

Dear Client:

As 2012 draws to a close, there is still time to reduce your 2012 tax bill and plan ahead for 2013. This letter highlights several potential tax-saving opportunities for you to consider. I would be happy to meet with you to discuss specific strategies.

As a general reminder, there are several ways in which you can file an income tax return: married filing jointly, head of household, single, and married filing separately. A husband and wife may elect to file one return reporting their combined income, computing the tax liability using the tax tables or rate schedules for “Married Persons Filing Jointly.” If a married couple files separate returns, under certain situations they can amend and file jointly, but they cannot amend a jointly filed return and file separately. A joint return may be filed even though one spouse has neither gross income nor deductions. If one spouse dies during the year, the surviving spouse may file a joint return for the year in which his or her spouse died. Certain married persons who do not elect to file a joint return may be entitled to use the lower head of household tax rates. Generally, in order to qualify as a head of household, you must not be a resident alien, you must satisfy certain marital status requirements, and you must maintain a household for a qualifying child or any other person who is your dependent, if you are entitled to a dependency deduction for the taxable year for such person.

Basic Numbers You Need To Know

Because many tax benefits are tied to or limited by adjusted gross income (AGI)—IRA deductions, for example—a key aspect of tax planning is to estimate both your 2012 and 2013 AGI. Also, when considering whether to accelerate or defer income or deductions, you should be aware of the impact this action may have on your AGI and your ability to maximize itemized deductions that are tied to AGI. Your 2011 tax return and your 2012 pay stubs and other income- and deduction-related materials are a good starting point for estimating your AGI.

Another important number is your “tax bracket,” i.e., the rate at which your last dollar of income is taxed. The tax rates for 2012 are 10%, 15%, 25%, 28%, 31%, and 35%. However, for 2013, the tax brackets are scheduled to be 15%, 28%, 31%, 36% and 39.6%. Although tax brackets are indexed for inflation, if your income increases faster than the inflation adjustment, you may be pushed into a higher bracket. If so, your potential benefit from any tax-saving opportunity is increased (as is the cost of overlooking that opportunity).

IRA, Retirement Savings Rules for 2012

Tax-saving opportunities continue for retirement planning due to the availability of Roth IRAs, changes that make regular IRAs more attractive, and other retirement savings incentives.

Traditional IRAs: Individuals who are not active participants in an employer pension plan may make deductible contributions to an IRA. The annual deductible contribution limit for an IRA for 2012 is \$5,000. For 2012, a \$1,000 “catch-up” contribution is allowed for taxpayers age 50 or older by the close of the taxable year, making the total limit \$6,000 for these individuals.

Individuals who are active participants in an employer pension plan also may make deductible contributions to an IRA, but their contributions are limited in amount depending on their AGI.

For 2012, the AGI phase-out range for deductibility of IRA contributions is between \$58,000 and \$68,000 of modified AGI for single persons (including heads of households), and between \$92,000 and \$112,000 of modified AGI for married filing jointly. Above these ranges, no deduction is allowed.

In addition, an individual will not be considered an “active participant” in an employer plan simply because the individual's spouse is an active participant for part of a plan year. Thus, you may be able to take the full deduction for an IRA contribution regardless of whether your spouse is covered by a plan at work, subject to a phase-out if your joint modified AGI is \$173,000 to \$183,000 for 2012. Above this range, no deduction is allowed.

Spousal IRA: If an individual files a joint return and has less compensation than his or her spouse, the IRA contribution is limited to the lesser of \$5,000 for 2012 plus age 50 catch-up contributions, or the total compensation of both spouses reduced by the other spouse's IRA contributions (traditional and Roth).

Roth IRA: This type of IRA permits nondeductible contributions of up to \$5,000 a year. Earnings grow tax-free, and distributions are tax-free provided no distributions are made until more than five years after the first contribution and the individual has reached age 59¹/₂. Distributions may be made earlier on account of the individual's disability or death. The maximum contribution is phased out in 2012 for persons with an AGI above certain amounts: \$173,000 to \$183,000 for married filing jointly, and \$110,000 to \$125,000 for single taxpayers (including heads of households); and between \$0 and \$10,000 for married filing separately who lived with the spouse during the year.

