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Politics and Tax Planning – Much Uncertainty

Mid-term elections were in November and with the house changing parties it will be hard to tell what may or may not change. Federal income tax rates, some which have been in effect since 2001, are set to expire December 31, 2010. Rumors abound on what is going to happen, in Washington DC. What is the impact to you? Tax planning will be more difficult this year. Many expiring tax breaks will likely be extended in the lame-duck congressional session by year end or early in 2011.

TAX PLANNING FOR PERSONAL TAXES

ACT FAST...Items currently slated for expiration --

Tax Credits for energy savings home improvements. You can claim a tax credit for 30% of the cost of certain skylights, outside doors, insulation, water heater, electric heat pump hot water boiler, windows and pigmented roofs as well as for high-efficiency furnace and central air conditioners. The maximum credit is \$1,500, limited by the amount of any nonbusiness energy credits you took in prior years.

Currently long-term capital gains rates are scheduled to increase in 2011

Long-term Capital Gains Rates	<u>2010</u>	<u>2011</u>
Income Tax Bracket 10%	0%	10%
15%	0%	10%
25% and above	15%	20%

Give me some credit...on my taxes

The Making Work Pay Tax Credit will again be in effect for working individuals in 2010, \$400 for singles and \$800 married filing joint tax returns. The credit will be calculated at a rate of 6.2% of earned income and will phase out for taxpayers with a Modified AGI in excess of \$75,000 or \$150,000 married filing joint.

Solar Credits are still ablaze. Homeowners can also claim a 30% tax credit for the cost of solar energy systems used to heat air or water, fuel cell property, small wind energy property and geothermal heat pump property. Solar heaters for pools and hot tubs will not qualify. The credit is for property placed in service through December 31, 2016.

Arizona School Credits and "Working Poor" Donations for a Credit

The public school tax credit, \$200 single \$400 married and likely the private school tuition tax credit of \$500 and \$1000 married.

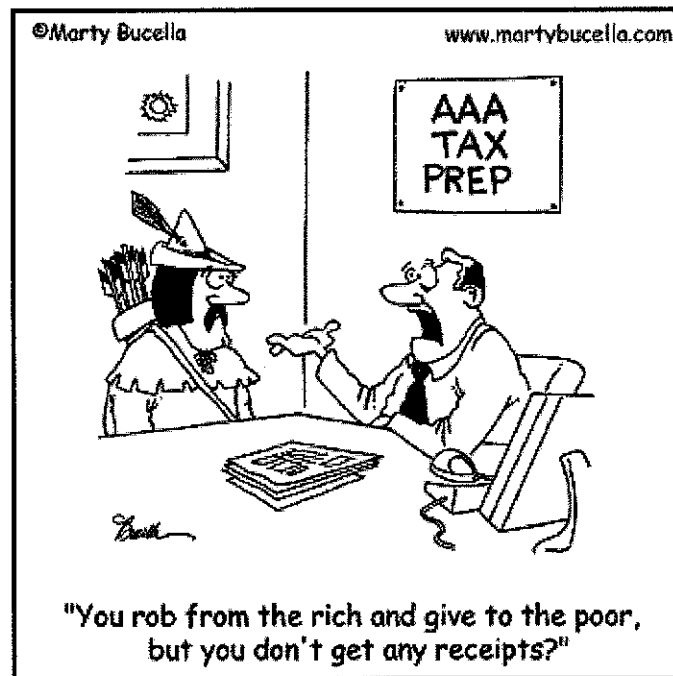
The private school tuition tax credit is being challenged in the US Supreme Court. What does that mean about the credit, we are not sure? If it is deemed to violate separation of church and state, we do not think they would repeal it retroactively.

In 2010, if you made a donation to a qualifying "**Working Poor**" charity, if you itemize, you can take an Arizona Tax Credit (\$200 filing single / \$400 married filing jointly). Any unused credit can be carried forward 5-years!

Check the link for "Working Poor" charities and updates.

