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FILE NO.

October 12, 2011

2011 YEAR END TAX PLANNING

Dear Client:

Year end tax planning is especially challenging this year because of uncertainty over whether Congress will enact sweeping tax reform that could have a major impact in 2012 and beyond. Even if there is no major tax legislation in the immediate future, next year Congress will still have to grapple with a host of difficult issues, such as whether to once again “patch” the alternative minimum tax (e.g., to avoid a drastic drop in post-2011 exemption amounts), 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 the tax breaks that are currently on the books for 2011 but may be gone next year. For individuals, these include: 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 70½ or older from IRAs for charitable purposes. For businesses, these include: 100 percent bonus first-year depreciation for most new machinery, equipment, and software, an

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extraordinarily high \$500,000.00 expensing limitation (and within that dollar limit, \$250,000.00 of expensing for qualified real property), and the research tax credit.

We 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. Although lengthy, this is not an exhaustive list. We ask that you please review the following and contact us at your earliest convenience so that we can narrow down the specific actions that you can take, and consider additional actions that you might consider, to save your valuable tax dollars.

### **Year-End Tax Planning Moves for Individuals**

- 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 that 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, then buy back the same securities at least 31 days later. It may be advisable for us to meet to discuss year-end trades you should consider making.

- 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 child tax credits, higher education tax credits, the above-the-line deduction for higher-education expenses, and deductions for student loan interest. Postponing income is also desirable for those taxpayers who anticipate being in a lower tax bracket next year due

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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 person's 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 a Roth IRA if eligible to do so. Keep in mind, however, that such a conversion will increase your AGI 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-is, you will wind up paying a higher tax than is necessary. You can back out of the transaction by recharacterizing 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.

- It may be advantageous to try to arrange with your employer to defer a bonus that may be coming your way until 2012.

- Consider using a credit card to prepay expenses that can generate deductions for this year.

- If you expect to owe state and local income taxes when you file your return next year, consider asking your employer to increase withholding of state and local taxes (or pay estimated tax payments of state and local taxes) before year-end to pull the deduction of those taxes into 2011 if doing so won't create an alternative minimum tax (AMT) problem.

- Take an eligible rollover distribution from a qualified retirement plan before the end of 2011 if you are facing a penalty for underpayment of estimated tax and the increased withholding option is unavailable or won't sufficiently address the problem. Income tax will be withheld from the distribution and will be applied toward the taxes owed for 2011. You

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can then timely roll over the gross amount of the distribution, as increased by the amount of withheld tax, to a traditional IRA. No part of the distribution will be includible in income for 2011, but the withheld tax will be applied pro rata over the full 2011 tax year to reduce previous underpayments of estimated tax.

- Estimate the effect of any year-end planning moves on the AMT for 2011, keeping in mind that many tax breaks allowed for purposes of calculating regular taxes are disallowed for AMT purposes. These include the deduction for state property taxes on your residence, state income taxes (or state sales tax if you elect this deduction option), miscellaneous itemized deductions, and personal exemption deductions. Other deductions, such as for medical expenses, are calculated in a more restrictive way for AMT purposes than for regular tax purposes. As a result, in some cases, deductions should not be accelerated.

- Accelerate big ticket purchases into 2011 in order to assure a deduction for sales taxes on the purchases if you will elect to claim a state and local general sales tax deduction instead of a state and local income tax deduction. Unless Congress acts, this election won't be available after 2011.

- 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.

- If you are a homeowner, make energy saving improvements to the residence, such as putting in extra insulation or installing energy saving windows and energy efficient heaters or air conditioners. You may qualify for a tax credit if the assets are installed in your home before 2012.

- Unless Congress extends it, the up-to-\$4,000.00 above-the-line deduction for qualified higher education expenses will not be available after 2011. Thus, consider prepaying eligible expenses if doing so will increase your deduction for qualified higher education expenses. Generally, the deduction is allowed for qualified education expenses

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paid in 2011 in connection with enrollment at an institution of higher education during 2011 or for an academic period beginning in 2011 or in the first three months of 2012.

- You may want to pay contested taxes to be able to deduct them this year while continuing to contest them next year.

- You may want to settle an insurance or damage claim in order to maximize your casualty loss deduction this year.

- Purchase qualified small business stock (QSBS) before the end of this year. There is no tax on gain from the sale of such stock if it is (1) purchased after September 27, 2010 and before January 1, 2012; and (2) held for more than five years. In addition, such sales won't cause AMT preference problems. To qualify for these breaks, the stock must be issued by a regular (C) corporation with total gross assets of \$50 million or less, and a number of other technical requirements must be met. Our office can fill you in on the details.

- For those who are age 70½ 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.

- If you plan on making a charitable contribution in 2012 and you expect to be in a higher marginal tax bracket in 2011 than 2012, consider making the gift this year in order to accelerate the deduction into 2011. On the other hand, if you expect to be in a higher tax bracket in 2012, you should consider deferring charitable gifts to next year. To the extent possible, make any such gifts with appreciated capital gain property. That way, the deduction is generally obtained for the full value of the gifted property, and income tax on the appreciation is avoided. Note that contributions of appreciated capital gain property are subject to a 30 percent of adjusted gross income ceiling, not the usual 50 percent ceiling. Also note that such favorable treatment is not available for a gift of tangible personalty unless the donated item is related to the exempt purpose of the done charity.

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□ Further, if you wish to contribute appreciated property to a private foundation, the rule that allows the deduction to be based on the full fair market value of the property does not apply (in which case, the deduction is limited to the tax basis), unless the property is “qualified appreciated stock” (generally, stock that is capital gain property and is traded on an established securities market). To claim a deduction in 2011, the private foundation must be set up, and the contribution made, before 2012.

