

The Legend Group

Your Partner in Retirement Planning

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2005 GUIDE FOR TAXPAYERS



- **BASIC TAX PLANNING**
- **RETIREMENT PLAN RULES**
- **SOCIAL SECURITY BENEFITS**
- **PAYING FOR HIGHER EDUCATION**

The Legend Group

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Securities offered through Legend Equities Corporation, Member NASD and SIPC

This guide is intended for informational purposes only. Although the information provided within this guide is believed to be true and accurate, The Legend Group makes no guarantee of this. The Legend Group nor its affiliates offer tax advice. It is recommended that you seek the services of a tax professional before making any decisions based on the information enclosed.

***§529 Plan Disclosures:** Under a “sunset provision”, these changes are scheduled to expire on December 31, 2010, in the absence of reenactment. As with all tax-related decisions, consult with your tax advisor.

Federal income tax on the earning and a 10% penalty may apply if monies within a §529 plan are not used for qualified educational expenses.

The estate planning information herein is general in nature and should not be considered legal or tax advice. Legend does not provide legal or tax advice. Laws of a particular state or a particular situation may affect this information. Consult with an attorney or tax professional regarding any specific legal or tax situation.

The Legend Group does not render tax or legal advice. For tax or legal advice specific to your situation, please consult your tax advisor or attorney.

Section 529 plans offered: Are Not FDIC Insured; May Lose Value; Are Not Bank Guaranteed.

Before investing in a §529 Plan, consider its investment objectives, risks, charges and expenses carefully. The official statement, which contains this and other information about the §529 Plan, can be obtained by contacting Legend Equities Corporation. Please read the official statement carefully before you invest or send money.

This requires that no more gifts be made to the Beneficiary during the five-year period, and that the gift is treated as a series of five equal annual gifts on the next federal gift tax return after the gift is made. If additional gifts are made, they may be subject to federal gift taxes.

Subject to an “add back” rule in the event of your death with in 5 years.

BRC-0021B/01-05

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BASIC TAX PLANNING

Most taxpayers wish to keep their tax bills as low as feasibly possible. But with all the complications of the Federal tax code – deductions, credits, exemptions, exclusions, phase-outs, etc. – you may feel overwhelmed. This Guide may help by delineating some of the tax planning basics.

TAX BRACKET

The Job and Growth Tax Relief Reconciliation Act (JGTRRA) of 2003 introduced many new rules, accelerated the timing of planned reductions in our tax rates, expanded the new 10% bracket, and provided some relief for the marriage penalty. Table 1 below reflects the individual tax rates for 2005.

Filing Status	Rate (%)	Taxable Income Brackets (\$)
Married Filing Jointly	10	0 - 14,600
	15	14,601 - 59,400
	25	59,401 - 119,950
	28	119,951 - 182,800
	33*	182,801 - 326,450
Head of Household	10	0 - 10,450
	15	10,451 - 39,800
	25	39,801 - 102,800
	28	102,801 - 166,450
	33*	166,451 - 326,450
Single	10	0 - 7,300
	15	7,301 - 29,700
	25	29,701 - 71,950
	28	71,951 - 150,150
	33*	150,151 - 326,450
Married Filing Separately	10	0 - 7,300
	15	7,301 - 29,700
	25	29,701 - 59,975
	28	59,976 - 91,400
	33*	91,401 - 163,225

*Income in excess of these amounts is taxed at 35%

CAPITAL GAINS

JGTRRA also lowered the maximum long-term capital rate as follows:

Tax Bracket	1/1/03–5/5/03	5/6/03–12/31/07	1/1/08–12/31/08	1/1/09 & On
25% or higher	20%	15%	15%	20%
10–15%	10%	5%	0%	10%

Tip: Consider gifting children over age 13 (and exempt from the “kiddie” tax) with appreciated assets. Assuming that the child’s bracket is otherwise lower than 25%, a sale of the asset in 2008 will not be taxed at all – a great way to contribute to a college fund.

