

2012 YEAR-END INCOME TAX PLANNING FOR INDIVIDUALS

INTRODUCTION

It's time to begin developing year-end planning strategies for 2012. Year-end planning for 2012 is a greater challenge than in previous years because we are facing the most significant tax uncertainty in recent memory, largely caused by:

1. the scheduled expiration of the so-called *Bush-Era* tax cuts *after 2012*,
2. new "Medicare Surtaxes" *starting in 2013*,
3. a host of popular tax breaks that *expired after 2011* which have historically been retroactively extended,
4. another long list of tax breaks scheduled to expire *after 2012*, and
5. the scheduled reduction in the exemption from estate and gift taxes from \$5,120,000 to \$1,000,000 *after 2012*.

It's possible that Congress may postpone the scheduled tax rate increases and reinstate many of the expired or expiring tax breaks. Some are predicting that Congress will at least address the expired or expiring tax breaks in an "extender's bill" during the lame-duck session after the November election. However, others believe Congress will not deal with these tax issues until early 2013. Due to this uncertainty, we believe the best approach for year-end planning in this volatile tax environment is to become familiar with the tax changes that are *currently scheduled* to occur *after 2012*, and to be *prepared to act quickly near the end of 2012* based upon the tax climate at that time. In addition, whether or not Congress takes action by the end of 2012, this letter outlines several "*traditional*" *year-end planning strategies* that can save taxes for many individuals.

The purpose of this issue of *PointSheet* is to:

1. Identify potential year-end tax strategies that exist in light of the major tax changes scheduled to take effect in 2013;
2. Suggest alternative considerations if Congress changes the law late in 2012; and,
3. Remind you of traditional year-end planning opportunities that could likely save 2012 taxes no matter what course Congress takes with future legislation.

To help you locate items of interest, we have divided planning ideas into the following topics:

- A. Preparing For Potential Tax Rate Increases
- B. Expired, Expiring, And Scaled Back Tax Breaks
- C. Traditional Year-End Tax Planning In Light Of Tax Uncertainties
- D. Maximizing Family Gifts
- E. Miscellaneous Year-End Tax Planning Opportunities

Tax Planning Alert!

Our firm is monitoring potential 2012 tax legislation, so please call us if you want a status report. Also, tax planning strategies that we discuss in this letter may subject you to the alternative minimum tax (AMT). For example, many deductions are not allowed for AMT purposes, such as: personal exemptions; state and local income taxes; real estate taxes; and interest on home equity loans (unless the loan proceeds were used to improve, build, or buy your residence). Also, AMT can be triggered by taking large capital gains or exercising incentive stock options.

Therefore, we encourage you to *call our firm before implementing any tax planning technique* discussed in this letter. You cannot properly evaluate a particular planning strategy without calculating your overall tax with and without that strategy.

Please Note! This letter contains ideas for *Federal tax planning only*. State tax issues are not addressed.

A. PREPARING FOR POTENTIAL TAX RATE INCREASES

1) Starting In 2013 – Scheduled Significant Rate Increases.

Unless Congress changes current law, individuals are facing an increase in their federal income tax rates beginning next year. **In 2013**, the top regular individual income tax rate on income, other than long-term capital gains, is scheduled to jump from 35% to 39.6%. The maximum tax rate on long-term capital gains is scheduled to increase from 15% to 20%. And, the top tax rate on dividends is scheduled to increase from 15% to 39.6%.

Furthermore, **starting in 2013**, the *Health Care Act* imposes *an additional Medicare Surtax of .9%* on the wages and self-employment income of higher-income individuals as well as a *new 3.8% Medicare Surtax* on their *net investment income*. Thus, the Federal tax rates for individuals taxed in the *highest income tax brackets* in **2013** who are also subject to these new Medicare surtaxes could be as high as: **40.5%** for wages and self-employment income; **23.8%** for long-term capital gains; and **43.4%** for dividend and interest income.

