

2011 TAX HIGHLIGHTS INDIVIDUAL

Here are highlights of changes & other important tax information. Many deductions and credits are limited by one's Adjusted Gross Income (AGI) or modified AGI (MAGI).

Important Rates & Amounts - 2011

Standard deduction (non-itemizers):

Single	\$ 5,800	Over 65, unmarried – add \$1,450
Married filing Joint (MFJ)	\$11,600	Over 65, unmarried & blind – add \$2,900
Married Filing Separate(MFS)	\$ 5,800	Over 65, married – add \$1,150
Head of Household (HH)	\$ 8,500	Over 65, married & blind – add \$2,300
Personal Exemption	\$ 3,700	

	2011		2012
Standard Mileage rates (allowed/deductible per mile):	1/1-6/30	7/1-12/31	
Business	\$.51	\$.555	\$.555
Medical & moving	.19	.235	.23
Charity	.14	.14	.14

Maximum FICA Wage Base (2011 & 2012) \$106,800 & \$110,100

Maximum Social Security Tax Withheld 2011 - \$4,485.60 & 2012 - \$6,826.20

Here are the marginal individual income tax rates on taxable income up to:

RATE	Individual	MFJ	MFS	HH
10%	\$0 - \$8,500	\$0 - \$17,000	\$0 - \$8,500	\$0 - \$12,150
15%	34,500	69,000	34,500	46,250
25%	83,600	139,350	69,675	119,400
28%	174,400	212,300	106,150	193,350
33%	379,150	379,150	189,575	379,150
35%	Above the previous amount			

Taxpayer-Friendly Changes

Current tax rates extended. The 2010 marginal individual income tax rates will remain the same through the 2012 tax year. After that they are scheduled to increase as follows:

Current 2010 – 2012 marginal rate	10%	15%	25%	28%	33%	35%
Scheduled 2013 increase	N/A	15%	28%	31%	36%	39.6%

Capital Gains

The maximum long-term capital gain & qualified dividend tax rate remains 15% through 2012. Rates may be lower depending on the year & the tax bracket. Collectibles are taxed at a 28% rate.

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There are significant changes to Schedule D, Capital Gains & Losses. There is a new form, 8949, that will forward information to D. The new forms require more detail. Broker statements must include detail for gross proceeds from a "covered security", including the adjusted basis & whether the security is short or long-term. Basis must now be transferred when accounts are transferred between brokers.

Itemized/Standard Deductions

Before 2010, & after 2012, itemized deductions were reduced for taxpayers with incomes greater than a "phase-out" amount. For 2010-2012, there is no phase-out.

A deduction for state & local sales tax on large purchases (in lieu of state income tax) was extended through 2011.

2011 is the last year to deduct mortgage insurance premium deduction. AGI must be < \$110,000 & the loan must have been made after 12/31/2006.

Premiums paid for long-term care insurance may be deductible as a medical expense.

Charity

All money contributions must have written supporting documentation.

Cash donations of \$250 or more require written acknowledgement from the charity.

Non-cash donations must be in "good" condition or better. "Good" is not defined.

Non-cash donations of any amount require a receipt from the donee.

Non-cash donations > \$500 require tax return detail – date & how acquired, cost, etc.

Donations of more than \$5,000 require attaching a "qualified appraisal."

A contribution substantiation matrix is on the website.

The provision allowing taxpayers over 70 ½ to exclude up to \$100,000 from gross income for money distributed from an IRA (& some other retirement accounts) sent directly to a charity was extended through 2011. This can be a great strategy for those that are having some of their social security benefits taxed, those that don't itemize, etc.

Credits (dollar-for-dollar reductions of tax).

The child tax credit of \$1,000 per child, maximum 2 children, was extended through 2012. It may be refundable if earned income exceeds \$3,000. There is an AGI phaseout.

The adoption credit has been extended through 2012. However, after the 2011 tax year it will no longer be refundable but may be carried forward. The maximum credits in 2011 & 2012 are \$13,360 & \$12,650, respectively. No credit is allowed for the adoption of non-US citizens until the adoption is final.

