

Taxes - Year-End Planning

The year-end is always a scramble. Aside from the holidays, HNW and affluent clients need to consider last minute tax planning opportunities. The client's accountant is typically involved, running year-end estimates. But if you're the client's primary Advisor, you'll want to make sure that the client and his or her accountant are considering all the possibilities.

The Usual Suspects

To begin with, it's important not to overlook the usual tax planning ideas that essentially seek to defer income and accelerate deductions. Accelerating deductions may be even more important in 2009 because many believe income taxes, especially for the wealthy, are poised to rise in the near future. Discuss the following with your clients:

Charitable donations—Although substantiation requirements for charitable gifts are more extensive than prior to 2007, year-end charitable giving continues to make sense. Outright gifts of most types of property to public charities are deductible up to 50 percent of AGI. Amounts above the limit may be carried over for five years. Clients need to know that the Obama Administration has proposed further limiting charitable deductions for taxpayers in the highest (35 percent) tax bracket, beginning in 2011. Under the Administration's plan, the tax benefit from a charitable deduction would be limited to that available for taxpayers in a 28 percent bracket. For example, while a taxpayer in a 35 percent bracket would normally receive a \$350 tax benefit from a \$1,000 charitable contribution, the Administration's proposal would limit the benefit to only \$280.

State taxes—Most HNW and affluent clients pay quarterly estimated taxes. Assuming state law allows prepayment of the final quarterly installment in the current year, taxpayers can accelerate the deduction by paying prior to December 31. Similarly, to the extent prepayment of real estate and personal property taxes is allowed under state law, clients may wish to take advantage of the opportunity.

Retirement Plan Contributions—Although contributions to IRAs, Individual 401(k) plans, and SEPs are deductible for the current year, so long as they are made prior to April 15 of 2010, the plan must be established this year in order for the taxpayer to take the deduction. Getting the paper work completed before year end can take anywhere from a few days to a week or more, so make sure self-employed clients get the ball rolling early enough to make the year-end cut-off.

Minimum distributions from retirement plans—Minimum distribution requirements from IRAs and qualified retirement plans, are waived in 2009. But some clients may have received a minimum distribution anyway, if their financial institution made a mistake or didn't have its payment system shut down earlier in the year. Fortunately, clients can rollover these errant distributions into an IRA or other retirement account and avoid current taxation. Better hurry, though. The rollover must be completed by Dec. 1, 2009, or within 60 days of the receipt of the distribution, whichever is later.

Non-qualified Plans—Many highly-compensated executives participate in non-qualified deferred compensation plans. As a general rule, in order for the deferral to be effective, the executive must defer the income before it is earned. Be aware of the plan details and make sure your clients are maximizing deferral opportunities.

Tax Planning for Investments—This has been a mostly up year for the equity market. But for those clients who have experienced losses, there is a silver lining at tax time. Up to \$3,000 of a net capital loss can be applied to offset other income, for example salary. Excess net losses can be carried over until next year subject to the same limit. Remember, however, that just because a particular stock dropped in value, doesn't mean the client has a deductible loss. First, the loss must be realized, i.e. the stock must be sold for a loss prior to December 31. Second, keep in mind, that the amount of the deductible loss is *not* measured by the amount of value the stock lost from its "high," but rather the difference in basis and sales price. Thus, for example, a client whose stock in Company A dropped from a high of \$40 per share to \$30 per share, doesn't necessarily incur a *taxable* loss. If the client bought at \$22 per share, he or she would actually have a *taxable* gain of \$8 per share, if the stock were sold for \$30 per share.

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Special Considerations for 2009

In addition to the usual planning, 2009 presents some unique year-end planning opportunities. Clients, or their businesses, need to "use or lose" these deductions and credits.

Bonus Depreciation—Businesses and self-employed individuals may qualify for the 50 percent bonus depreciation on qualified business property purchased in 2009. Bonus depreciation is available to all businesses and applies to most types of tangible personal property and computer software acquired and placed in service in 2009. Taxpayers may deduct 50 percent of the entire cost of qualifying property *in addition to* regular depreciation. Unless this special bonus

depreciation is extended, it will not be available after December 31, 2009.

A great way for clients to get a double-bang for their buck is to make a cash gift (taking advantage of the gift tax annual exclusion), which the donee uses to make a first-time home purchase (taking advantage of the first-time homebuyer's credit). It's a nifty transfer of wealth to younger-generation family members that completely circumvents the tax system.

Section 179 Depreciation Deduction—The Section 179 deduction has been increased through 2009, up to \$250,000 for machinery, equipment, vehicles, furniture, and other qualifying property placed in service during the year. Section 179 deduction allows businesses to “expense” an item in one year, rather than depreciating its cost over several years.

COBRA Subsidy—The American Recovery and Reinvestment Act of 2009 (ARRA) provides for premium reductions and additional election opportunities for health benefits under COBRA. Eligible individuals pay only 35 percent of their COBRA premium. The remaining 65 percent is subsidized by the employer, then reimbursed through a tax credit. Through 2009 only, the employer may reduce employment tax deposits to reflect the anticipated credit.

Charitable Rollover—Clients over age 70½, who have a Traditional or Roth IRA, may direct distributions to be made to a public charity (Charitable Rollover) without being taxed on the distributions. This tax break, which expires at the end of 2009, is limited to \$100,000 and doesn't apply to SEP IRAs or SIMPLE IRAs. Note, this is a better deal than simply taking an IRA distribution,

including it in income, and contributing a like amount of cash to charity. In this case, the contribution is subject to the 50 percent of AGI limit. With the Charitable Rollover the entire distribution (up to \$100,000) escapes tax.

First Time Home Buyer Credit—Not many HNW and affluent clients are first-time homebuyers, qualifying for the \$8,000 credit. But these clients often have children and grandchildren who are looking to make that first big purchase. A great way for clients to get a double-bang for their buck is to make a cash gift (taking advantage of the gift tax annual exclusion), which the donee

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New-car sales tax deduction—A similar approach can be used with this deduction that is set to expire at the end of 2009. New car buyers may be eligible to write off state and local sales taxes from a new car purchased. Single tax filers who earn less than \$125,000 and joint filers who earn less than \$250,000 are eligible. This is an above the line tax deduction, which means your client's children and grandchildren don't even need to itemize deductions to receive the benefit. Eligible vehicles include new cars, motorcycles, light vehicles, and RV's.

Energy Star Appliance Rebate—Another tax break available in 2009 relates to purchases made of certain Energy Star rated appliances. These programs are federally funded, but the money and rebates are being handled by the individual states, so the details may vary. Eligible appliances include heat pumps, furnaces, central and window air conditioners, refrigerators, freezers, dishwashers, washing machines, and water heaters. Again, HNW and affluent clients may not need these items, but children and grandchildren just starting out probably do.

The Bottom Line

It's a busy time of the year, but not too busy for year-end tax planning. Make sure your clients are getting their share of "government gimmes" and "stimulus goodies" for the holidays.

Taxes and similar topics are covered in great detail in many of Cannon's professional development solutions. To find out more visit: www.cannonfinancial.com.

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