Tip: The capital gains rate is not “across the board.” Gains from some assets, such as collectibles, remain subject to a 28% rate.

Tip: Deductions of capital losses against ordinary income continue to be limited to \$3,000 per year.

EXEMPTIONS

Personal and dependency exemptions may reduce your taxable income by as much as \$3,200 each in 2005. The exemption amount is indexed to inflation for subsequent years. However, deductions for exemptions are phased out if your adjusted gross income falls in the range indicated for your filing status in the table below and your exemptions will be nondeductible if your AGI exceeds the top of the applicable range.

2005 Personal Exemption			(table 2)
Filing Status	Phase out begins	Phase out ends	
Married Filing Jointly	\$218,950	\$341,450	
Head of Household	\$182,450	\$304,950	
Single	\$145,950	\$268,450	
Married Filing Separately	\$109,475	\$170,725	

Tip: A child you support qualifies as your dependent until reaching age 24 if s/he is a full-time student. A parent may be your dependent if you provide more than half of his/her support.

Tip: Your dependent child under the age of 17 may qualify you to claim a \$1,000 tax credit in 2005. As with exemptions, the child tax credit is reduced for those with higher incomes.

PLANNING STRATEGIES

Defer as much income as the limits allow into your employer’s retirement plan or in a traditional IRA.

If you change jobs, leave the assets accumulated in your employer’s retirement plan where they are or roll them over to an IRA or to your new employer’s plan. In 2001 you could only roll assets from one plan to a like plan but now you may roll assets to any plan your new employer maintains.

RETIREMENT PLAN RULES

Salary deferrals to §401(k), §403(b), §457, SAR-SEP IRA and SIMPLE IRA plans

Salary deferrals to these plans reduce your current taxable income dollar for dollar. Earnings on your deferrals grow tax deferred. You will pay taxes on the earnings and the amounts deferred when you take distributions from the plan. The following table shows the limits for salary deferrals in 2005 and 2006 to these plans.

Plan Type	2005		2006	
	Basic Lesser of	Catch-up*	Basic Lesser of	Catch-up*
§401(k)	\$14,000 or 100% of compensation	\$4,000	\$15,000 or 100% of compensation	\$5,000
§403(b)	\$14,000 or 100% of compensation	\$4,000**	\$15,000 or 100% of compensation	\$5,000**
SAR-SEP	\$14,000 or 100% of compensation	\$4,000	\$15,000 or 100% of compensation	\$5,000
SIMPLE IRA	\$10,000	\$2,000	\$10,000	\$2,500

* Employees who have attained age 50 are eligible for this catch-up.
 ** Employees who have 15 or more years of service with the current employer may be eligible for a further catch-up of up to \$3,000.

Contributions to IRAs

In 2005 the maximum contribution to an IRA (traditional or Roth) is the lesser of 100% of earned income or \$4,000 plus \$500 for an over age 50 catch-up. Contributions to traditional IRAs may be tax deductible, depending on whether you are an active participant in an employer’s retirement plan and on your tax filing status. See Table 4. But even if you are not eligible to deduct your contribution, you can still make the maximum contribution (lesser of 100% of earned income and the applicable year’s limit) – the earnings will still grow tax deferred. You

will pay taxes on the earnings but not the amounts that were nondeductible when you take distributions from the IRA.

Although contributions to Roth IRAs are not tax deductible, earnings accumulate tax deferred and may eventually be distributed tax free. You can qualify for the tax free treatment if you have had a Roth IRA for five years *and* you are 59½ or older. Tax free distributions after a five year holding period are also allowed for first time homebuying expenses (with a \$10,000 lifetime cap) or on account of disability or death. Check with your Legend Retirement Advisor to see if you are eligible to make a Roth IRA contribution in any particular year.