Roth IRA Conversion Rule: Funds in a traditional IRA (including SEPs and SIMPLE IRAs), [§401\(a\)](#) qualified retirement plan, [§403\(b\)](#) tax-sheltered annuity or [§457](#) government plan may be rolled over into a Roth IRA. Such a rollover, however, is treated as a taxable event, and you will pay tax on the amount converted. No penalties will apply if all the requirements for such a transfer are satisfied.

In past years, a taxpayer's AGI (whether married filing jointly or single) was limited to \$100,000 to make such a conversion and the taxpayer must not be a married individual filing a separate return. The AGI limitation does not apply to conversions from a Roth designated account in a [§401](#) or [§403\(b\)](#) plan. For 2012, the \$100,000 income limit on Roth IRA conversions does not apply, and taxpayers will be able to make Roth IRA conversions without regard to their AGI. If you convert to a Roth IRA in 2012, the tax on the converted amount will have to be paid in the year of conversion. Also, if you already made a conversion earlier this year, you have the option of undoing the conversion. This is a useful strategy if the investments have gone down in value so that if you were to do the conversion now, your taxes would be lower. This is a complicated calculation and we should meet to determine what your best options are.

In addition, for 2012, if your [§401\(k\)](#) plan, [§403\(b\)](#) plan, or governmental [§457\(b\)](#) plan has a qualified designated Roth contribution program, a distribution to an employee (or a surviving spouse) from such account under the plan that is not a designated Roth account is permitted to be rolled over into a designated Roth account under the plan for the individual.

401(k) Contribution: The [§401\(k\)](#) elective deferral limit is \$17,000 for 2012. If your [§401\(k\)](#) plan has been amended to allow for catch-up contributions for 2011 and you will be 50 years old

by December 31, 2011, you may contribute an additional \$5,500 to your [§401\(k\)](#) account, for a total maximum contribution of \$22,500 (\$17,000 in regular contributions plus \$5,500 in catch-up contributions).

SIMPLE Plan Contribution: SIMPLE plan deferral limit is \$11,500 for 2012. If your SIMPLE plan has been amended to allow for catch-up contributions for 2012 and you will be 50 years old by December 31, 2012, you may contribute an additional \$2,500.

Catch-Up Contributions for Other Plans: If you will be 50 years old by December 31, 2012, you may contribute an additional \$5,500 to your [§403\(b\)](#) plan, SEP or eligible [§457](#) government plan.

Saver's Credit: A nonrefundable tax credit is available based on the qualified retirement savings contributions to an employer plan made by an eligible individual. For 2012, only taxpayers filing joint returns with AGI of \$57,500 or less, head of household returns with AGI of \$43,125 or less, or single returns (or separate returns filed by married taxpayers) with AGI of \$28,750 or less, are eligible for the credit. The amount of the credit is equal to the applicable percentage (10% to 50%, based on filing status and AGI) of qualified retirement savings contributions up to \$2,000.

Required Minimum Distributions: For 2012, taxpayers must take their required minimum distribution from IRAs or defined contribution plans ([§401\(k\)](#) plans, [§403\(a\)](#) and [\(b\)](#) annuity plans, and [§457\(b\)](#) plans that are maintained by a governmental employer).

Maximize Retirement Savings: In many cases, employers will require you to set your 2013 retirement contribution levels before January 2013. If you did not elect the maximum 401(k) contribution for 2012, you can increase your amount for the remainder of 2012 to lower your AGI in order to take advantage of some of the tax breaks described above. In addition, maximizing your contribution is generally a good tax-saving move.

Deferring Income to 2013

If you expect your AGI to be higher in 2012 than in 2013, or if you anticipate being in the same or a higher tax bracket in 2012, you may benefit by deferring income into 2013. Deferring income will be advantageous so long as the deferral does not bump your income to the next bracket. Deferring income could be disadvantageous, however, if your deferred income is subject to [§409A](#), thus making the income includible in gross income and subject to additional tax. Some ways to defer income include:

Delay Billing: If you are self-employed and on the cash-basis, delay year-end billing to clients so that payments will not be received until 2013.