<http://www.azdor.gov/LinkClick.aspx?fileticket=fHenh3bja6w%3d&tabid=133>)

In addition to the qualifying "**Working Poor**" charity credit there is a **Military Family Relief Fund Credit**. A donation made to the Arizona Department of Veterans' Affairs' may qualify as a dollar for dollar Arizona tax credit. The Military Family Relief Fund Tax Credit, assists families of Arizona service members injured or killed fighting. Please visit the website to download the application. http://dvs.az.gov/benefits/relief_fund.aspx Taxpayers need to have a receipt from AZDVS that indicated they are eligible for the \$200 single or \$400 married credit. This credit is in effect through December 31, 2013.



Arizona Withholding

For wages paid after July 1, 2010, the amount of Arizona tax withheld from an employee's wages will not be a percentage of the federal withholding. The amount required to be withheld is based on new Arizona withholding tables. Please review the new A-4 to adjust your withholding

First Time Homebuyer Credit, First Year Repayment

If you took the first time homebuyers credit, for a home purchased between April 9, 2008 and January 1, 2009, your first of 15 even payments is due for the tax year 2010. The maximum credit was 10% of the purchase price up to \$7,500. So if you receive the full credit of \$7,500 your first payment of \$500 is due with the 2010 tax return.

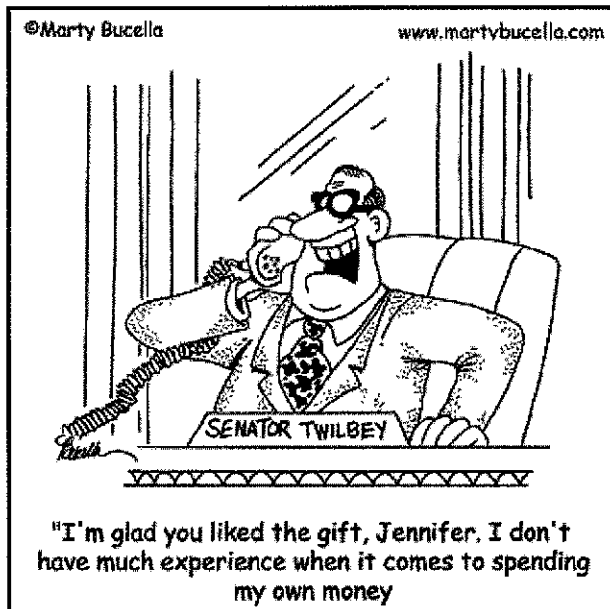
Flex Spending Accounts

If you have a balance in your FSA you can use it on over-the-counter (OTC) medicines or drugs in 2010. Starting January 1, 2011 you cannot purchase OTC and get reimbursed. This change does not effect purchasing insulin, medical devices, (i.e. eye glasses, contact lenses) co-pays, and deductibles. Distributions from HSA or MSA that are not used for qualifying expenses will be subject to a 20% penalty.

A similar rule goes into effect for Acher MSAs and Health Savings Accounts.

Great Savings for Self Employed (Schedule C Filers)

If you are self employed, you can now deduct self-employed medical premium on your Schedule C, saving you on self-employment taxes. This will be a very nice deduction for the Schedule C filers.



Social Security 2011

In 2011 there will be no Cost of Living Adjustment for the second straight year. This is the result of no change in the Consumer Price Index for Urban Wage Earners and Clerical Workers, again. Social security wage base remains at 2010 level of \$106,800 for 2011. Since there is no COLA then by law this amount remains the same. This means for 2010 the non-Medicare portion of social security remains at \$13,244 (\$6,622 employer, \$6,622 employee).

Unemployment Benefits Taxable in 2010

Unemployment benefits will be taxable in 2010. In 2009 the first \$2400 of unemployment benefits were excluded from tax, however there has not been an extension of that provision for 2010 benefits.

Year-End Tax Planning-Overview

In the past the general rule-of-thumb for year-end tax planning was always to defer income to the next year and accelerate deductions into the current year. Now, with the strong possibility of changes to the upper-end of the tax tables for 2010, it may make more sense to do the opposite in anticipation of the top brackets increasing from 33% and 35% to something significantly higher.

