



Advanced Planning Strategies

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The American Recovery and Reinvestment Act of 2009 passed earlier this year extended many popular tax breaks retroactive to January 1st, but **only** through the end of this year. As in the past, many or all of these extenders may be further extended, but this might not be accomplished until 2010, retroactive to the beginning of the year. One development too late to make the inside report is "The Worker, Homeownership, and Business Assistance Act of 2009" which extends the first-time homebuyer \$8,000 credit until April 30, 2010 (a binding contract needs to be entered into before May 1). There is also a non-first-time buyer credit of \$6,500 included in the law. The phase-out levels were also increased to make this available at higher levels of income. The House passed its version of the Health Care legislation, but there will have to be significant compromise with the Senate before the possibility of sending a final bill to the President.

The inflation-indexed tax numbers for 2010 have been released. However, the formula utilized in indexing for inflation reflects only an insignificant adjustment. There was actually a rumor that some numbers might be reduced. The standard deduction will remain the same for joint filers (\$11,400) and for single or married individuals filing separately (\$5,700). However, a modest increase of \$50 is provided for those filing as head of household (\$8,400). The additional standard deduction for individuals age 65 or older or who are blind will remain at \$1,100 for married individuals and surviving spouses, and \$1,400 for single or unmarried head of household filers. The personal exemption amount will also remain the same for 2010 and is again \$3,650. For estate and gift tax planning for 2010, the annual gift tax exclusion will unfortunately remain at \$13,000 per individual donee.

There has been some activity in Congress related to the expected reform of the federal estate and generation-skipping taxes. A new bi-partisan bill (Estate Tax Relief Act of 2009) was introduced in the House late last month. The bill would eliminate the repeal of the tax in year 2010 and gradually increase the exemption from \$3.5 million in 2009 to \$5 million in 2019 with inflation-indexing thereafter. Over the same timeframe, the maximum rate would be reduced from 45 to 35 percent. There are several other bills proposed at this time. This new legislation would be relatively costly since current law would return the estate tax to its 2001 level after 2010. Without new legislation, the tax would be repealed in 2010, but return in 2011 with a \$1 million exemption and marginal rates that reach 60 percent. It is still quite likely at this point that the 2009 levels of \$3.5 million and 45 percent will be extended for at least one year. We'll stay on top of this for you.

Knowledge is not power. Only knowledge in use is power.

YEAR-END TAX PLANNING TIPS FOR 2009

There is always a plethora of ideas to make some last-month adjustments to reduce taxes at the end of a calendar year. This year proves to be no exception. Planning for 2009 requires us to carefully balance the traditional strategies of income deferral and deduction acceleration, since many phase-outs encountered in 2009 will disappear in 2010 allowing for a full deduction for many common itemized deductions. There has been some concern about the statements made by President Obama concerning potential tax increases to Americans with income over \$250,000. These changes could occur in many forms besides simply increasing the maximum rate. Some statements have emanated from Congress that significant tax reform may be more than a year away. However, any year-end strategy must reflect the individual taxpayer's feelings about the direction of tax legislation next year; a speculative risk at best. The discussion below provides some food for thought for this year and some new changes impacting all taxpayers for next year.

Some Individual And Business "Extenders" Are Set To Expire!

The following individual and business tax provisions are scheduled to expire by year-end and could generate a tax benefit if action is taken before the end of December:

- the itemized deduction for state and local sales taxes (in lieu of state and local income taxes);
- the deduction for state and local sales taxes or excise taxes on the purchase of a new vehicle costing no more than \$49,500 (note this is available as a tax benefit even if you don't itemize, but is not available if a taxpayer chooses to deduct state taxes in lieu of income taxes);
- the limited addition to the standard deduction for real property taxes paid by non-itemizers (\$1,000 for joint filers and \$500 for others);
- the provision that allows taxpayers to roll over (trustee to trustee) distributions of up to \$100,000 per year to qualified charities from their IRAs;
- the above-the-line \$250 deduction for teachers' classroom expenses.
- 15-year cost recovery for leasehold and restaurant improvement;
- Enhanced charitable deduction for contributions of food and contributions of books and computer hardware to schools is extended, and S corporation shareholders can receive pass-through charitable deductions of appreciated property equal to fair market value rather than the S corporation basis in the property through December 31, 2009.

Phase-Out Of Itemized Deductions And Personal Exemptions Eliminated in 2010

Taxpayers can, however, lose a good portion of the value of personal exemptions and itemized deductions when their incomes rise above certain levels. For 2009, married couples filing jointly will begin to lose some of their itemized deductions when their adjusted gross income (AGI) exceeds \$166,800. However, some gradual relief from this reduction was provided several years ago and the tax benefits from itemized deductions will be allowable in full for taxpayers above the AGI limits in 2010. This is a complex calculation, but there may be significant benefits for higher income taxpayers to defer expenditures that generate itemized deductions until 2010.