Year	Married Participants	Single Participants
2002	\$54,000 - \$64,000	\$34,000 - \$44,000
2003	\$60,000 - \$70,000	\$40,000 - \$50,000
2004	\$65,000 - \$75,000	\$45,000 - \$55,000
2005	\$70,000 - \$80,000	\$50,000 - \$60,000
2006	\$75,000 - \$85,000	\$50,000 - \$60,000
2007	\$80,000 - \$100,000	\$50,000 - \$60,000

If an active participant's spouse is not an active participant in any employer plan, a special dollar threshold applies in determining the deductible contribution for the non-active participant spouse. This threshold is \$150,000 - \$160,000.

Converting to a Roth IRA

You are eligible to convert a traditional IRA to a Roth IRA if your modified AGI (not including the converted amount) is \$100,000 or less. (If you are married, you must be filing jointly to qualify.) The amount converted must be included in your income in the year of conversion which could significantly increase your tax liability. This must be weighed with the eventual tax free distributions – your Legend Retirement Advisor can help you evaluate the possibility of conversion.

Retirement Plan Distributions

Before you take a distribution from a retirement plan, be sure to consider the tax consequences. Normally, all of the distribution will be taxable to you at your ordinary income tax rate in the year received. (Individuals who were at least 50 years old prior to 1/1/1986 may be eligible to use 10-year forward averaging for lump sum distributions from some types of plans.)

If you have terminated employment and want to take your retirement assets out of an employer's plan, consider rolling over to a traditional IRA. All or any portion of the distribution can be directly rolled over to your IRA or can be deposited within 60 days of receipt in your IRA. Either way, you will avoid current taxation.

Another consequence of taking receipt of a distribution after termination of employment is the 10% premature penalty exacted if you have not attained age 59½ or, if the plan is a §401(k) or §403(b), if you had not attained at least age 55 in the year you separated from service.

Tip: *You can avoid the 10% premature penalty for IRA distributions before you reach 59½ to pay medical expenses over 7.5% of your AGI, to pay for medical insurance if you have been unemployed for 12 weeks or more, for qualified higher education expenses or for first time homebuying expenses (with a lifetime cap of \$10,000), or on account of disability or death. You can also avoid the penalty by taking “substantially equal payments” for the longer of five years or until you reach age 59½. Ask your Legend Retirement Advisor for details.*

Current retirement plan law requires that you begin minimum distributions in the year you attain age 70½ (you actually have until April 1st of the following year to take this first minimum distribution). If you don't take a minimum distribution in a timely manner, a 50% excise penalty is levied so it is important to make sure you are in compliance each year. Your minimum is determined by dividing your account balance as of the previous calendar year end by a factor derived from the Uniform Table.

If you inherit a retirement plan account, generally you must begin minimum distributions from that account in the year following the owner's death. Once again, if you don't take a minimum distribution in a timely manner, a 50% excise penalty is levied. Your minimum is determined by dividing the account balance as of the previous calendar year end by a factor determined initially by your life expectancy in the year following the owner's death – after that first year, one is subtracted from the prior year's factor to determine each subsequent factor. This results in the entire account being distributed to you within a certain time period.

If you inherit a retirement plan account from your spouse, however, you have more options available. If your spouse had not attained age 70½ before death, you can delay taking minimums until s/he would have attained 70½ and/or you can roll the account over to an IRA or other retirement plan in your name, taking minimum distributions based on your age.

SOCIAL SECURITY BENEFITS

Earning Benefits

Once you join the labor force in the US, your employer(s) will withhold FICA taxes from your wages. Currently, 7.65% is withheld, consisting of 6.20% for Social Security and 1.45% for Medicare. In addition, your employer(s) must match your contributions. The Social Security portion applies to the first \$90,000 you earn in 2005 (indexed to inflation each year). The Medicare portion applies to all of your income – i.e., there is no cap.

If you are a self-employed individual, you must pay your own Social Security taxes and, since you are the employer and employee, you must pay the total (15.3% in all) using your net profit from self-employment as the basis of the calculation.

In either case, it is recommended that you check on your Social Security account from time to time to make sure you have been credited with the proper amounts. You can complete a *Request for Social Security Statement* at any time to verify the information. Call 800-772-1213 to request the form.