Some energy credits were extended through 2011 but the benefits were reduced:

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- A. The **non-business energy credit** (IRC §25C). It was reduced from 30% in 2010 (maximum \$1,500) to 10% in 2011 of qualifying energy improvements to a *principal residence*. They include insulation systems, exterior windows & doors, metal & asphalt roofs & biomass fuel stoves. In 2011 there is a \$500 lifetime limit.
- B. The **Residential Energy Efficient Property Credit** (IRC §25D) It is 30% (no maximum) of the cost of solar, photovoltaic, fuel cell, wind & geothermal heat pump equipment improvements. Must be to a U.S. residence but it does not need to be a primary residence. Pools & hot tubs don't apply. The credit runs through 2016.
- C. **Alternative Fuel Motor Vehicle Credit** now consists of 5 separate credits for vehicles that include several technologies.

**Advanced lean burn. New Qualified Plug-in Electric Drive Motors.
Alternative fuel vehicles. Plug-in Electric Conversion Credit. Qualified fuel cell.**

The **hybrid vehicle credit** expired 12/31/10.

The **Plug-in conversion credit** is 10% of the cost of converting vehicle. Maximum credit is \$4,000. It applies to property placed in service between 2/17/09 -12/31/11.

The **Plug-in Electric credit** now has a maximum amount of \$7,500 per return.

The **Savers Credit** is a nonrefundable credit for contributions by an eligible taxpayer (low income) to a qualified retirement plan. The maximum credit is \$2,000. For taxpayers receiving social security payments there may be multiple benefits.

Beginning with the 2012 filing season, any tax return claiming the **Earned Income Tax Credit** will require the due diligence checklist to be filed also.

Education

The \$250 (max) deduction for educator expenses (supplies) was extended through 2011.

Up to \$4,000 for qualified post-secondary education tuition is deductible through 2011

The deduction for student loan interest, up to \$2,500, was extended through 2012.

The **American Opportunity Tax** (formerly Hope) **Credit** was extended through 2012.

- A. It's available for the first 4 years of college (formerly 2).
- B. The maximum credit is **\$2,500 per student (formerly \$1,800)**.
- C. It may offset Alternative Minimum Tax (AMT).
- D. Qualified expenses include tuition, fees & materials.
- E. Up to 40% of the credit may be refundable.
- F. It's available to people with AGI of \$160k - \$180k married (\$80k - \$90k single).

The **Lifetime Learning Credit** is still available with a maximum of \$2,000 per return.

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IRC §529 plans. Beginning 2010, qualifying expenses include computer technology used for post-secondary education (in addition to tuition, fees, books, supplies, etc.).

The Coverdell Education Savings maximum contribution amount is \$2,000 through 2012.

Neither §529 or Coverdell accounts are tax deductible. Earnings are tax-free if used for education.

Real Estate

Taxpayers have been able to exclude up to \$250,000 (\$500,000 for MFJ) of gain on the sale of a house if it was the principal residence 2 out of the previous 5 years. The gain from the sale of a principal residence might not be excluded from gross income for periods that the home was not used as the principal residence (nonqualified use). The "nonqualified" use period does not include any portion of the 5-year period after the last date the property was used as a principal residence. Translation: If you rented the house out **after** you lived there you may avoid tax on the gain.

The **Energy-efficient property deduction** is **\$1.80 per square foot** for buildings that achieve a 50% (overall) energy saving.

RETIREMENT PLANNING

Avoid early (before age 59 ½) distributions from retirement accounts. Besides income taxes, there is a 10% federal & 2 ½% California excise tax unless an exception is met.

The Social Security Administration suspended mailing annual benefit statements in April. They've announced that mailings will resume in 2012 but only to those 60 & older.

If you receive social security benefits prior to reaching full retirement age, \$1 in benefits will be deducted for each \$2 earned above the annual limit. In the year full retirement age is reached, \$1 in benefits is deducted for each \$3 earned above the limit. Following is the maximum earned income allowed before for Social Security benefits are reduced:

	PERIOD	ANNUAL LIMIT
Under Full Retirement Age	2011 & 2012	\$14,160
Year of Full Retirement Age	2011	\$37,680
Full Retirement Age or Older	All	No Limit

Medicare Part B premiums are normally withheld from one's benefit check. For those with MAGI of < \$170,000 MFJ, \$85,000 single, the monthly withholding is \$99.90. As income increases, that 2012 amount can reach \$319.70, a decrease from \$369.10 in 2011.

