

# YEAR END TAX PLANNING TIPS

*Last Minute Strategies to Reduce Your 2011 Tax Bill*

## RETIREMENT CONTRIBUTION PLANNING:

- **IRA:** Remember to plan your cash flow to make an IRA contribution by April 17, 2012. The maximum 2011 IRA contribution is \$5,000. If you are age 50 or older by December 31, 2011, the maximum amount is \$6,000. Roth IRA contributions are restricted to adjusted gross income phaseout amounts, with complete phaseout at \$122,000 for single taxpayers and \$179,000 for married taxpayers. IRA plans can be set up as late as April 17, 2012.
- **401K:** The maximum 2011 contribution to your 401K is \$16,500. If you are age 50 or older by December 31, 2011 and your plan has been amended to allow it, the maximum amount is \$22,000.
- **SEP:** The maximum 2011 SEP contribution is \$49,000. You have until the due date of your tax returns, including extensions, in which to make the 2011 contribution and to set up the plan.
- **Roth IRA rollover:** There is no adjusted gross income limitation that restricts the rollover of a regular IRA into a Roth IRA. Funds rolled over from a regular IRA to a Roth IRA will be taxed under the regular IRA distribution rules, but no penalties will apply. For 2010 rollovers only, there was the option of deferring this tax to 2011 and 2012. This option has expired and a rollover in 2011 will be fully taxable in 2011.
- **Required minimum distribution (RMD):** Required minimum distributions must be made in 2011 for taxpayers that have reached age 70 ½. Failure to take a required withdrawal by 12/31/11 could result in a penalty up to 50% of the amount not withdrawn. You do have the option of delaying the required distribution to 2012, but if you do, you will have to take a double distribution in 2012 (this only applies to the year in which you turn 70 ½). With the possibility of higher tax rates in 2012, delaying the distribution could have a detrimental tax impact.

## DEDUCTION AND CREDIT PLANNING:

- **Medical expenses:** Amounts are only deductible if they exceed 7.5% of your adjusted gross income. (See the Business Expense Planning section for health insurance premiums for the self-employed person.) Only expenses that are paid or charged on a credit card by December 31, 2011 are eligible. Health Savings Account (HSA) contribution limits for 2011 are \$3,050 if single or \$6,150 for a family. For taxpayers aged 55 or older, the limits are \$4,050 if single and \$7,150 for a family.
- **Taxes:** State taxes are deductible on your federal tax return. State estimated income tax payments and property taxes that are due in 2012 can be paid in 2011. **CAUTION:** If you are subject to AMT (alternative minimum tax), there is no tax benefit by prepaying these taxes in 2011. In addition, this is the final year for claiming state sales tax in lieu of state income taxes as an itemized deduction (unless otherwise extended).
- **Mortgage interest:** Mortgage interest is deductible to the extent the proceeds were used to acquire, construct or improve your personal residence(s) to a maximum principal amount of \$1,000,000. In addition, you are allowed a home equity loan up to \$100,000 that does not have any usage requirements. Refinancing a mortgage and taking cash proceeds may impact the amount of interest that is deductible. No part of a home equity loan is deductible for AMT purposes to the extent that it is not used to acquire, construct or improve a residence. For 2011, qualified mortgage insurance premiums (PMI) may be deductible as mortgage interest, subject to a phaseout based on adjusted gross income. Unless extended, this provision is set to expire on December 31, 2011.
- **Energy efficient improvements:** Unless extended, 2011 is the final year to qualify for the 10% credit for energy efficient home improvements. This includes putting in extra insulation, energy saving windows or doors, or installing an energy efficient furnace. There is a lifetime credit limit of \$500 (\$200 for windows and skylights). There is also a credit for energy *generating* equipment that is equal to 30% of the total cost for property such as solar electric panels or solar water heaters (excluding solar heaters installed for heating a swimming pool or hot tub). This credit remains available through 2016.
- **Charitable contributions:** Now is the time to make both cash (cash, check, charge) and non-cash donations (clothing, household items). Be sure to ask for receipts to substantiate all amounts for both non-cash donations and cash donations. Cash donations can also be substantiated by canceled checks or bank

