Arthur Lander C.P.A., P.C.
A professional corporation

3130 N. 10th Street
Arlington, Virginia 22201
phone: (703) 486-0700
fax: (703) 527-7207

# 2011 Year-End Tax Planning

December 3, 2011

Dear Client,

This letter highlights several potential tax-saving opportunities for you to consider. I would be happy to meet with you to discuss specific strategies.

## IRA, Retirement Savings Rules for 2011

More tax-saving opportunities continue for retirement planning in 2011.

*Traditional IRAs:* Individuals who are not active participants in an employer pension plan may make deductible contributions to an IRA. The annual deductible contribution limit for an IRA for 2011 is $5,000. Individuals who are active participants in a plan may also make deductible contributions to an IRA, but limited in amount depending on their AGI. For 2011, the AGI phase-out range for deductibility of IRA contributions is between $90,000 and $110,000 of modified AGI for married filing jointly. Above these ranges, no deduction is allowed.

For 2011, a $1,000 "catch-up" contribution deduction is allowed for taxpayers age 50 or older by the close of the taxable year who meet the other qualifications for IRA deductions. Thus, the total deductible limit for these individuals may be as high as $6,000.

In addition, an individual will not be considered an "active participant" in an employer plan simply because the individual's spouse is an active participant for part of a plan year. Thus, you may be able to take the full deduction for an IRA contribution regardless of whether your spouse is covered by a plan at work, subject to a phase-out if your joint modified AGI is $159,000 to $169,000. Above this range, no deduction is allowed.

*Roth IRAs:* This type of IRA permits nondeductible contributions of up to $6,000 a year. Earnings grow tax-free, and distributions are tax-free provided no distributions are made until more than five years after the first contribution and the individual has reached age 59 ½ . Distributions may be made earlier on account of the individual's disability or death. The maximum contribution is phased out for persons with AGI above certain amounts: $169,000 to $179,000 for joint filers, and $107,000 to $122,000 for single filers (including heads of households). For 2011, a $1,000 "catch-up" contribution is allowed for taxpayers age 50 or older by the close of the taxable year, making the total limit $6,000 for these individuals.

*Roth IRA Conversion Rule:* Funds in a traditional IRA may be rolled over into a Roth IRA. Such a rollover, however, is treated as a taxable event, and you will pay tax on the amount converted. No penalties will apply if all the requirements for such a transfer are satisfied.

For 2011, there is no AGI limit for taxpayers wishing to convert their traditional IRA.

*401(k) Contribution:* The 401(k) elective deferral limit is $16,500 for 2011. If your 401(k) plan has been amended to allow for catch-up contributions for 2011 and you will be 50 years old by December 31, 2011, you may contribute an additional $5,500 to your 401(k) account, for a total maximum contribution of $22,000 ($16,500 in regular contributions plus $5,500 in catch-up contributions).

> *For the self-employed:* If you are self-employed, your business is allowed to contribute up to a 25% match of your salary. The maximum of all contributions for a self-employed person to a 401(k) plan is $49,000 after both employee and business contributions. For example, if your salary is $122,000 for 2011 and you personally make a $16,500 contribution, you can reach the max contribution of $47,000 if your business contributes $30,500.

*SIMPLE Plan Contribution:* The SIMPLE plan deferral limit is $11,500 for 2011. If your SIMPLE plan has been amended to allow for catch-up contributions for 2011 and you will be 50 years old by December 31, 2011, you may contribute an additional $2,500.

*Catch-Up Contributions for Other Plans:* If you will be 50 years old by December 31, 2011, you may also contribute an additional $5,500 to your 403(b).

**** Before the year end 401K plans and defined benefit plans must be set up. ****

**Deferring Income to 2011**

One of the unknowns is what the changes will be in the tax laws for 2012. The typical advise is to defer income.

If you expect your AGI to be higher in 2011 than in 2012, or if you anticipate being in the same or a higher tax bracket in 2011, you may benefit by deferring income into 2012. Some ways to defer income include:

*Delay Billing:* If you are self-employed, delay year-end billing to clients so that payments will not be received until 2012.

*Interest and Dividends:* Interest income earned on Treasury securities and bank certificates of deposit with maturities of one year or less is not includable in income until received. To defer interest income, consider buying short-term bonds or certificates that will not mature until next year. If you have control as to when dividends are paid, arrange to have them paid to you after the end of the year.

**Deduction Planning**

Deduction timing is also an important element of year-end tax planning. Deduction planning is complex, however, due to factors such as AGI levels and filing status. If you are a cash-method taxpayer, remember to keep the following in mind:

*Deduction In Year Paid:* An expense is only deductible in the year in which it is actually paid.

*Payment By Check:* Date checks before the end of the year and mail them before January 1, 2012.

*Promise To Pay:* A promise to pay or providing a note does not permit you to deduct the expense. But you can take a deduction if you pay with money borrowed from a third party. Hence, if you pay by **credit card** in 2011, you can take the deduction even though you won't pay your credit card bill until 2012.

*Itemized deductions and personal exemption No Phase Out:* You get the full benefit of your exemption and itemized deductions without any reduction if you income is over certain amounts.

Certain deductions may be claimed only if they exceed a percentage of AGI: 7.5% for medical expenses, 2% for miscellaneous itemized deductions, and 10% for casualty losses.

