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Ready or Not, Here Comes Higher Taxes

There is no question in my mind. Ready or not, higher taxes are coming. The 2001 Bush Tax Cuts are scheduled to sunset by the end of this year. In addition, people in the higher tax brackets will be subject to higher taxes in 2013. Since it is unlikely that we will see major tax changes by the end of the year, let's review what to expect under current law.

Higher Marginal Tax Rates

Marginal federal income tax brackets will increase to a maximum of 39.5%. We will lose the 10% bracket.

2010 Marginal Brackets	2011 Marginal Brackets
10%	15%
15%	15%
25%	28%
28%	31%
33%	36%
35%	39.5%

Additional Medicare Surcharge on Earned Income:

Under the new Health Bill, individuals will be charged an additional 0.9% Medicare tax on income above $250,000 (married) or $200,000 (single) beginning 1/1/2013.

Return of the Marriage Penalty

If you are married, the size of the 15% bracket will become smaller. In addition, the standard deduction for married individuals will be reduced. Once again, married couples will pay more income taxes than 2 single taxpayers living in the same household with comparable income.

Limits on Personal Exemptions

In 2011, married taxpayers with Adjusted Gross Income (AGI) above $256,700 and singles with AGI above $171,000 will once again be subject to a phase-out of their personal exemptions.

Limits on Itemized Deductions

Similarly, the phase-out repeal of the overall limitation on itemized deductions is scheduled to sunset. This means that itemized deductions for taxpayers with AGI above $171,000 will once again be reduced.

Simplifying life.

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<u>Higher Long-term Capital Gains Rates</u>

The maximum long-term capital gains rate will return to 20%. We will lose the 0% capital gains rates for individuals in the 10 – 15% marginal brackets.

Marginal Bracket	2010 Capital Gain Rates	2011 Capital Gain Rates
10-15% brackets	0%	15%
Higher brackets	15%	20%

<u>Higher Qualifying Dividend Rates</u>

Currently, the maximum tax rate on qualifying dividends is tied to the maximum long-term capital gains rate. In 2011, dividends will be taxed as ordinary income, which means that qualified dividends could be taxed up to 39.5%.

<u>Unearned Income with be subject to Medicare Tax</u>

Married individuals with incomes greater than $250,000 and singles with incomes greater than $200,000 will be charged an additional 3.8% Medicare tax on unearned income beginning January 1, 2013.

<u>Tax Strategies:</u>

So what can you do?

- Consider a Roth IRA conversion in 2010.
- Build a diversified, tax-free municipal bond portfolio if you are in the higher tax brackets.
- Give an appreciated asset to a family member who will qualify for the 0% capital gains rate in 2010.
- If you receive income from installment sales, it might make sense to offer the buyer a discount to accelerate payments into this year.
- Use 529 plans to save for education.
- Shift income to 2010.
- Maximize retirement deductions.
- Recognize capital gains in 2010.