Interest and Dividends: Interest income earned on Treasury securities and bank certificates of deposit with maturities of one year or less is not includible in income until received. To defer interest income, consider buying short-term bonds or certificates that will not mature until next year. If you have control as to when dividends are paid, arrange to have them paid to you after the end of the year.

Accelerating Income into 2012

In limited circumstances, you may benefit by accelerating income into 2012. For example, you may anticipate being in a higher tax bracket in 2013, or perhaps you will need additional income in order to take advantage of an offsetting deduction or credit that will not be available to you in future tax years. Note, however, that accelerating income into 2012 will be disadvantageous if you expect to be in the same or lower tax bracket for 2013. In any event, before you decide to implement this strategy, we should “crunch the numbers.”

If accelerating income will be beneficial, here are some ways to accomplish this:

Accelerate Collection of Accounts Receivable: If you are self-employed and report income and expenses on a cash basis, issue bills and attempt collection before the end of 2012. Also see if some of your clients or customers might be willing to pay for January 2013 goods or services in advance. Any income received using these steps will shift income from 2013 to 2012.

Year-End Bonuses: If your employer generally pays year-end bonuses after the end of the current year, ask to have your bonus paid to you before the beginning of 2013.

Retirement Plan Distributions: If you are over age 59^{1/2} and you participate in an employer retirement plan or have an IRA, consider making any taxable withdrawals before 2013. You may also want to consider making a Roth IRA rollover distribution, as discussed above.

Deduction Planning

Individual Deductions

Deduction timing is also an important element of year-end tax planning. Deduction planning is complex, however, due to factors such as AGI levels, AMT, and filing status. If you are a cash-method taxpayer, remember to keep the following in mind:

Deduction in Year Paid: An expense is only deductible in the year in which it is actually paid. Under this rule, if your tax rate is going to increase in 2013, it is a smart strategy to postpone deductions until 2013.

Payment by Check: Date checks before the end of the year and mail them before January 1, 2013.

Promise to Pay: A promise to pay or providing a note does not permit you to deduct the expense. But you can take a deduction if you pay with money borrowed from a third party. Hence, if you pay by credit card in 2012, you can take the deduction even though you won't pay your credit card bill until 2013.

AGI Limits: For 2012, the overall limitation on itemized deductions is terminated. In addition, certain deductions may be claimed only if they exceed a percentage of AGI: 7.5% for medical expenses, 2% for miscellaneous itemized deductions, and 10% for casualty losses. However, for

2013, the overall limitation on itemized deductions is scheduled to be reinstated making deductions more valuable in 2012. However, too many itemized deductions in 2012 could trigger AMT. Also, for 2013, medical expenses may be deducted only if they exceed 10% of AGI (7.5% for taxpayers age 65).

Standard Deduction Planning: Deduction planning is also affected by the standard deduction. For 2012 returns, the standard deduction is \$11,900 for married taxpayers filing jointly, \$5,950 for single taxpayers, \$8,700 for heads of households, and \$5,950 for married taxpayers filing separately. As you can see from the numbers, for 2012, the standard deduction for married taxpayers is twice the amount as that for single taxpayers. For 2013, the standard deduction for married taxpayers is scheduled to be less than 200% of the standard deduction for single taxpayers. If your itemized deductions are relatively constant and are close to the standard deduction amount, you will obtain little or no benefit from itemizing your deductions each year. But simply taking the standard deduction each year means you lose the benefit of your itemized deductions. To maximize the benefits of both the standard deduction and itemized deductions, consider adjusting the timing of your deductible expenses so that they are higher in one year and lower in the following year. You can do this by paying in 2012 deductible expenses, such as mortgage interest due in January 2013.

Medical Expenses: Medical expenses, including amounts paid as health insurance premiums, are deductible only to the extent that they exceed 7.5% of AGI. With the percentage scheduled to increase to 10% in 2013 (but staying at 7.5% for taxpayers age 65), it would be wise to consider accelerating medical expenses into 2012, especially if your AGI is lower.

State Taxes: If you anticipate a state income tax liability for 2012 and plan to make an estimated payment most likely due in January, consider making the payment before the end of 2012. However, too high a payment could lead towards being subject to the AMT. Note that for 2012, the election to deduct as an itemized deduction state and local sales taxes instead of state and local income taxes expired at the end of 2011.

