

The Advisor

The C&P Advisors companies are happy to bring our latest newsletter to you. If you have questions on any of these topics, contact your C&P Advisor or the individuals listed.

November 2010

2010 Year-End Tax Planning

January marks my 30th anniversary with the firm. In those years I have experienced many different tax environments. But, I have never experienced such an unsettled tax situation as we have today. Here we are in November, and Congress is still waffling on huge income and estate tax issues.

- Will they allow most 2011 individual tax rates to increase at least 10%, as currently scheduled?
- Will most 2011 dividends be taxed at 15%, 39.6%, or somewhere in between?
- Will long-term capital gains be taxed at 15% or 20%?
- Will the alternative minimum tax be eased for 2010, as done in prior years?
- Will numerous expiring business tax deductions and credits previously allowed be retroactively permitted for 2010?
- Will the estate tax return in 2011, and if so, will it be at the harsh 2001 levels, or at some lower level?

I went to Washington DC last week to get the latest information, and get a feel for where the government is leaning. Unfortunately, there is no consensus. Although Congress will attempt to address these issues during the last few weeks of the year, we do not know whether either party has the ability to actually get much resolved before year-end. We therefore find ourselves with only weeks to wrap up our year-end planning without knowing what the rules will end up being. Because of this uncertainty, it is important that we work together develop a flexible game plan for your situation.

The federal government is under tremendous pressure to extend the so called “Bush tax cuts”. This includes retaining the lower personal income tax rates, dividend tax rates, and long-term capital gain tax rates. The Republicans want to extend these items for all taxpayers, while the Democrats want to exclude “wealthier” taxpayers. There is a very good chance that we will see at least a one year extension of these breaks for those not meeting the President’s definition of wealthy. But it can go either way for the wealthy. We need to plan accordingly.

With the possibility that individual rates may increase next year, some of the income deferral or expense acceleration techniques generally employed at year-end may actually cost you more in taxes in the long run. This includes many businesses. If your business is a sole-proprietor, Partnership, LLC, or S corporation, your business income is taxed at the owners’ personal tax rates.

Listed on the following pages are some general year-end tax planning ideas that may apply to your situation. Each of the items listed has to be carefully considered before implementation. Your C&P professional can analyze your tax situation and tailor your year-end planning to meet your specific personal and/or business needs.



Jim Komos, Partner

Business Tax Planning

Section 179 Deductions

Consider purchasing and placing in service qualifying fixed assets before year-end. For 2010, the Code Section 179 expensing is available on new or used property. The limit on expensing is \$500,000, and the threshold for reducing the deduction starts at \$2,000,000 (for 2011 the threshold will revert back to \$800,000). The new law also expands the definition of qualified Section 179 property to include “qualified real property” which includes the following:

- Qualified Leasehold Improvement Property
- Qualified Restaurant Property
- Qualified Retail Improvement Property

The amount of Section 179 expense that may be taken for “qualified real property” will be limited to \$250,000 for 2010 and 2011. Unlike Section 179, there are no limits or thresholds to claim the 50% bonus depreciation which was extended under the new tax law retroactive to January 1, 2010. To be eligible for bonus depreciation, the property has to be new and it has to be qualifying property. They also increased the amount of first year depreciation expense allowed on passenger autos and light duty trucks to \$11,060 and \$11,160 respectively.

S Corporation Built in Gain Period

Recent legislation shortened the length an S Corporation must hold appreciated assets owned at the time of the conversion from a C Corporation from ten years to seven years. This has been further reduced by the Small Business Jobs Act from seven years to five years for tax years beginning in 2011.

Like-Kind Exchanges

Like-kind exchanges of property enable you to delay recognizing the taxable gain from the disposal of property. The exchanged property has to be business use property and of the same nature and character as the exchanged asset. Property may be relinquished before the replacement is identified, but the taxpayer will only have 45 days to identify the replacement property. By doing this, you do not have to recognize the gain on the asset traded in. Thus, you will have more cash available for the business.

Cost Segregation

Have you ever considered a cost segregation study for your business? A cost segregation study reclassifies assets to maximize the use of shorter depreciable lives, optimizing depreciation deductions which could result in substantial cash flow benefits. If you have acquired business properties through purchase, new construction, renovation, or leasehold improvements, you may benefit from a cost segregation study. It is also possible to look-back currently deduct additional depreciation for prior years.

Qualified Retirement Plans

Does your company have a qualified retirement plan? A qualified retirement plan can be an excellent way to reduce your business taxes and also help you save for retirement. Certain plans have to be in place by a specific date in order to be eligible for 2010 contributions.

If you do have a qualified retirement plan, does the plan meet your goals by allocating employer contributions to the right employees? This is a good time to make changes to be implemented for 2011.