*Standard Deduction Planning:* Deduction planning is also affected by the standard deduction. For 2011 returns, the standard deduction is $11,600 for married taxpayers filing jointly, $5,800 for single taxpayers, and $8,500 for heads of households.

If your itemized deductions are relatively constant and are close to the standard deduction amount, you will obtain little or no benefit from itemizing your deductions each year. But simply taking the standard deduction each year means you lose the benefit of your itemized deductions. To maximize the benefits of both the standard deduction and itemized deductions, consider adjusting the timing of your deductible expenses so that they are higher in one year and lower in the following year.

*Medical Expenses:* Medical expenses, including amounts paid as health insurance premiums, are deductible only to the extent that they exceed 7.5% of AGI. Consider bunching medical expenses into years when your AGI is lower.

If you are self-employed, consider hiring your spouse and deducting all of the family medical expenses using a Medical Reimbursement Program.

*Charitable Contributions:* Consider making your charitable contributions at the end of the year. You can use a credit card to charge donations in 2011 even though you will not pay the bill until 2012.

A mere pledge to make a donation is not deductible, however, unless it is paid by the end of the year. Note, however, for claimed donations of cars, boats and airplanes of more than $500, the amount available as a deduction will significantly depend on what the charity does with the donated property, not just the fair market value of the donated property. If the organization sells the property without any significant intervening use or material improvement to the property, the amount of the charitable contribution deduction cannot exceed the gross proceeds received from the sale.

**Health Savings Accounts and Flexible Spending Accounts.**

For those of you who are participating in a health insurance program with a high deductible you can still make a contribution to your Health Savings Account of $3,050 for individuals and $6,150 for families.

Please remember to use or you will lose the money in the Flexible Spending Account.

**Business Deductions**

*Self-Employed Health Insurance Premiums:* Self-employed individuals are allowed to claim 100% of the amount paid during the taxable year for insurance that constitutes medical care for themselves, their spouses and dependents as an above-the-line deduction, without regard to the 7.5% of AGI floor.

*Equipment Purchases:* If you are in business and purchase equipment, you may make a "Section 179 Election," which allows you to expense (i.e., currently deduct) otherwise depreciable business property. There is also available a 100% bonus depreciation for property that may not qualify for the Section 179 election.

*NOL Carryback Period:* If your business suffers net operating losses in 2011, you may apply those losses against taxable income going back two tax years. Thus, for example, the loss could be used to reduce taxable income—and thus generate tax refunds—for tax years as far back as 2009.

**Education and Child Tax Benefits**

*Child Tax Credit:* A tax credit of $1,000 per qualifying child under the age of 17 is available on this year's return. The credit is phased out at a rate of $50 for each $1,000 (or fraction of $1,000) of modified AGI exceeding the threshold.

*American Opportunity Tax Credit (AOTC) and Lifetime Learning Credit*: The maximum AOTC credit is $1,800 (100% on the first $1,200, plus 50% of the next $1,200) for qualified tuition and fees paid on behalf of a student (i.e., the taxpayer, the taxpayer's spouse, or a dependent) who is enrolled on at least a half-time basis. The credit is available for only the first two years of the student's post-secondary education.

The Lifetime Learning credit maximum in 2011 is $2,000 (20% of qualified tuition and fees up to $10,000). A student need not be enrolled on at least a half-time basis so long as he is taking post-secondary classes to acquire or improve job skills. As with the HOPE credit, eligible students include the taxpayer, the taxpayer's spouse, or a dependent.

For 2011, both the HOPE credit and the Lifetime Learning credit are phased out once your income reaches a certain limit.

*Qualified Tuition Deduction* up to $4,000 is available in 2011 for those taxpayers with limited income.

Rules are in effect to coordinate education provisions to prevent double benefits.

*Student Loan Interest*: You may be eligible for an above-the-line deduction for student loan interest paid on any "qualified education loan." The maximum deduction is $2,500. The deduction for 2011 is phased out at a modified AGI level between $110,000 and $140,000 for joint filers, and between $55,000 and $70,000 for individual taxpayers.

**Tax credits for home improvements**

If you have not taken the credit in past years there is still time in 2011 to use this benefit for insulation, heating and air conditioning, and exterior windows up to $500.

**Investment Planning**

The following rules apply for most capital assets in 2011:

- Capital gains on property held one year or less are taxed at an individual's ordinary income tax rate.

- Capital gains on property held for more than one year are taxed at a maximum rate of 15% (0% if an individual is in the 10% or 15% marginal tax bracket).

*Timing of Sales:* You may want to time the sale of assets so as to have offsetting capital losses and gains. Capital losses may be fully deducted against capital gains and also may offset up to $3,000 of ordinary income ($1,500 for married filing separately). In general, when you take losses, you must first match your long-term losses against your long-term gains, and short-term losses against short-term gains. If there are any remaining losses, you may use them to offset any remaining long-term or short-term gains, or up to $3,000 (or $1,500) of ordinary income.

*Dividends:* Qualifying dividends received in 2011 are subject to rates similar to the capital gains rates. Therefore, qualifying dividends are taxed at a maximum rate of 15%. Qualifying dividends includes dividends received from domestic and certain foreign corporations.

If you have any questions, please do not hesitate to call. I would be happy to meet with you at your convenience to discuss the strategies outlined above. There is still time to implement these strategies to minimize your 2011 tax liability.

Very truly yours,

Arthur Lander