Charitable Contributions: Consider making your charitable contributions at the end of the year. This will give you use of the money during the year and simultaneously permit you to claim a deduction for that year. You can use a credit card to charge donations in 2012 even though you will not pay the bill until 2013. A mere pledge to make a donation is not deductible, however, unless it is paid by the end of the year. Note, however, for claimed donations of cars, boats and airplanes of more than \$500, the amount available as a deduction will significantly depend on what the charity does with the donated property, not just the fair market value of the donated property. If the organization sells the property without any significant intervening use or material improvement to the property, the amount of the charitable contribution deduction cannot exceed the gross proceeds received from the sale.

To avoid capital gains, you may want to consider giving appreciated property to charity. Regarding charitable contributions please remember the following rules: (1) no deduction is allowed for charitable contributions of clothing and household items if such items are not in good used condition or better; (2) the IRS may deny a deduction for any item with minimal monetary value; and (3) the restrictions in (1) and (2) do not apply to the contribution of any single clothing or household item for which a deduction of \$500 or more is claimed if the

taxpayer includes a qualified appraisal with his or her return. Charitable contributions of money, regardless of the amount, will be denied a deduction, unless the donor maintains a cancelled check, bank record, or receipt from the donee organization showing the name of the donee organization, and the date and amount of the contribution.

A special provision that gave taxpayers the ability to distribute tax-free to charity up to \$100,000 from a traditional or Roth IRA maintained for an individual whose has reached age 70^{1/2} expired at the end of 2011. However, Congress may decide to extend this provision retroactively for 2012 before the end of the year.

Business Deductions

Self-Employed Health Insurance Premiums: Self-employed individuals are allowed to claim 100% of the amount paid during the taxable year for insurance that constitutes medical care for themselves, their spouses and dependents as an above-the-line deduction, without regard to the 7.5% of AGI floor.

Equipment Purchases: If you are in business and purchase equipment, you may make a “Section [179](#) Election,” which allows you to expense (i.e., currently deduct) otherwise depreciable business property. For 2012, you may elect to expense up to \$139,000 of equipment costs (with a phase-out for purchases in excess of \$560,000) if the asset was placed in service during 2012. Note that for assets placed in service in 2012, taxpayers can expense 50% of their business equipment purchases under a provision giving taxpayers bonus depreciation, mitigating the need for the [§179](#) election.

In 2013, the dollar amounts for [§179](#) expensing are scheduled to be \$25,000, with a phase-out amount of \$200,000. Although there is a chance the 2013 figures will go up if Congress acts, it would be wise to place more assets in service in 2012 if you have yet to hit the \$139,000 figure. In addition, careful timing of equipment purchases can result in favorable depreciation deductions in 2012. In general, under the “half-year convention,” you may deduct six months worth of depreciation for equipment that is placed in service on or before the last day of the tax year. (If more than 40% of the cost of all personal property placed in service occurs during the last quarter of the year, however, a “mid-quarter convention” applies, which lowers your depreciation deduction.) A popular strategy in recent years is to purchase a vehicle for business purposes that exceeds the depreciation limits set by statute (i.e., a vehicle rated over 6,000 pounds). Doing so would not subject the purchase to the statutory dollar limit, \$11,160 for 2012 (due to bonus depreciation rules); \$11,360 in the case of vans and trucks (due to bonus depreciation rules). Therefore, the vehicle would qualify for the full equipment expensing dollar amount. However, for SUVs (rated between 6,000 and 14,000 pounds gross vehicle weight) the expensing amount is limited to \$25,000.

NOL Carryback Period: If your business suffers net operating losses for 2012, you generally apply those losses against taxable income going back two tax years. Thus, for example, the loss could be used to reduce taxable income—and thus generate tax refunds—for tax years as far back as 2010. Certain “eligible losses” can be carried back three years; farming losses can be carried back five years.

Bonus Depreciation: Taxpayers can claim 50% bonus depreciation for assets placed in service in 2012. Bonus depreciation is also allowed for machinery and equipment used exclusively to collect, distribute, or recycle qualified reuse and recyclable materials and qualified disaster assistance property. In 2013, bonus depreciation generally does not apply.