Accrued Vacation and Bonuses

Accrued vacation and bonuses for employees are tax deductible for accrual basis taxpayers if paid within two and one-half months after year-end. To be currently deductible, you cannot require the employee to still be employed by you at the time of payment. Bonuses for C Corporation owners (owning more than 50% of the business) are not tax deductible if accrued for at year-end and paid the next year. Consult your C&P professional as the 50% rule is complex.

Accrued Charitable Contributions

If elected, accrued charitable contributions are tax deductible if paid within two and one-half months after year-end. If accrued charitable contributions are accrued for longer time periods, it is important to note that the deduction cannot be taken in the current tax year.

Inventory

Review inventory for goods that have become damaged or obsolete and write them off.

A few highlights of the “Small Business Jobs Act of 2010” are as follows:

- Increased Section 179
- Extended Bonus Depreciation
- S Corporation Built in Gain Period
- Gain Exclusion on Qualified Small Business Stock
- Increased Start-Up Expense Deduction
- Health Insurance Costs Deductible for Computing 2010 Self Employment Tax
- Eligible Business Credit Carryback
- Promoting Retirement Savings
- Higher Failure to File Penalties on Information Returns

Personal Tax Planning Ideas

Alternative Minimum Tax

Currently, the Alternative Minimum Tax patch has not been extended to 2010. If you itemize, and normally pay your fourth quarter state and local tax payments and real estate taxes prior to year-end, you may want to contact your C&P professional to determine if this is more beneficial than waiting until 2011 when they are due. We hope that this is one item the government extends prior to year-end. You may therefore want to hold off on any payments until closer to year-end.

Roth IRA Conversions

Before 2010, only individuals with modified adjusted gross income of \$100,000 or less could convert their traditional IRA to a Roth IRA. If you were married and filed a separate tax return, you could not convert irrespective of income. The rules have changed for 2010, and they will even allow you the option to spread the tax on the conversion over a two year period 2011 and 2012. If you are unable to make a Roth contribution for 2010 due to your filing status and/or modified adjusted gross income, you may want to consider making a non-deductible traditional IRA contribution and then convert it to a Roth IRA in 2010.

If you have already made a Roth conversion and the value of your account has decreased, you may be able to save taxes by reconverting your Roth back into a regular IRA by year-end.

For distributions after September 27, 2010: 401(k), 403(b), and 457(b) governmental plans will allow participants to roll over qualified distributions into a designated Roth account within their plan. The rollover will be taxable, except for any after-tax contributions, and the participant will be able to spread the tax over a two year period 2011 and 2012.

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Personal Tax Planning Ideas continued

Educational Credits

The Hope Scholarship education credit has been renamed as the “American Opportunity Tax Credit.” For 2010, it applies to all four years of college and adds course materials to qualifying expenses. The income phase outs were increased to \$80,000 to \$90,000 for single filers and \$160,000 to \$180,000 for joint filers.

Energy Credits

Are you in the market for energy-efficient windows, insulation, doors, roofs, heating and cooling equipment, or a water heater for your principal home? If so, act now. The Residential Energy Property Credit is set to expire at the end of 2010. The credit is 30% with a maximum aggregate cap of \$1,500 for qualifying purchases.

Summary

This briefly summarizes some potential year-end tax planning ideas for your business. It is not meant to be all inclusive. Most of the above items have to be implemented by December 31, 2010 to be effective for 2010. Please contact us at 216.831.7171 if you would like to know more or want to discuss your business or personal tax situation.

For additional information on tax saving ideas, please visit our website: www.cp-advisors.com.

For marrieds filing jointly, the three most likely 2011 scenarios (in no particular order) are as follows:

Married Filing Jointly (& Surviving Spouse)

Tax Rate	2011 Taxable Income		
	Complete Sunset	2010 Rates	Obama Proposal
10%	–	\$0 – \$17,000	\$0 – \$17,000
15%	\$0 – \$57,650	\$17,000 – \$69,000	\$17,000 – \$69,000
25%	–	\$69,000 – \$139,350	\$69,000 – \$139,350
28%	\$57,650 – \$139,350	\$139,350 – \$212,300	\$139,350 – \$237,300
31%	\$139,350 – \$212,300	–	–
33%	–	\$212,300 – \$379,150	–
35%	–	\$379,150+	–
36%	\$212,300 – \$379,150	–	\$237,300 – \$379,150
39.6%	\$379,150+	–	\$379,150+

Source: Dollar estimates from Commerce Clearing House® 2010

NOTE: This newsletter is issued to provide you with information about minimizing your taxes. Many of the items noted may be subject to phase-out rules at higher income levels. Do not apply this general information to your specific information without additional details. Be aware that tax laws contain varying effective dates and numerous limitations and exceptions that cannot be summarized easily. For details and guidance in applying the tax rules to your individual circumstances, please contact us.