The general rules of year-end income shifting are still valid for most people.

Postpone Income Until Next Year:

Income from employment may not be easily switched from year to year, but there could be some flexibility for bonuses and commissions. If your company has a 401(k) or a Simple plan, consider investing your year-end bonus in the plan if you have not reached the maximum amount.

Business owners have flexibility in deferring income. Sales and billing can be deferred until the following year.

Social security recipients need to be aware that their social security can become taxable as modified adjusted gross income exceeds \$32,000 married, \$25,000 single. A sudden increase in other income may make Social Security as much as 85% taxable.

Also, increases in income reduce amounts available for medical deductions and miscellaneous deductions.

Take Deductions Now:

Pay State Income Tax – If you will owe state income taxes, (and will not be subject to alternative minimum tax) pay them by year-end. Either have more state taxes withheld or make the state fourth quarter estimated tax payment in December rather than by January 15, 2011.

Medical – Remember ALL medical is fully deductible in Arizona. Schedule and pay for medical deductions by year-end (eyeglasses, dental, surgery, etc.). Remember, medical is subject to federal limitations (7.5% of adjusted gross income), so it may pay to “bunch” them into one year instead of over two years.

Deduct Points Paid on a Primary Residence – Mortgage points can be deducted in full by the buyer in year of home purchase. Same is true of points paid on home improvement loans. Points being amortized on an old loan may be fully written-off in the year of a refinance.

Mortgage Interest – You may deduct mortgage interest on two residences. The limits on the deduction are \$1,000,000 combined total mortgage on the two homes. You can also deduct the interest on an additional \$100,000 of home equity loans. Boats and motor homes qualify as residences if they have a stove, bed and toilet.

Home Mortgage Insurance Deduction – If your adjusted income is under \$109,000, mortgage insurance premiums on a new policy (acquired in 2008) are now deductible as interest expense. This deduction has been extended through 2010.

Donate To Charity By Year-End – Donations of \$250 or more require a statement from the charity (your cancelled check is not good enough). Cash donations (Salvation Army kettle or church basket) must have a receipt from the charity in order to qualify for a deduction. **UNBELIEVABLE!!!!**

Noncash donations of appreciated stocks usually get full fair market value deduction. Used donated items (such as clothing and household goods) should be valued at what the charity could sell them for. A list of the items (and possibly photos) and a receipt from the charity would be good support. Items are required to be in good or better condition. Go to salvationarmyusa.org for their valuation guide. The donation of a car or boat requires an IRS form from the charity (Form 1098-C) showing what it sold for.

Take Sufficient Capital Losses to Offset Any Capital Gains – For 2010, most people with stock market investments have an unrealized gain. If you can create realized losses (not in IRA or other retirement plans) by selling stocks you have no desire to keep, sell enough to offset any capital gains from other sources plus an additional \$3,000 to offset other ordinary income. Any capital loss in excess of this carries forward to future years.

Didn't we do this last year?

Homebuyers credit:

Please call us to discuss if you qualify for a homebuyers credit. A personal residence that was under contract prior to April 30, 2010 and settled before September 30, 2010 may qualify. There is no credit for purchases that were under contract after May 1, 2010.

California Friends: They will be delaying tax refunds again this year due to a stalemate on budget approval. Returns filed after October 7, 2010 will be subject to this delay. The controller's website does not mention if this will be in effect for 2010 tax returns filed in 2011, however it is a possibility.

College – Less Taxing !?