Your working career is measured in units called quarters of coverage. For every calendar quarter that you earn a certain amount (\$920 in 2005) you are credited one quarter of coverage. Generally, in order to become “fully insured” and to receive benefits at retirement, you must have accumulated 40 quarters of coverage – i.e., ten years in jobs covered by Social Security.

The amount of your Social Security retirement benefits will depend on how much you earned in your career. If you earn a low or average salary, for instance, your benefit will not be as high as the benefit paid to someone who earned a much higher salary in his career and therefore contributed more to their Social Security account during his working years.

Retirement income is only one benefit of the Social Security system. If you become disabled or die before you reach retirement age, you or your family will be entitled to other benefits, such as disability benefits, hospital insurance benefits and survivors’ benefits.

Year of Birth	Age for Full Benefits	Year of Birth	Age for Full Benefits
1937 or earlier	65 years	1943-1954	66 years
1938	65 years 2 months	1955	66 years 2 months
1939	65 years 4 months	1956	66 years 4 months
1940	65 years 6 months	1957	66 years 6 months
1941	65 years 8 months	1958	66 years 8 months
1942	65 years 10 months	1959	66 years 10 months
		1960 or later	67 years

Obtaining Benefits

Contact the Social Security Administration if any one of the following occurs:

- You are injured or sick and you will not be able to work for a year or longer;
- You are ready to retire at age 62 or older;
- You are within 3 months of age 65, even if you don’t plan to retire;
- Someone in your family dies; or
- You, your spouse or a dependent child suffers permanent kidney failure.

In 2005, you can retire with reduced Social Security benefits (80% of full benefits) at age 62 and with full benefits at age 65 and 6 months (see Table 5). The retirement age for full benefits will gradually increase to 67 as shown in Table 5. In addition, once this change is fully implemented, those who retire early will only receive 70% of full benefits.

Trying to estimate your retirement benefits is complicated. Your actual earnings record is compared to the national average to arrive at the primary insurance amount or PIA, which is then converted to your actual benefit. Starting in 2000, all workers age 25 or older should receive an annual statement of credited earnings and projected benefits at normal retirement age.

TAX ON SOCIAL SECURITY BENEFITS

A portion of a Social Security recipient’s benefit could be taxable if other sources provide too much income. See Table 6. Keep these income ranges in mind when you plan to take withdrawals from your retirement assets after your Social Security benefits begin. See IRS Publications 554 and 915.

	Single	Married/Joint
No tax on benefits	Provisional income under - \$25,000	Provisional income under - \$32,000
Includible in taxable income is lesser of 1/2 of benefits or 1/2 of income in excess of base amount	Provisional income from \$25,000 to \$34,000	Provisional income from \$32,000 to \$44,000
Up to 85% of benefits can be taxable	Provisional income over \$34,000	Provisional income over \$44,000
Provisional income is modified adjusted gross income plus 1/2 of Social Security benefits.		

WORKING AFTER RETIREMENT

If you are under full retirement age (currently age 65 and 6 months) when you start getting your Social Security payments, \$1 in benefits will be deducted for each \$2 you earn above the annual limit. For 2005, that limit is \$12,000 (\$1,000 per month). In the year you attain full retirement age, \$1 in benefits will be deducted for each \$3 you earn above a different limit, but only counting earnings before the month you reach the full benefit retirement age. For 2005, this other limit is \$31,800 (\$2,650 per month). Starting with the month you reach full retirement age, you will get your benefits with no limit on your earnings.

PAYING FOR HIGHER EDUCATION

Financing a higher education for yourself, your spouse or your dependents can be a very expensive undertaking. But Congress has provided certain tax incentives to encourage and support this effort. See IRS Publication 970 for more detailed information.

