

ANSPACH FINANCIAL GROUP

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Year-End Newsletter

November, 2010

Due to the inaction by Congress, tax law for 2010 and 2011 is still very uncertain.

The midterm elections have changed the Congressional landscape, with Republicans winning control of the House of Representatives and picking up seats in the Senate. Even so, it's still too early to know exactly how this will affect open tax issues for 2010 and 2011.

Specifically, when the "lame-duck" Congress meets on December, it must decide whether to "patch" the alternative minimum tax (AMT) for 2010 (increase exemption amounts, and allow personal credits to offset the AMT), as it has done in past years. It also must decide whether to retroactively extend a number of tax provisions that expired at the end of 2009. We will post updates on our Website as soon as new tax legislation is passed.

In addition, Congress must decide whether to extend the Bush tax cuts for some or all taxpayers. These and other Bush-era tax rules expire at the end of this year. Without Congressional action, individuals will face higher tax rates on their income, including capital gains. Also, unless Congress changes the rules, the estate tax, which isn't in effect this year, will return next year with a 55% top rate.

There has been significant new federal and state legislation effective for 2010 and 2011, and, in California, some new laws may be repealed by a Constitutional amendment approved by the voters in November.

We always encourage our clients to do whatever tax planning is appropriate for them. We also acknowledge the lack of tax law certainty for 2010 and beyond. Year-end planning—which always involves some educated guesswork—is a bigger challenge this year than in past years. Following are a few tips that will be useful regardless of Congressional action (or non-action).

Year-End Moves for Individuals

- Increase the amount you set aside for next year in your employer's health flexible spending account (FSA) if you set aside too little for this year. Don't forget that you cannot set aside amounts to get tax-free reimbursements for over-the-counter drugs, such as aspirin and antacids (2010 is the last year that FSAs can be used for nonprescription drugs).
- Realize losses on stock while substantially preserving your investment position. There are several ways this can be done. For example, you can sell the original holding, then buy back the same securities at least 31 days later. It may be advisable for us to meet to discuss the tax consequences of year-end trades you may be considering.
- Increase your withholding if you are facing a penalty for underpayment of federal estimated tax. Doing so may reduce or eliminate the penalty.
- Take an eligible rollover distribution from a qualified retirement plan before the end of 2010 if you are facing a penalty for underpayment of estimated tax and the increased withholding option is unavailable or won't sufficiently address the problem. Income tax will be withheld from the distribution and will be applied toward the taxes owed for 2010. You can then timely roll over the gross amount of the distribution, as increased by the amount of withheld tax, to a traditional IRA. No part of the distribution will be includible in income for 2010, but the withheld tax will be applied pro rata over the full 2010 tax year to reduce previous underpayments of estimated tax.

- Make energy saving improvements to your main home, such as putting in extra insulation or installing energy saving windows or buying and installing an energy efficient furnace, and qualify for a 30% tax credit. The total (aggregate) credit for energy efficient improvements to the home in 2009 and 2010 is \$1,500. Unless Congress acts, this tax break won't be around after this year. Additionally, substantial tax credits are available for installing energy generating equipment (such as solar electric panels or solar hot water heaters) to your home. This break stays on the books through 2016.
- Convert your traditional IRA into a Roth IRA if doing so is expected to produce better long-term tax results for you and your beneficiaries. Distributions from a Roth IRA can be tax-free, but the conversion will increase your adjusted gross income for 2010. However, you will have the choice of when to pay the tax on the conversion. You can either (1) pay the tax on the conversion when you file your 2010 return in 2011, or (2) pay half the tax on the conversion when you file your 2011 return in 2012, and the other half when you file your 2012 return in 2013.
- Take required minimum distributions (RMDs) from your IRA or 401(k) plan (or other employer-sponsored retired plan) if you have reached age 70 1/2. Failure to take a required withdrawal can result in a penalty of 50% of the amount not withdrawn. A temporary tax law change waived the RMD requirement for 2009 only, but the usual withdrawal rules apply in full force for 2010. So, individuals age 70 1/2 or older generally must take the required distribution amount out of their retirement account before the end of 2010 to avoid the penalty. If you turned age 70 1/2 in 2010, you can delay the required distribution to 2011, but if you do, you will have to take a double distribution in 2011—the amount required for 2010 plus the amount required for 2011. Think twice before delaying 2010 distributions to 2011—bunching income into 2011 might push you into a higher tax bracket or have a detrimental impact on various income tax deductions that are reduced at higher income levels.
- If you have a business or rental property, you may need to issue Forms 1099-MISC to report payments for business or rental services or rents paid on behalf of your business. Now is the time to secure the information necessary to prepare the forms in January. You can download Form W-9 from our Website under “useful forms & tools”. Send this “Request for Taxpayer Identification Number” to potential recipients before the end of the year. Please let us know as early in the year as possible if you want us to prepare the Forms 1099 for you.
- Make charitable contributions by year-end to get a 2010 deduction. Contributions must have a receipt or cancelled check to be deductible. Contributions over \$250 must also have a letter of acknowledgement from the charity, and additional documentation is required when your total non-cash contributions exceed \$500 for the year.
- Make annual exclusion gifts before year-end to save gift tax (and estate tax if it is reinstated). You can give \$13,000 in 2010 or 2011 to an unlimited number of individuals free of gift tax. However, you can't carry over unused exclusions from one year to the next. The transfers also may save family income taxes where income-earning property is given to family members in lower income tax brackets who are not subject to the “kiddie tax”.
- If you have dependent children who will be required to file income tax returns, be sure to discuss with them the importance of coordinating with you to determine who can take the dependency exemption. Our firm prepares a considerable number of amended tax returns each year because students eagerly file their own tax returns and claim their own personal exemption. Even when the students don't claim the dependency exemption, they may fail to comply with the “kiddie tax” requirement to compute the tax at the parents' higher tax rate.

