TaxTips

Keeping you informed...

Winter 2004/2005

Where is My Refund?

How long can you expect to wait?

Are you expecting a refund when you file your 2004 tax return? If you file a paper tax return, your refund should be issued in about six to eight weeks from the date the IRS receives your return. If you file your return electronically, your refund should be issued in about half the time.

You can have a refund check mailed to you, or you may be able to have your refund electronically deposited directly into your bank account. Direct deposit into a bank account is faster and more secure because there is no check to get lost. A word of caution – some financial institutions do not allow a joint refund to be deposited into an individual account. Check with your bank or other financial institution to make sure they will accept your direct deposit.

Environmentally Conscious Auto Buyers Get a Tax Break

Certain vehicles qualify for a deduction to income

If you purchased a gasoline-electric hybrid auto in 2004, you can write off $2,000 of the vehicle's cost. The IRS has deemed those vehicles eligible for the clean-burning-fuel tax deduction. The deduction is claimed directly on Form 1040. There is no form to fill out or income thresholds to meet. Simply enter the amount on line 33 of your Form 1040 and write "Clean Fuel" on the adjacent dotted line.

This deduction is not new. It's been offered for the last few years to owners of autos that operate on natural gas, liquefied natural gas, liquefied petroleum gas, hydrogen, or any other fuel that's at least 85 percent alcohol. The IRS's certification of hybrid vehicles has simplified and expanded the tax break. However, there are some requirements that must be met. First, your auto must be one of the following vehicles:

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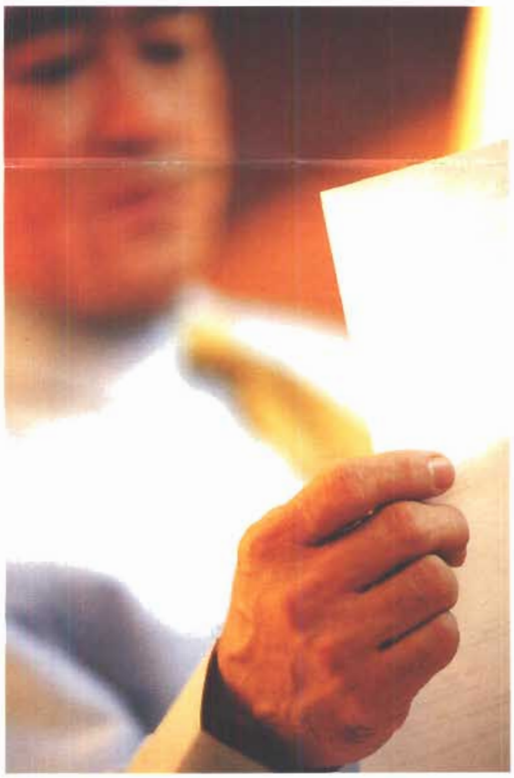
- Toyota Prius model years 2001 through 2004;
- Honda Insight model years 2000 through 2004; or
- Honda Civic Hybrid model years 2003 and 2004.

Second, it's a one-time deduction allowed only in the year you bought the car. And third, only the car's original purchaser can claim the tax break. If you bought the car used, you do not qualify for the tax deduction.

Purchasers of fully electric autos may qualify for an even larger tax break. If your new auto runs primarily on an electric motor powered by rechargeable batteries, fuel cells, or other portable electric-current sources, you may be eligible to claim a tax credit of ten percent of the auto's cost, up to a maximum of $4,000. Tax credits reduce your tax liability dollar for dollar, where a tax deduction reduces your overall taxable income.



Have You Changed Jobs?

Double check your FICA withholding

It is not uncommon to hold several different jobs throughout the year. If this applies to you, double check your withholding statements to make sure you have not unintentionally overpaid the Federal Insurance Contributions Act (FICA) tax. FICA tax is withheld at a rate of 6.2 percent from your paycheck by your employer and matched by you. The tax is credited to your account at the Social Security Administration and used to determine your social security benefits when you retire.

For 2004, the maximum wage subject to FICA withholding is $87,900. If you earned this amount with one employer last year, you put in $5,449.80, which was then matched by your employer. Once your pay went over the limit, FICA withholding stopped.

If you changed jobs and your combined income from all employers went over the limit, you probably overpaid your FICA taxes. This is because each employer withheld the tax, unaware of how much previous employers had already collected.

You are entitled to claim the excess withholding on your tax return. Include the amount that exceeds $5,449.80 on your tax return in the section where you report your other withholding and estimated tax payments.

Roth IRA or Traditional IRA

Which is better for you?

Roth IRA versus a traditional IRA. In almost all cases the Roth IRA is a better deal than the traditional IRA. Contributions to Roth IRAs are not deductible on your tax return, but there won't be any taxes on the money you take out of your account after age 59½.

A Roth IRA is advantageous if your tax bracket will be the same or higher when you retire than what it is currently or if you don't want to take mandatory distributions from your account when you reach age 70½. With a Roth IRA, you can keep your money in a nest egg for future use past age 70½ or pass it on to your beneficiaries as an income-tax-free inheritance. A Roth IRA is absolutely better than a traditional IRA if your contribution to a traditional IRA will be nondeductible.

