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### **MIDYEAR TAX PLANNING: IT CAN BE GOOD FOR THE BANK ACCOUNT**

Many financial planners say it's time to think about next year's income taxes. Yes, it was just a few weeks ago you put your 1999 return in the mail (or zapped it electronically if you are Internet-hip). You may have no desire to go through that torture again until next spring. But there is a method behind their madness that could save you tax dollars in the long run.

One reason it's wise to start thinking about next year's taxes now is that many tax strategies and adjustments require time to carry out. For example, did you receive a sizable refund from 1999? This means you overpaid your taxes throughout the year, and the government got to keep your money as a tax-free loan. Some people view this as forced savings, but generally it's better to invest or put the money in the bank. Instead of a refund, did you owe enough in taxes that you had to pay interest and penalties? Perhaps you received a large bonus and your employer didn't withhold enough.

You can reduce the amount you owe or receive as a refund by adjusting the allowances you claim on your W-4 form. To reduce the size of a refund next year, increase the number of allowances; decrease the number to reduce the amount you owe. Try to more accurately calculate any estimated payments you may need to make, such as for income from retirement accounts, investments or self-employment, so they more closely match your anticipated tax liability.

Another common strategy that takes advance planning is "deduction bunching." Certain itemized deductions must meet thresholds before you can claim them. For example, you can deduct only those medical expenses that exceed 7.5 percent of your adjusted gross income (AGI). That is, for \$75,000 in AGI, you can't deduct the first \$5,625 in medical expenses. Only the amounts that exceed that can be deducted. Many families-fortunately-don't exceed the threshold in a given year, or they don't have enough itemized

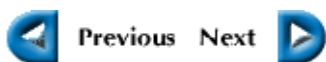
deductions exceed the standard deduction. However, bunching elective expenses into a single year, such as prepaying an orthodontia bill or doing elective (nonemergency, noncosmetic) surgery, might push you over the threshold. However, review any itemized deduction strategies to see if they increase your vulnerability to the alternative minimum tax.

Planning to get married before the year's out? Romance aside, a December wedding may not be a good idea from a tax standpoint if both of you are wage earners, because you could be hit by the "marriage penalty"-when married couples pay more in combined taxes than they would have paid as single taxpayers. Postponing the wedding into January could save you enough in taxes to help pay for the wedding. The opposite strategy applies to couples in which one person doesn't work. They may find it more financially beneficial to marry before the year's out.

Midyear is an excellent time to review your investments from a tax perspective. Generally, financial planners recommend basing investment decisions on your needs and on the economics of the investments themselves, not on taxes. However, if you've already sold off some winners this year, you could offset some of that gain by selling off, before the year's out, those losers you've been meaning to sell, anyway.

Make charitable plans now, such as donating stock or mutual fund shares. Consider increasing charitable contributions in bigger income years, or "bunching" contributions in a single year.

Determine from your 1999 tax return what marginal tax bracket you're in. That's the rate at which your last dollar of taxable income is taxed. Marginal rates are important when making investment and other financial decisions. When weighing the benefits of investing in tax-free bonds versus a taxable bond, for example, knowing your marginal tax rate lets you compare the investments on an after-tax basis. The rate also helps you determine the tax benefits of charitable contributions and other deductions, as well as employee benefits such as retirement plans and flexible spending accounts.



Review with your tax advisor any significant changes in your life this year, such as marriage or divorce, the birth of a child, or a death in the family. All these can have major tax consequences. Reviewing them now gives you time before the year is out to make appropriate plans. The planning door closes December 31, 2000.

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