

Effective Tax Planning Strategies

With April 15th growing closer, most people are focusing on getting their taxes done and planning their tax-saving strategies for the new year. This year there is a special need to also plan for changes made by the Taxpayer Relief Act of 1997 (TRA '97), many of which became effective in 1998. Normally, the shrewdest tax planning is to receive income in the year you are in the lowest tax bracket and to take deductions in the year you are in the highest tax bracket. This year that might not be the best strategy.

To qualify for many of the new tax breaks created by TRA '97, your income cannot exceed certain limits. For example, only taxpayers with adjusted gross income (AGI) of \$100,000 or less (excluding the rollover) are permitted to rollover regular IRAs to the new Roth IRA. In 1998 only, the income that results from the rollover can be spread over four years. Therefore, you may want to

accelerate income into 1997 in order to keep your 1998 AGI under \$100,000. Other new tax breaks which have AGI phase outs include education tax credits, student loan interest deductions and contributions to Traditional, Roth and Education IRAs.

You should re-examine your investment strategies keeping in mind the new, more favorable long-term capital gains tax for assets held longer than 18 months. For assets held longer than 18 months and sold on or after July 29, 1997, the maximum capital gains tax rate is 20 percent (10 percent for persons whose income remains

in the 15 percent tax bracket including the gain). The 28 percent capital gains rate still applies for assets held longer than one year, but 18 months or less and sold on or after July 29, 1997. Thus, you may want to consider holding capital gain assets for longer than 18 months and selling capital loss assets while their holding period is short term.

There were also transitional rules for assets sold between May 7, 1997 and July 28, 1997. The new 20 percent rate is effective for gains from the sale of assets held for more than one year that occurred on or after May 7, 1997 through July 28, 1997.

Many investors will have profits from stock transactions that they will want to offset with losses from other capital assets. Review your portfolio for unrealized "paper" losses which you can use to offset capital gains without limit and ordinary income up to \$3,000 per year. Any unused capital loss may be carried forward for an unlimited time. December 31st was the last trade date in 1997. Remember any 1996 capital loss carryovers!

Under TRA '97, a taxpayer must recognize a gain on a "constructive sale" of appreciated stock, which includes short sales, at the time of the sale. There is an exception for a short sale if closed within 30 days after the end of the tax year, and if after closing the transaction the taxpayer holds the appreciated stock for 60 days unhedged. Effectively, you will have to use newly acquired shares to close the transaction. A short sale can still protect investors against market swings as long as they are willing to go unprotected for 60 days after they close the transactions.

When it comes to your investments, don't overlook the opportunity to reduce your tax liabilities and improve investment opportunities. ☑

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