

Individual Tax Strategies

2011 Year-End Tax Planning



The end of the year is often the preferred time for tax planning. You may have the flexibility to shift income and deductions to your tax benefit. However, tax planning in 2011 is shrouded in doubt as talk of major tax reform heats up. At this writing, there has been no definitive resolution of the federal budget dilemma by the government, which has commissioned a "super panel" to make recommendations. This could ultimately result in new tax legislation.

Nevertheless, several tax strategies for individuals appear to be relatively "safe" in this uncertain environment. Here are some prime examples.

Tax Strategies

Funding a retirement plan: One of the most effective ways to reduce your taxes is to fund a retirement account. Depending on your employment, you may have a company plan to which you can make contributions. By maximizing your 401(k) or 403(b) contributions, you reduce your gross income and therefore your tax. You may also qualify to make traditional IRA contributions that are a deduction against income on your tax return. Contributions to these type of plans reduce your current taxes and help you save for future retirement.

Retirement plan withdrawals: If you have reached age 70½, you should take the required minimum distributions (RMDs) from your IRA or 401(k) plan (or other employer-sponsored retirement plan). Failure to take a required withdrawal can result in a penalty of 50 percent of the amount of the RMD not withdrawn.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 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.

Capital gains and losses: If it is warranted, you may realize capital losses to offset capital gains from earlier in the year. Any excess can offset up to \$3,000 of ordinary income in 2011. Conversely, capital gains realized at year-end may absorb prior capital losses. For 2011, net long-term capital gain for the year is taxed at a maximum rate of 15 percent, while the rate is 0 percent for taxpayers in the regular 10 percent or 15 percent brackets (these tax breaks are scheduled to expire after 2012).

Family income-splitting: You may be able to reduce the overall family tax bill by shifting income-producing assets to family members, such as your children, in lower tax brackets. However, the "kiddie tax" may undermine this strategy. Generally, unearned income over \$1,900 received in 2011 by a child younger than 19 or a full-time student younger than 24 is taxed at the parents' top marginal tax rate.

Alternative minimum tax: Despite another bump in the exemption amounts, you still may be among the millions who owe the alternative minimum tax (AMT). It might make sense to shift certain "tax preference items" to 2012 to avoid or reduce AMT liability. Alternatively, you might accelerate income into this year if the AMT rate is lower than your expected top tax rate. The AMT rate is 26 percent on taxable income up to \$175,000, and 28 percent on taxable income above \$175,000.

Itemized deductions: Are your 2011 itemized deductions likely to wind up being just under, or just over, the standard deduction amount? If so, consider the strategy of bunching together expenditures for itemized deduction items every other year, while claiming the standard deduction in the intervening years. The 2011 standard deduction for married joint filers is \$11,600. The magic number for single filers is \$5,800. It is \$8,500 for heads of households. Examples of deductible items that can be bunched together every other year to lower your federal income taxes include charitable contributions and state income and property tax payments.

Charitable gifts: Generally, you can deduct the full amount of cash donations made before the end of the year. If a donation is made by credit card, you can deduct the gift on your 2011 return, even if the charge is not actually paid until next year. *Caveat:* The tax law includes strict substantiation rules for monetary contributions and additional record-keeping requirements for gifts of property.

Big ticket purchases: You may want to consider accelerating 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.

Estimated tax penalties: An "estimated tax penalty" may be assessed if you do not pay sufficient income tax during the year through any combination of withholding or quarterly installments. However, no penalty is imposed if payments equal to 90 percent of your 2011 liability or 100 percent of your 2010 liability (110 percent if adjusted gross income (AGI) was above \$150,000) are made. When possible, adjust withholding to qualify under one of these "safe harbor" exceptions or increase estimated tax payments to stop the penalty.

Remember that this is only an overview of several common year-end tax-planning strategies. Also, as noted above, the tax laws are subject to change. However, one item that does not change is the advantage of good organization of financial records. Providing your tax advisor with all of your relevant tax information in a timely manner could not only potentially reduce your taxes, it also makes filing your tax return by the filing deadline a less daunting task.

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We hope this information is helpful. If you would like more details, please contact a Kerkering Barberio professional tax advisor at 941-365-4617.