



2011 Tax Update and Tax Planning Strategies

SAVE TAX NOW...
While you still can

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Director & Tax Department
Manager

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The Agenda

- ◆ Tax law update
- ◆ Tax planning basics
- ◆ Charitable giving
- ◆ Investing
- ◆ Business



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Tax Law Update

◆ 2010 Tax Relief Act December 2010.

- Income tax rates retained for 2011 and 2012 top rate 35%, 15% on qualified dividends and long term capital gain property.
- Employees and self employed receive reduction in social security tax in 2011 of 2%.
- Two year AMT patch 2010 and 2011
- Key tax credits for families (Child Tax Credit and American Opportunity Credit)
- Business write off of 100% of new equipment and machinery purchases (9/8/2010 – 12/31/2011)

Tax Law Update - Continued

◆ Small Business Jobs Act of 2010 (Covered in seminar last year)

- Increased Section 179 expensing Limit \$500K on \$2MM (2010 and 2011)
- Qualified real property expensing \$250K limit (2010 and 2011) Leasehold Improvement, Restaurant, Retail Improvement.
- 50% Bonus depreciation. (through 9/7/2010)
- Increased start-up expense deduction 10K
- Unused eligible small business credits could be carried back 5 years and can offset AMT liability.

Tax Law Update - Continued

◆ 2011 - Proposals

- October 10 **American Jobs Act** Introduced in the senate
 1. It would have extended through 2012 100% bonus first year depreciation.
 2. Cut employer portion of social security tax from 6.2% to 3.1%.
 3. New hires after enactment date there would be a tax credit of up to \$4,000 for hiring workers who have been looking for a job for 6 months.
- Paid for by 5.6% surtax on MAGI in excess of 1MM

5

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Tax Law Update - Continued

◆ 2011 - Proposals

- October 17 - **Teachers and First Responders Back to Work Act 2011** - 30 Billion to hire and retain teachers, 5 Billion to hire and retain first responders. Paid for by .5% surtax on MAGI in excess of 1MM begins after 12/31/2012.
- October 26 - **Rebuild America Jobs Act** - 50 Billion to rebuild roads, rails and airports, plus 10 Billion for a National Infrastructure Bank. Paid for by .7% surtax on MAGI in excess of 1 MM.
- October 27 - Tax Reform proposal to include a lower corporate tax rate (35% to 25%) and shift to a territorial tax regime.

6

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TAX PLANNING BASICS

Tax planning shouldn't be just a year end activity



Timing of income and expenses is key

- ◆ Smart timing can reduce your tax liability
- ◆ Poor timing can unnecessarily increase it

TIP: If you don't expect to fall victim to the AMT this year or next, consider deferring income to 2012 and accelerating deductible expenses into 2011



Know which items to time - Individuals

◆ On the income side

- Bonuses and self-employment income
- U.S. Treasury bill income
- Real estate or other nonpublicly traded property sales
- Retirement plan distributions, if not required

◆ On the expense side

- State and local income taxes
- Real estate taxes
- Mortgage or margin interest
- Charitable contributions

Keep in mind: Higher-income taxpayers may have an opportunity for some larger deductions through 2012

AMT triggers

- ◆ State and local income tax deductions
- ◆ Real estate and personal property tax deductions
- ◆ Interest on home equity loan or line of credit not used to buy, build or improve your principal residence
- ◆ Miscellaneous itemized deductions subject to 2% of AGI floor
- ◆ Long-term capital gains and dividend income
- ◆ Accelerated depreciation adjustments and related gain or loss differences when assets are sold
- ◆ Tax-exempt interest on certain private-activity municipal bonds
- ◆ Incentive stock option exercises

Education credits and deductions

◆ American Opportunity credit

- Covers 100% of first \$2,000 of tuition and related expenses; 25% of next \$2,000 of expenses
- Maximum credit is \$2,500 per year for first four years of college
- Extended through 2012

◆ Lifetime Learning credit

- Up to \$2,000 per tax return for college expenses beyond first four years

◆ Tuition and fees deduction

- Up to \$4,000

◆ Student loan interest deduction

- Up to \$2,500 of interest per tax return



Estimated payments

◆ Make sure estimated payments or withholding equals at least 90% of 2011 tax liability or 110% of 2010 tax liability