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Beginning 2011, the same high-income beneficiaries who pay the Plan B premium surcharge pay a graduated surcharge on Plan D premiums if they are enrolled in Plan D.

The increased premium can be appealed using additional information or based on a life-changing event. The deadline is within 60 days of the notice date.

The maximum deductible **employee** retirement plan contributions are as follows:

<u>Plan</u>	<u>Maximum Amount</u>		<u>Additional Amount if Age 50+</u>	
	<u>2011</u>	<u>2012</u>	<u>2011</u>	<u>2012</u>
IRA	\$5,000	\$5,000	\$1,000	\$1,000
401(k), 403(b), 457	\$16,500	\$17,000	\$5,500	\$5,500
SIMPLE	\$11,500	\$11,500	\$2,500	\$2,500

The IRA contribution amount is the same for a Roth and spousal IRA.

The maximum total deduction for **defined contribution retirement plans** (employee & employer) - SEP, 401(k), 403(b) & 457 plan – for 2011 is \$49,000 & 2012 is \$50,000.

If the taxpayer is an “active participant” in an employer-sponsored retirement plan, the IRA deduction is phased out when the AGI exceeds the following amounts:

	<u>SINGLE</u>	<u>JOINT</u>	<u>MARRIED FILING SEPARATE</u>
2011	\$56,000 - \$66,000	\$90,000 - \$110,000	\$0 - \$10,000
2012	\$58,000 - \$68,000	\$92,000 - \$112,000	\$0 - \$10,000

If an individual is not but the **spouse is an active participant in a qualified retirement plan**, the IRA deduction is phased-out in with AGI's as follows:

2011	\$167,000 - \$177,000	2012	\$173,000 - \$183,000
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Pension benefits received by a non-spouse beneficiary may be transferred into an inherited IRA. If the decedent hasn't started taking distributions, the beneficiary may elect to have the balance distributed (& taxed) over his/her life expectancy.

Partial Annuitization. Beginning 2011, taxpayers may partially annuitize a life insurance contract, nonqualified annuity or endowment over a period of at least 10 years.

Subject to IRS levy. Unemployment pay? No. Pensions, social security benefits? Yes.

There is a once-in-a-lifetime direct trustee-to-trustee rollover from an IRA to a Health Savings Account (HSA). It's not subject to tax or penalty.

The required minimum distribution tables will be posted on our website.

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Roth IRA's.

Roth IRA's are not deductible but not taxable when distributed if rules are followed. The maximum contribution to a Roth is phased out as follows (by filing status):

	SINGLE or HOH	JOINT	MARRIED FILING SEPARATE
2011	\$107,000 - \$122,000	\$169,000 - \$179,000	\$0 - \$10,000
2012	\$110,000 - \$125,000	\$173,000 - \$183,000	\$0 - \$10,000

Traditional-to-Roth IRA conversions no longer have a \$100,000 AGI limitation. Also, MFS filers may now do Roth conversions.

If someone doing a Roth conversion later get buyers remorse & decides that it wasn't such a great idea, the **conversion can be recharacterized**, i.e., undone, as late as the extended due date of the returns (October 15) even if the return is not extended.

HEALTHCARE BILLS

The Patient Protection & Affordable Care Act of 2010 & the Health Care & Education Reconciliation Act of 2010 together include over \$400 billion in revenue raisers. Their provisions will affect everyone. They mandate that all individuals (with a few exceptions) have health care coverage by 2014 or pay a penalty. For those that don't have employer-sponsored coverage, insurance "exchanges" will be set up to facilitate shopping for insurance. Available plans must be "qualified health plans" that meet government standards. Financial assistance will be available to ensure that individuals are not spending over a certain percentage of their income on health insurance. Starting 2010 & phasing in through 2018 there will be new & lost tax deductions, credits & taxes.

We have booklets that detail the bills. The U.S. Supreme Court will hear arguments regarding the constitutionality of the law so it or parts of it may or may not stick around.

