DECEMBER 2007

MURPHY FINANCIAL SERVICES, INC.

Tax & Financial Guide

Business and Personal ACCOUNTING, TAX, SOFTWARE & FINANCIAL PLANNING SERVICES

Fourth quarter Federal tax estimates are due January 15, 2008 and state tax estimates are due December 31, 2007 or January 15, 2008. Call us if you aren't sure when to pay your state tax estimate. Please get your income and expenses to our office by December 20, 2007 if you want us to calculate your estimates.

Please call our office to discuss any of the items in this newsletter that may pertain to you.

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Tax Relief and Health Care Act of 2006

Health Savings Account Enhancements. HSA enhancements in the new law are permanent and most take effect for tax years beginning after 2006.

FSA/HRA Rollovers. Employees with a health flexible spending account (FSA) or a health reimbursement account (HRA) can make a one-time transfer of the balance in their FSA or HRA to an HSA. The maximum transfer amount is the lesser of the balance as of the date of transfer or September 21, 2006. The transfer must be made before January 1, 2012.

IRA Rollover. For tax years beginning after 2006, taxpayers may make an irrevocable election to rollover funds from their IRAs into an HSA. The once-in-a-lifetime rollover is nondeductible and the amount is limited to the otherwise maximum deductible HSA contribution amount, based on the type of coverage under the taxpayer's HDHP at the time of the contribution. The rollover amount also reduces the otherwise allowable HSA contribution amount.

Energy Extenders. The new law does not extend the residential energy property credit, which expires at the end of 2007. The new law does extend the tax credit for solar water heaters, solar electricity equipment and fuel cell plants through 2008.

Earned Income Tax Credit for Combat Pay. The Act extends for one year (in tax years ending before Jan. 1, 2008) the provision allowing the use of combat pay to calculate the earned income tax credit.

Crackdown on Tax Protesters. Congress has given the IRS enhanced authority to penalize taxpayers who file frivolous returns and other bogus submissions. These tax protesters claim, for example, that the federal income tax is unconstitutional or that wages are not taxable. The IRS has heard - and rejected - all of these arguments for years. Now it can fine individuals who make these false claims up to $5,000 .

Additional Details That May Reduce Your Taxes

Standard Mileage Rate. Taxpayers can use the standard mileage rate (in lieu of actual expenses) to compute the deductible costs of operating automobiles owned or leased by them (including vans, pickups or panel trucks) for business purposes. Here are rates for the 2007 tax year: Business 48.5¢, Medical .20¢, Moving .20¢, Charitable .14¢

An employee may deduct an amount computed using the standard mileage rate only as an itemized deduction, subject to the 2% floor on miscellaneous itemized deductions.

Substantiating Cash Contributions. You are not allowed a charitable deduction for contributions of cash or other monetary gifts, regardless of the amount, unless you maintain a written record of the contribution. That includes a bank record (such as a cancelled check) or a written

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Small Business and Tax Act of 2007

Married Business Couples. Under the 2007 Small Business and Work Opportunity Tax Act, married couples who jointly operate an unincorporated business and file a joint return can elect not to be a partnership for federal tax purposes.

All items of income and expenses are divided between the spouses, on their separate Schedule Cs, according to their respective interests in the venture.

Each spouse will receive credit for his or her self-employment tax contributions in determining Social Security benefits.

Unearned Income of Minors. The "kiddie tax"age has been raised to under 19 (or under 24 for students) for tax years after 2007.

Some ideas on investments for your children that will produce little or no current taxable income include stocks and mutual funds oriented toward capital growth; vacant land expected to appreciate in value; stock in a closely-held family business that pays little or no cash dividends; tax-exempt municipal bonds and bond funds; and U.S. series EE savings bonds for which interest reporting may be deferred.

Small Business Expensing Expanded (Sec. 179). Tax laws allow you to deduct some business expenses that would otherwise have to be depreciated. The new law raises the dollar limitation from $112,000 to $125,000 and the income limitation from $450,000 to $500,000, retroactive to the start of 2007.

Murphy Financial Services, Inc. web site is at www. murphyEA.com If you misplace your newsletters, or your information sheets that I have given you (i.e. contributions, enrolled agents, etc.), you will be able to find them on the web site.