Wealth-Shifting Opportunity Provided By Lower Tax Rates On Dividends And Capital Gains

Most corporate dividends and long-term capital gains are taxable at a maximum rate of 15 percent for individual taxpayers. However, for taxpayers whose marginal rate does not exceed 15 percent (i.e., taxpayers whose taxable income does not exceed the 10 or 15 percent tax bracket amounts - \$33,950 for singles and head of households and \$67,900 for married couples filing jointly), the tax rate on dividends and long-term capital gains is ZERO percent for 2009! This presents an opportunity for income shifting by means of transferring dividend-paying stocks (and long-term appreciated capital assets) to lower-bracket family members who are not subject to the kiddie tax (i.e., not under the age of 19 or age 24 if the recipient is a full-time student). To effectively transfer taxation of income, however, the ownership of the asset itself must be transferred to the lower-bracket taxpayer (unless an appropriate form of trust is used), rather than just an income interest in the asset. Lifetime gifts are a great estate-planning idea, but this provides the additional benefit of reducing the tax on capital gains if the appreciated property is transferred to the lower-bracket family member.

Uncertainty Surrounds AMT's Future

The AMT exemption (i.e., the AMT Patch) increased again with the passage of February's American Recovery and Reinvestment Act. The exemption amounts for 2009 are \$46,700 for single and head of households, \$70,950 for married couples filing jointly, and \$35,475 for married couples filing separately. The intent of the increased exemption is to leave the number of taxpayers subject to the AMT at about four million. However, absent real AMT change, the Treasury estimates that at least 30 million taxpayers would be subject to the AMT in 2010. Although 2010's exemption amounts have not been set, the Obama administration has made some statements that indicated that AMT relief is on a very short list of tax relief provisions that will be signed without offsetting tax increases or spending reductions.

The impact of AMT should not be ignored in taking advantage of year-end tax planning because many common deductions are added back in calculating the AMT. Some of the itemized deductions that are added back include: state and local income taxes (including sales taxes), real estate taxes, and miscellaneous itemized deductions in excess of 2 percent of AGI. In addition, for those taxpayers claiming the standard deduction in lieu of itemizing their deductions, the standard deduction is added back to taxable income in calculating the AMT. Furthermore, both personal and dependency exemptions are not allowable in computing the AMT. In planning the timing of year-end deductions (i.e., taxes), what may seem tax deductible may prove to be an illusion due to an AMT issue.

Business Opportunities

In addition to last year's Economic Stimulus Act of 2008, the American Recovery and Reinvestment Act of 2009 has extended some of the more popular business provisions provided in 2008's legislation, only through year-end. The expensing limit (providing a current deduction rather than expensing under depreciation rules) under Section 179 was increased to \$250,000, with an increased phase-out level.

These higher limits only apply to taxable years beginning in 2008 and 2009. For fiscal year

taxpayers, this provision could be used in the first year beginning in 2008, but qualifying purchases would continue until the end of that fiscal year. For example, a 2009 fiscal year taxpayer, with a fiscal year beginning December 1, 2009 would only be permitted to make purchases on or after December 1, 2009, but the taxpayer could continue to purchase qualifying assets through November 30, 2010.

The Economic Stimulus Act passed in 2008 also permitted a trade or business to depreciate an additional 50 percent of the cost of a new asset acquired and placed into service in 2008 and this was extended for 2009, but appears to be expiring as of December 31, 2009. The types of property eligible for "bonus" depreciation will be the same as included under previous "bonus" depreciation legislation (i.e., tangible property that has a recovery period not exceeding 20 years, purchased computer software, water utility property, and qualified leasehold improvement property). Similar to prior "bonus" legislation, the original use of the property must commence with the taxpayer. Qualifying property must be placed in service after December 31, 2007, and before January 1, 2010. The additional bonus depreciation deduction will be allowable under the AMT.

In addition, depreciation deductions allowed with respect to certain passenger automobiles (Section 280F) are increased in the first year by an \$8,000 "bonus" for qualifying automobiles (for those not electing out of the increased first year deduction). As a result, for those contemplating a new car purchase by December 31, a deduction of \$10,960 may be available for a 100 percent business-use automobile. However, the Economic Stimulus Act did not alter the \$25,000 expensing limit for business owners acquiring an SUV or truck weighing between 6,000 and 14,000 pounds.

There are a number of considerations concerning retirement plans and IRAs. First, for this year only, a minimum distribution does not have to be taken for individuals who have reached their required beginning dates. Second, all taxpayers can make a Roth conversion of traditional IRAs in 2010 without any income limitations. We'll provide you the planning applications in an upcoming report.

This letter prepared, with the help of a nationally recognized tax authority, intends to promote interest in more comprehensive tax and estate planning. References are intentionally brief. If a topic interests you, you should investigate it more thoroughly with your qualified tax advisor. Effective tax and estate planning should involve competent advisors in relevant law, accounting, trusts, life insurance and investments. The knowledge and experience of each in their specialties can make the difference between a wealth transfer that works as intended and one that does not. Please seek competent counsel to determine and satisfy your individual needs. Securities and Investment Advisory Services offered through Capital Analysts Incorporated, Member FINRA/SIPC. AEG and CAI are independent non-affiliated entities.

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for the future*



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