College Tax Credits– The Hope Credit, has been replaced by the American Opportunity Tax Credit (AOTC). The AOTC is calculated by taking 100% of the first \$2,000 and 25% of the next \$2,000 of expenses for a maximum of \$2,500. This is available for 2009 and 2010 and applies to the first four years of college. The income phase out starts at \$80,000 single and \$160,000 joint filing. The Lifetime Learning Credit is equal to 20% of expenses up to \$10,000 (maximum credit \$2,000). Those credits are phased out based on income, the phase out begins at \$100,000 on a joint return. (Note: you cannot claim both credits for the same student). Instead of the credit you may be able to take up to a \$4,000.00 deduction

Student Loan Interest – You can deduct up to \$2,500 of interest paid on an education loan in 2009 and 2010, but the deduction begins to phase out as your gross income goes from \$60,000 to \$75,000 for singles and from \$120,000 to \$150,000 for married filing joint.

Housing Woes

What to do with Residential Foreclosure, Repossessions or Short Sales

If your **principle residence** was foreclosed, repossessed, or short-sold and you received a 1099-A or a 1099-C it is imperative that you provide that to us so we can correctly prepare your tax return.

In addition, if you had a **second home or rental property** that was foreclosed, repossessed, or short-sold and you received a 1099-A or a 1099-C it is imperative that you provide that to us so we can correctly prepare your tax return. Since this is not your primary residence it is reported differently.

Debt Forgiven on a Residence Repo

Up to \$2 million of debt discharge can be excluded from tax if the debt was used to purchase or improve the home. Amount excluded goes to reduce property basis. If you are contemplating walking from your principle residence, please keep in mind that this mortgage relief for solvent taxpayers is in effect through 2012.

Conversion of Traditional IRA to a Roth IRA In 2010, the income and filing status restrictions on converting a traditional IRA into a Roth IRA no longer apply. Please plan with us if you are looking to do this, you may face tax consequences. If you did convert a traditional to a Roth IRA you have the option to spread the tax consequences equally to 2011 and 2012.

Regular IRA Accounts

You can contribute \$5,000 to an IRA for 2010 (Plus \$1000 additional catch up if you are over 50).

You can contribute \$5,000 for a NON-WORKING SPOUSE.

Contributions to regular IRA accounts must be made by April 15, 2011 to qualify for the deduction this year.

If you are covered by an employer retirement plan, you can still deduct an IRA contribution for yourself, but this deduction phases out when modified adjusted gross income for 2010 reaches between \$56,000 to \$66,000 for singles, and \$89,000 to \$109,000 for married filing joint.

However, if you are covered by an employer retirement plan and your spouse is not, your spouse may make an IRA contribution if modified adjusted gross income is less than \$177,000.

Roth IRA's Are Generally Tax Free Forever!!

If age 59 ½ and held 5 years, no tax on interest, dividends or appreciation.

If age 59 ½ but not held 5 years, taxed but no penalties.

If you are under 59 ½ and not held 5 years, both tax and penalties apply upon distribution.

Nondeductible contributions of \$5,000 may be limited based on modified adjusted gross income.

Can make contributions after age 70 ½ (unlike current IRA's).

No required minimum distribution at age 70 ½.

You may still be in employer retirement plan and have a ROTH IRA.

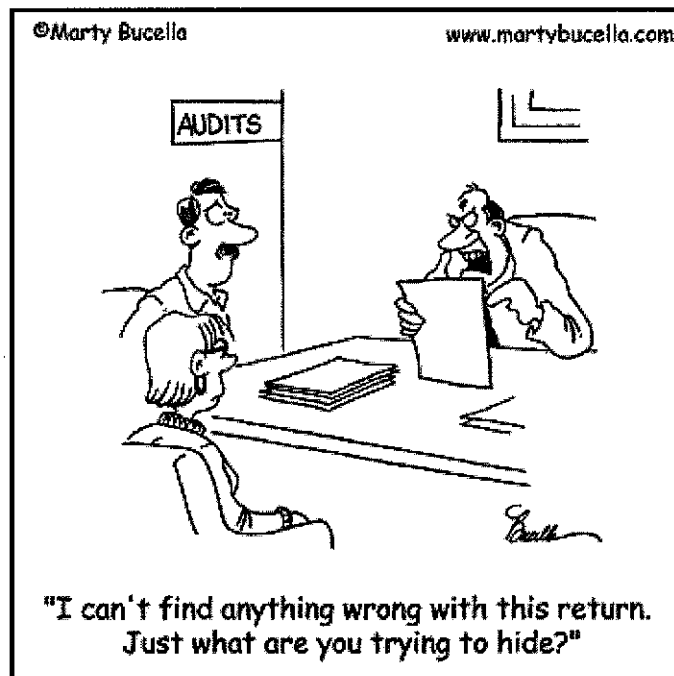
Other Retirement Plans – Think about contributing more to your 401(k) or 403(b) plan at work. If self-employed, set up a Keogh plan by year-end. A SEP Plan may be set-up and funded as late as the extended due date of your 2010 tax return. A 401(k) for sole proprietors combines the deferrals of a 401(k) with the flexibility of a profit sharing plan. This also must be set up prior to year-end.

