finances and you

Sid Mittra

Brief rundown of changes in new tax law

In this final column on New Tax Law, you'll find an overview of the major changes.

Table A presents the key changes brought about by the Tax Reform Act of 1986.

Table B lists the key elements of the current law that remain unchanged. I hope that you have found the series of articles on the new tax law helpful.

On behalf of the Observer & Eccentric Newspapers and myself I wish to thank you for your continued support, your understanding and your helpful suggestions.

We wish you and your family a happy and prosperous new year.

Sid Mittra is director of certificate program in personal finance at Oakland University and president of Coordinated Financial Planning Inc.

Table B

Item	Current Law	Tax Reform Act
State, local income real-estate and personal-property taxes	Fully deductible	No change
Short-term losses	Losses offset gains and up to $3,000 of income	No change
Child-care credit	Maximum $720 one child, $1,440 two	No change
Gain on home sale	Nontaxable if more expensive home is bought	No change
Gain on home sale,	One-time $125,000 exclusion for those 55 or older	No change
Keogh deduction	Annual deduction up to$30,000	No change
Life-insurance	Annual earnings accumulate tax-free	No change
Social Security	Half of benefits taxed if adjusted gross income is more than $32,000 on joint returns, $25,000 on singles	No change

table A

Item	Current Law	Tax Reform Act
Individuals' tax rate	15 rates: 11-50%	'87 5 rates: 11-38.5% '88 3 rates 15-33%
Standard deduction	$3,670 joint $2,480 single	1987 $3,760 joint $2,540 single 1987 $5,000 joint $3,000 single
Personal exemption	$1,080	1987 $1,900 1988 $1,950 1989 $2,000
Extra personal exemption for age 65 or blind	Allowed	Repealed, but extra $600 added to standard deduction for each person over 65 or blind on joint returns, $750 single
Inflation	Yearly adjustments of tax brackets, personal exemption, standard deduction	Tax brackets and standard duduction indexed beginning in 1989, personal exemption in 1990
2-earner couples	Deduct up to $3,000	Repealed
Investment interest	Deductible against income + $10,000	Deduct against just investment income
Dividends	$200 income exclusion for joint returns, $100 for single	Repealed
Mortgage interest	Fully deductible	Deductible for principal and second residence up to purchase price plus home improvements
Other consumer, personal interest	Fully deductible	Not deductible
State, local sales tax	Fully deductible	Deduction repealed
Medical expenses 5% of adjusted gross income	Deductible if over 7.5% of adjusted gross income	Deductible if over
Money to charities	Deductible	Deductible for itemizers only
Business meals, entertainment	Fully deductible	80% deductible
Employee business expenses	Fully deductible	Deductible when combined with miscellaneous itemized deductions
Misc. deductions	Fully deductible	Deductible above 2% of adjusted gross as itemized deduction
Capital gains	Top rate: 20%	Top rates: 28% in '87 33% in '88
Short-term gains	Top rate: 50%	Top rates: 38.5% in '87 33% in 1988
Long-term losses investments	Losses offset gains, 50% of losses offset income up to $3,000	Losses offset gains, entire loss up to $3,000 can offset income
Losses from passive investments	Deductible against earned and other income	Deductible against passive income only
Income averaging	Allowed	Repealed
Alter. Min. tax	20% rate	21% rate, tighter rules
IRAs	Up to $2,000 deductible yearly	Deductible for those without qualified plans
401 (k) plans	Annual tax-deferred contributions up to $30,000	Annual tax-deferred contributions up to $7,000
Lump sums	10-year foward averaging and capital-gains provisions	10-year averaging capital-gains rules repealed in most cases replaced with five-year forward averaging

Prepay expenses to cut tax bill

Prepaying certain expenses is one way of softening the blow of the new tax law. So advises Andrew A. Dincolo, tax partner in the Detroit office of Peat Marwick, the international accounting tax and consulting firm.

"Because of the lower tax rates in future years, most deductions will provide a greater tax benefit in 1986. Therefore, it is more advantageous than ever to shift deductions into this year," Dincolo says.

