

This might influence the decisions you make now; for example, if you're currently working but aren't eligible to contribute to a Roth IRA, you might consider making a contribution to a traditional IRA for 2009 in anticipation of making a 2010 Roth conversion. Or, if you plan on making a 2010 Roth conversion and opting to pay the conversion tax on your 2010 return, you might consider trying to defer deductions until next year to offset that conversion tax.

Bonus depreciation and expensing

If you're self-employed or a small-business owner, you'll want to take note of the special depreciation rules that are scheduled to expire at the end of the year. Depreciation rules for 2009 allow an additional 50% first-year depreciation deduction for qualifying property purchased for use in your business on or before December 31.

In lieu of depreciation, Section 179 deduction rules allow for the deduction, or "expensing," of up to $250,000 of the cost of qualifying property placed in service during 2009. Currently, that limit is scheduled to drop to $125,000 (adjusted for inflation) in 2010.

Also worth noting

- A tax credit of up to $8,000 is available in 2009 for qualified first-time homebuyers (only homes purchased before December 1, 2009, qualify).
- The first $2,400 of unemployment compensation received in 2009 is excluded from income for federal income tax purposes.
- If you itemize deductions, 2009 is the last year you'll have the option to deduct state and local sales tax instead of state and local income tax.
- Individuals who do not itemize deductions are able to claim an additional standard deduction of up to $500 ($1,000 for married couples filing jointly) for real estate property taxes paid for 2009, the last year this deduction will be available.
- The temporary deduction for sales and excise tax relating to the purchase of a qualified new automobile, light truck, or motorcycle applies to vehicles purchased through December 31, 2009.
- The above-the-line (maximum $4,000) deduction for qualified tuition and related expenses expires at the end of 2009, as does the above-the-line deduction for up to $250 in out-of-pocket classroom expenses paid by educational professionals.
- Individuals age 70½ or older have only until December 31, 2009, to make charitable contributions of up to $100,000 directly from an IRA to a qualified charity, without including the distribution in income.

Talk to a professional

When it comes to year-end planning, there's always a lot to think about. A financial professional can help you evaluate your situation and determine if any year-end moves make sense for you.

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