



## Wealth Resources Network

*The Wealth Achievement Center of CNY*

### **2010 MID-YEAR TAX PLANNING MEMO**

With the tax law changes currently swirling around Congress, tax planning for 2010 is like trying to hit a moving target. But even in this period of uncertainty, there are definite steps you can take to score a tax-cutting bull's eye.

#### **WATCH YOUR WITHHOLDING AND ESTIMATED TAXES**

A few tax-smart moves remain the same every year, such as maximizing your retirement account contribution, keeping good records, and reviewing your tax withholding or quarterly estimated payments. An added twist this year might be how the economic and job market conditions affect your withholding or tax estimates. If you recently had a job change, received taxable unemployment benefits, or made an emergency withdrawal from your retirement account, you may need to adjust your withholding. A new home mortgage, change in dependents, or a forgiven business loan can also move you off track. And getting your estimated taxes right is particularly important in 2010. Last year certain taxpayers could base their estimates on 90% of the previous year's taxes. This year the old 100% and 110% rules apply once more and underpayments are penalized.

#### **REVIEW YOUR RETIREMENT PLAN**

Back in the mix for 2010 are required minimum distributions (RMDs) from retirement plans. After a one-year hiatus, taxpayers age 70½ and older (and those who inherited a retirement account) are again required to take taxable annual distributions. 2010 distributions must be taken by December 31, 2010, with no grace period. Taxpayers who turn 70½ in 2010 may choose to delay taking their first distribution until April 1, 2011. Note that annual distributions are not required for Roth IRAs. On a positive note, the \$100,000 income limitation for converting a traditional IRA to a Roth IRA is gone, opening the door to many taxpayers who were otherwise excluded from this popular strategy. Contribution limits for retirement plans stay the same in 2010. For 401(k) and 403(b) plans, the maximum you can put away is \$16,500. If you are 50 or older, a catch-up contribution is allowed and you can contribute up to \$22,000. The contribution limit for SIMPLE plans is \$11,500 (\$14,000 if you are 50 or older).

#### **THE ROTH QUESTION: SOME FACTS TO HELP YOU DECIDE**

No matter what the recent flurry of news coverage might lead you to believe, Roth IRA conversions are not new. They have been around since 1998, when Roth IRAs first became available – and so have the when-how-who planning questions you're pondering now. So what is new? Effective January 2010, the income and filing status restrictions that limited who could transfer money from existing retirement accounts to a Roth IRA disappeared. Now any taxpayer at any income level and with any filing status is able to convert all or part of a traditional IRA to a Roth IRA. Here are some additional facts to help you decide whether you should consider a Roth conversion. In 2010 and future years, you can convert traditional IRAs, SEP IRAs, SIMPLE IRAs, and certain other retirement accounts to a Roth no matter what your income is. If your retirement accounts contain nondeductible contributions, part of the conversion may be tax-free. Nondeductible contributions are amounts you contributed with after-tax dollars. The rules for making regular contributions to your Roth have not changed. For 2010, when you are married filing jointly and your adjusted gross income (AGI) is less than \$167,000, you can contribute up to \$5,000 (plus \$1,000 catch-up if you are 50 or older). The AGI limit for a

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maximum contribution is \$105,000 if you are single. If you convert to a Roth during 2010, you can choose to include one-half of the income on your 2011 federal income tax return and one-half on your 2012 return. Because the amount you convert is generally subject to ordinary income tax, you might need to adjust your federal and state tax estimates to avoid an underpayment penalty. Get the most benefit from a conversion by using non-IRA funds to pay the tax. Amounts withheld from your conversion distribution or that you withdraw from your IRA – even when you apply the money to your tax bill – can be subject to a 10% penalty. If you are over the AGI limit for regular Roth contributions, you can make nondeductible contributions to a traditional IRA, and then convert them to a Roth. If you change your mind, you have until October 17, 2011, to “undo” a Roth conversion made during 2010 (called a recharacterization). Some states tax IRA distributions, including conversions, which may influence your decision. Future qualified withdrawals of your converted assets are tax-free. Even better is the fact that with a Roth IRA, you are not required to take withdrawals at all. Need more information about Roth conversions? Give us a call. We can answer your questions and help you decide the best strategy for your situation.

### **MAXIMIZE YOUR DEDUCTIONS AND CREDITS**

Many itemized deductions and tax credits are in Congressional limbo right now. For example, some tax breaks that have expired or are about to expire might be renewed. To minimize your taxes, you need to stay aware of the status of credits and deductions so that you can adjust your planning accordingly. One definite tax break for 2010: the phase out of itemized deductions and personal exemptions for high-income taxpayers has been removed. The 2001 tax law gradually restored the full deduction for personal exemptions and itemized deductions for higher-income taxpayers. Effective this year, high-income taxpayers are entitled to the full \$3,650 deduction for each personal exemption they take, and there will be no income-based reduction in their total itemized deductions. As with most other provisions in the 2001 tax law, this change ends after December 31, 2010, and itemized deductions and personal exemptions will again be limited for high-income taxpayers in 2011. If you missed the homebuyer tax credit, you are out of luck unless Congress decides to bring it back. But homeowners can still score an energy tax credit! For 2009 and 2010, you can receive a tax credit of 30% of the cost of qualifying home improvements made over the two-year period. The maximum credit is \$1,500 for both years combined. Qualifying improvements include a new heating and air conditioning system, insulation, doors, and windows. Energy tax credits for big-ticket items, such as geothermal systems, are also available.

