



Financial Perspectives

TAKING TIME TO UNDERSTAND THE 2006 TAX CHANGES

Special points of interest:

- *You may be able to put more into your employers retirement plan.*
- *Tax brackets were adjusted for inflation.*
- *Standard Deduction and Personal Exemption amounts both increased.*

The Internal Revenue Code is not ordinarily thought of as a gift that keeps on giving, but, with 2005 having given way to 2006, it does contain several sections which provide for keeping more of what you will be earning and saving more for your retirement—on a tax-sheltered basis—out of what you keep.

They also provide, in some cases, for siphoning slightly more of what you earn—as your income increase with inflation—but these cases are far less numerous.

Therefore, as you make spending and saving plans for 2006, it should be helpful to note of significant federal income tax changes that became effective on New Year's Day, such as:

TAX RATES:

For married couples filing jointly and surviving spouses, for example, the 25 percent marginal tax rate begins to apply to those with taxable income of from \$61,301 to \$123,700, instead of \$59,401 to \$119,950, after adjustment for inflation. For single taxpayers, the 25 percent bracket was increased to

taxable income of \$30,651 to \$74,200, from \$29,701 to \$71,950. Similar changes were made for lower and higher tax brackets, and for married individuals filing separately, heads of household, and trusts and estates. (See IRS Form 1040 booklet and the Internal Revenue Service's Web site, <http://www.irs.gov>.)

SOCIAL SECURITY AND MEDICARE:

The Social Security tax rates for employers and employees were maintained at 6.2 percent, but the maximum amount of salaries and wages subject to the tax was raised from \$90,000 to \$94,200. The maximum earnings for a beneficiary under full retirement age increased from \$12,000 to \$12,480 annually.

The additional Medicare hospital tax on both employers and employees of 1.45 percent also was unchanged, but monthly Medicare Part B premiums went up from \$78.20 to \$88.50.

STANDARD DEDUCTION:

The standard deduction for married taxpayers who do not itemize deductions and who file



jointly, as well as for qualifying widows and widowers, was increased to \$10,300 from \$10,000, for single taxpayers and married taxpayers filing separately to \$5,150 from \$5,000, and for heads of household to \$7,550 from \$7,300.

DEDUCTIONS FOR USE OF CAR:

Standard rates per mile of deductions for use of a car for business purposes was changed to 44.5 cents from 40.5 cents in 2005's first eight months and 48.5 in the last four and for medical or moving purposes, to 18 cents from 15 and 22 cents, respectively. The rate for use of a car for charitable purposes was held at 14 cents per mile except for taxpayers using a vehicle only in connection with aid to Hurricane Katrina victims, whose deduction is 70 percent of the business mileage rate in effect on the date of the contribution.



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LONG-TERM CARE INSURANCE DEDUCTIONS:

Limits on annual deductions for premiums for eligible long-term care insurance policies were raised across the board—for those over 70, from \$3,400 to \$3,530; for those 61 to 70, from \$2,720 to \$2,830, and for younger taxpayers, significantly less.

EXEMPTIONS:

The amount that may be deducted for each exemption was increased from \$3,200 to \$3,300, as were the levels of adjusted gross income at which exemptions begin phasing out, from \$218,950 to \$225,750.

RETIREMENT PLAN CONTRIBUTIONS:

Just when slippage in average annual returns on stock and bond investments underscores

the importance of having more money at work for a retirement nest egg, the annual limit on contributions to IRS-qualified retirement plans has gone up again, making it easier.

Under salary reduction agreements permitting deferral of income taxes for contributions to 401(k)s, 403(b)s, SAR-SEPs, and the Thrift Savings Plan for federal employees (456(b)s), participants may now contribute \$15,000 instead of \$14,000, some or all of which may be matched by employers. The limit on additional “catch-up” contributions to 401(k), 403(b) and 457(b) plans by individuals of 50 or older was raised from \$4,000 to \$5,000, with a resulting higher limit on total contributions of \$20,000. The 2006 limit on contributions to traditional and Roth IRAs is \$4,000, the same as 2005; but the “catch-up” limit was lifted,

from \$500 to \$1,000.

GIFT TAX:

The annual exclusion from gift tax was increased from \$11,000 to \$12,000 per person.

ESTATE TAX:

The exclusion from federal estate tax of estates’ market values was raised from \$1.5 million for people dying in 2005 to \$2 million for people dying in 2006, and the maximum tax rate for taxable estates was reduced from 47 percent to 46 percent.

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