

# 2011 YEAR-END TAX LETTER

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## IT'S TAX TIME AGAIN...

**The good news:** Taxes are the lowest ever, thanks to Congress. In the very last moments of 2010, Congress compromised on a tax bill that saved all US taxpayers from what would have been a substantial tax hike for 2011.

Even though tax rates are low, money is still tight. The following pages are filled with tax saving ideas to help you save tax dollars and keep more of your hard-earned money in your pocket.

## Time to get organized

*The following checklist will help you collect the documents you'll need to file your tax return. When all of the boxes are checked, you're ready.*

- Your last 3 years' tax returns (new client).** Maybe we can amend and save money.
- Social Security numbers and dates of birth** are needed for all taxpayers, spouses and dependents.
- W-2 Forms.**
- Your last paycheck stub of the year** is full of information.
- 1099 Forms for interest, dividends, retirement, Social Security, debt cancellation, and unemployment** need to be entered correctly to comply with the IRS matching program.
- Property tax statements** contain important information. They list the tax (deductible) and special assessments (not deductible).
- Forms 1098 for mortgage interest** need to be entered as printed. The IRS cross checks.
- Year-end statements from mutual funds** showing the transaction detail for the year.
- Purchase and sale information**, including dates, relating to anything sold during 2011 is needed.
- Child care provider information** (name, address, SS#, amount paid) is needed for the child care credit (even if you are reimbursed at work).
- Names, addresses, and Social Security numbers** from whom you received interest, or to whom you paid interest.
- Bankruptcy or divorce papers** (if applicable).
- If you paid an individual person \$600 or more for services rendered in connection with your business**, please provide their name, address, and Social Security number.
- Records showing income and expense for any small business or rental property you own** will be needed.
- If you have an investment in a Partnership, S Corporation, Estate or Trust** you will need to bring Form K-1.
- Bring IRA year-end statements.**
- Bring all other statements of income**, whether you think they are taxable or not.
- Forms 1098-T** and amounts paid for post-secondary tuition are needed.
- Bring your records of estimated taxes paid.**
- Student loan interest 1098-E.**
- Adoption costs** if applicable. Also bring the legal adoption documents. You will have to attach copies of all documents to your tax return.
- Form 1098-C for donations of automobiles or boats.**
- Details on all noncash donations greater than \$500.** In-



clude date, place, fair market value, and original cost.



**Caution:** the IRS is very attentive to taxpayers who write off local travel costs.

A daily log is essential.

To avail yourself of tax deductions, you need to be organized and well documented.

Save proof of all tax deductible purchases.



## DEDUCTING MILEAGE?

Did you drive for charity? If so, you can deduct 14¢ for every mile you drove.

If your medical expenses exceed 7.5% of your income, you may want to calculate a mileage deduction. Medical miles for 2011 are calculated at 19¢ per mile from 1/1/11 through 6/31/11, and 23.5¢ thereafter.

If you drove for business purposes, the situation is a little more complicated: First decide which miles qualify.

Use the following three scenarios to determine how many miles you can deduct. Keep in mind the following statement: In general, commuting is not deductible.

If you have an office or regular place of business outside your home, you may not deduct miles commuting to and

from work or to your first or from your last stop, but you may deduct mileage to drive to a temporary work place (less than one year's duration or less than 35 times a year) and mileage to and from different work locations during the day.

If you have an office in your home that qualifies for a home office deduction, all of your business-related mileage is deductible.

If you work out of your home but do not qualify for the home office deduction, the distance between home and your first stop and between your last stop and home are nondeductible commuting miles. You should carefully plan to have your first and last stops close to home to maximize the mileage deduction. A trip to the bank, post office, or a nearby supplier can help increase deductible business miles.

Once you have determined which miles to count, you need to decide whether to use the standard mileage rate or actual expenses.

The standard mileage rate for qualified business use for 2011 is 51¢ per mile from 1/1/11 through 6/30/11, and 55.5¢ thereafter.

Don't forget to record the year-end odometer reading if you are planning on a business mileage deduction.

Which method is best?

In general, the standard method works best if your business miles are high or your vehicle is economical to run.

The actual expense method works best if your vehicle weighs over 6000 pounds, is costly to run, or you do not have that many miles in total.

## DO YOU WORK AT HOME?

If you are self-employed, you may qualify for the home office deduction if you use a portion of your home exclusively as your principal place of business, to store inventory, or to conduct substantial management or administrative activities. There can be no other fixed location where the above activities can be done.

If you are an employee, your home office must be required by your employer.

The office space still needs to be used regularly and exclusively for business. You can not have any other usage of the area whatsoever. Using your office for personal or investment reasons eliminates the deduction as far as the IRS is concerned, so be careful to keep your office space and computer usage all business.

Having a deductible home office means you can deduct all of your local business travel as described earlier, and you will

not have to keep a log of computer usage because your computer will be used exclusively for business.