2010

There is an **income tax credit for small employers** that provide employee health care benefits. To qualify, there can't be more than 25 full-time equivalent employees (FTE) & average annual wages must not exceed \$50,000 per employee.

Small employers are not required to provide A) Employee coverage B) Dependents coverage C) Coverage extended to a dependent's spouse or dependents. For those that do, there were important changes to dependency coverage that are tricky. Any plan that offers dependent coverage must now provide coverage for adult children up to the day the dependent turns 26. An employer may voluntarily offer coverage until the end of the plan year in which the dependent turns 26. California did not conform to all the federal changes. Here is a link: www.irs.gov/newsroom/article/0,,id=220839,00.html

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Other Health Care Changes

The penalty for non-qualified distributions from Health Savings Accounts (HSA's) & Medical Savings Accounts (MSA's) after 12/31/10 will increase to 20%. For this purpose, qualified expenses for drugs or insulin must be prescribed by a physician.

Effective for tax year 2012, i.e., on W-2's issued in January, 2013, employers must include **the value of the employee's health insurance coverage** paid by the employer. This requirement is for reporting purposes & **will not affect taxable income.**

2013 – NEW TAXES

Beginning 2013, individuals will pay an **additional .9% Medicare Hospital Insurance (HI) tax** on wages & self-employment income on amounts earned above certain thresholds. The employer's share will not change. The threshold amounts are below.

There will also be an additional HI tax on individuals, estates & trusts of **3.8% on net investment income.** For individuals, the tax is 3.8% of the lesser of A) Net investment income or B) The excess of MAGI over the threshold amount. The thresholds are:

\$250,000 Joint Returns \$125,000 Married Filing Separate \$200,000 All Others

Net investment income generally includes dividends, interest, rents, annuities, royalties & capital gains. There are some restrictions & exceptions. Specifically excluded items include tax-exempt bond interest, veterans' benefits, the non-taxable gain from the sale of a principal residence, social security benefits & retirement plan distributions. It is possible to be subject to both taxes.

In 2013, the threshold for deducting medical expenses as an itemized deduction will increase from 7.5% to 10% of AGI. Exception: For 2013 – 2016, those 65 & older can continue to use the 7.5% threshold.

2014

In 2014, some taxpayers will be allowed a refundable credit to help subsidize the purchase of health insurance through a state health benefit exchange. To qualify, the taxpayer must A) Have "household income" at least 100% but not more than 400% of the federal poverty line & B) Not have health insurance under an employer plan. The current poverty line is \$10,830 plus \$3,740 for each additional family member. The IRS will pay the premium assistance directly to the insurer.

Failure to maintain qualifying health coverage for oneself & one's dependents will make one subject to a "shared responsibility penalty". The penalty will be reported & paid on the individual income tax return.

Large employers will be liable for not offering affordable basic health insurance coverage. Large is generally defined as having 50 or more full-time employees. The

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penalty can be assessed for either not offering coverage or offering coverage that is “inadequate” for at least one employee.

2018 – “Cadillac Tax”

Beginning 2018, there will be a 40% excise tax on the amount by which the employee’s health coverage premiums exceed certain thresholds. The starting amounts are \$10,200 for single & \$27,500 for family coverage.

COBRA. Workers who were involuntarily terminated between 9/1/08 – 5/31/10 were eligible to receive a 65% government subsidy for COBRA (employer-sponsored health insurance) for a maximum of 15 months. High-income (defined as having MAGI over \$125,000) beneficiaries are required to have the subsidized portion recaptured as taxable income. The IRS sent out letters to potential candidates.

BUSINESS

Here are the 2011 marginal C corporation tax rates on taxable income up to:

15%	25%	34%	39%	34%	35%
\$0 - \$50,000	\$75,000	\$100,000	\$335,000	\$10,000,000	\$15,000,000

New Form 1099-K. Beginning in the 2011 tax year, regulations require all businesses that process credit cards & electronic payments to send a 1099-K to sellers with more than 1) 200 transactions & 2) \$20,000 gross income paid to them. It will list gross merchant card & 3rd party network payments processed by month. This information will need to be reported on the business’s income tax return (for 2011 report \$0).