statements that verify the charity's name, date and amount. Donations charged on a credit card by December 31, 2011 are eligible as a deduction for 2011. Donations of cars, boats, and airplanes need to be reported at their fair market value. If fair market value is more than \$500 and the charity does not keep the vehicle, your deduction is limited to the amount for which the charity later sells the vehicle. Charitable contributions have varied limitations based on your adjusted gross income. Any amounts not eligible due to these limitations can be carried forward for five years. Any donation deduction amount for cars, boats and airplanes of more than \$500 requires your tax return to include a statement from the charity identifying the vehicle and stating the amount for which it was sold. Be sure to obtain these statements from the charity and include them with your organizer package.

#### **BUSINESS EXPENSE PLANNING:**

- **Health insurance premiums:** As a self-employed person, you are able to deduct 100% of health insurance premiums paid for yourself, your spouse, and your dependents. This also includes dental and vision insurance, plus limited amounts for long-term care insurance. It does not include disability or life insurance.
- **Depreciation:**
  - **"Section 179 deduction"** The increased depreciation limits resulting from the "2008 Economic Stimulus Act" continue for 2011. Equipment purchases are eligible for a "Section 179 deduction" of up to \$500,000 for 2011 (\$139,000 in 2012). The equipment must be "placed in service" by December 31, 2011. Note that purchasing too much equipment (over \$2,000,000 in 2011 and \$560,000 in 2012) will restrict your total "Section 179 deduction".
  - **100% bonus depreciation** A special 100% depreciation allowance can be deducted for certain kinds of property placed in service in 2011. To be eligible, the equipment must be "original use" (not used).
  - **Vehicle limits** Luxury vehicles are limited to a maximum deduction of \$11,060 for autos and \$11,260 for light trucks or vans for 2011 (this includes bonus depreciation). An SUV placed in service in 2011 and weighing between 6,000 and 14,000 pounds gross vehicle weight (GVW) is limited to a maximum "Section 179 deduction" of \$25,000 for 2011, with the remaining cost depreciated over a 5 year life.

#### **INVESTMENT PLANNING:**

- **Capital gains and losses:** Income that results from the sales of stock, investment property, and rental property (above depreciation recapture) is considered capital. Long-term gains result from sales that have been held over one year. The federal income tax rate on long-term capital gains is limited to 15% in 2011 and 2012 (unless the applicable provision is extended, this will increase in 2013 to 20% or 18% for assets held over 5 years). Losses are deductible to the extent of gains plus \$3,000. Any excess loss is carried over to subsequent years for an unlimited amount of time. **CAUTION:** If you are subject to AMT (alternative minimum tax), the capital gains rate benefit may be partially offset by an increased AMT liability.
- **Gifts:** Amounts transferred up to \$13,000 per person per year are considered exempt from gift taxation. Amounts given above this amount require the "giver" to file a gift tax return and either elect to use part of their "life-time exclusion" or to pay a gift tax. This tax return is due April 17, 2012 or October 15, 2012 if an extension is filed. There are no requirements for the recipient of the gift. The 2012 limit is also \$13,000.
- **Social security:** Up to 85% of social security benefits may be taxable depending on your modified adjusted gross income. For one-time events you should give consideration to the year of receipt. Please call us for an individualized analysis.
- **Net operating loss (NOL):** A net operating loss occurs if certain non-personal income and expenses create a negative amount. This loss is first carried back to the previous two years by filing an amended tax return to claim a refund and then forward for twenty years, unless an election is made to forgo the carry back period and only go forward.

#### **ALTERNATIVE MINIMUM TAX:**

- Some of the standard year-end planning ideas will not reduce tax liability if you are subject to the alternative minimum tax (AMT) because different rules apply. Because of the complexity of the AMT, we recommend a personalized analysis of your AMT exposure, which will include the preparation of a tax projection report.