The uncertainty concerning the extension of the *Bush-era* tax cuts makes tax planning during 2012 extremely challenging. Our firm is available to help you accelerate ordinary income, capital gains, and dividends into 2012 and to defer deductions into 2013, if doing so would result in significant tax savings. However, it is uncertain at this point whether Congress will allow the scheduled rate increases to take effect in 2013 or continue 2012 tax rates at least for the short term. Therefore, we recommend that individuals who will be significantly hurt by the scheduled 2013 rate increases *begin planning now* to accelerate income into 2012 and possibly defer deductions into 2013.

However, it seems prudent to postpone the actual acceleration of the income until later in 2012 when we will, hopefully, have a better handle on Congress's plans. In addition, please remember that the only way to determine the benefit from accelerating income into 2012 or deferring deductions until 2013 is by performing detailed calculations with and without such acceleration or deferral. With and without calculations will take into account regular Federal income taxes, the AMT, the new Medicare Surtaxes, and state income taxes.

Although the overall tax rates for 2013 are currently in a state of flux, the temporary **2% Social Security tax holiday** scheduled to expire after 2012, and the new **Medicare Surtaxes** enacted under the "*Patient Protection Act of 2010*" (Health Care Act), discussed below, may warrant action **before 2013** that could save you taxes.

2) **The "Temporary" 2% Social Security Tax Holiday Scheduled To Expire After 2012.**

Last February, Congress extended **through December 2012** the temporary reduction in the Social Security tax rate from 6.2% to 4.2% **for employees**, and from 12.4% to 10.4% for **self-employed individuals**. Therefore, **if you are an employee, for 2012**, the normal 6.2% "employee" portion of your Social Security tax rate has been reduced to 4.2%. Since Social Security taxes apply only to the first \$110,100 of compensation in 2012, your **maximum savings for 2012** is generally **\$2,202** (i.e., \$110,100 x 2%). Likewise, **if you are self-employed**, your Social Security taxes are reduced by 2% of your self-employment income for 2012 (up to \$110,100).

Tax Tip. You and/or your spouse should consider accelerating into 2012 compensation (e.g., by accelerating a bonus, commission, etc.) or self-employed income (e.g., encouraging a customer or client to pay early) in order to save the 2% Social Security tax to the extent the additional income does not cause either of you to exceed the \$110,100 cap, and **does not cause you to pay more income taxes**. Moreover, the compensation or self-employed income that **you accelerate into 2012** will not be subject to the new .9% Medicare Surtax (discussed in the next segment) **which becomes effective in 2013**.

3) **New .9% Medicare Surtax On Earned Income Of High Income Individuals Begins In 2013.** Generally, effective for wages and self-employed earnings received after 2012 that exceed certain thresholds, the *Health Care Act* imposes an **additional .9% Medicare Surtax**. This surtax applies to the amount by which the sum of your *W-2 wages* and your *self-employed earnings* exceeds \$250,000 if you are married filing a joint return (exceeds \$200,000 if you are single, or \$125,000 if married filing separately).

Note! For married individuals filing a joint return, the .9% Medicare Surtax will apply to the extent **the sum of** both spouses' *W-2 earnings* and the self-employed earnings exceeds the \$250,000 threshold.

4) **New 3.8% Medicare Surtax On Net Investment Income Of High Income Taxpayers Begins In 2013.**

Starting in 2013, higher-income individuals may be subject to a new 3.8% Medicare Surtax on *net investment income* (e.g., interest, dividends, annuities, royalties, rents, certain "passive" income, and capital gains – less applicable expenses). The tax will apply to individuals with *net investment income* where their modified adjusted gross income (MAGI) exceeds the following **"threshold amounts"** – \$250,000 for married individuals filing jointly; \$200,000 if single; and \$125,000 if married filing separately.