- 100% of 2010 tax liability if 2010 AGI was \$150,000 or less or, if married filing separately, \$75,000 or less

◆ Use annualized installment method

- Best for those who have large variability in income per month

◆ Estimate tax liability and increase withholding

- If you've underpaid, withhold the tax shortfall from your salary or year end bonus



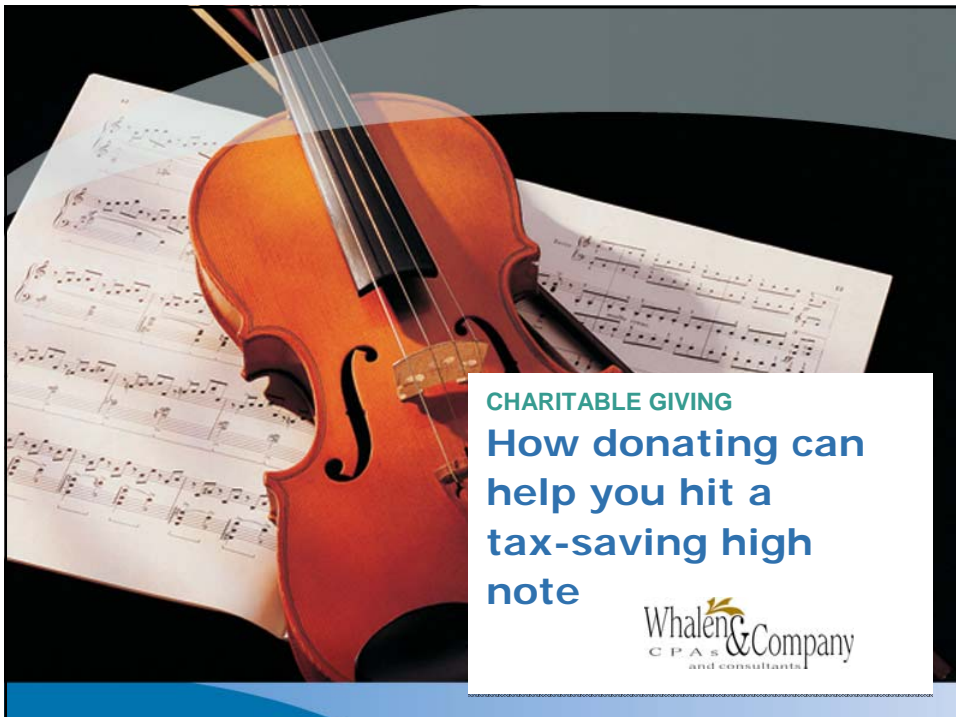
Employment taxes

- ◆ **Social Security and Medicare taxes**
 - Apply to earned income, such as salary and bonuses
- ◆ **For 2011 only**
 - Employee portion of Social Security tax reduced to 4.2% (from 6.2%)
 - Maximum taxable wage base for Social Security taxes is \$106,800
 - Maximum tax savings from tax break is \$2,136 ($\$106,800 \times .02$)
- ◆ **Even high-income taxpayers can enjoy maximum benefit of this tax break**

Warning! All earned income is subject to the 2.9% Medicare tax

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A photograph of a violin and sheet music. The violin is in the foreground, and the sheet music is open behind it. The background is dark with a blue gradient at the bottom.

CHARITABLE GIVING
How donating can help you hit a tax-saving high note

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Cash donations

◆ Gifts of cash

- Under \$250: gift supported by canceled check, credit card receipt or written communication from charity
- \$250 or over: gift substantiated by the charity
- Deductions for cash gifts can't exceed 50% of AGI (30% for nonoperating private foundations); excess can be carried forward five years

Keep in mind: Charitable contributions are allowed for AMT purposes, but your tax savings may be less

Stock donations

◆ Donating publicly traded stock held more than one year

- No tax on gain from selling the assets
- Can deduct current fair market value
- Deduction limit is 30% of AGI for gifts to charities (20% for nonoperating private foundations)
- In certain situations, it may be better to deduct tax basis rather than fair market value

TIP: Don't donate stock worth less than your basis; sell it and donate the proceeds

