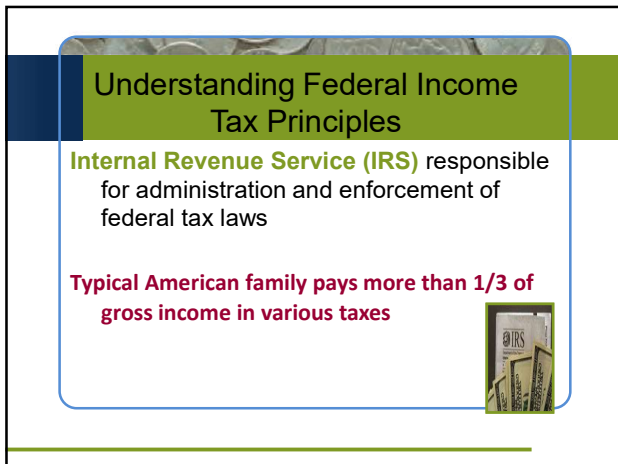
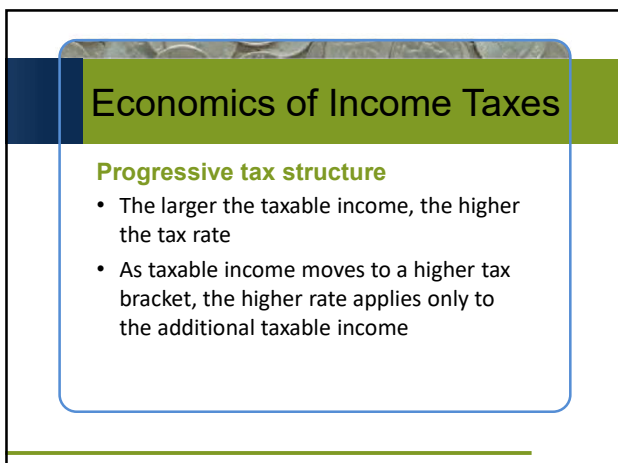


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3

Single Taxpayer 2010 Tax Return

| Taxable Income | Tax Rate |
|------------------------|----------|
| \$1 to \$8,375 | 10% |
| \$8,376 to \$34,000 | 15% |
| \$34,001 to \$82,400 | 25% |
| \$82,401 to \$171,850 | 28% |
| \$171,851 to \$373,650 | 33% |
| Over \$373,650 | 35% |

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Economics of Income Taxes (continued)

Marginal Tax Rate

- Tax rate paid on the next dollar of taxable income

Average Tax Rate

- Rate at which each dollar is taxed on average
 - Divide tax liability by taxable income

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Sam and Burt's Taxes

| Name | Taxable Income | Tax Calculation | Tax Liability |
|------|----------------|---|-----------------|
| Sam | \$45,000 | $= [(\$45,000 - \$34,000) \times 0.25]$ $+ [(\$34,000 - \$8,375) \times 0.15]$ $+ [\$8,375 \times 0.10]$ $= \$2,750 + \$3,844 + \$838 =$ | <u>\$7,432</u> |
| Burt | \$90,000 | $= [(\$90,000 - \$82,400) \times 0.28]$ $+ [(\$82,400 - \$34,000) \times 0.25]$ $+ [(\$34,000 - \$8,375) \times 0.15]$ $+ [\$8,375 \times 0.10]$ $= \$2,128 + \$12,100 + \$3,844 + \$838 =$ | <u>\$18,910</u> |

6

Filing Status Categories

- **Single** – Unmarried or legally separated
- **Married filing jointly** – married couples who combine income and deductions on 1 return
- **Married filing separately** – spouses file separately
- **Head of household** – considered unmarried pays more than ½ for self and dependent
- **Qualifying widow/widower with dependent child** – spouse died within 2 years, has dependent child

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Your Take-Home Pay

- Taxes due on a **pay-as-you-go** basis
 - Employer withholds taxes all year
 - Self-employed deduct and pay taxes
- Taxes include:
 - Federal, State, & Local income taxes
 - FICA and other withholding taxes



8

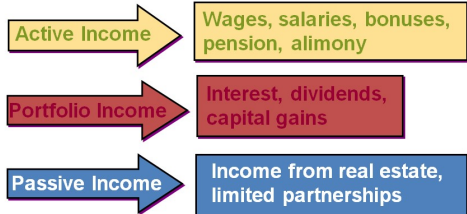
It's Taxable Income That Matters

Taxable Income = the amount of income subject to taxes

Calculating income taxes is a complex process involving several steps and many computations

9

Three Kinds of Income



10

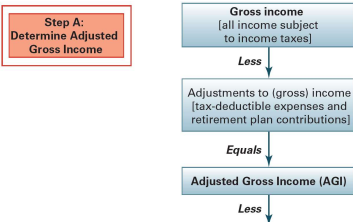
Gross Income

Gross income- any and all income subject to federal taxes.