Trusts and estates that have *net investment income* and have *adjusted gross income* (AGI) in excess of \$11,950 for 2013 will also be subject to the 3.8% Medicare Surtax, unless the *net investment income* is timely distributed to beneficiaries. Fortunately, the following types of income are *exempt from* the 3.8% Medicare Surtax:

- tax-exempt income (e.g., municipal bond interest);
- gain on the sale of a principal residence *excluded from income* under the *home-sale exclusion* rules (i.e., up to \$250,000 on a single return, up to \$500,000 on a joint return), and;
- distributions from qualified plans (e.g., IRAs, §403(b) annuities, etc.).

Caution! Although distributions from retirement plans are not directly subject to the 3.8% Medicare Surtax, these distributions increase MAGI and may cause your investment income to be hit with the tax.

Planning Alert! The following are actions you might *take before 2013* to reduce the amount of income subject to the 3.8% Medicare Surtax in 2013:

- **Consider Investments That Generate Tax-Exempt Income.** Investments generating tax-exempt income will become more attractive in 2013. For example, tax exempt municipal bond interest may provide higher-income individuals with a double tax benefit: **1)** the interest will not be included in MAGI thus reducing the chance that MAGI will exceed the income thresholds for the 3.8% Medicare Surtax, and **2)** the tax-exempt interest itself is exempt from the Medicare Surtax.

Planning Alert! Always consider the economics of the investment first!

- **Consider “Tax-Deferred” Investments.** The 3.8% Medicare Surtax does not apply to earnings generated by a *tax-deferred annuity* (TDA) contract *until the earnings are distributed*. Thus, investing in a TDA in your higher-income years may allow you to defer the annuity income until later years when your MAGI is below the Medicare Surtax thresholds. **Caution!** The economics of the TDA should always be considered before investing.
- **Recognizing Capital Gains In 2012 And Deferring Capital Losses Beyond 2012.** With the scheduled increase in the maximum long-term capital gains rates from 15% to 20% **in 2013**, and the imposition of the new 3.8% Medicare Surtax on capital gains starting **in 2013**, timing your sales of stocks, bonds, or other securities for 2012 is even more important than in previous years. If you are a higher-income taxpayer, you may save taxes by selling investments producing long-term capital gains **that have increased in value** in 2012, instead of waiting until 2013 or later. Likewise, overall tax savings may occur if you postpone selling investments producing a capital loss until 2013 or later, so that those losses can shelter capital gains that otherwise would be subject to the higher 20% capital gains rate and the 3.8% Medicare Surtax.

Tax Tip. Under the so-called “wash sale” rules, you are not allowed to recognize a loss on the sale of securities if, within 30 days before or after the sale, you acquire substantially identical securities. However, the “wash sale” rules *do not* apply if you sell securities *at a gain*. Thus, you can accelerate capital gains by selling your appreciated securities *before 2013*, even if you

purchase *identical securities* before or after the sale. Furthermore, by purchasing the replacement securities at their current appreciated values, you will obtain a higher tax basis in the newly-purchased securities. This higher basis in the replacement securities will reduce any gain you recognize from the sale of the securities after 2012.

Caution! If the replacement securities go down in value after your purchase, you could face the “capital loss” limitations when you sell the investment. Also, you should always *consider the economics* of a sale or exchange first!

- **Consider Roth IRA Conversions.** Tax-free distributions from a Roth IRA are exempt from the 3.8% Medicare Surtax, and do not increase your MAGI (and, thus will not increase your exposure to the Medicare Surtax). Therefore, these new tax-favored features should be factored into any analysis of whether you should convert your existing IRA to a Roth. However, if the conversion occurs *after 2012*, the income triggered by the conversion increases your MAGI and, therefore, increases your potential exposure to the 3.8% Medicare Surtax on your *net investment income* (e.g., capital gains, dividends, interest, rents). Thus, by converting to a Roth *in 2012 rather than in 2013*, you might avoid the higher income tax rates in 2013 and avoid any 3.8% Medicare Surtax on your *net investment income* that might otherwise apply for 2013 because of the conversion.

Planning Alert! If you want the Roth conversion to be *effective for 2012*, you must transfer the amount from the regular IRA to the Roth IRA *no later than December 31, 2012* (you do not have until the due date of your 2012 tax return).