Education and Child Tax Benefits

Child Tax Credit: A tax credit of \$1,000 per qualifying child under the age of 17 is available on this year's return. In order to qualify for 2012, the taxpayer must be allowed a dependency deduction for the qualifying child. Another qualifying determination is that the qualifying child must be younger than you. The credit is phased out at a rate of \$50 for each \$1,000 (or fraction of \$1,000) of modified AGI exceeding the following amounts: \$110,000 for married filing jointly; \$55,000 for married filing separately; and \$75,000 for all other taxpayers. A portion of the credit may be refundable. For 2012, the threshold earned income level to determine refundability is set by statute at \$3,000. In 2013, the per child credit amount is scheduled to be reduced to \$500.

Credit for Adoption Expenses: For 2012, the adoption credit limitation is \$12,650 of aggregate expenditures for each child, except that the credit for an adoption of a child with special needs is deemed to be \$12,650 regardless of the amount of expenses. The credit ratably phases out for taxpayers whose income is between \$189,710 and \$229,710. While for 2011, the credit was refundable, for 2012, unless Congress acts before the end of the year to change it, the credit is nonrefundable. In addition, beginning in 2013, the adoption credit will only be available for adoption of special needs children with a reduced dollar amount. If you plan on adopting a non-special needs child, you should consider adopting the child in 2012 because there is no guarantee that this law will change in 2013.

Education Credits: Back in 2009, significant changes were put in place for the Hope credit, including a name change to the American Opportunity Tax Credit. These changes continue for 2012. The maximum credit for 2012 is \$2,500 (100% on the first \$2,000, plus 25% of the next \$2,000) for qualified tuition and fees paid on behalf of a student (i.e., the taxpayer, the taxpayer's spouse, or a dependent) who is enrolled on at least a half-time basis. The credit is available for the first four years of the student's post-secondary education. For 2012, the credit is phased out at modified AGI levels between \$160,000 and \$180,000 for joint filers, and between \$80,000 and \$90,000 for other taxpayers. Forty percent of the credit is refundable, which means that you can receive up to \$1,000 even if you owe no taxes. The term "qualified tuition and related expenses" includes expenditures for "course materials" (books, supplies, and equipment needed for a course of study whether or not the materials are purchased from the educational institution as a condition of enrollment or attendance). One way to take advantage of the credit for 2012 is to prepay the spring 2013's tuition. In addition, if your child's books for the spring semester are known, those can be bought and the costs qualify for the credit. After 2012, unless extended by Congress, the American Opportunity credit reverts back to the Hope Scholarship credit, with lower dollar amounts and more restricted definitions of qualified expenses.

The Lifetime Learning credit maximum in 2012 is \$2,000 (20% of qualified tuition and fees up to \$10,000). A student need not be enrolled on at least a half-time basis so long as he or she is

taking post-secondary classes to acquire or improve job skills. As with the Hope (American Opportunity Tax Credit in 2012) credit, eligible students include the taxpayer, the taxpayer's spouse, or a dependent. For 2012, the Lifetime Learning credit are phased out at modified AGI levels between \$104,000 and \$124,000 for joint filers, and between \$56,000 and \$66,000 for single taxpayers.

Coverdell Education Savings Account: This is an important year to maximize post-secondary savings in a Coverdell ESA. For 2012, the aggregate annual contribution limit to a Coverdell education savings account is \$2,000 per designated beneficiary of the account. However, in 2013, the amount is scheduled to decrease to \$500. The limit is phased out for individual contributors with modified AGI between \$95,000 and \$110,000 and joint filers with modified AGI between \$190,000 and \$220,000. For 2013, the AGI limits are scheduled to be reduced to \$150,000 and \$160,000 for joint filers, while the AGI amounts for others remains the same. The contributions to the account are nondeductible but the earnings grow tax-free. If you file a joint return and your income is approaching the phaseouts, 2012 is a better year to contribute than 2013.