- Wages and Salaries
- Bonuses, commissions, and tips
- Interest and dividends received
- Alimony received
- Income from pensions and annuities
- Prize, lottery, and gambling winnings

11

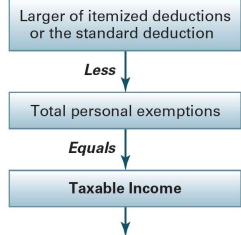
Taxable Income and Liability Part 1



12

Taxable Income and Liability Part 2

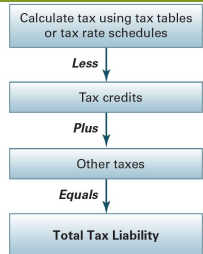
Step B: Calculate Taxable Income



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Taxable Income and Liability Part 3

Step C: Calculate Tax Liability



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Capital Gains

Capital gain (loss) – when an asset is sold for more (less) than its original cost

- Capital gains are taxed at different rates, depending upon holding period.
- Most capital gains are included in portfolio income.
- IRS limits capital losses during a given year.
- A capital loss must result from sale of some income-producing asset to qualify as “deductible”.

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Capital Gains Tax Categories as of 2011

Capital gains tax rates are as low as 5% or 15% for holding periods over 12 months, depending on the tax bracket (year 2011).

| Holding Period | Tax Brackets (2010) | Tax on Capital Gains |
|---------------------|--|-------------------------|
| Less than 12 months | All (10%, 15%, 25%, 28%, 33%, and 35%) | Same as ordinary income |
| Over 12 months | 10%, 15% | 0% |
| | 25%, 28%, 33%, 35% | 15% |

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Adjustments to Gross Income

These can be **subtracted** from gross income

- Higher education (limited)
- IRA contributions (limited)
- Self-employment tax – (limited to 50%)
- Alimony paid
- Penalty on early withdrawal of savings
- Moving expenses (limited)

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Deductions: Standard or Itemized

Standard deduction – a fixed amount that depends on filing status

- filing status
- age
- vision



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Deductions: Standard or Itemized (continued)

Itemized deductions

- specific personal expenditures
- itemize if expenses are greater than standard deduction

- Medical, dental expenses
- State, local, foreign taxes
- Mortgage interest
- Charitable contributions
- Casualty and theft losses
- Moving expenses

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Exemptions

Deductions from AGI based on number of persons supported by taxpayer's income

- You are an exemption on your own return unless claimed by someone else
- Children, spouses, elderly parents can be other exemptions

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Tax Credits

Subtracted from amount of taxes owed

Credits include:

- Child & dependent care expenses
- Adoption tax credit
- Foreign tax credit
- Credit for Qualified electric car

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Tax Credits versus Tax Deductions

Which results in lower taxes?

Credits

directly reduce amount of taxes owed

versus

Deductions

subtracted from AGI and reduce taxable income

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Tax Forms and Schedules

When more detail is required, taxpayers also must file other forms and schedules



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Tax Forms and Schedules-1040EZ

Form 1040EZ — Simple 1 page form

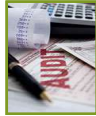
- Under age 65
- Taxable income under \$100,000
- Don't claim
 - adjustments to income
 - itemized deductions
 - tax credits



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Other Filing Considerations

- Quarterly payment of estimated taxes
- April 15 filing deadline
- Filing extensions
- Amended returns (1040X)
- Audited returns



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Tax Preparation Services

- Do it yourself or get help from
 - Private tax preparers
 - Tax services
 - CPA's
 - Enrolled agents
 - Tax attorneys
 - Computer-based tax returns
- Taxpayer is responsible for accuracy!



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Effective Tax Planning

Tax avoidance is legal - tax evasion is not!

- Reduce taxes
 - Maximize deductions, credits
- Shift taxes
 - Use gifts or trusts
- Defer taxes
 - Postpone to future through IRA or annuity



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