Solo 401(k) If you are self employed and have no employees a Solo 401(k) is a good way to accelerate your deductions. Please contact us to discuss the benefits of this retirement plan option.

Retirement Plan Required Minimum Distributions are again required for 2010 and 2011. If you are 70 ½ years young you are required to take distributions from your IRA, 401(k), Profit-Sharing, Money Purchase Plan or 403(b) Plan.

Standard Mileage Rates for 2010 and 2011

	<u>2009</u>	<u>2010</u>	<u>2011</u>
Business Use	55.0	50.0	50.0
Medical & Moving	24.0	16.5	16.5
Charity	14.0	14.0	14.0



LETS GET DOWN TO BUSINESS!

If you are starting a new business new regulations allow you to deduct start up expenditures up to \$10,000 subject to a \$60,000 total start up expense phase-out. The old amounts were \$5,000 and \$50,000.

PAYROLL and EFTPS

If you are a small business and have payroll liabilities greater than \$2,500 quarterly you will need to enroll in the Electronic Federal Tax Payment System (EFTPS) to make your 2011 payroll tax deposits and corporate income tax payments. The old Form 8109 payment coupons will not be accepted after December 31, 2010.

Failure to enroll may result in a 10% penalty. See www.eftps.gov or call 800-555-4477 for more information.

NEED NEW ASSETS?

Section 179 keeps getting better and better! You may be able to deduct up to \$500,000 in 2010 and 2011 for new asset purchases. The deduction phases out if you have purchased more than \$2.0 million in assets each year. New to Section 179 are renovations of restaurants, retail stores plus improvements landlords make for retail tenants. The amount available for improvements under Sections 179 is limited to \$250,000.

We still have 50% bonus depreciation in 2010, on qualified new property purchased and placed in service in 2010.

WHAT IS THE CREDIT CARD PROCESSING COMPANY SENDING?

Starting with payments received on or after January 1, 2011, credit card processing companies are required to send a 1099-type form to businesses. This will be sent if your credit card sales are greater than \$20,000 or total transactions are greater than 200.

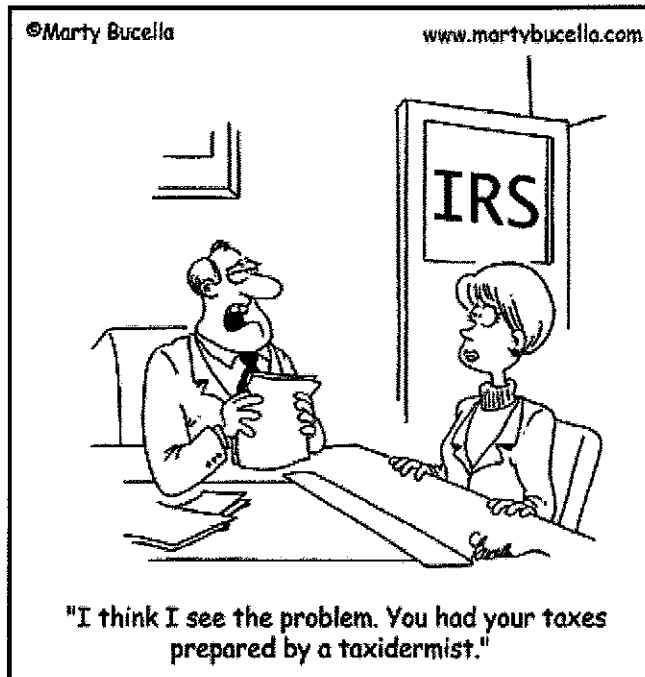
START COLLECTING INFO NOW FOR EMPLOYEE MEDICAL PREMIUMS

Start specifying medical premiums amounts paid to each employee. In the future this will likely be reported on the W-2 for the employee.