Caution! Whether you should convert your traditional IRA to a Roth IRA can be an exceedingly complicated issue, and this new 3.8% Medicare Surtax is just one of many factors that you should consider. *Please call our firm* if you need help in deciding whether or not to convert to a Roth IRA.

B. **EXPIRED, EXPIRING, AND SCALED BACK TAX BREAKS**

Selected Individual Tax Breaks That Expired After 2011. There is an ever-expanding list of temporary tax breaks that expire every few years. However, even though Congress often waits until the last minute, it has *historically* extended most of the more popular provisions. Unfortunately, as we complete this letter, Congress has yet to extend a host of tax breaks that *expired at the end of 2011*, including: School Teachers' Deduction (Up to \$250) for Certain School Supplies; Deduction for State and Local Sales Tax; Deduction (Up to \$4,000) for Qualified Higher Education Expenses; Qualifying Tax-Free Transfers from IRAs to Charities for Those at Least 70½; Higher Alternative Minimum Tax (AMT) Exemption Amounts; Increased Charitable Deduction Limits for Qualifying Conservation Easements; Lifetime \$500 Credit for Qualified Energy-Efficient Home Improvements; and Deduction for Qualified Home Mortgage Insurance Premiums.

Planning Alert! If recent history is a guide, Congress will likely extend these provisions eventually, but there is no guarantee. Our firm will monitor the status of these expired provisions.

Tax Breaks Currently Scheduled To Expire (Or To Be Reduced) After 2012. As discussed previously, the so-called *Bush-era tax rate cuts* are scheduled to expire **after 2012**. In addition, there are many other tax breaks that were enacted or expanded in 2001 and 2003 that are also scheduled to *expire* or to be *reduced*, including: Student Loan Interest Deduction; Adoption Credit; Child Tax Credit; Earned Income Tax Credit; Child and Dependent Care Credit; Exclusion for Income From Principal Residence Mortgage Cancellations; Various Marriage Penalty Relief Provisions; and the Moratorium on Phase-Outs of Personal Exemptions and Itemized Deductions.

C. TRADITIONAL YEAR-END TAX PLANNING IN LIGHT OF TAX UNCERTAINTIES

Traditional year-end tax planning typically includes strategies to postpone taxes until later years. Classic techniques to accomplish these goals include *deferring the recognition of taxable income* into future years, and *accelerating deductible expenses* into the current tax year. Although these strategies may still be advisable for individuals whose effective tax rates for 2013 are equal to or less than their rates for 2012, they are not advantageous for individuals whose effective tax rates are scheduled to increase dramatically after 2012. Therefore, the following are suggested planning ideas for individuals whose tax rates will increase significantly after 2012.

Caution! We encourage you to *call our firm before implementing any tax planning technique* discussed below. You cannot properly evaluate a particular planning strategy without calculating your overall tax (including the AMT and any state income tax) with and without that strategy.

Year-End Planning For Investments. As mentioned earlier in this letter, the maximum long-term capital gain rate is scheduled to increase from 15% to 20% *after 2012*, and to **23.8%** if the new 3.8% Medicare Surtax applies. In addition, *through 2012*, long-term capital gains that would otherwise be included in the 15% (or below) ordinary income tax bracket, are taxed at zero percent. *After 2012*, this zero percent bracket is scheduled to increase to 10% (8% if the asset is held more than 5 years).

Planning Alert! After *fully evaluating the economic factors*, the following are year-end tax planning ideas that could save you 2012 taxes for sales of capital assets:

- **Planning With Temporary Zero Percent Capital Gains Tax Rate.** For 2012, all ordinary income (e.g., W-2, interest income) up to \$70,700 for those filing joint returns (\$35,350 if single) is taxed at the 15% rate, or below. Thus, married taxpayers filing jointly can benefit from the zero percent capital gains rate if (and to the extent) they have 2012 ordinary taxable income under \$70,700 (\$35,350 if single). For example, if a married couple has taxable income of \$50,700 for 2012 before considering their long-term capital gains, up to \$20,000 (i.e., \$70,700 - \$50,700) of their long-term capital gains could be subject to the zero percent capital gains rate.

