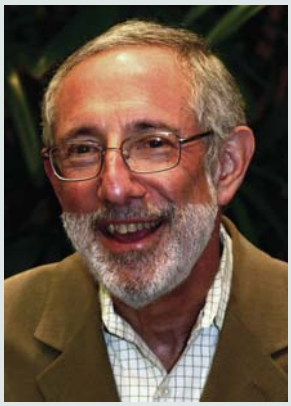

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Social Security: You pay social security tax when working. Generally, you qualify for retirement benefits after working for 10 years. Full benefits are earned by age 66 for those born between 1973 and 1954. The full retirement age increases gradually to age 67 for those born in 1960 or later. Reduced Social Security benefits can be claimed as early as age 62. The benefits will be reduced by about 25% if claimed at age 62.
The benefits will be the same over your life time if you live to the average age used by Social Security. If you live longer you will have collected more if you waited until full retirement age. There are other factors that should be considered in determining when to claim benefits. Make the decision based on your own circumstances.
Enjoy Thanksgiving.
Thank you for your referrals.
Joe

November 2011

Current Financial Topics

Food for Thought

Qualified Charitable Distributions Qualify for RMDs

If you're an IRA owner who must take a required minimum distribution (RMD) in 2011, you can avoid some or all of the resulting income tax liability by donating a portion of it to charity. A qualified charitable distribution (QCD), also known as an IRA charitable rollover, can not only save you income taxes, it can help minimize your taxable estate and fulfill your philanthropic desires. Through December 31, you can make tax-free transfers of up to $100,000 directly from your IRA to qualified charities. Here are the details.

Background

The QCD provision was enacted in 2006, and was scheduled to end in 2009, but last-minute legislation extended it into 2010 and 2011.

Prior to 2006, if a donor withdrew funds from a traditional IRA in order to contribute to charity, the withdrawal had to be reported as ordinary income and was taxed at regular income tax rates. Once the contribution was made, the donor was generally entitled to an income tax deduction for the value of the charitable contribution, calculated and reported on Schedule A of Form 1040 (subject to certain limitations), which could potentially offset some or all of the taxable income generated by the withdrawal.

With a QCD, you can exclude from taxable income any IRA funds directly transferred to a charity as an outright contribution.

Note: *There is currently legislation being considered in Congress that would make this provision permanent. It would also get rid of the $100,000 cap, reduce the minimum age at which taxpayers are able to take advantage of certain giving vehicles (e.g., charitable remainder trusts) from 70½ to 59½, and make it easier for donors to give through supporting organizations, private foundations, and donor-advised funds.*

Who might consider this strategy?

You would benefit most from implementing this strategy if you:

- Do not need all of the income from your RMDs
- Make charitable gifts, but don't itemize deductions (generally, only taxpayers who itemize get federal income tax-saving benefits from charitable donations)
- Make large charitable gifts, but are unable to deduct all of them in a given year because of adjusted gross income limitations
- Want to avoid being taxed on your RMDs

Certain limitations apply

Certain limitations apply to these nontaxable charitable distributions from an IRA:

- You must be at least 70½ years of age when the gift is transferred
- Total gifts cannot exceed $100,000 per year, per IRA owner or beneficiary (married taxpayers with separate IRAs can give up to $200,000 total per year, but no more than $100,000 may be distributed from each spouse's IRA)
- Gifts must be made directly from your IRA to a public charity (i.e., they cannot be made to a private foundation, a supporting organization, or a donor-advised fund)
- The gifts must be outright (i.e., they cannot be used to establish a charitable gift annuity or fund a charitable remainder trust)

Note: *Transfers must come from the IRAs directly to the charity. If you have retirement assets in a 401(k) or 403(b), for example, you must first roll those assets into an IRA, and then make the transfer from the IRA directly to the charity.*

Note: *You cannot do a QCD from a SEP-IRA or SIMPLE IRA.*

What are the income tax implications?

- Federal--You do not recognize the transfer as income, as long as it goes directly from the IRA to the charity. However, you are not eligible for an income tax charitable deduction.
- State--State laws vary, so check with your financial professional.

Gift Tax Strategies

Now may be a great time to make gifts that take advantage of the current large gift tax applicable exclusion amount, low gift tax rates, depressed property values, and low interest rates.

The current large gift tax applicable exclusion amount, low gift tax rates, depressed property values, and low interest rates create a favorable environment for making certain gifts.

Federal gift tax basics

Annual exclusion. Each year, you can give a certain amount ($13,000 in 2011 and 2012) to as many individuals as you like gift tax free.

Qualified transfers exclusion. You can give an unlimited amount on behalf of any individuals for tuition or medical expenses gift tax free. You must pay the amount directly to the educational or medical care provider.

Applicable exclusion amount. Gifts can also be sheltered by the applicable exclusion amount, which can protect gifts of up to $5,120,000 (in 2012; $5,000,000 in 2011). The dollar limit applies to all taxable gifts you make during life and to your estate at your death for federal estate tax purposes.

