D.K. Briery, CPA, PLC

"The Tax Pro You Can Trust"

12627 San Jose Boulevard, Suite 601 904) 880-3200
Jacksonville, FL 32223 www.dkbrierycpa.com

YEAR-END INDIVIDUAL TAX NEWSLETTER

Dear Valued Client, November 1, 2010

By now, you have probably heard the rumbling of the upcoming tax law changes and the significant impact they may have if the currently scheduled changes actually take place. However, no one quite knows what to expect. There is much debate about the tax policies that will come from Congress in the upcoming months. The purpose of this letter is not to alarm, but to educate and inform our clients on the potential impact and possible tax scenarios for 2010 and 2011. Additionally, we have offered some tax planning provisions that may help hedge against future tax liabilities. We encourage you to share this newsletter with others so they, too, will be informed on the most recent tax developments. If you would like further information or to schedule a tax planning appointment, please contact our office at (904) 880-3200. See my website, www.dkbrierycpa.com, for both this newsletter and the business one.

Many current tax provisions were originally enacted in 2001 and 2003. The "Bush Tax Cuts" passed in those years and other recently passed tax laws are currently scheduled to expire on 12/31/10 unless Congress acts to change this. Some of these expiring provisions are listed in this newsletter. Even though Congress may extend some of these, strong uncertainty remains as to which, if any, will continue and how they may be modified.

In prior years, forcing a large amount of income into one year or the other did not always make sense because the higher income may trigger a higher phase-out of exemptions and itemized deductions. **But in 2010, there are no phase-outs of these**!

In past years, alternative minimum tax (AMT) has affected taxpayers when certain situations applied. An "AMT patch" has shielded many taxpayers from this tax. However, currently, there is no AMT patch for 2010. It is estimated that 1 in 5 taxpayers will fall subject to this additional tax, if nothing is done.

Minimizing future tax bills will require a true balancing act, but could also be a planning opportunity for taxpayers who have the ability to control the timing and/or nature of their income (employment bonuses, retirement distributions, capital gains, certain other income items and deductions, etc.). Unless you have very sophisticated tax projection software and are fully educated on the tax laws, the **smartest move is to talk to your CPA as soon as possible to develop your best tax plan.**

Tax provisions currently set to expire on 12/31/10 (note these are subject to change)

- *Current income tax rates - will revert to 15%, 28%, 31%, 36%, and 39.6%.* Current rates of 10% & 25% will disappear; the brackets will then be 15%, 28%, 31%, 36%, & 39.6%. It is not clear what the taxable income that falls into each bracket will be.
- *Current capital gains rates - will revert to 10% and 20%.* Current preferred gains tax rates of 5% and 15% will disappear, and the lowest rate will be 10% with a maximum of 20%.
- *Lower rates for qualified dividends - will disappear.* Qualified dividends have previously been taxed as low as 0%, but will now be taxed as ordinary income under the rules above.
- *Homebuyer Tax Credit* - Although this credit expired on 9/30/10, filers who claimed the 2008 credit will be required to start repayment on their 2010 tax returns at $500/yr for a maximum of 15 years, or $7,500 total. Also, homeowners that claimed the credit in 2009 or 2010 may be required to repay up to $8,000 if the home is sold within 3 years of purchase.
- *Making Work Pay Credit – will disappear.* The 2009 and 2010 credit of up to $400 for singles and $800 for couples is not available in 2011.
- *$1,000 Child Tax Credit – will revert to $500.* This credit ends in the year the child turns 16.
- *Child Care Credit* – Amounts allowed per dependent and credit % will decrease.
- *Earned Income Tax Credit* – The additional amount for a 3rd child will no longer apply.
- *Credit for hybrid and alternative fuel vehicles – will disappear.*
- *Educator deduction ($250 for teachers) – will disappear.*
- *Standard deductions – will decrease.*
- *State and local sales tax – will disappear.* This will really hurt Florida and Texas residents!.
- *American Opportunity Tax Credit – will disappear.*

Alternative Minimum Tax (AMT) – Alternative Minimum Tax applies to certain taxable income amounts based on filing status. AMT income is recalculated to add back, or disallow, certain deductions and a flat tax rate then applies at 26%. If the regular tax is lower than the AMT, the higher tax amount is due. In prior years, an "AMT patch" increased the amounts to which AMT applies. *Currently, there is no AMT patch for 2010*, so the thresholds below will apply if there are no modifications.