If your office qualifies, you will need additional information: Measure the business space and the total space. You will also need your mortgage interest, taxes, insurance, association fees, repairs, maintenance, utilities, garbage, security, and rent paid. Also, provide an accounting of the total investment in your home.

## COMPUTER & CELL PHONE GUIDELINES

Did you buy a computer that you would like to deduct? You can use the following guide to determine what is deductible.

If you are an employee, a computer must be required as a condition of employment and for the convenience of your employer to be deductible.

If you are self-employed, the business percentage of computer usage, measured by time, is deductible.

If you use your computer for investments, the business percentage of use may also be deductible if you itemize.

If you are a student, the use of a computer is not deductible, but you can tap your 529 plan for a computer purchase.

Keep a log of computer usage to support your deduction.

Cell phone deductions are as follows:

Employers providing cell phones do not have to require records of use to provide tax-free cell phones to employees.

Employees required to use cell phones for work can deduct cell phone use to the extent used for business.

Self employed individuals can deduct business cell phone usage. The IRS, however, still has a hard time believing a cell phone is 100% for business. It's wise to keep a log of use.

# WHAT'S NEW FOR 2011?

## How will you fare?

Every taxpayer benefits from the same low rates as in 2010, thanks to Congress:

In the very last moments of 2010, Congress compromised on a tax bill that saved all US taxpayers from what would have been a substantial tax hike for 2011.

**A little tax history...** In 2001 Congress passed a tax bill to slowly revive the economy over a ten year period. After the ten year period of increasingly lower taxes, the tax rates were to revert back to pre-2001 conditions. 2010 would be as good as it gets, and 2011 would be a real tax shocker. It became evident that a tax shocker would not be appropriate for our shaky economy, so Congress went to work.

If it weren't for this Congressional action, the lowest tax rate would have jumped from 10% to 15% and the highest rate from 35% to 39.6%.

**Are you a worker?** You may have noticed an increase in pay. Congress is giving you a "payroll tax holiday" for 2011. Instead of extracting 6.2% from your paycheck for Social Security, 4.2% was taken. If you spent it all, you did exactly what Congress wanted.

**Are you self-employed?** You will also benefit at tax time. Your self-employment tax calculation will be reduced by 2%. In addition, special 100% expensing rules are in effect to encourage investment in new business assets.

**Did you get a payroll tax break for hiring employees in 2010?** You may qualify for a new tax credit if the employee lasted a year.

**Are you married?** You were saved from the marriage tax penalty for 2011.

**Do you have young children?** You can still benefit from the Child Tax Credit, the Earned Income Credit, and the Dependent Care Credit at the same levels as in the past.

**Do you have children in college?** The American Opportunity Tax Credit is still a part of your tax picture if you meet the qualifications. The credit of up to \$2,500, which was scheduled to expire, helped a lot of taxpayers in 2010. Thank you Congress.

**Are you an investor?** You are still in luck. Capital gains and qualified dividends are still free of Federal tax in the 10% and 15% tax bracket and 15% for all other filers.

**Are you paying on student loans?** The interest on old loans of up to \$2,500 is still deductible as it was in 2010.

**Did you do a 2010 Roth conversion?** If you deferred the tax to 2011 and 2012, the first installment is due. If it was a bad idea to defer, you can always amend your 2010 to pay all of the tax in one year.

**Did you make energy saving home improvements in 2011?** The rules are stricter than 2010, but you may still be able to qualify for a credit of up to \$500.

**Various IRS rulings have clarified the following expenses as medical deductions:**

- Lactation expenses
- The cost of a caregiver for a dementia patient (even if the caregiver is non-licensed)
- A portion of a special diet prescribed by a doctor can be deductible if the cost of the diet exceeds the cost of what would normally be eaten.
- Fees remitted to alternative medical practitioners can be deducted.
- The cost to repair hearing aids can be deducted.

## Going, Going, gone....

2011 is your last chance to take advantage of the following tax breaks:

- Mortgage insurance premiums on your personal residence
- The teachers special deduction for up to \$250 in classroom supplies
- Sales tax instead of state income tax as an itemized deduction
- The adjustment deduction for post secondary tuition.
- Direct charitable contributions of IRA proceeds.

**The Health Care legislation that was passed in 2010 is still a part of the tax picture.** The tax provisions that still may affect you are listed below:

### Changes taking effect in 2011:

- Over-the-counter medicines will no longer be reimbursed through flex plans.
- Nonqualifying HSA/MSA distributions will be penalized at 20%.
- Drug manufacturers will pay new fees.

### Changes taking effect in 2013:

- High earning workers will pay an additional Hospital insurance tax of .9%.
- High income individuals will pay a surtax on unearned income.
- The threshold for deducting medical expenses will increase.
- Annual FSA contributions will be capped at \$2,500.
- Health plans will pay an annual fee.
- Retiree drug coverage will be eliminated.

