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## It's Not What You Earn, It's What You Keep



### It's Not What You Earn, It's What You Keep

You work hard for your money. So why shouldn't you try to keep as much of it for yourself as you can? Here are some ways to pay less tax and keep more of your hard-earned dollars.

#### Tax deferrals rule

Take advantage of tax-deferred retirement plans, such as 401(k), 403(b), and 457 (b) plans, offered by your employer. They all allow you to make pretax contributions of up to \$15,500 in 2008 (\$20,500 if you're age 50 or older), and 403 (b) and 457(b) plans may also have special catch-up rules that might let you defer even more. The tax savings can be significant. For example, if your marginal tax rate is 28% and you defer \$15,500, you'll save \$4,340 in current taxes. Your \$15,500 contribution will generate tax-deferred earnings for you until you withdraw the funds from the plan, when you may be in a lower tax bracket. And, if your employer matches your contributions, the deal is even sweeter.

Another common way to use tax deferrals to save more of what you earn is by setting up a health-care flexible spending account (FSA) at work. Your contributions reduce your taxable income, saving current taxes, and the funds you set aside can be withdrawn tax free to pay a wide variety of health-related expenses that aren't covered by your health plan. See IRS Publication 502, *Medical and Dental Expenses*, for a list of qualifying expenses.

And don't forget traditional IRAs. If neither you nor your spouse is covered by a retirement plan at work, and you're not yet 70½, you can make a deductible contribution of up to \$5,000 to an IRA in 2008 (\$6,000 if you're age 50 or older). Even if you or your spouse is covered by a plan, all or part of your contribution may be deductible, depending on your income.

#### But tax free is even better

If you're an income-oriented investor, consider investing in municipal bonds. The income generated is free from federal income taxes and, in some cases, state income taxes as well. (Be sure to compare yields between taxable and tax-free securities, and keep in mind that certain municipal bond income may be subject to the alternative minimum tax.)

We believe that a successful wealth management relationship starts with clarity of purpose.

Before embarking on any plans or strategies with our Client, we first seek to develop a clear understanding of your personal and financial goals.

We then work with you to select and implement strategies that will help you move toward your goals.

Another way you can generate tax-free income is by contributing to a Roth IRA, Roth 401(k), or Roth 403(b) plan. Unlike pretax deferrals, Roth contributions don't reduce your income, so there's no current tax savings. Because you've already paid tax on your contributions, they won't be taxed again when you withdraw them from the plan. But what really sets Roth contributions apart, and makes them so appealing, is that all earnings are also tax free if you satisfy a five-year holding period and certain other requirements are met.

If you have children, don't pass up the tax incentives offered by Section 529 plans and Coverdell education savings accounts (ESAs). Again, your contributions to these plans aren't tax deductible, but your savings grow tax deferred and withdrawals are tax free at the federal level (and typically at the state level too) when used to pay qualifying educational expenses. You can contribute up to \$2,000 to a child's Coverdell ESA in 2008, and most 529 plans let you contribute more than \$300,000 over the life of the plan. In Vermont, the maximum was \$240,000 as of early 2007.

The Vermont Higher Education Investment Plan is Vermont's official 529 plan. As such, it's the only 529 plan that qualifies for a Vermont income tax credit on contributions and a Vermont income tax exemption on earnings (when withdrawals are used for qualified education expenses). As of the 2007 tax year, the tax credit is 10 percent of the first \$2,500 contributed annually, or up to \$250, per taxpayer per beneficiary. (Source: Vermont Higher Education Investment Plan)

### **Think long-term--for capital gains**

Long-term capital gains tax rates are currently very attractive--a maximum of 15% through 2010. Short-term capital gains, on the other hand, are generally taxed at ordinary income tax rates--currently as high as 35%. To qualify for long-term capital gains treatment, make sure you hold your securities and other capital assets for more than one year before selling them.

Warmest Regards,

Stage 2 Planning Partners

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The Patrick Group | 20 Kimball Avenue | Suite 201 | South Burlington | VT | 05403