1099 Filing. Business returns for individuals, corporations & partnerships will ask whether all required 1099 forms have been or will be filed.

Schedule E. The form on the individual tax return where rental income is reported will now also ask:

- A. The property type (single family residence, commercial).
- B. The Number of “fair rental days” & “personal use days”.

Payroll

Credit for Retained Workers (2011). Workers qualifying for the payroll tax holiday (hired after 2/3/10 & before 1/1/11, & prior to hire, worked no more than 40 hours in the 60-day period ending on the date that employment began) may qualify for an employer credit of up to \$1,000 if they remain employees for at least 52 weeks. The employee’s wages for the last 26 weeks must equal or exceed 80% of those for the first 26 weeks.

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Social Security Tax Cut (2011). The 2011, the employee social security tax rate was reduced from 6.2% to 4.2%. The employer “match” remained at 6.2%. Those rates will remain in effect through February, 2012.

The federal unemployment tax (FUTA) rate dropped from 6.2% to 6% 7/1/11 but because California hasn’t repaid federal borrowings our federal rate may actually increase.

The IRS has a Voluntary Classification Settlement Program (VCSP) that allows employers to reclassify independent contractors as employees. The motivation is reduced penalties & protection from employment tax audits. Form 8952 must be submitted.

As of 1/1/11, most businesses are required to pay federal payroll taxes electronically via EFTPS. Most banks no longer accept payments. There are penalties for non-compliance. Payments may be made by phone: (800) 555-3453. Information is at www.eftps.gov.

Other Business

100% Bonus Depreciation. For qualifying fixed assets placed in service after 9/8/10 & before 1/1/12, 100% of the cost may be expensed (50% of the cost for assets purchased 1/1/10 – 9/8/10 & 2012). Qualifying means the property A) Is original-use (new) B) Has a tax life of 20 years or less C) Is tangible D) Must be used inside the U.S. “Listed property” (such as autos) are excluded. Unlike §179 property, the deduction is not limited by business income or the amount of property purchased or subject to recapture.

Asset Expensing (§179). For tax years 2010 & 2011 qualifying asset purchases, up to \$500,000 can be deducted in the year of acquisition. This benefit starts to phase-out when asset purchases exceed \$2 million (it’s gone after \$2.5 million). Unlike bonus depreciation, used property qualifies. The deduction decreases to \$139,000 in 2012 & to \$25,000 beginning in 2013.

15-year depreciation for qualified real property was extended through 2011. Qualified real property includes qualified A) Leasehold improvements B) Restaurant property & C) Retail improvement property. It is also eligible for §179 expensing up to \$250,000.

Business vehicle depreciation is more restrictive. An \$8,000 increase in first-year depreciation of qualified autos & light trucks was extended through 2012. Therefore, the maximum first-year depreciation for a vehicle that is used 100% for business is \$11,160. Vehicles with a gross vehicle weight (GVW) of 6,000 lbs. or more are still allowed up to a \$25,000 write-off. Vehicle GVW is on www.intellichoice.com.

Start-up businesses can deduct (instead of amortize over 15 years) up to \$5,000 of organization costs & organization expenses.

Small Business Stock Exclusion – future benefit. For qualified small business stock acquired after 2/17/09 & before 9/28/10, 75% of the gain on the sale is excluded from

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income. For purchases between 9/28/10 – 12/31/11 the exclusion is 100%. For acquisitions before 2/18/09 & after 12/31/11 the exclusion is 50%.

Draconian 1099 Reporting Changes Nixed. The Health Care Act requirement mandating the issuance of 1099's A) To corporations & B) For goods & tangible property beginning in 2012 (for 2011 business year) was struck down.

Information Return (1099) penalty increases. Effective 1/1/11, a penalty of \$100 per 1099 is imposed for:

- Failure to file before the required due date.
- Failure to include all the information required to be shown.
- Inclusion of incorrect information on a 1099

Make sure that you file & that the information is correct.

Health insurance premiums paid by an S corporation for its shareholder(s) should be included on the shareholder's W-2.

S corporations & partnerships that file late will be penalized \$195 per shareholder or partner per month (maximum 12 months of penalties).

