

LEGAL ALERT!

THE TAX MAN COMETH

To many, the end of the holiday season and the attendant chaos is truly bitter sweet. As we all know, the month of January signifies the beginning of the dreaded tax season. Many believe that generally, new tax legislation tends to favor the wealthy. This month's **LEGAL ALERT!** will not attempt to debunk that notion. However, there are some significant tax law changes that will allow some tax benefits to "trickle down" into all of our pockets – Ronald Reagan would be proud.

This article briefly summarizes the following three tax law changes that will affect you in **tax year 2004** or beyond:

- Taxpayers who itemize their deductions have the option of deducting their state and local income taxes or their state and local sales taxes on their federal return;
- Charitable deductions taken for items donated to charities such as cars will be limited to gross proceeds received by the charities from the sale of the item; and
- Required minimum distribution income from a regular IRA does not impact a taxpayer's gross income for purposes of converting to a Roth IRA.

TAXPAYERS CAN NOW ITEMIZE THEIR STATE & LOCAL SALES TAXES

Along with its many notable distinctions, New York has always had a bad reputation for having high sales taxes. Indeed, many New Yorkers residing near sales tax friendly states, such as New Jersey, engage in a mass weekend exodus across the border to shop in order to economize. Beginning in tax year 2004, such draconian measures may no longer be necessary.

Specifically, in tax year 2004, taxpayers will have the option of itemizing their state and local income taxes or sales taxes, but not both. How will that benefit the taxpayer? By way of example, for tax years that a taxpayer buys big ticket items, e.g., car or boat, it may be more prudent to utilize the sales tax deduction instead of the income tax deduction, as that would result in less tax paid to the IRS.

Indeed, a taxpayer need not wait to purchase big ticket items to utilize the sales tax deduction. It is conceivable that taxpayers who make frequent purchases, such as those with large families, may

benefit from the sales tax deduction due to the sheer volume of their yearly purchases.

TAXPAYERS CAN NO LONGER RELY ON THE BLUE BOOK VALUE WHEN TAKING DEDUCTIONS FOR CARS DONATED TO CHARITY

Under current law, taxpayers can generally deduct the “blue book”, or fair market, value of items such as cars donated to charity, notwithstanding the amount it is later sold for. However, Congress has summarily ended that practice. Specifically, effective in 2005, charitable deductions for car donations made where the car value exceeds \$500 is limited to the gross proceeds from the sale of the car by the charity.

Moreover, the charity is required to provide a written acknowledgement to the donor within 30 days of the sale of the car stating the amount of the gross proceeds. Taxpayers should heed the new rules as the IRS is certain to be more vigilant in its enforcement efforts.

MORE TAXPAYERS CAN NOW CONVERT FROM A TRADITIONAL TO A ROTH IRA

Historically, many taxpayers could not convert from a Roth IRA to a regular IRA because their gross income included required minimum distributions from the regular IRA, thus pushing them above the

threshold amount of \$100,000 Adjusted Gross Income limit. For tax years beginning in 2004, Congress has chosen to exclude the required minimum distribution from the Adjusted Gross Income limitation. Accordingly, the number of taxpayers qualifying for the conversion will increase.

Why should a taxpayer convert from a regular IRA to a Roth IRA? A Roth IRA has many advantages that a regular IRA does not. Specifically, income generated by a Roth IRA is never taxable! Also, a Roth IRA does not have a required minimum distribution for those 70 ½ and older. Thus, a taxpayer may choose to leave his money to grow tax free in the Roth IRA for his children or spouse. Lastly, withdrawals from the Roth IRA by the account holder or her beneficiary(ies) are generally tax free!

CONCLUSION

As we embark upon this new tax year, it is important to remember how fortunate we are to live in this great country where our biggest problem is paying too much in taxes. At the writing of this newsletter, more than 155,000 people lost their lives to the wrath of the tsunamis that hit South East Asia and Africa. If you can, please lend a hand to those less fortunate. President Bush recently declared that any contributions made in the month of January to organizations that assist the victims of the tsunamis can be recognized as a charitable contribution for tax year 2004. May you have a prosperous year.

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