Please note that our e-mail address is: info@murphyea.com.

PRIVACY POLICY

We do not disclose any non-public personal information about our clients or former clients to anyone, except as instructed to do so by such clients, or required by law. We restrict access to non-public personal information only to IRS or state authorities and we maintain physical, electronic, and procedural safeguards to guard your personal non-public information.

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communication from the donee showing their name and the date, and the amount of the contribution. This rule applies to cash contributions *made after December 31, 2006*.

Non-cash Contributions. If you donate clothing or other household items to a charitable organization *on or after August 17, 2006*, the item must be in “good or better” condition before you are allowed a deduction for its value. This rule applies if the value of the item is less than $500. For *single items* whose established value exceeds $500, you must attach a current appraisal to gain tax return.

Because the IRS does not define “good or better” condition, the determination is left to your best judgment. This eliminates deductions for items with little or no monetary value.

Contributions of tangible personal property (other than publicly traded securities) with a fair market value deduction of more than $5,000, have a new recapture rule. If the charity sells the property within three years, the donor has to make an adjustment.

Charitable Contributions from an IRA. If you are age 70-1/2 or older, own IRAs (or Roth IRAs), and are planning a charitable gift before year-end, have the gift made directly by the IRA trustee. That can achieve important tax savings but *it will no longer be available after 2007* under current law.

Year-End Planning. End of year is an ideal time to examine winning and losing investments for the year to minimize capital gains income and maximize capital losses. Long-term capital losses can be used to fully offset long-term capital gains. Losses taken in excess of gains can also be used to offset up to $3,000 in ordinary income (or $1,500 for a married couple filing separately).

Starting in 2008, strategies for capital gains and losses should include a special, nontraditional opportunity: the 0% net capital gain rate for tax years 2008 through 2010. While this zero rate is only available for individuals in the 10 or 15 percent income tax brackets, for families, retirees, and others it’s well worth it to manage their income tax brackets starting in 2008. *Management starts at year-end 2007,* as does the decision to postpone a sale of a capital asset until January 2008 to take advantage of this favorable zero tax rate.

Gift-giving. Take advantage of the 2007 annual and lifetime gift-giving limits to reduce your income and estate tax liabilities. For 2007 and again in 2008, you can transfer $12,000 per person, per year, without paying gift tax on the amounts transferred. Married couples can gift $24,000 per person, per year without tax liability on the amounts transferred. That strategy not only avoids possibly paying a hefty estate tax later, but it removes earnings from those gifts from your taxable income bracket into that of the lower-bracket gift recipient.

Flexible Spending Accounts. If you set aside too little this year, increase the amount you set aside next year in your employer’s health flexible spending account. You can also set aside $$ to get tax-free reimbursements for over-the-counter drugs, such as aspirin and antacids.

Grace Period. Instead of cafeteria plan account balances and employer contributions left over at the end of a plan year being forfeited (under the “use-it-or-lose-it” rule), a plan may provide a “grace period”.

An employer may amend its cafeteria plan to give all participants a grace period lasting no longer than 2-1/2 months immediately following the end of each plan year. Participants with a balance in their FSAs at the end of the plan year can use the balance for qualifying expenses within the grace period.

Hybrid vehicles. If you want to buy a hybrid vehicle eligible for a tax credit, buy it before year-end after confirming that you and the particular model qualify for the credit.

The IRS hybrid vehicle tax credit for 2008 Toyota and Lexus hybrid models applies only to vehicles purchased prior to October 1, 2007. For purchases made April 1, 2007 through September 30, 2007, the credit amounts are: 2008 Toyota Prius Hybrid $787.50, 2008 Toyota Camry Hybrid $650, 2008 Toyota Highlander Hybrid, 4WD $650, 2008 Lexus LS 600h L Hybrid $450, 2008 Lexus RX 400h 2WD and 4WD $550.

Minimum Wage Increases: To $5.85 per hour beginning July 24, 2007. To $6.55 per hour beginning July 24, 2008. To $7.25 per hour beginning July 24, 2009.

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