CLIENT LETTER

2011 Year-End Tax Planning for Individuals

Dear Client,

Year-end tax planning for 2011 presents many opportunities for individual taxpayers like you to reduce or defer your federal income tax liability. You may benefit from an "income shifting" strategy, which equalizes income over a two-year period by properly timing income and deductions. Although the tax cuts enacted in 2001 (EGTRRA) and 2003 (JGTRRA) were extended by the Tax Relief Act of 2010, many of the extended provisions are due to expire at the end of the 2011 or 2012 tax year. This uncertainty over the fate of the expiring tax provisions makes 2011 year-end tax planning a challenge.

Individual income tax provisions that were extended through 2012 by the Tax Relief Act of 2010 include:

- Reduced marginal tax rates of 10, 15, 25, 28, 33, and 35 percent
- Lower rates of zero- and 15-percent for capital gains, dividends and certain property held for more than five years
- Marriage penalty relief for taxpayers filing joint returns
- Repeal of exemption and itemized deduction phaseouts
- Various education-related incentives including (1) exclusion from income and employment taxes for employer-provided education assistance; (2) exclusion from income for National Health Service Corps Scholarship and Armed Forces Scholarship programs; (3) student loan interest deduction; (4) Coverdell Education Savings Accounts contribution limit and related provisions; and (5) American Opportunity Tax Credit (AOTC).
- Amendments made to the child tax credit by EGTRRA, including the increased credit amount of $1,000 per qualifying child
- Child and dependent care credit enhancements, including the increased maximum credit percentage of 35 percent, higher income limits, and increased maximum amount of qualifying expenses
- Increased maximum amount of the earned income tax credit and broader AGI phaseout ranges for taxpayers with three or more qualifying children

The following tax incentives, including some that were new with EGTRRA and others that were introduced when the Tax Relief Act of 2010 was enacted, are available in 2011. Barring further extension by Congress, they will not be available for 2012:

- Payroll tax cut for employees and self-employed individuals
- Tax-free IRA distributions to charity
- Increased (to 100%) exclusion for sales of qualified small business stock
- Above-the-line deduction for higher education tuition costs
- Above-the-line deduction for certain out-of-pocket classroom expenses

- Deduction for state and local general sales taxes in lieu of state and local income taxes
- Mortgage premium insurance deduction
- First-time homebuyer credit for purchase of a principal residence in the District of Columbia
- Plug-in conversion credit for vehicles converted from standard to plug-in electric drive motor vehicles
- Residential energy property credit for qualified energy efficient improvements and expenditures
- Increased AMT exemption amounts for individuals
- Nonrefundable tax credit offset of your entire regular and AMT tax liability

Other tax incentives have already expired. For example, the deduction provided by the 2010 Jobs Act for a self-employed individual’s health insurance costs in computing self-employment tax and the self-employment tax deduction was only available for the 2010 tax year.

For 2011, the maximum dollar limit for the adoption credit and the adoption assistance program was increased to $13,170 by the Tax Relief Act of 2010. If you are planning to expand your family through adoption, you should know that this limitation decreases to $13,360 in 2012. For tax years after 2012, the maximum dollar limit drops to $5,000 with no inflation adjustment ($6,000 for children with special needs).

As you may know, regulations governing basis and sales reporting by securities brokers were finalized early in 2011. What you may not know is that you have the right to choose the method that is used to determine your stock or other security's basis. If your broker uses the average basis method, you may affirmatively elect that method also. However, you may change from that method to another at any time during the year; for example, you may choose to specifically identify stock on a sale-by-sale basis. Alternatively, you may authorize your broker to select a basis determination method for you as allowed under general agency principles. The basis determination rules can be complicated, but they provide you with some flexibility in determining the gain or loss when you sell your securities.

If you make a contribution to your retirement plan before year-end, you can generally deduct at least a portion of the contribution amount to reduce your taxable income. An additional “catch-up” contribution is allowed for an individual who is over age 50 by the end of the tax year. Although Roth IRA contributions are not deductible because they are made after-tax, their earnings are tax-free.

Beginning in 2010, Roth IRAs were made available to all individuals, regardless of income amount or filing status. This enhancement enables you to make nondeductible IRA contributions, and periodically convert them into a Roth IRA. Remember, if you made a Roth IRA conversion in 2010 and chose to recognize the income ratably over two years, you must report half of the total amount in 2012.

With the year drawing to a close, now is an ideal time to review your tax situation and evaluate strategies that may help minimize your tax bill. Hopefully, this letter provides some alternatives that you would like to discuss in greater detail. Please call our office at your earliest convenience to arrange an appointment.

Sincerely,

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