Health Insurance & medical expense deduction – Sec. 105 medical reimbursement plan & sec. 106, health insurance premium plans allow sole proprietors to hire a spouse & deduct health insurance premiums, medical reimbursements, etc.

ESTATE & GIFT TAX

For estates of individuals who died in 2010, the estate & generation-skipping transfer tax (GST), as well as the global step-up (or step-down) in asset bases upon death, until December 17, 2010, disappeared. It was replaced with "modified basis" changes:

- 1) A \$1.3 million overall step-up in basis.
- 2) \$3 million step-up to a surviving spouse.
- 3) Other basis additions equal to the decedent's capital loss carryovers, NOL's, etc.

To elect the "modified basis" option, form 8939 must be filed by January 17, 2012.

The 2010 Tax Relief Act enacted the following: A) Utilize the above rules or B) Return to the pre 2010 rules with the following changes:

1. The estate tax & the generation skipping tax (GST) exclusion amount jumps from \$3.5 million to \$5 million in 2011 & \$5,120,000 in 2012.
2. The top tax rate drops from 45% to 35%.

For deaths in 2011 & 2012, the estate of the surviving spouse may qualify to use the unused exclusion amount of the predeceased spouse. The exclusion is the sum of: A) The

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basic exclusion (currently \$5 million) & B) The unused exclusion of the predeceased spouse. To make this election, form 706, U.S. Estate Tax Return, must be filed.

Gift Taxes. The 2010 Tax Relief Act increased the lifetime gifting exclusion amount, the amount that can be gifted over a lifetime without incurring a gift tax liability, from \$1 million to \$5 million for 2010 – 2012. The maximum tax rate is 35%. The 2011 annual gift tax exclusion is \$13,000. That's the amount that can be gifted year to any individual without affecting the \$5 million lifetime exclusion.

MISCELLANEOUS

Effective 2010, any individual who holds an interest in a "specified foreign financial asset" greater than specified thresholds must attach to his tax return the "Required Information" (on form 8938). The threshold starts if the aggregate value of all the individual's foreign assets exceeds \$50,000 on the last day of the year or more than \$100,000 at any time during the year. An exception applies if an income tax return is not required to be filed. This is in addition to previously existing law that U.S. persons report annually account information if the aggregate value of all foreign financial accounts exceeds \$10,000 (FBAR, form TDF 90-22.1).

Registered Domestic Partners (RDP's). Recent IRS rulings state that California RDP's must each report one-half of community income on their federal tax returns, putting their filing more in line with California. Unlike California, they must file as single.

A U.S. individual living abroad can exclude up to \$92,900 of foreign earned income if he/she satisfies certain requirements. The 2012 exclusion is \$95,100.

Preparer & Filing Restrictions. Effective 1/1/11, there are 2 new federal tax preparer requirements: A) All preparers must be registered with the IRS & obtain a Preparer Tax ID Number (PTIN) & B) They will be subject to a competency exam & continuing education requirements. This covers preparers of payroll tax & other federal forms.

Also effective 1/1/11, tax preparers that file more than federal 100 tax returns are required to electronically file them. Tax preparers are subject to a penalty of \$50 per return filed on paper that should have been e-filed. California has had an e-filing requirement for about 8 years. Any federal tax return not e-filed must include form 8948, Preparer Explanation for not Filing Electronically.

Credit Card Payment. The IRS accepts payments for most types of taxes by credit card, including payroll taxes. The firms that facilitate the activity charge a 2.5% "convenience fee". They are

A. Official Payments Corporation, 800-272-9829; www.officialpayments.com.

B. Link2Gov Corporation 888-729-1040; www.pay1040.com

Information is on the IRS website, www.IRS.gov, then, credit card options page.

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Not frequently enforced, there is a late-filing individual income tax penalty of \$135.