### **HEALTH CARE REFORM FOR YEARS TO COME**

2010 • A 10% tax is imposed on indoor tanning services. • Adoption tax credit increases to \$13,170, made refundable, extended through 2011. 2011 • Small businesses with up to 25 employees may qualify for a tax credit of up to 35% of the cost of purchasing health insurance for their employees. • A long-term care insurance program is created, financed by voluntary payroll deductions. • Value of health insurance coverage must be reported on employees' annual Form W-2s. • Participants cannot buy over-the-counter medication with funds in medical savings accounts. • Penalty tax increases to 20% on nonqualified distributions from HSAs. 2012 • Form 1099s must be filed with the IRS for payments of \$600 or more made to corporations. 2013 • Health flexible spending account contributions limited to \$2,500 per year, indexed for inflation. • The 7.5% income threshold for deducting unreimbursed medical expenses increases to 10% for those under age 65. For those 65 and older, the threshold remains at 7.5% through the year 2016. • The payroll Medicare tax increases from 1.45% of wages to 2.35% on amounts above \$200,000 earned by individuals and above \$250,000 earned by couples filing joint returns. • A 3.8% Medicare tax is imposed on unearned income for

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single taxpayers with income over \$200,000 and couples with income over \$250,000. 2014 • Individuals are generally required to maintain health insurance coverage or pay a penalty calculated on a percentage of their income or a flat dollar amount. • Large employers generally must provide coverage for employees or face penalties. • Maximum small business tax credit for providing health insurance for employees increases from 35% to 50%. 2018 • Insurance companies will be assessed a 40% excise tax on health insurance plans with annual premiums exceeding \$10,200 for individual coverage and \$27,500 for family coverage. Higher thresholds apply for those 55 and older and those in high-risk jobs.

### **MIND YOUR BUSINESS (TAXES)**

New legislation in 2010 has brought a fresh set of opportunities and challenges for businesses. The HIRE Act passed in March gives employers a tax incentive to hire workers who have been unemployed for a while. Employers can receive an exemption from social security payroll taxes for every qualified worker hired after February 3, 2010, and before January 1, 2011. For new hires kept on the payroll for at least 52 weeks, employers may qualify for a tax credit for each retained worker of the lesser of \$1,000 or 6.2% of wages paid during the 52-week period. The payroll tax forgiveness provided in the law does not apply to the Medicare portion of the tax. In addition, the new employee cannot displace a current employee unless that employee quit or was fired for cause. Relatives of the employer are not considered qualified employees for these tax breaks. The HIRE Act also reinstates for 2010 the \$250,000 expensing limit for purchasing new or used business equipment. This is a one-year extension only, and it does not include an extension of bonus depreciation allowed last year. The health care reform legislation passed in March will bring tax changes for years to come. One immediate benefit is a tax credit available for small businesses that provide qualified employee health insurance benefits. The credit is generally available to small companies and tax-exempts that pay at least 50% of the cost of single coverage for their employees. For 2010, the maximum credit is 35% of premiums paid by businesses and 25% of premiums paid by tax-exempt organizations. The maximum credit goes to those employers with ten or fewer full-time equivalent employees who pay annual average wages of not more than \$25,000. The credit gradually phases out for firms with average wages between \$25,000 and \$50,000 and between 10 and 25 employees.

### **SUMMER TAX TIPS**

Make your summertime fun even more enjoyable by adding tax savings. With some planning, you can make it happen. Here are some ideas to consider. Combine business and vacation travel. Travel expenses are deductible if the travel is undertaken primarily for business purposes; thus, you may wish to combine attendance at an out-of-town business conference with a visit to family or friends. The expenses attributable to the personal part of the trip, though, remain nondeductible. When doing any business traveling, make a distinction in your records between expenses for lodging and transportation and those for meals and entertainment. Only the latter are subject to a 50% deduction limitation. If you are going to be out of town for a while, consider renting out your home while you are gone. The IRS allows you to receive up to 14 days of rental income per year completely tax-free. In fact, you do not even have to report the income on your return. If you itemize your deductions, you can deduct the mortgage interest and property taxes paid for your vacation home. A boat or RV can qualify as a vacation home if it has sleeping quarters, cooking facilities, and a bathroom. If a retreat also serves as rental property, you can control your tax deductions by changing the number of days you use it for vacation. If you and your spouse work, the cost of sending your children to a summer day camp may qualify for the childcare credit. If you own a business, consider hiring your child for the summer. Your child can

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earn up to \$5,700 tax-free this year, and your business is entitled to a deduction for the wages paid. You must pay your child a reasonable wage for the work performed. If your business is not incorporated, your child under 18 is not subject to FICA taxes.

### **SUMMARY**

Developing a solid tax plan from year to year is difficult enough, but responding to this year's fluid tax law environment is especially challenging. Even so, the best tax tip remains the same: stay in touch with us. We will be monitoring legislation for changes that could affect your tax and business situation. For a midyear tax review, give us a call today.

*NOTE: This newsletter is issued at midyear to provide you with information about minimizing your taxes. Do not apply this general information to your specific situation without additional details. Be aware that the tax laws contain varying effective dates and numerous limitations and exceptions that cannot be summarized easily. This information is not intended to be a substitute for specific individualized tax, legal or investment planning advice. We suggest that you discuss your specific tax issues with a qualified tax advisor. For details and guidance in applying the tax rules to your individual circumstances, please contact us at (315) 471-7833.*

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