Basic planning

The first gifts you consider should generally be annual exclusion and qualified transfer gifts. You can make annual exclusion gifts to anyone for any purpose. The annual exclusion is lost in any year in which you do not use it. You can make unlimited gifts using the exclusion for qualified transfers, but gifts are limited to educational and medical purposes.

You and your spouse can split gifts that either of you make. Doing so allows you and your spouse to effectively use each other's annual exclusions and applicable exclusion amounts. For example, if you have 2 children, you and your spouse could make annual exclusion gifts totaling $52,000 to your children (2 spouses x 2 children x $13,000). If you make gifts of $52,000 for 10 years, you will have transferred $520,000 to your children gift tax free.

Next, consider gifts that are sheltered by the applicable exclusion amount. But remember that use of the applicable exclusion amount during life reduces the amount available for estate tax purposes at your death.

If you are likely to have a very large taxable estate at your death that could not be sheltered by the applicable exclusion amount, it might even make sense to make gifts that cause you to pay gift tax. For example, let's assume any additional transfer you make would be subject to the current top gift or estate tax rate of 35% and you make a taxable gift of $1 million to your child on which you pay $350,000 of gift tax. If instead you retained the $1,350,000 until death, $472,500 of estate tax would be due ($1,350,000 x 35%) and only $877,500 of the $1,350,000 would remain for your child. By making the taxable gift and paying gift taxes that reduced your taxable estate, you reduced taxes by $122,500 while increasing the amount transferred to your child by the same $122,500.

Gift considerations

If you have property whose value is depressed, now may be a good time to make a gift of it. The gift tax value of a gift is its fair market value, and a lower value means a smaller gift for gift tax purposes. However, you generally should not make gifts of property that would produce an income tax loss if sold (basis in excess of sales price). The person receiving the property would have a carryover basis and would not be able to claim the loss. In these cases, instead consider selling the property, claiming the loss, and making a gift of the sales proceeds.

Future appreciation on gifted property is removed from your gross estate for federal estate tax purposes. However, while property included in your estate generally receives a basis stepped up (or stepped down) to fair market value when you die, lifetime gifts do not. Therefore, you may wish to balance the gift tax advantage of a gift with carryover basis and income tax on gain if the property is sold against the income tax advantage of a stepped-up basis and estate tax (if any) if you retain the property until your death.

In the current low interest rate environment, you may wish to consider a grantor retained annuity trust (GRAT). In a GRAT, you transfer property to a trust, but retain a right to annuity payments for a term of years. After the trust term ends, the remaining trust property passes to your beneficiaries, such as family members. The value of the gift of a remainder interest is discounted for gift tax purposes to reflect that it will be received in the future. Also, if you survive the trust term, the trust property is not included in your gross estate for estate tax purposes. Any appreciation in the trust property that is greater than the IRS interest rate used to value the gift escapes gift and estate taxation. The lower the IRS interest rate, the more effective this technique generally is.

In the current low interest rate environment, you may also wish to consider a low-interest loan to family members. You are generally required to provide for adequate interest on the loan, or interest will be deemed for gift tax purposes. However, with the current low interest rates, you can provide loans at a very low rate and family members can effectively keep any earnings in excess of the interest they are required to pay you.

The Problem with Do-It-Yourself Estate Planning

The one-size-fits-all fill-in-the-blank forms that do-it-yourself estate planning sources provide may be attractive to some individuals because they cost a fraction of what attorneys typically charge. But is saving a few dollars worth the risk and potentially high cost of doing things incorrectly?

As the number of Internet websites and software packages have quickly multiplied, along with the many books and stationery store kits that have always been available, do-it-yourself (DIY) estate planning is on the rise. The one-size-fits-all fill-in-the-blank forms that these sources provide may be attractive to some individuals because they cost a fraction of what attorneys typically charge. But is saving a few dollars worth the risk and potentially high cost of doing things incorrectly?

Cheap, easy, and better than nothing?

Proponents of DIY estate planning typically have two arguments:

1. It's cheap and easy: A will, for instance, can be completed online in about 15 minutes for about $69. In comparison, working with an experienced attorney to create common estate planning documents (wills, trusts, health-care directives, and powers of attorney) may cost you anywhere from $800 to $3,000 or more, depending on the complexity of your estate.
2. It's better than nothing: The consequences of dying without estate planning documents are that the state will make important decisions for you, such as how your property will be distributed, who will care for your minor children, and what medical care you'll receive if you are unable to make your wishes known.

These points are valid; for those who cannot afford to pay an attorney, DIY may be the only economical alternative available. For others, a poorly drafted will is better than no will at all, especially where the naming of a guardian for minor children is involved. But the chances that DIY estate planning will effectively accomplish exactly what you intend is slim. Here's why.

It's too easy to make mistakes

DIY sources typically only handle simple estates, and can't deal with even the most common complexities such as children from a prior marriage, children with special needs, property that has appreciated in value resulting in capital gains, or estates that are large enough to be subject to estate taxes. And, DIY sources generally fail altogether to take advantage of sophisticated estate planning strategies because they typically can't account for an individual's unique circumstances.