2009 AMT thresholds:	$46,700	Single Filers	$70,950	Married Filing Joint
2010 AMT thresholds:	$33,750	Single Filers	$45,000	Married Filing Joint

*This change is expected to affect a whopping **1 in 5 taxpayers!***

Estate Tax – The estate tax expired on 1/1/10. Currently, inherited property is treated as a gift and special cost basis rules apply. However, the "no estate tax" free-for-all only applies to 2010. It is set to return on 1/1/11 with an exemption of $1 million and a top tax rate of 55%!

Additionally, the following expired in 2009 and will NOT apply in 2010:

- Up to $2,400 tax-free unemployment income (now fully taxable)
- Additional standard deduction for property tax (was up to $1,000 on Schedule L)

Individual Retirement Accounts (IRAs)

- Remember, if you are 70 ½ or over, you **generally** must take your required minimum distribution (RMD) prior to December 31 to avoid substantial penalties. There are exceptions, if this is your initial year.
- Review your contributions to retirement plans and IRAs to be certain they are not in excess.
- Review beneficiary designations—be certain there is both a primary and contingent beneficiary. Beneficiaries should be adult individuals—not living trusts or minor children.
- Roth conversions must be completed by December 31 to be counted in this tax year.
- In 2010, Regardless of income, anyone can convert their traditional IRA to a Roth. In addition, neither traditional IRAs or Roth IRAs will have their contribution limited due to a taxpayer's income. *But, **deductible** traditional IRA contributions may be limited if one of the taxpayers participate in a retirement plan.*
- *Tax Planning Tip:* Consider a conversion to a Roth if your income is lower than normal in 2010. Max out the bottom bracket with the conversion. In this way, money that would generally have been taxed at a higher bracket could be received at a lower bracket,
- Consider rolling over old 401(k)s into an IRA where you have better control.
- If you converted a traditional IRA into a Roth IRA and you now wish you had not for various reasons, reconvert (or reverse) the conversion back to a traditional IRA. (This is common when the stock market declines.)

Other areas of recent tax developments:

- Income information sharing is being implemented by the IRS, Department of Revenue, Social Security Administration, merchant services for credit cards and other third-party payment processors.
- Identity theft is a rapidly increasing problem, as is fraudulent tax returns. The IRS has established a new Identity Protection Specialized Unit (IPSU). Please contact our office immediately if you suspect fraudulent, fictitious filings, or identity theft. See my business newsletter on my website, www.dkbrierycpa.com.
- "Debt indicators" will no longer be issued by the IRS, which will eliminate refund anticipation loans for filers such as H&R Block, Jackson Hewitt, Liberty Tax Service, etc.
- The IRS now requires most tax returns to be e-filed.
- Foreign bank accounts are now a target area for the IRS and **must** be disclosed on Schedule B. Additional reporting could be required.
- The IRS has issued guidance for homeowners who have suffered property losses due to the effects of certain imported drywall **installed** in homes between 2001 and 2009. This guidance applies to both original and amended federal income tax returns filed after September 29, 2010. If this situation applies to you, please contact our office so we can advise you of the requirements to claim these losses.

- As of January 1, 2011, over-the counter drug costs are no longer reimbursable from medical reimbursement accounts such as HSAs, FSAs, and Archer MSAs. The penalty for using these funds for non-qualified use will be 20%--rather than the 10% on early distribution of IRAs.