Tax Tip. If you anticipate your taxable income to be below these levels and you own appreciated securities, please call our firm and we will help you determine if it is possible for you to take advantage of this zero percent capital gains rate.

Planning Alert! Don't forget, long-term capital gains that currently qualify for the zero percent rate will be taxed at 10% (8% if you have held the asset more than 5 years) starting in 2013, unless Congress extends the zero percent rate beyond 2012.

- **Timing Your Capital Gains And Losses.** If you have already recognized capital gains in 2012, and you want to shelter those gains from the current 15% maximum capital gains rate, you should consider selling securities that have declined in value **prior to January 1, 2013**. These losses will be deductible on your 2012 return to the extent of your recognized capital gains, plus \$3,000.

Tax Tip. These losses may have the added benefit of reducing your income to a level that will qualify you for other tax breaks, such as the: \$2,500 American Opportunity Tuition Tax Credit, \$1,000 child credit, \$12,650 adoption credit, etc.

Planning Alert! If within 30 days before or after the sale of loss securities, you acquire the same securities, the loss will not be allowed currently because of the “wash sale” rules (although the disallowed loss will increase the basis of the acquired stock).

Caution! As we previously warned in the discussion of the new 3.8% Medicare Surtax, it may be better tax-wise for high income individuals to wait to sell investments that are worth less than cost until **after 2012**. That way, the capital losses may offset 2013 capital gains that might otherwise be hit with the higher 20% capital gains rate and the new 3.8% Medicare Surtax.

Postponing Taxable Income. Even if all or some of the currently-scheduled tax rate increases become effective after 2012, it is still generally a good idea to defer income into 2013 if you believe that your marginal tax rate for 2013 will be equal to or less than your 2012 marginal tax rate (for example if your taxable income is significantly less in 2013, you are subject to the AMT in 2012 and 2013, etc.).

Tax Tip. This classic tax planning strategy may be particularly valuable for 2012 if it also keeps your 2012 income below the phase-out thresholds for the many tax breaks that are currently scheduled to expire or be scaled back after 2012 (e.g., adoption credit, student loan interest deduction, American Opportunity Tax Credit, child tax credit).

Taking Advantage Of Deductions. After considering the currently-scheduled tax rate increases for 2013, if you believe that your marginal tax rate for 2012 will be equal to or greater than your 2013 marginal tax rate, you may save taxes by accelerating deductions into 2012. Likewise, accelerating into 2012 items that are deductible in calculating adjusted gross income “AGI” may be particularly valuable if the deductions keep your 2012 AGI below the phase-out thresholds for the many tax breaks that are currently scheduled to *expire* or to be *scaled back* after 2012 (e.g., adoption credit, student loan interest deduction, American Opportunity Tax Credit, child tax credit).

Accelerating Deductions Into 2012. As a cash method taxpayer, you can generally accelerate a 2013 deduction into 2012 by “paying” for the deduction item in 2012. Accelerating an “above-the-line” deduction (e.g., IRA contribution, Health Savings Account (HSA) contribution, health insurance premiums for self-employed individuals, qualified student loan interest, qualified

moving expenses, deductible alimony) into 2012 may allow you to reduce your “adjusted gross income” (AGI) or “modified adjusted gross income” (MAGI) below the thresholds needed to qualify for many other tax benefits (e.g., child credit, education credits, adoption credit, ability to contribute to an IRA, etc).

Caution! “Itemized” deductions (i.e., below-the-line deductions) do **not** reduce your AGI or MAGI and, therefore, will not affect your 2012 deductions and credits that are reduced as your income increases. *Itemized deductions* generally include charitable contributions, state and local income and property taxes, medical expenses, unreimbursed employee business expenses, and home mortgage interest.

