

December 20, 2011

It is time once again to begin organizing your financial information in order to prepare your 2011 tax returns.

Year-end tax planning is challenging this year because of uncertainty over whether Congress will enact sweeping tax reform that could have a major impact in 2012 and beyond. And even if there's no major tax legislation in the immediate future, Congress next year still will have to grapple with a host of thorny issues, such as whether to once again "patch" the alternative minimum tax (e.g., to avoid a drastic drop in post-2011 exemption amounts), and what to do about the post-2012 expiration of the Bush-era income tax cuts (including the current rate schedules, and low tax rates for long-term capital gains and qualified dividends), and the expiration of favorable estate and gift rules for estates of decedents dying, gifts made, or generation-skipping transfers made after December 31, 2012.

Regardless of what Congress does late this year or early the next, there are solid tax savings to be realized by taking advantage of tax breaks that are on the books for 2011 but may be gone next year unless they are extended by Congress. These include, for individuals: the option to deduct state and local sales and use taxes instead of state and local income taxes; the above-the-line deduction for qualified higher education expenses; and tax-free distributions by those age 70 ½ or older from IRAs for charitable purposes. For businesses, tax breaks that are available through the end of this year but won't be around next year unless Congress acts include: 100% bonus first year depreciation for most new machinery, equipment and software; an extraordinarily high \$500,000 expensing limitation (and within that dollar limit, \$250,000 of expensing for qualified real property); and the research tax credit.

I have compiled a checklist of actions based on current tax rules that may help you save tax dollars if you act before year-end. Not all actions will apply in your particular situation, but you will likely benefit from many of them.

- 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 you can **no** longer set aside amounts to get tax-free reimbursements for over-the-counter drugs, such as aspirin and antacids.
- If you become eligible to make health savings account (HSA) contributions in December of this year, you can make a full year's worth of deductible HSA contributions for 2011.
- 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, and then buy back the same securities at least 31 days later.
- Postpone income until 2012 and accelerate deductions into 2011 to lower your 2011 tax bill. This strategy may enable you to claim larger deductions, credits, and other tax breaks for 2011 that are phased out over varying levels of adjusted gross income (AGI). These include IRA and Roth IRA contributions, conversions of regular IRAs to Roth IRAs, child credits, higher education tax credits, the above-the-line deduction for higher-education expenses, and deductions for student loan interest. Postponing income also is desirable for those taxpayers who anticipate being in a lower tax bracket next year due to changed financial circumstances. Note, however, that in some cases, it may pay to actually accelerate income into 2011. For example, this may be the case where a marginal tax rate is much lower this year than it will be next year.
- If you believe a Roth IRA is better than a traditional IRA, and want to remain in the market for the long term, consider converting traditional-IRA money invested in beaten-down stocks (or mutual funds) into Roth IRAs if eligible to do so. Keep in mind, however, that such a conversion will increase your adjusted gross income for 2011.
- If you converted assets in a traditional IRA to a Roth IRA earlier in the year, the assets in the Roth IRA account may have declined in value, and if you leave things as it, you will wind up paying a higher tax than is necessary. You can back out of the transaction by re-characterizing the rollover or conversion, that is, by transferring the converted amount (plus earnings, or minus losses) from the Roth IRA back to a traditional IRA via a trustee-to-trustee transfer. You can later reconvert to a Roth IRA.

- Consider using a credit card to prepay expenses that can generate deductions for this year.
- You may be able to save taxes this year and next by applying a bunching strategy to “miscellaneous” itemized deductions, medical expenses and other itemized deductions.
- Businesses should consider making expenditures that qualify for the business property expensing option. Unless Congress changes the rules, for tax years beginning in 2012, the dollar limit will drop to \$139,000 and expensing won’t be available for qualified real property. What’s more, the expensing deduction is not prorated for the time that the asset is in service during the year. This opens up significant year-end planning opportunities.
- If you are self-employed and have not done so yet, set up a self-employed retirement plan.
- If you are age 70 ½ or older, own IRAs and are thinking of making a charitable gift, consider arranging for the gift to be made directly by the IRA trustee. Such a transfer, if made before year-end, can achieve important tax savings.
- Make gifts sheltered by the annual gift tax exclusion before the end of the year and thereby save gift and estate taxes. You can give \$13,000 in 2011 to each of an unlimited number of individuals. 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.

These are just some of the year-end steps that can be taken to save taxes. Again, by contacting me, I can tailor a particular plan that will work best for you.

The Internal Revenue Service has announced the Cost of Living adjustments applicable to dollar limitations for 2012 retirement plans:

- 401(k) and SEP maximum \$17,000 plus \$5,000 “catch up”, if applicable.
- Defined contribution maximum is \$49,000.
- SIMPLE maximum \$11,500 plus \$2,500 “catch up”, if applicable.
- IRA maximum \$5,000 plus \$1,000 “catch up”, if applicable.

I will prepare your 2011 Federal and State income tax returns from information that you provide to me. I will not audit or otherwise verify the data you submit, although I may ask for clarification of the information. By submitting your tax data, you represent that, to the best of your knowledge, the information is correct and complete. You are responsible for keeping the necessary records for your deductions, business expenses, and business and personal use of any property.

An additional service that I offer is electronic tax filing. In most cases, New Jersey now requires electronic filing. I also offer filing Federal returns electronically. The electronic returns have the same information as a comparable return filed on paper; however, the electronic filing process involves fewer steps at the taxing agencies. This service for the Federal Tax Return has an additional charge of \$30 per return.

In order to provide me with enough time to adequately review your data and prepare your tax returns, I am requesting that your information be in my office no later than **March 9, 2012**. Information received after this date may require that your return be placed on extension.

You are a valued client of my firm, and I understand that your loyalty needs to be earned through trust, quality of service, dependability and honesty. Thank you for your support in 2011 and I wish you and your families a peaceful and healthy year ahead.

Very truly yours,

David T. Black, CPA

PS I had a Peer Review completed and was, again, given the highest standard of “passed without any deficiency.” Also, please look at my new web site at www.dblackcpa.com and let me know of any comments you may have. On a personal note, I was elected Captain of the West Essex First Aid Squad.