Inflation-adjusted 2011 Health-Care Numbers

- Long-term care premiums—deduction amount determined by age:
  - 40 or less-- $340
  - 41-50--$640
  - 51-60--$1,270
  - 61-70--$3,390
  - 71+--$2,240
- Payments received under qualified long-term care insurance are excludable as amounts received for personal injuries and sickness, subject to a per diem limitation of $300.
- For Archer Medical Savings Account purposes, a high deductible health plan will be one with an annual deductible of $2,050-$3,050 for self-coverage and $4,100-$6,150 for family coverage AND the out-of-pocket expenses do not exceed $4,100 for self-coverage and $7,500 for family coverage.

Special Rules for 2010 – Some special rules apply for 2010 related to phase-out levels for certain tax items. For 2010 ONLY, there are no income phase-out levels for:

- Itemized deductions (Schedule A)
- Personal exemptions
- Dependency exemptions
- Converting traditional IRAs to Roth IRAs—Taxable Income from 2010 IRA conversions can be spread equally between 2011 & 2012, unless an election is made to recognize the full income in 2010.

A Word of Caution…

- Often, taxpayers with working teenagers or college students will either prepare the child's return or let them prepare it themselves. When this occurs, the child will usually be claimed as an exemption on his return—thus, causing major problems on their parent's return. The dependency exemption is usually much more beneficial to the parents with higher tax rates than the child at lower rates. In addition, the parent generally benefits more from the education credit. Although, a child's return seems simple, there are complex rules regarding a dependent's return. The cost of correcting these issues GREATLY exceeds the cost of our preparing the return. Please contact us to assist with your dependent's return.
- As a result of the difficult economic times, increasing numbers of individuals are participating in short sales, foreclosures, cancelled credit card debt, etc. This is "cancellation of debt" or "abandonment" can trigger taxable income, resulting in receiving a 1099-C or 1099-A. If you have filed bankruptcy or can show that you are insolvent, you may be able to exempt this income. Please contact our office for advice.
- If a short-sale is in your future, please have an attorney review your agreement to be certain that you will be relieved of liability. There have been reports of fraud in this area.

- If you have had a significant change in income, tax deductions, or lifestyle (marriage, retirement, birth, etc.), you may also have a much different tax position than in the past. We welcome the opportunity to advise you on these matters.
- There has been a large increase in fraudulent tax returns being filed—returns filed with improper, excessive refunds, and refunds being deposited into the preparer's bank account rather than the taxpayer's account. In these cases, the individual is sometimes responsible for repaying the fraudulent refund and/or does not receive the refund to which they were entitled. More of these are occurring on the local level—within our community! To prevent this from happening to you, REMEMBER:
    - YOU are responsible for the return.
    - Use a reputable CPA.
    - Be certain that you get a copy of the return and review it before signing.
    - You must sign a Form 8879 to allow someone else to e-file it.
    - The paid preparer must sign underneath your signature area.
    - Until 2010, only CPAs, attorneys, and Enrolled Agents were registered with the IRS to file tax returns. ALL preparers must now register with the Service, but, at this time, ONLY these three groups have met testing and education requirements.
    - There is no "State Licensing Board" that holds the preparer responsible, other than for these three groups.

CONCLUSION

A recent analysis by Deloitte Tax LLP, a national tax consulting firm, estimated that a typical **family of four with a household income of $50,000 a year would pay $2,900 more in taxes** in 2011 if the current tax cuts expire in 2010.

There is a high-stakes debate as to what will or may occur with our tax future. If Congress fails to act, every employee will see more taxes being withheld from their paychecks beginning in January. Dual income households with standard withholding will experience insufficient tax payments due to higher rates applied to combined income amounts. Additionally, a loss of a tax credit has a significant effect, because credits act as tax payments, vs. deductions which reduce the income to be taxed. Taxpayers that do not plan appropriately may face unpleasant tax liabilities with major financial impacts.

For more information, visit our website at www.dkbrierycpa.com **AND**

Schedule your tax planning appointment today.
Contact our office at (904) 880-3200.