Tax Tip. “Payment” typically occurs in 2012 when your check is delivered to the post office, when your electronic payment is debited to your account, or when an item is charged in 2012 on a *third-party credit card* (e.g., Visa, MasterCard, Discover, American Express).

Planning Alert! Until 2010, *itemized deductions* (other than medical expenses, investment interest, casualty and theft losses, and gambling losses) were generally reduced by a percentage of an individual’s AGI above a threshold amount. For **2010, 2011, and 2012**, all individuals are exempt from this phase-out. However, beginning in 2013, *itemized deductions* (other than medical expenses, investment interest, casualty and theft losses, and gambling losses) are scheduled to be reduced by 3% of an individual’s AGI above the 2013 threshold amount. Thus, if you anticipate that your income will exceed the beginning phase-out threshold in 2013 (projected to be **\$178,150**), accelerating 2013 itemized deductions into 2012 can avoid the phase-out.

Starting In 2013 – Medical Deduction Threshold Increases From 7.5% To 10% Of AGI. Currently, you are generally allowed an *itemized deduction* for un-reimbursed medical expenses (including un-reimbursed health insurance premiums) to the extent that the expenses exceed **7.5%** of adjusted gross income (10% for alternative minimum tax purposes). **Starting in 2013**, the *Health Care Act* generally increases this threshold from 7.5% of adjusted gross income (AGI) **to 10% of AGI**.

Exception For Seniors. If either you or your spouse is at least age 65 before the close of the tax year, the 7.5% of AGI threshold will continue to apply **through 2016** (whether you file a joint return or separate returns).

Tax Tip. If you will be subject to the 10% threshold in 2013, you should consider accelerating (i.e., bunching) your anticipated discretionary medical expenses into 2012 if your total medical expenses will exceed the 7.5% threshold, but not the 10% threshold.

Charitable Contributions. A charitable contribution deduction is allowed for 2012 if the check is *mailed on or before December 31, 2012*, or the contribution is made by a credit card charge in 2012. However, if you merely give a note or a pledge to a charity, no deduction is allowed until you pay off the note or pledge.

Planning Alert! For the past several years, we have had a popular (but *temporary*) rule that allowed a taxpayer at least age 70½, to make a *qualifying* transfer of up to \$100,000 from his or her IRA directly to a qualified charity, and exclude the distribution from income. The IRA transfer to the charity also counted toward the owner’s “required minimum distributions” (RMDs) for the

year. Although this provision *expired after 2011* and is not currently available for 2012, it is possible that Congress may retroactively reinstate this provision for 2012. If so, and you wish to use this provision if retroactively extended, be prepared to make the transfer from your IRA to the charity on short notice. Also, if you are eligible for this provision and you have not taken your 2012 RMD from the IRA, consider waiting until later in 2012 to take the distribution. That way, if Congress retroactively extends this provision through 2012, you will have the option of transferring up to \$100,000 directly to a charity and reduce (or eliminate) your RMD for 2012. **Caution!** There is generally a 50% penalty for failure to make the RMD by the end of 2012.

D. **MAXIMIZING FAMILY GIFTS**

Utilize Annual Gift Tax Exclusion. For individuals dying in **2012**, there is generally a **35%** estate tax to the extent the value of the estate, plus any taxable gifts made during the decedent's life, exceeds **\$5,120,000** (the estate and gift "*unified exclusion amount*"). This current *unified exclusion amount* is scheduled to **drop to \$1 million** for *gifts made after 2012* and for estates of individuals *dying after 2012*. Also, the top estate and gift tax rate is scheduled to **increase to 55% after 2012**. If your estate is large enough to be exposed to the estate tax, and you want to minimize that exposure, you can reduce your estate without using any of your *unified exclusion amount* by making annual gifts up to \$13,000 per donee (projected to be \$14,000 for 2013). Your spouse can do the same, bringing your combined 2012 gift to \$26,000 per donee, without reducing either your or your spouse's *unified exclusion amount*.

