

Possible 2011 Tax Changes And Their Impact On You

As the close of 2010 is coming before too long, it is good to review some interesting financial and tax changes. As you have probably heard, several tax provisions expired at the end of 2009 and without action from Congress, numerous changes to both income and estate taxes will automatically take effect in 2011. The following is a summary and a general description only of some of those changes.

In 2010, there were changes to deductions, credits and taxes:

- The Required Minimum Distribution (RMD) rules were made optional for 2009, but back in force for 2010. If you are over age 70½ and have balances in an IRA or other cash balance retirement account, you will be required to take distributions again.
- The first \$2,400 of unemployment compensation may not be excluded from taxable income, as was allowed in 2009.
- Several other established tax breaks expired in 2009. The following have not been reinstated:
 - The above-the-line deduction for qualified tuition and related expenses, up to \$4,000, for taxpayers who itemize deductions.
 - The ability to deduct sales taxes paid instead of state and local income taxes.
 - For taxpayers over age 70½, the ability to make charitable contributions up to \$100,000 directly from IRA accounts without generating taxable income, but satisfying RMD rules.
 - The \$250 above-the-line deduction for classroom expenses of K through 12 educators.

Again, without action by Congress, several provisions in 2010 **MAY** be changed significantly beginning in 2011:

- The Hope Credit, modified for 2009 and 2010 by the American Opportunity Tax Credit, allows for a credit of up to \$2,500 for the first four years of college applies only to 2009 and 2010.
- The 30% credit for energy efficient improvements to your principal residence, up to a combined maximum of \$1,500 for 2009 and 2010, and for installation of certain alternative energy source property like solar electric systems, terminates in 2010. Qualifying improvements to your home must be completed before January 1, 2011, to take advantage of the credit.
- Both the homebuyer credit and the long-time resident homebuyer credit expired after April 30, 2010, but the period allowed to close on a home contracted before May 1 was extended to October 1, 2010.
- The child tax credit drops from \$1,000 to \$500 per qualifying child beginning in 2011.
- The lower income tax rates and the elimination of the estate tax passed in 2001 will reset to pre-2001 levels. Therefore, the initial 10% income tax bracket is eliminated and the other rates increase by 3% or more, with the top rate going back to 39.6%.
- The estate tax will return to the \$1 million exemption level in 2011.
- The 15% long-term capital gains rate increases to 20% and the rate applied to qualified dividend income will revert from the capital gains rate to ordinary income rates. In other words, qualified dividends taxed at 15% for 2010 will be taxed at rates as high as 39.6%.

Alternative Minimum Tax

The Alternative Minimum Tax (AMT) is a separate tax system that you may fall into if your AMT liability is greater than your regular tax liability. For 2010, the exemption amounts drop to \$45,000 for married joint filers and \$33,750 for singles. As it stands, if the AMT exemption amounts revert to their pre-2001 levels, the number of individuals subjected to the AMT will increase from 4 million in 2009 to an expected 27 million in 2010.

Congress and the administration have discussed numerous alternatives to the above changes.

Roth Conversions

If you have a traditional IRA, you have an option to convert to a Roth IRA. Special rules apply for 2010. The AGI limit was eliminated beginning in 2010, so many IRA contributors whose adjusted gross income was too high to use a Roth IRA can now convert. Any income recognized is taxed half in 2011 and half in 2012 unless you elect to claim it all in 2010. You may want to consider that election if you believe your tax rate will increase after 2010. There is also a "redo" provision. You can re-characterize a conversion back to a regular IRA and avoid the tax by the extended due date of your income tax return for the year of conversion.

We do not provide legal or tax advice, so please contact your tax advisor to determine application issues of these potential changes to your situation, along with any applicable limitations, restrictions or conditions, as well as what changes actually come from Washington DC before the end of the year.

We look forward to speaking to you at your next review; don't hesitate to contact us in the meantime.

Source:

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