A traditional IRA may be a good choice if your contribution is deductible and you believe your tax bracket will be lower than it currently is after you retire. However, the younger you are, the more advantageous the Roth IRA is.

QUIK TIPS

1 The child tax credit for 2004 is $1,000. Each child under the age of 17 whom you can claim as a dependent will save you $1,000 in tax dollars.

2 In 2004, the maximum adoption credit increased to $10,390. The exclusion from income of benefits under an employer's adoption assistance program also increased to $10,390. A taxpayer who adopts a special needs child is considered to have qualified adoption expenses, regardless of whether or not he or she has $10,390 of qualified adoption expenses.

3 Watch out for missed alimony deductions. If you must make all the mortgage payments on a jointly owned home, you may be able to deduct one-half of the total payments as alimony and the other half on Schedule A as an itemized deduction. The same is true for real estate taxes and insurance paid on the home. If you are legally required to pay any medical expenses for your ex-spouse, deduct the expenses as alimony instead of on Schedule A as an itemized deduction.

4 The holding period for inherited property is always considered to be long-term regardless of the actual holding period. Thus, all sales of inherited capital gain property are taxed at the applicable long-term capital gain tax rate. The maximum long-term capital gain tax rate is 15% in 2004.

5 For 2004, if you are covered by a retirement plan at work, your deduction for contributions to a traditional IRA will be reduced if your modified adjusted gross income (MAGI) is: 1) More than $65,000 but less than $75,000 for a married couple filing a joint return or a qualifying widow(er); 2) More than $45,000 but less than $55,000 for a single individual or head of household; or 3) Less than $10,000 for a married individual filing a separate return. For all filing statuses other than married filing separately, the upper and lower limits of the phaseout range increase by $5,000.

6 Don't throw away your mutual fund's annual statements. If the mutual fund reinvests the dividends, the records are needed to calculate the cost basis in the mutual fund shares. Reinvested dividends increase your basis and reduce the gain on the sale. If you do not have accurate records, the IRS does not allow the reinvested dividends to be added to basis.

7 Teachers of students in grades K through 12 are allowed an above-the-line deduction of $250 for amounts they spend on classroom supplies.

8 If you win a prize in a lucky number drawing, television or radio quiz program, beauty contest, or other event, you must include the fair market value of the prize in your income.

9 Qualified scholarships and fellowships are treated as tax-free amounts if all of the following conditions are met: 1) The taxpayer is a candidate for a degree at an educational institution; 2) The amounts received as a scholarship or fellowship are used for tuition and fees required for enrollment or attendance at the educational institution, or for books, supplies, and equipment required for courses of instruction; and 3) The amounts received are not a payment for services.

10 Beginning in 2004, the amount of qualified education expenses that taxpayers may take into account for computing the tuition and fees deduction increases from $3,000 to $4,000 if their modified adjusted gross income (MAGI) is not more than $65,000 ($130,000 if they are married filing jointly). No tuition and fees deduction will be allowed if the taxpayer's MAGI is more than $80,000 ($160,000 if they are married filing jointly).

Need Cash?

Your retirement plan may provide the funds you need

Many employer provided retirement plans offer employees the option of taking a loan from their account. This can provide some much needed cash for any number of purposes. However, there are a few IRS rules to keep in mind.

If the plan allows the loan, you must repay it in full within five years. An exception applies if the loan is for the purchase of your home. In that case, the loan can be repaid over a longer period. No specific time limit is placed on a home loan; however, the loan must provide for substantially level amortization with payments to be made at least quarterly.

There are also dollar limits on the amount an employee may borrow. Generally, the amount of the loan may not exceed the lesser of \$50,000 or one-half the present value of the employee's vested amount in the plan.

Plan loans that do not meet these requirements will be treated as a distribution to you. Distributions from a retirement plan are generally taxable and subject to an additional ten percent penalty if you are under the age of 59½, unless another exception applies. Check with your employer first for the specifics regarding your particular retirement plan.

Selling Your Home

IRS has clarified rules for excluding the gain

In 1997, the rules for taxing the gain on the sale of your home drastically changed. Simply put, if you owned and occupied your home for at least two years during the five-year period before the sale, you can exclude up to \$250,000 of the gain, \$500,000 if you file a joint return. Taxpayers who did not meet the ownership and use tests are allowed a reduced exclusion if certain unforeseen circumstances caused them to sell their home. Confusion surrounded the definition of "unforeseen circumstances."

The IRS has clarified situations that will meet the unforeseen circumstances exception. A sale will be considered as occurring primarily because of unforeseen circumstances if any of these events occur during the taxpayer's period of use and ownership of the residence:

- Death;
- Divorce or legal separation;
- Becoming eligible for unemployment compensation;
- A change in employment that leaves the taxpayer unable to pay the mortgage or reasonable basic living expenses;
- Multiple births resulting from the same pregnancy;
- Damage to the residence resulting from a natural or man-made disaster, or an act of war or terrorism; or
- Condemnation, seizure, or other involuntary conversion of the property.

Any of the first five situations listed above must involve you, your spouse, co-owner, or a member of your household to qualify.