CALIFORNIA – INDIVIDUAL

California tax law is more similar to federal law but important differences include:

1. California Registered Domestic partners must file as married.
2. US Social security & unemployment benefits are not taxable by CA. Foreign social security is taxable.
3. CA does not have exclusion for foreign earned income.
4. CA doesn't have bonus depreciation, the §179 expense is \$25,000 & the ceiling for equipment purchases is \$200,000, i.e., above that no sec. 179 is allowed. CA also does not conform to the more generous shorter-lives for qualified restaurant, leasehold improvements & retail improvements.
5. CA doesn't allow loss carry-backs.
6. CA doesn't recognize Health Savings Accounts.
7. CA doesn't have different tax rates for various kinds of income, i.e., no capital gain no qualified dividend rates, no self-employment tax, etc.

California's Child & Dependent Care Expenses Credit is nonrefundable effective 1/1/11.

The California renter's credit is nonrefundable & can't be carried over.

The dependent exemption is scheduled to increase from \$297 to \$315.

The FTB had tried to require that returns with deductions for property taxes also include the address & parcel no. of the property. Lobbyists dissuaded this rule for 2011. The state's motivation is their (correct) belief that taxpayers are over-deducting. Most tax preparers deduct the entire bill payment; the reality is that there are often assessments included that are not deductible. The FTB will continue to pursue this.

Big Brother. The FTB is creating a new data-matching program that will result in the forwarding of quarterly bank information from financial institutions to them. This information will be used to assist in collection of state taxes. The institutions may or may not inform their customer. The projected start date is April, 2012 & related levies may start June, 2012. The FTB is estimating that this will result in an increase of 50,000 levies per year.

Big Brother Snitching. The FTB has information-sharing agreements with 107 California cities. From income tax returns filed, the FTB identifies self-employed individuals to cities. The cities check to see if those people are filing & paying city business licenses & taxes. Conversely, cities forward business license information to the FTB so they can investigate whether business tax returns are being filed.

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Big Brother Stealing. The FTB participates in the Treasury Offset Program, a debt collection program where federal tax refunds are intercepted for payment of past-due California tax debts. Specifically, IRS refunds may be reduced by unpaid FTB debts.

Sales Tax Decrease. The 1% increase in sales & use tax expired 7/1/11, dropping the statewide rate from 8.25% to 7.25%.

California conforms to the federal provision that allows a surviving spouse a \$500,000 exclusion of gain on the sale up to 2 years from the date of death of the decedent spouse.

All 2011 state **estimated tax payments** are still on a fast track & due as follows:

	1 st Qtr.	2 nd Qtr.	3 rd Qtr.	4 th Qtr.
2011	30%	40%	0%	30%

California has implemented the following income tax withholding rules:

Backup Withholding: Effective 1/1/10, individuals subject to federal backup withholding (28%); are also subject to California backup withholding of 7%.

Real Estate: For applicable sales, sellers must withhold 3 1/3% of the sales price or 9.55% of the estimated gain. For property sold by an S corporation, the rate is 11.05%.

Out-of-state Income Payments: Payments to non-resident payees for income from California sources (i.e., partners, shareholders, etc.) are also subject to 7% withholding.

California has conformed to the federal late-filing penalty of \$135.

Getting information. The Franchise Tax Board (FTB) website, www.ftb.ca.gov/, has a "MyFTB" section that allows taxpayers to check information about their current year returns, including refund status, setting up installment agreements, estimates paid, etc.

Electronic payment is mandatory if the taxpayer has made a single FTB payment > \$20,000, or filed a CA tax return with a tax liability > \$80,000 for a tax year on or after 1/1/09. Effective 2011, the FTB began assessing a 1% penalty on individuals that failed to comply. It may be possible to opt out of the e-pay requirements by filing form FTB 4107. Access FTB WebPay at www.ftb.ca.gov/online/webpay.

The FTB has also implemented a variety of methods for making payments, including credit cards, pay by phone, E-pay, Web pay & On-line banking. The latter 3 allow for scheduling payments in advance. Only the credit card option has a fee.

Dependent Adult Protection. State law protects dependent adults from dishonest custodians. It creates a presumption that a gift > \$5,000 to a care custodian is the result

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of fraud or undue influence. An independent attorney must certify that the gift is not the result of fraud or undue influence.

CALIFORNIA BUSINESS

California has a flat 8.84% tax rate for most C corporations. S corporations pay the greater of \$800 or 1.5% of their net income.