Year-End Moves for Business Owners

- Hire a worker who has been unemployed for at least 60 days before year-end if you are thinking of adding to payroll soon. Your business will be exempt from paying the employer's 6.2% share of the Social Security payroll tax on the formerly unemployed new-hire for the remainder of 2010. Plus, if you keep that formerly unemployed new-hire on the payroll for a continuous 52 weeks, your business will be eligible for a nonrefundable tax credit of up-to-\$1,000 after the 52-week threshold is reached. This credit will be taken on the business's 2011 tax return. In order to be eligible, the formerly unemployed new-hire's pay in the second 26-week period must be at least 80% of the pay in the first 26-week period.
- Put new business equipment and machinery in service before year-end to qualify for the 50% bonus first-year depreciation allowance. Unless Congress acts, this bonus depreciation allowance generally won't be available for property placed in service after 2010. (Certain specialized assets may, however, be placed in service in 2011.)
- Make purchases qualifying for the \$500,000 business property expensing option. The maximum amount you can expense for a tax year beginning in 2010 is \$500,000 of the cost of qualifying property placed in service for that tax year. The \$500,000 amount is reduced by the amount by which the cost of qualifying property placed in service during 2010 exceeds \$2 million. Also, within the overall \$500,000 expensing limit, you can expense up to \$250,000 of qualified real property (certain qualifying leasehold improvements, restaurant property, and retail improvements). Note that at tax return time, you can choose not to use expensing (or bonus depreciation) for 2010 assets. This is something to consider if tax rates go up for 2011 and future years, and you'd rather have more deductions in future years.
- Set up a self-employed retirement plan if you are self-employed and haven't done so yet. We can advise you on which types of plans are available to you and which can provide the flexibility and maximum benefit for your needs.
- S Corporation owners have the opportunity to give themselves a salary bonus before year-end that can be used to cover withholding taxes and avoid underpayment penalties and ensure that the reasonable compensation requirements are met.
- Increase your basis in a partnership or S corporation if doing so will enable you to deduct a loss from it for this year. A partner's share of partnership losses is deductible only to the extent of his partnership basis as of the end of the partnership year in which the loss occurs. An S corporation shareholder can deduct his pro-rata share of an S corporation's losses only to the extent of the total of his basis in (a) his S corporation stock, and (b) debt owed to him by the S corporation.
- Consider whether to defer cancellation of debt (COD) income from the reacquisition of an applicable debt instrument in 2010. The business can elect to have the COD income included in gross income ratably over five tax years beginning with the fourth tax year following the tax year in which the repurchase occurs (i.e., beginning with 2014).
- Contractors will be able to form Limited Liability Companies (LLCs) effective January 1, 2011. The State Contractors License Board will be issuing Contractor's licenses to LLCs by January 1, 2012. A bond requirement (\$1,000,000 liability insurance or \$500,000 of liquid assets) must be met for a contractor to form a California LLC.

ANSPACH FINANCIAL GROUP *TAX AND FINANCIAL PLANNING*

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At Anspach Financial Group, we are committed to providing valuable and personalized services to each of our clients. We strive to solve complex tax and related issues by combining technical expertise with creative planning and problem solving. The experience, professional credentials and personal attention of our partners provide our clients with superior services at reasonable cost.

Calendar

Tax Due Dates

December 12	Final due date for property tax installment
December 31	Deadline for establishment of 401(k) and other qualified retirement plans for 2011
January 15	Fourth quarter 2010 estimated tax payments due
January 31	Fourth quarter payroll tax returns and annual payroll reports due Final date for mailing Forms 1099 to recipients and Forms W-2 to employees
March 15	Calendar year corporation tax returns due
April 11	Final due date for second property tax installment
April 18	Due date for individual, partnership, and calendar year fiduciary returns

Anspach Financial Group Calendar

December	Last opportunity for year-end tax planning
January 3	Tax organizers sent out