Life Planning Newsletter
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Planning ....Taxes

The "Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010." basically extends the Income Tax reduction enacted in 2003 (Bush tax cuts). This means that for 2011 and 2012 the income tax brackets stay at 10, 15, 25, 28, 33 and 36 percent rather than revert to the 2002 rates of 15, 28, 31, 36 and 39.6 percent, which is an average savings of about $3,500 per year for a single person making $50,000. Since there is no guarantee that the law will stay the same in 2013, It might make sense to put your income into 2011 and 2012 rather than 2013. This means that you might want to accelerate any income you may have coming to you and to decelerate some deductions. Because the deductions would be worth more in 2013. Stay tuned to the news though. Also if you do pay substantial tax or have investment or rent income you might want to consider investing some time and money with a tax lawyer who specializes in income tax. A few hundred dollars spent may save thousands. The tax laws are comples enough when they don't change and we now live in changing times. As with any change there are opportunities for those who keep up to take advantage of the change. Here are some other changes the Tax Reduction Act of 2010.

CAPITAL GAINS/DIVIDENDS: Currently taxed at maximum 15% (0% for those in the 10 and 15% bracket). This was scheduled to increase to 20% for everyone, so you can see that if you hold mutual funds, stocks or sell property this is a big deal, especially if your income is less than $30,000 per year (as in retired). However, stay tuned because installment payments are taxed in the year paid not the year sold. So if you plan retirement with a structured sale of an investment now, only the payments made in 2011 and 2012 are treated with the lower tax rate. In 2013 the rate is scheduled to jump to 20% for everyone so you could find yourself going from zero tax on your investment pay-out to 20%.

DEDUCTIONS: Of course as we learned in the 80's the elimination of deductions is a backhanded way to increase your tax. Under the old law many deductions (such as interest expense for your home) started to phase out if a single person had income of over $84,775 or a married couple $169,550. For example for the average home in SoCal, if you were single making $150,000 you could not take a deduction for the interest paid on your home, and if you made over $100,000 you could take only 1/2 the interest paid. So your tax simply increased at the 36% rate on the amount you couldn't deduct. The company you paid it to had to pay tax on it as well. Talk about double dipping! Well, there is no income limitation on this deduction...for 2011 and 2012. But in 2013 it comes back. Same for the personal exemption phase out. Before 2010 a single person making over $84,775 had their personal tax exemption of $2,500 phased out so that at an income of about $150,000 they could not take the exemption at

all. Under the Tax relief act the Exemption will be $3,650 for 2010 and $3,700 for 2011 and will be available to all tax payers.

CHILD TAX CREDIT: This Tax Relief Act also extends the $1,000 Child tax credit that was to expire.

ADOPTION CREDIT: The Tax Relief Act also extends the $10,000 or $11,000 (indexed for inflation) adoption credit for all non step parent adoptions. This is a direct tax credit or if your employer pays you, the amount paid will not be included as income. Note though that it is only extended though 2012.

EMPLOYER PROVIDED CHILD CARE: The new law extends the Credit an employer could take for providing employee child care through 2012.

EDUCATION: The act also eliminates the income phase out (over$80,000) of the Hope Tax Credit and the Employer provided education deductions. Same with student loan interest. (before, if you got a good job ,over $80,000 per year) you couldn't deduct all the interest on your student loans). Same with savings accounts which extend the deduction to a student's savings account from $500 to $2,000 makes elementary and secondary school savings eligible for the deduction as well. and finally the law extends the exclusion for certain scholarships and fellowships from inclusion as income. [National Health Service and Armed Forces Fellowships in particular]. But all this comes back in 2013.

OTHER: There are also a number of things that will still be available for 2011 and 2012 including indexed EITC, State tax deduction, Teacher's classroom deduction, and many Charitable deductions including appreciated property for conservation purposes. There are certain other Business incentives But most all of those end in 2011. Since most businesses like to hire people for the long term this is not expected to have much of an impact.

AMT: The Alternative Minimum Tax will be re indexed so that most retirees will not be affected.

SOCIAL SECURITY TAX: Individuals will see a 2% reduction in their SS tax line for 2011 ONLY. The employers share remains the same at 6.2% of the employees income. Self Employed will pay 10/2% up to earnings of 106,800.

FE**DERAL ESTATE TAX:** in 2010 there was no FET. However only 1.3 million dollars were exempt from the 33% capital gains step up (the Step-up increased the base value of property to the value of the property on the date of the deceased person's death so there were no capital gains owed on the date of death) so in some cases where a person bought the lot in Newport Beach in 1947 for $12K then died when the lot value was $3 million or so would have a high Capital Gain tax in 2010. (but would have paid no tax in 2009). Now the Capital Gain tax is optional for 2010 decedent's and eliminated for those dying in 2011 and 2012. In addition the floor for the Estate Tax is $5,000,000 per person (35% after that) and the Step-up is back. This makes most estates totally tax free. In addition, the Generation Skipping Tax (where your bequest to a grandchild was taxed at double rate) is now also exempt up to $5,000,000. And, most importantly for many people the GIFT TAX exclusion for 2011 and 2012 has been raised from $1,000,000 to $5,000,000. Keep in mind that after 2012 the old law goes back into effect (estate pays about 46% tax on the value over $1,000,000 (which includes all the reportable gifts you have given over your life)

Remember this law is only temporary and the coach turns into a pumpkin at midnight 12/31/2012 (and 12/31/2011 for most businesses).

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