Other types of donations

Type of donation	Ordinary-income property	Tangible personal property used for tax-exempt function	Tangible personal property <i>not</i> used for tax-exempt function	Use of property	Vehicle <i>sold</i> by the charity	Vehicle <i>used</i> by the charity
Examples	Stocks or bonds held one year or less, inventory	Artwork donated to museums	Artwork donated to charity auction	Use of vacation home; loan of artwork	Charity sells vehicle within specified period	Vehicle used to deliver meals to elderly
Deduction	Lesser of fair market value (FMV) or tax basis	FMV	Your basis	Generally no deduction	Amount charity receives from sale	FMV

Note: Additional limits apply. Please check with your tax advisor.



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Distribute IRA funds to charity

- ◆ Distribute up to \$100,000 from IRA directly to charity
 - Must be age 70½ or older
- ◆ No charitable deduction allowed for amounts that would have been taxable
 - You save the tax you would otherwise have owed
- ◆ Donation from traditional IRA can help satisfy your required minimum distribution

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Making gifts over time

- ◆ Private foundation gives you significant control over how your donations will be used
- ◆ Donor-advised fund (DAF) enables you to influence how your donations are spent; avoids a foundation's tight rules and high expenses

Keep in mind: To deduct a DAF contribution, obtain written acknowledgment from sponsoring organization that it has exclusive legal control over assets contributed



INVESTING
Consider locking in lower rates while they're still available

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Capital gains tax and timing Short Term vs. Long Term

Time – not timing – is generally the key to long-term investment success



Timing can have a dramatic impact on tax consequences of investment activities

21

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Using unrealized losses to absorb gains

- ◆ **Appreciating investments that don't generate current income aren't taxed until sold**
 - Defer tax
 - Possibly allow you to time sale to your advantage

- ◆ **If you've cashed in big gains**
 - Look for unrealized losses in your portfolio
 - Sell them to offset gains



22

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Wash sale rule

- ◆ With the wash sale rule, you won't take a loss on a security if you buy a substantially identical security within 30 days before/after selling the security that created the loss
- ◆ Loss recognized only when replacement security is sold.

TIP: To avoid the wash sale rule, buy securities of a different company in the same industry or shares in a mutual fund that holds securities like the ones you sold

Loss carryovers

- ◆ **Capital losses are netted against capital gains to determine capital gains tax liability**
 - Deduct up to \$3,000 of losses per year against ordinary income
 - Carry forward excess losses to future years
- ◆ **Determine if you have excess losses**
 - Time sales of other investments before year end to achieve your tax-planning goals

Loss carryovers — the tax perspective

- ◆ **If not enough gains to absorb more losses**
 - May not make sense to sell more investments at a loss
 - If you hold on to the investment, it may recover its lost value
- ◆ **If you're ready to drop a poorly performing stock**
 - Don't hesitate solely for tax reasons



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Tax-deferral strategies for investment property

- ◆ **Installment sale**
 - Defer gains by spreading over several years as you receive the proceeds
 - Ordinary gain is recognized in year of sale, even if no cash is received
- ◆ **Section 1031 exchange**
 - Allows you to defer paying tax on gain until you sell replacement property
 - Restrictions and significant risks apply



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Roth IRAs

- ◆ Qualified distributions are tax-free, but aren't required during your life
- ◆ Contributions don't reduce current-year taxable income
- ◆ Roth conversions
 - Tax on conversion
 - Tax-free distributions
 - Estate planning opportunities
 - AGI limit on conversion eliminated



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A woman with blonde hair, wearing a grey business suit, is smiling and talking on a mobile phone. The background is a blurred office setting with a window showing a city view.

