

Protect Yourself from 2013 Tax Hikes with 2012 Tax Planning

Written by Ginny Grimsley
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3 Tips for Taking Advantage of This Year's Lower Tax Rates

Income taxes are going up next year, and not just for those who earn more than \$200,000 a year.

"Taxes are likely to be higher for everyone" says financial planner Rick Rodgers, author of *The New Three-Legged Stool: A Tax Efficient Approach To Retirement Planning* (www.RodgersSpeaks.com).

"We all know about the expiring Bush tax cuts, which may or may not be extended for everyone or just some," he says. "There are also new taxes that were part of the healthcare reform law passed in 2010; the expiring payroll tax cut; the alternative minimum tax that already expired in 2011, and many other provisions that have expired or will expire at year end."

Nearly everyone should prepare to pay more, Rodgers says.

The good news is you still have time to take advantage of 2012 tax rates, which may turn out to be the lowest we will see in some time. Rodgers offers these strategies that can be implemented before the end of 2012:

- Roth Conversion - No one knows for sure what will happen to the tax code next year, which is why a Roth conversion is one of the best tax-planning strategies available. Converting a

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traditional IRA to a Roth IRA creates a taxable event in 2012. All future earnings in the account will be tax-free, as long as you wait five years and are age 59½ or older when you take withdrawals. The biggest advantage to the Roth conversion strategy is the ability to “undo” the transaction as late as Oct. 15, 2013. Should the new Congress pass a major tax reform bill next year that lowers tax rates across the board, you can put the money back into your IRA. It will be like the transaction never happened.

- Harvest capital gains - Harvesting gains is similar to harvesting losses. Sell appreciated securities that you’ve held for at least 12 months to realize the long-term gain for tax purposes. You can immediately repurchase the same asset because there is no wash sale rule for realizing gains. This allows you to pay tax on the gain in 2012, when rates are low, and establish a new cost basis in the asset to minimize increased gains that may be taxed at higher rates. This strategy should appeal to anyone in the 15-percent tax bracket because capital gains are taxed at zero and may jump to 8 to 10 percent in 2013 if the tax cuts expire. The strategy is also appealing to anyone subject to the Medicare surtax. If the current tax laws expire, the tax rate on long-term capital gains will jump from 15 percent to 23.8 percent (21.8 percent for assets held more than five years).

- Pay medical expenses - Anyone who normally itemizes medical expenses on their tax return should accelerate those expenses into 2012 if they can. Medical expenses are deductible only if they exceed 7½ percent of adjusted gross income (AGI). This means if your AGI is \$50,000, you can deduct only medical expenses over \$3,750. Next year the threshold jumps to 10 percent of AGI. Pay your January medical insurance premium in December to move this deduction to 2012. Any routine eye exams or dental visits should be moved up to December. Paying with a credit card would give you the deduction this year and delay the actual payment until 2013.

Rodgers warns that a common mistake is to wait and see what happens. It has not been uncommon for Congress to make significant changes to the tax code late in December, leaving taxpayers little time to react. He advises a diversified approach to tax planning. Make a partial Roth conversion, harvest some capital gains but don’t wait until it’s too late to do anything about rising taxes.

Take a proactive approach to tax planning this year to cushion any fall from the fiscal cliff.

About Rick Rodgers

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Certified Financial Planner Rick Rodgers is president of Rodgers & Associates, “The Retirement Specialists,” in Lancaster, Pa. He’s a Certified Retirement Counselor and member of the National Association of Personal Financial Advisers. Rodgers has been featured on national radio and TV shows, including “FOX Business News” and “The 700 Club,” and is available to speak at conferences and corporate events (www.RodgersSpeaks.com).