Further, you may make an error by failing to understand the instructions or by following the instructions incorrectly.

The result is that the documents you create could be invalid, ineffective, or contain legal language having consequences you never intended. You might not know if that is the case during your lifetime, but at your death your loved ones will find out and may suffer the lasting consequences of your mistakes.

You're not getting legal advice

DIY sources provide forms but not legal advice. In fact, these sources clearly state that they are not a substitute for an attorney, and that they are prohibited from providing any kind of legal advice.

Estate planning involves a lot more than producing documents. It's impossible to know, without a legal education and years of experience, what the right legal solution is to your particular situation and what planning opportunities are available. The actual documents produced are simply tools to put into effect a plan that should be specifically tailored to your circumstances and goals.

Estate planning laws change

Laws are not static. They constantly change because of new case law and legislation, especially when it comes to estate taxes. Attorneys keep up with these changes. DIY websites, makers of software, and other sources may not do as good a job at keeping current and up-to-date.

Fixing mistakes can be costly

As previously stated, estate planning documents can be obtained from a lawyer for $800 to $3,000 or more, depending on the complexity of your estate. But these costs are minor in comparison to the costs that your loved ones may incur if there are serious errors in your DIY estate planning. Many more thousands of dollars may have to be spent by your loved ones to undo what was done wrong.

The bottom line

There are obvious savings in legal fees by using form wills and trusts, but there are also risks involved. One of them is that problems such as defective forms, violations of state law, or improper witnessing will not be apparent to you when the documents are signed. It may be only after death occurs many years later when the problems are discovered, and at that point it may be very costly, or even worse, too late to revise the documents.

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Will my broker calculate my cost basis for DRP stocks?

If you think you don't need to track cost basis on your own because brokers must now report to both you and the IRS the cost basis for any stock sold, there are some potential pitfalls to be aware of.

First, new cost basis reporting requirements are being phased in. New regulations requiring brokers to report cost basis generally apply only to stocks bought after January 1, 2011. (Mutual funds will become subject to the same provisions in 2012; bonds and options will follow in 2013.) However, for a stock bought as part of a dividend reinvestment plan, or DRP, the new provisions will apply only to purchases made on or after January 1, 2012. As a result, for most DRP stock purchased before that date, in most cases you or your tax preparer will still be responsible for calculating accurate cost basis information.*

Because DRPs typically involve many purchases over a long time, calculating the cost basis for a DRP stock could be challenging. Fortunately, there's also a provision that makes the calculation easier. For stocks held in DRPs, the cost basis of all purchases in the plan can be averaged to determine the cost basis for individual shares sold.

The ability to average sales from a DRP applies only to plans whose documents specify that at least 10% of every dividend paid must be reinvested in identical stock. To be considered identical, the stock must have the same CUSIP number, which would not apply to purchases of the same stock made outside the DRP.

Even after adjusted cost basis reporting is available for DRP stocks, you can still specify which shares are considered the ones sold for tax purposes. However, you must do so before the trade settles--typically, three days after the transaction.

You can include any transaction costs paid as part of your adjusted cost basis. And even though your adjusted cost basis may be calculated by someone else, it may still be a good idea to keep documentation of any purchases or sales to make sure it matches the information being supplied to the IRS.

***Note:** The reporting regulations already apply for DRPs that do not require reinvestment of at least 10% of every dividend paid.*

Are there exceptions to new cost basis reporting rules?

New provisions that went into effect in 2011, requiring brokers to track and report adjusted cost basis for stocks, have special provisions that apply in certain situations.

Wash sales: A wash sale occurs when a substantially identical security is purchased within 30 days before or after the security it replaces is sold; when that happens, any losses resulting from the sale are not immediately deductible for tax purposes. The new regulations still require taxpayers to comply with the IRS regulations governing wash sales. However, brokers are required to adjust the cost basis of a wash sale only if the newly acquired securities are identical to the securities sold (meaning the securities involved share the same CUSIP identification number).

Brokers also are not required to report adjusted cost basis for wash sales when the purchase and sale transactions occur in different accounts. However, taxpayers are still responsible for accurately reporting the proceeds of any wash sale transactions, regardless of whether the purchase and sale are made in the same account.

Short sales: In the past, the IRS required brokers to report a short sale for the year in which the short position was opened; however, the proceeds of a short sale generally were taxed in the year in which it was closed. The new regulations correct that discrepancy. In addition to requiring brokers to track cost basis, the new regulations mandate that the cost basis of a short sale will now be reported in the year in which the short is closed. For example, if you initiated a short position in July 2011 that was closed two months later, the cost basis should appear on the 1099-B form for 2011 that brokers must submit to the IRS in early 2012. However, if the position has not been closed before January 1, 2012, the cost basis will be reported to the IRS only after the position is closed. If you close the position after January 1, 2012, it would appear on the 1099-B due in early 2013.

Even though brokers must now supply additional information about the net proceeds of a stock sale, it's worth remembering that the individual taxpayer is still responsible for accurately reporting information to the IRS.