Hope Scholarship and Lifetime Learning Credits

These tax credits are available if you have paid any qualified tuition or related expenses at an eligible institution in the relevant tax year. You cannot claim both credits for the same student in one tax year. You could, however, claim the Hope Scholarship credit for one student and the Lifetime Learning credit for another student in the same tax year. The Hope Scholarship credit applies to your own expenses or those of your spouse or dependents but is limited to the first 2 years of higher education for a student attending at least half time. The maximum credit is \$1,500 for each eligible student; availability phases out for a taxpayer filing singly with an AGI of \$43,000 to \$53,000 (\$87,000 to \$107,000 for married filing jointly).

The Lifetime Learning credit is not restricted to the first 2 years of higher education and covers many undergraduate, graduate and professional degree courses as well as courses to acquire or improve job skills. The maximum credit in 2005 is \$2,000 per taxpayer return, regardless of the number of students. Your lifetime credit is calculated by multiplying 20% times the qualified education expenses you incur (capped at \$10,000). The credit is subject to the same phase out ranges as the Hope Scholarship credit.

Deduction for Student Loan Interest

In 2005, you can deduct up to \$2,500 of interest paid on qualified higher education loans. You can claim the interest deduction if your filing status is any filing status other than married filing separated AND no one else is claiming an exemption for you on his/her tax return AND you paid the interest on a qualified student loan. This deduction is phased out with a modified AGI between \$50,000 and \$65,000 (\$105,000 and \$135,000 on a joint return).

Coverdell Education IRAs

Anyone interested in contributing to a Coverdell Education IRA for a child under age 18 can do so if they meet income eligibility requirements, i.e., phasing out with a modified AGI between \$95,000 and \$110,000 (\$190,000 and \$220,000 on a joint return). In 2005, total contributions made for one child by all individuals cannot exceed \$2,000. In 2005, withdrawals may be used for elementary and secondary school tuitions, supplies, etc., in addition to higher education expenses.

Although Coverdell Education IRA contributions are not deductible, earnings are distributed tax free to pay the beneficiary's education expenses. No Hope or

Lifetime Learning credit can be claimed for the same expenses covered by a tax free Coverdell Education IRA distribution.

§529 College Tuition Plans

These plans guarantee a percentage of coverage for college education tuition for state specific colleges and universities. Under these plans the donor or the child has to be a resident of that state and the asset is owned by the child. Alabama, Colorado, Florida, Illinois, Kentucky, Maryland, Michigan, Mississippi, Nevada, New Mexico, South Carolina, Tennessee, Texas, Virginia, Washington and West Virginia currently have tuition paid plans.

§529 College Savings Plans *See front cover for disclosures

A college savings plan covers much more than just tuition. Withdrawals from college savings plans can pay for tuition, room and board, books and other required equipment and supplies. And these §529 plans do not tie the beneficiary to that state's schools – s/he can attend any college or university in the country and still draw on the account for qualified distributions. Most of these plans allow investment by residents of other states. (Using another state's plan, however, may effect how contributions and distributions are treated in the state of residence. More about this later.) Even though college savings plan contributions are counted as gifts to the beneficiary, the account remains under the control of the donor.

Each taxpayer can fund up to \$55,000 in one year per beneficiary without triggering gift tax consequences. This is considered an \$11,000 gift for the current year and the next four years. Overall contributions for any one beneficiary also cannot exceed a limit set by the plan, expressed by either total contributions or account value, that represents the projected expenses at a selected university. This overall limit includes any and all accounts established by any number of donors for one beneficiary under one plan.

If you contribute over \$11,000 for any one beneficiary, you must file Form 709 – the US Gift Tax Return – by your income tax filing deadline. Spreading out the contribution over more than one year is done by checking Box B on Schedule A and attaching information about the contribution.

As of 2001, the earnings on §529 plan accounts are distributed tax-free for qualified higher education expenses. In 2011, the earnings will again be taxable to the beneficiary if this provision of the Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001 is not made permanent by Congress.

Some states have opted to provide other tax incentives to those who save using that state's §529 plan by allowing a deduction against state income tax for contributions (e.g., Louisiana, New York, Oregon). A few states provide a partial matching contribution at certain low income levels (e.g., Louisiana and Michigan).