### Changes taking effect in 2014:

- Large employers not offering health insurance must pay a penalty.
- Individuals not having health insurance face a penalty.



*Thanks to Congressional action, the tax rates, exemptions, standard deduction, and many items related to the tax we pay are the same as 2010. The tax tables were slightly indexed, however, so 2011 should not bring any tax surprises. It will be as good as it gets.*

*These are only the highlights of the legislation and rulings that were passed affecting your 2011 tax return. A good tax preparer can help you use these new laws to the fullest. You can expect the help you get from a paid professional to be even better than before. The IRS has implemented a registration, testing and education requirement for preparers starting in 2011.*



# YEAR-END TAX SAVING TIPS

## GIVE TO CHARITY

Not sure of where to start? Try [charitynavigator.org](http://charitynavigator.org) for guidance.

**Short of cash? You can still make a last minute gift.** Charge your deductions on a credit card and pay later. Consider giving through [www.justgive.org](http://www.justgive.org). You can privately give to thousands of rated charities with a credit card. Your donation goes directly to the charity, and [www.justgive.org](http://www.justgive.org) will send you a confirmation and a year-end summary to satisfy documentation requirements.

Or, better yet, you don't even have to spend money to take a charitable deduction. Clean out your closets of unwanted items to make a noncash gift. Keep in mind, the items must be in at least good condition. You should omit items of minimal value (socks and underwear), and thoroughly document the donation.

If you plan on donating a vehicle before year-end, beware of the rules. Select a charity that will either use or improve the vehicle, and you will be able to deduct *fair market value*. Otherwise your deduction will be limited to the price the charity got when they sold the vehicle. The charity will give you a 1098C documenting the contribution. The 1098C needs to be attached to your tax return.

If you have a stock or piece of property that has increased in value, you can deduct the full value and avoid paying capital gains tax by donating it to charity. If you want to give stock that has fallen in value, sell the stock, take the loss, and give the money to charity.

**Keep in mind that proof of payment is needed for donations of any size.**

## CHECK YOUR TAX PAYMENTS TO AVOID PENALTIES

The IRS will charge a penalty if your tax for 2011 is less than 90% prepaid unless your payments are at least equal to last year's tax. (110% of last year's tax if your income exceeds \$150,000).

You can boost your itemized deductions, and possibly save yourself from a penalty, by sending your last state estimated tax payment before December 31<sup>st</sup> or by stepping up your state withholding.

## CHECK YOUR PORTFOLIO

If you are in the 15% tax bracket or lower (gross income under \$43,950 single or under \$87,900 married) you may be able to sell stocks or property at a gain in 2011 and pay no Federal tax. If you are in the above tax range, or even higher if you itemize, it might be wise to check out the possibility.

If you missed out on last year's credits or deductions because your income went over the limits, it might be wise to check your portfolio for some losses to reduce your income. You can offset up to \$3,000 of other income with stock losses. If you wish to repurchase the stock again, wait at least 31 days to avoid wash sale rules.

If you are planning on deducting worthless stock, remember that it's not deductible until it's completely worthless.

In buying mutual fund shares, avoid the year-end tax trap. Year-end dividends may include a years worth of capital gain in a large taxable payout. The value of your shares declines by the amount of payout, so you end up paying tax on profits that reduce your share value.

## SELF-EMPLOYED?

Shelter up to 20% of your net income in a SEP retirement plan. Besides current tax savings, money grows tax-deferred on these investments. A SEP contribution can be made up to the due date of your 2011 tax return, including extensions.

**Pay all bills already received** for operating expenses rather than deferring payment until 2012. If you need new equipment, save tax dollars now by purchasing before year-end. Remember that you can charge on a credit card and receive a current deduction.

**Need new business equipment?** 2011 is a great year to buy. Congress passed the special 100% expensing rules just for you. This special tax break expires on 12/31/11.

**To channel your income into next year for a cash basis business,** you must be certain it is not constructively received. You can delay your billing to next year to defer income to 2012.

## AND... THE FUTURE?



One thing is certain: The government can not afford to stimulate our economy. Taxes will be a big factor in our efforts to reduce the Federal deficit.

At present, lawmakers are talking about limiting the mortgage interest deduction and the deduction for charitable contributions as well as other tax adjusting measures. Stay tuned, and give to charity now while you still can deduct it.



*The basic strategy for year-end tax planning can be summed up in the following two statements:*

- Channel your income into the year where it will be taxed at a lower rate.
- Channel your deductions to the year where your income will be taxed at a higher rate.

*Money is still tight and Uncle Sam is waiting for some of your hard earned dollars. Keep more of those dollars in your pocket this year by concentrating on organization, documentation, and a good tax preparer to help you make the right decisions.*

