



TAX ISSUES FOR HIGHER-INCOME INDIVIDUALS

We know that you have worked hard for your money and would like to reap the benefits to the greatest extent possible. Your ultimate goal is to sustain a successful wealth-building strategy while avoiding unnecessary and expensive tax consequences. We are interested in helping you achieve these objectives.

Although it is generally beneficial to defer income and accelerate expenses, tax reform is looming on the horizon. The Obama administration's priority is to lower current unemployment rates and strengthen the fiscal health of the middle-class, rather than to provide tax relief for more affluent Americans. The president has proposed an increase in the income and capital gains tax rates for individuals effective for 2011.

To further complicate matters, individual marginal income tax rate reductions under the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) are set to expire at the end of 2010. If EGTRRA sunsets without modification by Congress, the temporary 10 percent regular income tax bracket will be eliminated, and the 33 and 35 percent brackets will be increased to 36 and 39.6 percent, respectively. Therefore, the focus of tax planning for 2010 shifts to balancing tax rates for the current and future years.

In addition to the possible changes in tax rates, tax planning is adversely affected by the status of extensions on tax breaks that expired at the end of 2009. It is anticipated that Congress will extend some or all of these provisions before year-end, but the uncertainty surrounding these incentives impedes the decision-making process:

- Additional standard deduction for state and local real property taxes
- Itemized deduction for state and local general sales taxes in lieu of state and local income taxes
- Motor vehicle sales tax deduction
- Above-the-line deduction for certain out-of-pocket classroom expenses
- Above-the-line higher education tuition deduction
- Moratorium on required minimum distributions
- Nonrefundable tax credit offset of entire regular and AMT tax liability
- Tax-free IRA distributions to charity
- AMT exemption amounts for individuals are scheduled to revert back to the amounts that applied prior to the 2001 tax year

Earlier this year, major foreign tax compliance and health care reforms were enacted. The foreign tax compliance provisions increase disclosure and information reporting requirements, and provide penalties for non-compliance. Numerous foreign tax credit provisions were intended to offset the tax benefits provided by the Education Assistance Act. At the same time, revenue-raising provisions that target higher-income individuals were included in the health care reform legislation.

Because of these changes, if you have global financial interests, you can expect greater scrutiny by the IRS. The recently concluded offshore voluntary compliance initiative added more than 14,700 individuals to the tax system going forward. The IRS has also undertaken a multi-year compliance strategy which plans to look at the entire complex web of business entities controlled by high-wealth individuals.

In spite of this, there are some tax incentives that may benefit higher-income taxpayers like you in 2010. The phase-outs for personal exemptions and itemized deductions are eliminated (they return in their original form in 2011). Because the adjusted gross income (AGI) and filing status limits no longer apply, you now have the opportunity to convert a traditional IRA to a Roth IRA. If you make a Roth IRA conversion in 2010, you have the option to recognize the conversion amount ratably in 2011 and 2012, or you may recognize it all in 2010.

However, the alternative minimum tax (AMT) may continue to negate your personal exemptions and many itemized deductions. The temporary legislative increases to AMT exemption amounts (AMT patches) cease to apply in 2010. Barring further legislative action, the AMT exemption reverts to the 2000 amounts for 2010 and later tax years. For this reason, a failure to take the AMT into account could jeopardize your tax-planning strategy.

Recently enacted and proposed legislation, as well as the increased scrutiny provided by IRS initiatives, create an especially challenging planning environment. If you would like to meet with us to discuss the options that are best suited to meet your personal financial goals, while minimizing your tax liability please contact our office at your earliest convenience to make an appointment.

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