Student Loan Interest: You may be eligible for an above-the-line deduction for student loan interest paid on any "qualified education loan." The maximum deduction is \$2,500. The deduction for 2012 is phased out at a modified AGI level between \$125,000 and \$155,000 for joint filers, and between \$60,000 and \$75,000 for individual taxpayers. However, in 2013, the AGI amounts are scheduled to go down to \$40,000 and \$55,000 for individual taxpayers, and \$60,000 and \$75,000 for joint filers with a slight increase for inflation. Another significant change scheduled for 2013 is the reinstatement of the 60-month rule for student loans. That rule provides that interest is only deductible on the first 60-months that interest payments are required. Any loans outstanding for more than 60-months will lose this deduction.

Kiddie Tax: For 2012, the kiddie tax applies to: (1) children under 18; (2) 18-year old children who have unearned income in excess of the threshold amount, do not file a joint return and who have earned income, if any, that does not exceed one-half of the amount of the child's support; and (3) children between the ages of 19 and 23 and if, in addition to the above rules, they are full-time students. For 2012, the kiddie tax threshold amount is \$1,900.

Energy Incentives

Residential Energy Efficient Property Credit: Until 2016, tax incentives are available to taxpayers who install certain energy efficient property, such as photovoltaic panels, solar water heating property, fuel cell property, small wind energy property and geothermal heat pumps. A credit is available for the expenditures incurred for such property up to a specific percentage, except that a cap applies for fuel cell property. The property purchased cannot be used to heat swimming pools or hot tubs. If you have made improvements to your home or plan to by the end of 2012, please contact me to discuss the amount of the credit you may qualify for.

Business Credits

Small Employer Pension Plan Startup Cost Credit: For 2012, certain small business employers that did not have a pension plan for the preceding three years may claim a nonrefundable income tax credit for expenses of establishing and administering a new retirement plan for employees. The credit applies to 50% in qualified administrative and retirement-education expenses for each of the first three plan years. However, the maximum credit is \$500 per year.

Employer-Provided Child Care Credit: For 2012, employers may claim a credit of up to \$150,000 for supporting employee child care or child care resource and referral services. The credit is allowed for a percentage of “qualified child care expenditures” including for property to be used as part of a qualified child care facility, for operating costs of a qualified child care facility and for resource and referral expenditures. Note that this credit is scheduled to expire at the end of 2012, therefore, it would be wise to make any planned qualified child care expenditures in 2012 to take advantage of the credit.

Work Opportunity Credit: The work opportunity credit is an incentive provided to employers who hire individuals in groups whose members historically have had difficulty obtaining employment. This gives your business an expanded opportunity to employ new workers and be eligible for a tax credit against the wages paid. Credit determined based on first-year wages paid for employees hired on or before December 31, 2011 (December 31, 2012, for qualified veterans).

Credit for Employee Health Insurance Expenses of Small Employers: For tax years beginning after 2009, eligible small employers are allowed a credit for certain expenditures to provide health insurance coverage for its employees. Generally, employers with 10 or fewer full-time equivalent employees (FTEs) and an average annual per-employee wage of \$25,000 or less are eligible for the full credit. The credit amount begins to phase out for employers with either 11 FTEs or an average annual per-employee wage of more than \$25,000. The credit is phased out completely for employers with 25 or more FTEs or an average annual per-employee wage of \$50,000 or more. The credit amount is 35% of certain contributions made to purchase health insurance (25% for a tax-exempt eligible small employer).

Investment Planning

The following rules apply for most capital assets in 2012:

- Capital gains on property held one year or less are taxed at an individual's ordinary income tax rate.
- Capital gains on property held for more than one year are taxed at a maximum rate of 15% (0% if an individual is in the 10% or 15% marginal tax bracket).

Note that Congress has yet to extend the reduced capital gains rates beyond 2012. If not changed, the maximum capital gains rate in 2013 will be 20% (10% for taxpayers in the 15% bracket). In addition, beginning in 2013, a 3.8% tax is levied on certain unearned income. The tax is levied on the lesser of net investment income or the amount by which modified AGI exceeds certain dollar amounts (\$250,000 for joint returns and \$200,000 for individuals). Investment income is: (1) gross income from interest, dividends, annuities, royalties, and rents (other than from a trade or business); (2) other gross income from any business to which the tax applies; and (3) net gain attributable to property other than property attributable to an active trade or business. Investment

income does not include distributions from a qualified retirement plan or amounts subject to self-employment tax. This rule applies mostly to passive businesses and the trading in financial instruments or commodities. With this additional tax, the maximum net capital gains rate could be as high as 23.8% in 2013. Because distributions from qualified retirement plans are not subject to the tax, taxpayers may want to invest in retirement accounts, if possible, rather than taxable accounts.

