Taxation Tidbit: Itemized Deductions – Sales Tax & Bunching

The 2004 Jobs Act signed by the President in October provides a new option in calculating itemized deductions. Itemized deductions are those expenses individual taxpayers can subtract from adjusted gross income to determine their taxable income. The “major items” of itemized deductions are: home mortgage interest, state income and property taxes, and contributions to charities. The new wrinkle, added by the Jobs Act, is the option to deduct the greater of your state income tax or general sales tax paid.

The first decision you must make is to claim either the standard deduction or itemized deductions. For 2004, the standard deduction is $4,850 for single taxpayers and $9,700 for married joint filers.

To calculate the sales tax amount – the IRS provides a sales tax table for each state which will enable you to determine the appropriate sales tax amount based on the level of your income and number of exemptions. To this “table amount of sales tax” you can add sales tax paid on acquisitions of motor vehicles, boat, home, or home building materials. Thus, if you acquired some expensive “toys” during 2004 – you will definitely want to investigate this new option.

As a side note: taxpayers with itemized deductions just under or just over the standard deduction amount should give consideration to bunching their itemized deductions. For example, doubling the annual contribution to your favorite charities in one year insures a healthy itemized deduction for that year and you would still qualify for the standard deduction the following year. If you make house mortgage payments, you could also make your January payment in December of the year you are bunching your itemized deductions. Additionally, if you were going to purchase a personal vehicle or “expensive toy” you would want to purchase it in the year you are bunching your itemized deductions.

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