Use Tax. Since 2009, the Board of Equalization (BOE) has required that “qualified purchasers” (QP) register & annually report purchases subject to use tax & file a return electronically. Use tax is California’s way of getting tax from sales that are not subject to sales tax, i.e., out-of-state purchases. QP’s are businesses with at least \$100,000 in gross receipts that are not required to hold a seller’s permit. This includes rental income, services, farms, not-for-profits, etc. Applicable tax must be paid by April 15. A return is due even if no tax is due. Form BOE 404-A must be completed to register. If you want assistance filing the BOE return please contact our office before the deadline. Returns can be e-filed at www.boe.ca.gov/electsrv/efiling/sutd.htm. Changes in 2011 include:

1. The BOE no longer automatically registers businesses just because they have \$100,000 of gross receipts. However, if the BOE determines that the business has a use tax liability, they will require registration & up to 8 years of returns.
2. The BOE is automatically deregistering & alerting taxpayers that have filed \$0 returns for 3 years. QP’s may close out their accounts if the \$100,000 threshold is no longer being met.

SOS No Longer Mailing Statement of Information (SOI). As of September 26, 2011, the California Secretary of State’s office will no longer send blank SOI forms to new corporations or LLC’s. They stopped sending forms to existing businesses over a year ago. Businesses need to monitor the due dates for these forms. Late filings are assessed \$250 instead of \$25. We can assist you with this.

California Net Operating Losses (NOL’s) are suspended in 2010 & 2011 for:

- A) Individuals, estates & trusts with federal MAGI of \$300,000 or more
- B) Corporations with pre-apportioned net income of \$300,000 or more.

NOL’s incurred after 12/31/07 have a 20-year carry-forward period. Suspended NOL’s will be allowed to tack-on the suspended years. Beginning in 2013, California is scheduled to start allowing NOL carry-backs.

California Limited Liability Companies (LLC’s) pay an annual tax of \$800. There’s also a fee on gross receipts in excess of \$250,000. It ranges from \$900 to \$11,790, depending on the amount. For a calendar year LLC, it is due June 15 of the current year.

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Licensed contractors will be permitted to form LLC's (previously disallowed). It appears that the effective date will be 1/1/12. Each licensed member of the LLC will be liable for up to \$1 million in damages occurring.

Effective 9/30/10 through 1/1/16, California will allow engineers & land surveyors to operate as limited liability partnerships (similar to LLC's).

Businesses are required to withhold 7% of payments to domestic non-residents partners, shareholders, members, etc. if the amount paid is expected to exceed \$1,500.

Jobs Credit. It provides up to a \$3,000 credit for each net increase in qualified full-time employees hired by a small business (20 or fewer employees). The credit is available for each full-time equivalent increase in employees over the previous (2010) year. It is not refundable but may be carried over 8 years. Of the \$400 million allocated to the credit, only \$70 million has been used. See form 3527.

Film & Television Credit. This began January 1, 2011 & has been extended to July, 2015. It allows a credit of 20% of production expenses for qualified motion pictures produced in California or 25% of expenses for an independent film or TV series that relocates to California.

Small Non-Profit Reporting. Beginning 2011, California requires small (gross receipts < \$25,000) tax-exempt organizations (other than churches) to file an annual notice electronically.

Amazon Bill. Last June, California enacted ABX1 28 which expanded the definition of a "retailer engaged in business" to include businesses that enter into an agreement to refer potential purchasers of taxable tangible property to the retailer. The purpose was to require online retailers to charge sales tax on purchases shipped to California. The legislature delayed implementation for a year (September 2012).

Form DE542. California requires, reporting of independent contractors when a contract is established or when \$600 or more is expected to be paid during the calendar year.

There is a penalty of \$18 per partner or shareholder per month, up to a maximum of 12 months, for filing partnership & corporate tax returns late.

File 1099's! The FTB has disallowed deductions for payments to individuals that either should have been treated as employees (tax withheld) or no 1099 was sent.

The FTB is taking the position, supported by cases, that a foreign (out-of-state) LLC that has a managing member in California is doing business in California, even if the activity occurs in another state. This means that the out-of-state LLC may be subject to the \$800 annual tax, the gross receipts fee & filing an LLC return for California.

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