Timing of Sales: You may want to time the sale of assets so as to have offsetting capital losses and gains. Capital losses may be fully deducted against capital gains and also may offset up to \$3,000 of ordinary income (\$1,500 for married filing separately). In general, when you take losses, you must first match your long-term losses against your long-term gains, and short-term losses against short-term gains. If there are any remaining losses, you may use them to offset any remaining long-term or short-term gains, or up to \$3,000 (or \$1,500) of ordinary income. When and whether to recognize such losses should be analyzed in light of the possible future changes in the capital gains rates applicable to your specific investments.

Dividends: Qualifying dividends received in 2012 are subject to rates similar to the capital gains rates. Therefore, qualifying dividends are taxed at a maximum rate of 15%. Qualifying dividends include dividends received from domestic and certain foreign corporations. Note that if Congress does not extend the reduced dividend rates, in 2013, dividends will be taxed at ordinary income rates, which could reach 39.6% (43.4% with the additional 3.8% tax on certain unearned income).

Selling Your (Underwater) Home: If you are currently underwater on your home and you are considering selling or getting a loan modification, you absolutely should get this done in 2012. In 2012, qualified mortgage debt relief from your lender is not considered income. However, if Congress fails to extend this tax benefit, any debt discharged on or after January 1, 2013, will be considered income and taxes will be owed on the amount forgiven.

Selling Your (Inherited) Home: If you received the residence you are using as your principal residence from a decedent who died in 2010 and whose executor elected not to have the estate tax apply, you can include the decedent's use and ownership of the home to qualify for the [§121](#) exclusion amounts. If by the end of 2012, you would meet the 2 of 5 year tests with this tacking, it could be a perfect time to sell and exclude up to \$250,000 of gain (\$500,000 if married and both spouses received the property).

Social Security: Depending on the recipient's modified AGI and the amount of Social Security benefits, a percentage — up to 85% — of Social Security benefits may be taxed. To reduce that percentage, it may be beneficial to defer receipt of other retirement income. One way to do so is to elect to receive a lump sum distribution from a retirement plan and to rollover that distribution into an IRA. Alternatively, it may be beneficial to accelerate income so as to reduce the percentage of your Social Security taxed in 2013 and later years.

Other Tax Planning Opportunities: We also can discuss the potential benefits to you or your family members of other planning options available for 2012, including [§529](#) qualified tuition programs.

Alternative Minimum Tax

For 2012, the alternative minimum tax exemption amounts are currently scheduled to be much lower that will most likely subject more taxpayers to the AMT effect. The exemption amounts in place for 2012 are: (1) \$45,000 for married individuals filing jointly and for surviving spouses; (2) \$33,750 for unmarried individuals other than surviving spouses; and (3) \$22,500 for married individuals filing a separate return. Also, for 2012, unless Congress acts to extend the previous years' rules, nonrefundable personal credits cannot offset an individual's regular and alternative minimum tax, and capital gains will not be taxed at lower favorable rates for AMT.

Some of the standard year-end planning ideas will not reduce tax liability if you are subject to the alternative minimum tax (AMT) because different rules apply. Because of the complexity of the AMT, it would be wise for us to analyze your AMT exposure.

Pricing Changes

While we are mindful of the economic times we currently live in, it has become necessary to adjust our fees. Our base 1040 tax return preparation fee will change from \$65 to \$70 effective January 1, 2013 and our 1099 preparation fees will change from \$50 to \$100 effective January 1, 2013. With increase legislation and documentation requirements the time and risk for these services has increased dramatically. We appreciate your understanding.

If you have any questions, please do not hesitate to call. I would be happy to meet with you at your convenience to discuss the strategies outlined above. While we are getting very close to the end of the year, there is still time to implement these strategies to minimize your 2012 tax liability.

We wish each of you a very Merry Christmas and an Extraordinary New Year!

Sincerely,

Jenkins CPA, LLC