BUSINESS

Taking advantage of new, extended and long-standing tax breaks

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Projecting income

◆ Allows you to time income and deductions to your advantage

- Deferring income to next year
 - If using cash method of accounting, defer billing for products or services
 - If using accrual method, delay shipping products or delivering services
- Accelerating deductions into current year
 - If cash-basis taxpayer, make estimated state tax payment before Dec. 31
 - Beware of AMT

Keep in mind: Think twice about these strategies if you're experiencing a low-income year — their negative impact on your cash flow may not be worth the potential tax benefit

Understanding depreciation

◆ MACRS

- Generally more advantageous than straight-line method
- Larger deduction in early years of asset's life

◆ Bonus depreciation

- 50% bonus depreciation for qualified assets placed in service from Jan. 1, 2008, through Sept. 8, 2010
- 100% bonus depreciation for assets placed in service from Sept. 9, 2010, through Dec. 31, 2011
- 50% bonus depreciation for assets placed in service from Jan. 1, 2012, through Dec. 31, 2012

◆ No bonus depreciation after Dec. 31, 2012

Section 179 expensing election

- ◆ **Allows you to write off rather than depreciate asset purchases**
 - Deduct up to \$500,000 of purchases
 - Deduction phases out dollar-for-dollar when 2011 asset purchases exceed \$2 million
 - Limits are scheduled to go down in 2012
 - Only Section 179 expensing can be applied to *used* assets



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Vehicle-related tax breaks

- ◆ **Deduct out-of-pocket expenses (fuel, insurance, depreciation, etc.) or mileage**
 - 51 cents per business mile in first half of 2011
 - 55.5 cents per mile for second half of 2011
- ◆ **Purchases of new or used vehicles may be eligible for Sec. 179 expensing**
- ◆ **New vehicles may be eligible for bonus depreciation**
- ◆ **Depreciation limit is \$3,060 for autos placed in service in 2011**
 - Increased by \$8,000 for autos eligible for bonus depreciation
- ◆ **Additional rules and limits apply**

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Cost segregation study

- ◆ Identifies property components and related costs that can be depreciated faster
- ◆ Increases your current deductions
- ◆ Qualifying assets include
 - Decorative fixtures
 - Security equipment
 - Parking lots
 - Landscaping
 - Architectural fees allocated to qualifying property



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Manufacturers' deduction

- ◆ Deductible amount is 9% of the lesser of qualified production activities income or taxable income, limited by W-2 wages paid
- ◆ Available also to businesses engaged in *nonmanufacturing* activities, such as
 - Construction
 - Engineering
 - Architecture
 - Computer software production
 - Agricultural processing
- ◆ Deduction can be used against the AMT

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Inventory donations

- ◆ Enhanced deductions for certain donations have been extended through 2011
- ◆ Types of donations include
 - Food inventory
 - Book inventory for public schools
 - Computer inventory for educational purposes
- ◆ Rules are complex
- ◆ Make contribution by Dec. 31, 2011, to take advantage of enhanced deduction



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More tax breaks

- ◆ NOL deduction
 - NOL can be carried back two years to generate current tax refund
 - Any loss that's not absorbed is carried forward up to 20 years
 - Additional rules apply
- ◆ Tax credits
 - Research credit extended through 2011
 - Work Opportunity credit extended through 2011
 - Equals 40% of first \$6,000 of wages paid to qualified employees
 - \$12,000 for wages paid to qualified veterans
 - HIRE Act retention credit available through 2011
 - Workers must be retained for 52 consecutive weeks

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Health care tax credit

◆ Through 2013

- Available for employers with 10 or fewer FTEs, who on average earn less than \$25,000 per year
- Partial credits available to businesses with fewer than 25 FTEs, who on average earn less than \$50,000

◆ Credit amount

- Maximum credit is 35% of premiums paid by employer
- Employer must contribute at least 50% of total premium



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Business structure

Pass-through entity or sole proprietorship	C corporation
One level of taxation: The business's income flows through to the owner(s).	Two levels of taxation: The business is taxed on income, and then shareholders are taxed on any dividends they receive.
Losses flow through to the owner(s).	Losses remain at the corporate level.
Top individual tax rate is 35%.	Top corporate tax rate is generally 35%. Income distributed as dividends is taxed a second time, generally at 15%.

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Consider the benefits of tax planning

- ◆ Your Whalen & Company advisor excels at helping you to plan for and minimize your taxes and achieve your financial goals.
- ◆ We welcome the opportunity to discuss your needs and answer your questions.
- ◆ Please let us know how we can be of assistance.

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39



**Thank you
for attending**

We are looking forward to assisting
you!

Patrick McClary, CPA

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