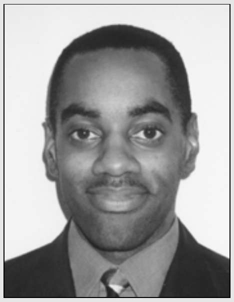
THE EMPOWERMENT CHANNEL

A newsletter designed to promote financial empowerment through stewardship

October 2004 **Volume III**



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Stewardship Emphasis

The winner of the game is not necessarily the one who collects the greatest number of coins but the one who is able to keep more of the coins that he collects.

Tips to Increase Your Tax Smarts - Part 3

In the previous two issues of The Empowerment Channel we have reviewed tax tips for improved tax planning and monitoring, less widely discussed retirement plan rollover situations, and tax deductions to take advantage of. In the final issue of this series, we will discuss some more tax strategy and the tax line item that is better for you than a deduction.

Tip #5 – Adjust Your Investment Portfolio and Give Your Taxes a Break

If you understand the value of asset allocation, you realize the need to periodically review your portfolio and make adjustments to keep your portfolio properly balanced. No matter how well you have done at investing your money, chances are you have made selections that did not turn out like you have hoped and have taken losses. While no one enjoys taking a loss on their investment, you can use that loss to your advantage if you need to make portfolio adjustments anyway. If you are investing in a taxable account and the investment has underperformed and/or no longer meets your needs, you can sell it at a loss and use that loss to offset capital gains on a sale where you have made a profit. Balancing out the gains and losses or at least using those losses to minimize the tax impact of the gains, keeps the IRS from taking as much of your profit. So, if you have a good performer that you want to re-position, evaluate your portfolio and see if you have a poor performer that you can sell and replace with an investment that better meets your needs.

Tip #6 – Do One Better than a Deduction and Take Advantage of Tax Credits

Make no mistake, tax deductions are a major part of a successful tax plan that most people can benefit from to some degree. Deductions, however, impact your taxes only to the level of your marginal tax rate. With that as the case, as you might expect, tax credits are a little harder to qualify for, but well worth the effort to look into. One such credit is the Child Tax Credit, which allows you, if you have dependent children, to take a credit of $1,000 per child (from 2003), provided that you meet the income limitations. Another major area where tax credits are offered is in the area of education. The HOPE and Lifetime Learning Credits have been around for a long time but are underused and in many cases misunderstood. Contrary to what some people may think, the HOPE and Lifetime Learning Credits can be used in the same year as distributions from a 529 College Savings plan, so long as they are not used for the same expense. While we are talking about education, although not as valuable as a tax credit, the tax code allows you to take a tax deduction for college tuition and fees up to $3,000 and student loan interest up to a maximum amount of $2,500 per year (also from 2003). With the combination of the available deductions and tax credits, you can at least take a bite out of the rising cost of higher education and reduce your outlay for one of the best investments you can make.

Tip #7 – Regardless of the Tax Impact, Make the Smart Financial Decision

Sometimes we get caught up in avoiding taxes or paying fewer taxes to the point where we make decisions based on tax impact alone. Be sure that any financial decision you make can stand on its own and is not driven strictly by taxes. If you are buying a home to get the mortgage interest deduction, make sure you can afford the mortgage payment; otherwise, your whole financial situation will be strained. In our Tip #5 of offsetting capital gains with capital losses, don't sell an investment just for the tax benefit alone, but use the tip as a part of your overall portfolio improvement strategy.

Effective tax planning is a part of being a savvy money manager. By being aware of some of the provisions in the tax rules and using your trusted tax advisor as a resource, you can help yourself make more effective use of your available funds by giving less to Uncle Sam and keeping more for yourself.

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