According to Dincolo, the items that lend themselves to prepayment include:

• State and local taxes. According to current tax law, state and local income, property and sales taxes are an itemized deduction in the year they are paid. Under the new law, sales taxes will no longer be deductible. Thus, it is especially important to accelerate sales tax payments into 1986 since such amounts will not be deductible in 1987.

In addition, because of the declining tax rates enacted by the new law, taxpayers may want to pay final installments of estimated state income taxes in 1986 and take the deduction this year. Likewise, taxpayers who can choose to pay real estate taxes in either 1986 or 1987 may want the deduction against 1986's higher rates. However, if real estate taxes are paid through an escrow agent, your deduction is in the year in which the agent pays them, not in the year in which they are paid into the escrow account.

• Unreimbursed medical expenses. This year, medical expenses — including medical insurance — are allowed as an itemized deduction to the extent they exceed 5 percent of the adjusted gross income (AGI). Next year, the new law raises this floor to 7½ percent. It may make sense to prepay any of these expenses in 1986 to take advantage of the lower threshold.

• Interest expenses. Despite the five-year phase-out period, most taxpayers will be affected by the repeal of the deductibility of personal interest expense starting in 1987. Neither current law nor the new law allows deduction of prepaid interest — that is, interest paid before it is incurred. But Dincolo points out that taxpayers can mail January loan payments in December to increase 1986 deductions, since interest is usually incurred the month before it is due.

Next year's stricter limits on investment interest — margin interest, for example — also call for greater attention this year. Under current law, investment interest is deductible to a limit of $10,000 plus any investment income. Starting in 1987, the $10,000 amount is phased out over five years. Dincolo suggests that taxpayers whose estimated 1986 investment interest expense will exceed this year's more generous limit may want to recognize unrealized short-term gains or convert tax exempt interest into taxable interest in order to increase investment income in 1986.

• Miscellaneous itemized deductions. In the past, expenses like union dues, business periodicals, uniforms, tax preparation fees, unreimbursed employee business expenses and job-related education expenses, were fully deductible. Next year, they will be deductible only to the extent they exceed 2 percent of adjusted gross income. Therefore, it makes sense to prepay in 1986 as many of these expenses as possible. For example, taxpayers can renew magazine subscriptions in December or pay anticipated tuition costs for next year's classes, recognizing that expenses paid by check in 1986 are considered deductible under current law, even though the check does not clear until 1987.

• Charitable deductions. For 1986, Dincolo notes, maximizing your charitable contribution deduction has added significance for two reasons. First, the deduction for unitemized charitable contributions will be eliminated in 1987. Second, the reduction in the top marginal tax rate will reduce the tax savings generated by charitable contributions after 1986. Therefore, it may be advantageous to maximize contribution deductions this year. Dincolo points out that certain gifts to charity of a future interest in property can result in a current tax deduction. There are various ways to do this, including charitable remainder trusts, pooled income funds, charitable lead trusts, and private foundations.

Dincolo advises that taxpayers whose total itemized deductions in 1986, excluding charitable contributions, are less than the zero-bracket amount should not itemize deductions and should claim a deduction for charitable contributions as a non-itemizer.

datebook

● **ACCOUNTING JOBS**

Tuesday, Jan. 6 — Free job opportunities seminar on accounting assistant field begins at 7:30 p.m. in Rochester. Information: 370-3120. Sponsor: Oakland University.

● **LEGAL ASSISTANTS**

Thursday, Jan. 8 — Free informational panel on legal assistant careers 7:30-9 p.m. in Rochester. Information: 370-3120. Sponsor: Oakland University.

First Federal mortgage unit due to open

First Federal of Michigan will open its wholly-owned mortgage banking subsidiary, County Mortgage Corp., at 706 N. Woodward in Birmingham in mid-January.

William J. Thiess, currently first vice-president and manager of residential loan administration at First Federal, will be president of the new County Mortgage subsidiary.

County Mortgage Corp. will offer several conventional home mortgage loans, including 30-year fixed-rate mortgages, 15-year fixed-rate and graduated payment mortgages, and one-year adjustable rate mortgages.