Now is the time to plan for tax season

By Rick Rodgers

Unlike last year, tax planning for 2013 is not hampered by uncertainties over a looming fiscal cliff. Unfortunately, there is always some uncertainty and a few expiring provisions to warrant special attention by taxpayers.

Managing income taxes at year-end involves techniques designed to address three issues:

• Accelerating or deferring income: If a taxpayer expects to be in the same or a lower tax bracket next year, it’s best to defer as much income as possible until after the year-end.

• Accelerating or deferring deductions: If a taxpayer’s overall tax rate is the same in both years, accelerating deductions achieves tax savings this year rather than waiting for those tax savings to materialize next year.

• Take advantage of tax provisions scheduled to expire at the end of 2013. There are several temporary tax provisions which can only be used this year.

Tax planning begins by projecting income and deductions for the year to determine your tax bracket and income thresholds that trigger higher and/or additional taxes, or limits the effectiveness of deductions. One of the impacts of the American Taxpayer Relief Act of 2012 is the reintroduction of the Pease limitation, which can greatly limit itemized deductions. Once a taxpayer knows what his or her income taxes will look like, it’s time to evaluate which techniques will help the most.

Strategies to accelerate or defer income:

• Adjust your elective deferral plans at work: Taxpayers who participate in 401(k), 403(b), most 457 plans, or in the Thrift Savings Plan can defer up to $17,500 this year. Taxpayers age 50 and older can defer up to $23,000.

• Harvest capital gains or losses: Long-term capital gains are taxed at zero percent for taxpayers in the 15 percent bracket. Capital losses can be used to offset capital gains and reduce other income up to $3,000.

• Use the IRA. Taxpayers age 59½ and older can accelerate IRA distributions in 2013. Contributions may be deductible depending on your income level and whether you're covered by a retirement plan through work. Taxpayers under age 59½ can convert traditional IRAs to Roth IRAs to accelerate income.

• Health-care assistance: People with health savings accounts — available with some high-deductible health insurance policies — can save up to $3,250 tax-deferred for an individual and $6,450 for a family. Those who are 55 and older can save an additional $1,000. Flex spending contribution limits are capped at $2,500 this year.

Strategies to accelerate or defer deductions:

• Medical expenses: The Affordable Care Act raises the income threshold this year to 10 percent of adjusted gross income for taxpayers under age 65. The threshold remains at 7.5 percent for those 65 and older. Taxpayers may need to prepare or defer medical bills to lump expenses in a single year to get the deduction.

• Gifts to charities: Use a donor advised fund (DAF) to maximize the tax savings from charitable giving. A DAF makes gifting appreciated securities easier. The DAF can be funded in tax years when the deduction will have the most impact. Distribution to charities can be made at any time without tax consideration.

• Qualified Charitable Distribution: This year only, taxpayers age 70½ or older can choose to direct up to $100,000 of their IRA-required minimum distribution to charity. By doing so, the distribution does not show up as taxable income, which can lower taxation of Social Security benefits and help reduce other threshold levels to further minimize taxes.

ATRA12 extended but did not make permanent several tax incentives for individuals.Taxpayers should consider whether they can benefit from these incentives this year and plan accordingly. The following provisions are set to expire on Dec. 31 unless extended again:

• State and local sales taxes deduction. Taxpayer can choose between deducting state and local income taxes or the sales taxes they've paid through the year.

• Deduction for teacher expenses. Eligible educators can deduct up to $250 of any unreimbursed expenses.

• Deduction of mortgage insurance premiums. Payments of Private Mortgage Insurance premiums can be treated as deductible home mortgage interest in 2013.

• Discharge of principal residence indebtedness. This can be excluded from gross income this year.

• Qualified Charitable Distribution. Taxpayers can make tax-free charitable donations from their required IRA distributions.

2013 is certainly an exciting year for tax planning. Start now in order to minimize your tax bill in April.

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