Planning Alert! If you make your 2012 gift by check, the IRS says that the donee must actually "*deposit*" the check **by December 31, 2012** in order to utilize the \$13,000 annual gift tax exclusion for 2012. Therefore, if gifts are made by check near the end of the year, instruct the donee to deposit the check **no later than December 31, 2012**, or consider using a cashier's check – which should constitute a gift when the check is delivered.

Larger Estates Should Consider Using The Temporary \$5,120,000 Unified Exclusion Amount For Lifetime Gifts. As mentioned above, the current *unified exclusion amount* of \$5,120,000, which may be used to reduce either gift taxes for lifetime gifts or estate taxes at death, is scheduled to drop to \$1 million **after 2012**. This dramatic drop in the *unified exclusion amount* has caused many high-wealth individuals to consider large family gifts before 2013. If you are in this situation, please call our firm and we will review with you the many tax and non-tax factors you should consider before implementing a significant year-end gift strategy.

Planning Alert! Maximizing the benefits of a 2012 gift may require appraisals, the establishment of trusts, etc. Therefore, we need to begin planning for the gift as soon as possible. That way, we will be in a position to "implement" the gift if it appears the unified exclusion amount will, in fact, drop in 2013 or postpone the gift if Congress extends the current \$5,120,000 unified exclusion amount and you wish to wait.

E. **MISCELLANEOUS YEAR-END TAX PLANNING OPPORTUNITIES**

Before wrapping up your *traditional* year-end planning review, here are several more strategies you might consider:

Consider Increasing Withholding If You Are Facing A Tax Underpayment Penalty. If you have failed to pay sufficient estimated taxes during 2012 potentially causing an underpayment penalty, *increasing your withholdings before the end of 2012* may solve the problem. Any income tax withholding (including withholdings at the end of 2012 from a year-end bonus or IRA distribution) is generally deemed paid 1/4 on April 17, 2012, June 15, 2012, September 17, 2012 and January 15, 2013. Therefore, amounts *withheld on or before December 31, 2012* may reduce or eliminate your penalty for underpaying estimated taxes.

IRA Owners Reaching Age 70½ During 2012. If you reached age 70½ at any time during 2012, you must begin distributions from a traditional IRA account *no later than April 1st of 2013*. A 50% penalty applies to the excess of the “required minimum distribution” over the amount actually distributed. If you wait until 2013 to take your first payment, you will still be required to take your second required minimum distribution no later than December 31, 2013, which will cause you to take two payments in 2013.

Planning Alert! This “bunching” of the first two annual payments into one tax year (2013) could cause your income to be taxed in a higher tax bracket and, therefore, result in more overall tax than if you received the first required payment in 2012. Also, taking your first required distribution *in 2012* may save even more taxes than in previous years, if the scheduled tax increases after 2012 actually occur.

Maximize Tax-Favored Medical Benefits For Children Under Age 27. An employer-provided health plan may provide tax-free reimbursements to an employee’s child **who is under age 27 at the end of the tax year**. This exclusion applies even if the employee cannot claim the child as a dependent for tax purposes.

Tax Tip. If your employer’s health insurance plan is currently covering your child who will turn age 27 in 2013, accelerating discretionary medical expenses for that child from **2013 to 2012** will allow your employer’s 2012 reimbursements to be tax-free. In addition, **if you are self-employed and you otherwise qualify**, you may take an “above-the-line” deduction (i.e., unrestricted by the limitations on “itemized deductions”) for health insurance premiums that you pay for your child who is **under age 27 at the end of the year**, even if the child is not your “dependent” for tax purposes.

FINAL COMMENTS

Please contact us if you are interested in a tax topic that we did not discuss. Tax law is constantly changing due to new legislation, cases, regulations, and IRS rulings. Our firm closely monitors these changes. In addition, please call us before implementing any planning ideas discussed in this letter, or if you need additional information.

Note: The information contained in this material represents a general overview of tax developments and should not be relied upon without an independent, professional analysis of how any of these provisions may apply to a specific situation.

Circular 230 Disclaimer:

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