BIG CHANGES FOR 1099 REPORTING

If you are a landlord you are required to send 1099's to service providers who you pay more than \$600. This includes, landscapers, handyman, plumber, and accountant. You are required to get name, address, and social security numbers to ensure proper work rights.

For calendar year 2012 it is required that you file a 1099-misc to everyone you pay more than \$600 in cash or checks, including the landlord. You will need your vendors to complete a form W-9. (Credit card purchases will be reported to the vendor by the credit card processing company) The link for W-9s, <http://www.irs.gov/pub/irs-pdf/fw9.pdf>



HEALTH CARE TAX CREDIT FOR HEALTH INSURANCE PAID

To be eligible for the credit here is what your company needs to do:

- A qualifying employer must cover 50% of the cost of health care coverage for some of its employees based on the single rate
- The firm must have the equivalent of less than 25 full time workers (fewer than 50 part time workers may qualify)
- Average annual wage must be less than \$50,000

The credit is up to 35% of small business premium costs in 2010. In 2014, the credit will increase up to 50%

The credit phases out gradually for firms with average wages between \$25,000 and \$50,000 and for firms with the equivalent of between 10 and 25 full time workers.

Please contact your payroll provider requesting employee reports on the credit. Or request an employee listing, showing total hours worked and total wages. Also tabulate the total your company paid for health insurance to each employee and we can help calculate the potential credit.

Note that the potential credit reduces the deduction for health insurance by the amount of the credit.

Business Deductions – Prepay business expenses (some limits). Write off obsolete inventory at year-end. Write off bad accounts receivable and look for additional accounts payable at year-end (if on accrual basis). Look for business deductions that were paid personally but are really business related – for example business travel and entertainment, dues, subscriptions, etc. Autos and light trucks also benefit if they are used for business. Maximum first-year depreciation write off for cars has increased to \$11,060 and trucks to \$11,160.

Tax Rate Schedules

There are currently 6 major tax brackets for individuals:

Single Individual 2010			Married Filing Jointly 2010		
Taxable Income			Taxable Income		
<u>Over</u>	<u>But not over</u>	<u>Tax Rate %</u>	<u>Over</u>	<u>But not over</u>	<u>Tax Rate %</u>
\$0	\$8,375	10	\$0	\$16,750	10
8,375	34,000	15	16,750	68,000	15
34,000	82,400	25	68,000	137,300	25
82,400	171,850	28	137,300	209,250	28
171,850	373,650	33	209,250	373,650	33
337,650	-----	35	373,650	-----	35

Head of Household 2010			Married Filing Separate 2010		
Taxable Income			Taxable Income		
<u>Over</u>	<u>But not over</u>	<u>Tax Rate %</u>	<u>Over</u>	<u>But not over</u>	<u>Tax Rate %</u>
\$0	\$11,950	10	\$0	\$8,375	10
11,950	45,550	15	8,375	34,000	15
45,550	117,650	25	32,550	68,650	25
117,650	190,550	28	68,650	104,625	28
190,550	373,650	33	104,625	186,825	33
357,700	-----	35	186,825	-----	35

- Personal exemptions are \$3,650 per person for 2010
- Long term capital gains rates for 2010:
 - 0% if tax bracket is 10% or 15% (10% rate in 2011)
 - 15% if tax bracket is over 15% (20% rate in 2011)
 - 25% Depreciation Recapture on Real Estate
 - 28% Collectables (i.e. 1957 Chevy)