□ If you are considering donating an automobile (or a boat or airplane) to charity, be aware of the special rules that apply. If the claimed value is more than \$500.00, the amount of the charitable deduction depends on the use of the vehicle by the charity. If the charity sells the vehicle (other than to a needy person) without “significant intervening use” or “material improvement” the charitable deduction cannot exceed the gross proceeds from the charity’s sale; otherwise, the deduction can equal the full fair market value. Charities are required to provide donors with acknowledgments of whether there will be a sale, use, or improvement of the vehicle. Inquiry should be made before the donation is made.

□ As noted below, there are certain incentives for C corporations contributing inventory to charity. For contributions made in 2011, some of these incentives are extended to individuals (as well as S corporations and partnerships). 2011 contributions of “apparently wholesome food” by individuals to charity are deductible to the extent of the lesser of (i) basis plus one-half of the excess of the fair market value over basis; and (ii) twice basis, but limited to the ceiling of 10 percent of the donor’s aggregate net income for the year from all trades and businesses from which such donations were made (computed without taking the enhanced deduction into account). If you are inclined to make such a gift, the gift must be made in 2011 in order to get the enhanced deduction.

□ Take required minimum distributions (RMDs) from your IRA or 401(k) plan (or other employer-sponsored retired plan) if you have reached age 70½. Failure to take a required withdrawal can result in a penalty of 50 percent of the amount of the RMD not withdrawn. If you turned age 70½ in 2011, you can delay the first required distribution to

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2012, but if you do, you will have to take a double distribution in 2012—the amount required for 2011, plus the amount required for 2012. Think twice before delaying 2011 distributions to 2012—bunching income into 2012 might push you into a higher tax bracket or have a detrimental impact on various income tax deductions that are reduced at higher income levels. However, it could be beneficial to take both distributions in 2012 if you will be in a substantially lower bracket that year; for example, because you plan to retire late this year.

- If you have formed a Charitable Remainder Trust, obtain a waiver from the grantor's spouse of his or her elective share rights in such trust. This would eliminate uncertainty that the IRS will assert that the trust is not tax exempt, because trust assets might have to be used to satisfy a future elective share election. This would comply with a proposed IRS safe harbor rule (that has not yet been finalized, pending the consideration by the IRS of alternative safe harbor rules).

- If you are considering a “qualified conservation contribution”, make the contribution this year, because the 30 percent contribution base limitation on capital gain property is generally lifted for such contributions made in 2011 to a 50 percent charity.

- 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 \$13,000.00 in 2011 to each of an unlimited number of individuals, but you can't carry over unused exclusions from one year to the next. 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. Note that for checks to be considered as 2011 payments, generally the check must be presented for payment by the donee prior to the end of the year.

### **Year-End Tax-Planning Moves for Businesses & Business Owners**

- Businesses should consider making expenditures that qualify for the business property expensing option. For tax years beginning in 2011, the expensing limit is \$500,000.00, and the investment ceiling limit is \$2,000,000. A limited amount of expensing

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may be claimed for qualified real property. However, unless Congress changes the rules, for tax years beginning in 2012, the dollar limit will drop to \$139,000.00, the beginning-of-phaseout amount will drop to \$560,000.00, and expensing won't be available for qualified real property. The generous dollar ceilings that apply this year mean that many small and medium sized businesses that make timely purchases will be able to currently deduct most, if not all, of their outlays for machinery and equipment. 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.

- Businesses also should consider making expenditures that qualify for 100 percent bonus first-year depreciation if bought and placed in service this year. This 100 percent first-year write-off generally won't be available next year unless Congress acts to extend it. Thus, enterprises planning to purchase new depreciable property this year or the next should try to accelerate their buying plans if doing so makes sound business sense.

- Nail down a work opportunity tax credit (WOTC) by hiring qualifying workers (such as certain veterans) before the end of 2011. Under current law, the WOTC won't be available for workers hired after this year.

- Make qualified research expenses before the end of 2011 to claim a research credit which won't be available for post-2011 expenditures unless Congress extends the credit.

- If you are self-employed and haven't done so yet, set up a self-employed retirement plan.

- Depending on your particular situation, you may also want to consider deferring a debt-cancellation event until 2012 and disposing of a passive activity to allow you to deduct suspended losses.

- If you own an interest in a partnership or S corporation, you may need to increase your basis in the entity so you can deduct a loss from it for this year.



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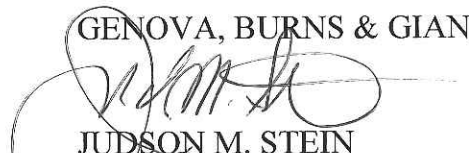
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□ If you are a C corporation, consider donating inventory to charity to be used for the care of the ill, needy, or infants. Although deductions for inventory donations are normally limited to basis, such donations by C corporations are eligible for an enhanced deduction equal to the lesser of (i) basis plus one-half of the excess of the fair market value over basis; and (ii) twice basis. For 2011, the enhanced deduction is also available to S corporations and partnerships (as well as individuals as noted above) for donations of “apparently wholesome food” inventory, subject to the ceiling of 10 percent of the donor’s aggregate net income for the year from all trades and businesses from which such donations were made (computed without taking the enhanced deduction into account).

These are just some of the year-end steps that can be taken to save taxes. Again, by contacting us, we can tailor a particular plan that will work best for you. We look forward to hearing from you.

Very truly yours,

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