

INCOME TAX IMPLICATIONS FROM THE 2010 TAX RELIEF ACT

Individual income tax rates // Capital gains/qualified dividends // Itemized deduction and personal exemption limitations
Alternative Minimum Tax (AMT) // Individual charitable contribution incentives

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 was signed into law on December 17, 2010. The Act generally only extends its tax breaks for two years – 2011 and 2012. Thus, there are two perspectives by which to view this act's provisions. The first is as a window into the immediate future of both estate tax and income tax rates. This view reflects the inertia that will settle in, requiring significant force and momentum to unwind what taxpayers have built into their financial and tax plans. The second view is that this truly is a brief respite ending late-2012 when the country will find itself in the same planning predicament we endured during 2009 and 2010

Regardless, knowledge is the key to surviving the ride and effectively updating estate and tax plans. This paper offers a review of the income tax changes enacted by the 2010 Tax Relief Act as well as insightful guidance and planning tips for investors to consider. What we may all find over the next two years is that planning may become more focused on what is really important: people, family security, nontax issues, asset preservation, management of investments, giving back and so on. And despite the fact that taxpayers and experts may all be put in the same frustrating position again of having to guess at where the law is going, effective planning can help better position investors going forward.

INDIVIDUAL INCOME TAX RATES

Expiring Law	2010 Tax Relief Act
With the scheduled expiration of the Bush tax cuts at the end of 2010, the lowest individual income tax bracket of 10% would have disappeared leaving the lowest tax rate at 15%. The remaining tax brackets would have reverted to the pre-Bush tax cut levels of 28%, 31%, 36% and 39.6%.	Individual income tax rates will remain at the current 2010 levels for 2011 and 2012. The lowest tax bracket will be 10% with 15%, 25%, 28%, 33% and 35% brackets in place for those with higher taxable incomes.

Key Takeaways: With rates holding steady there may be little incentive to accelerate income into 2011 or defer deductions into 2012.

Obviously each taxpayer's circumstances are different and warrant a close look to determine if a particular strategy will save money for a taxpayer in the long run.

CAPITAL GAINS/QUALIFIED DIVIDENDS

Expiring Law	2010 Tax Relief Act
Long-term capital gains and qualified dividends are taxed at a maximum rate of 15%. Taxpayers in the 10% and 15% tax brackets have a 0% tax rate on this income. With the expiration of the Bush tax cuts, long-term capital gains would have reverted to a maximum rate of 20% (18% for assets held more than five years) and the concept of qualified dividends would disappear. Further, dividends would be treated as ordinary income subject to the taxpayer's normal tax rate, which could be as high as 39.6%.	The 15% maximum tax rate for long-term capital gains and qualified dividends (as well as the 0% tax rate for taxpayers in the lowest two tax brackets) will continue through the end of 2012.

Key Takeaways: The popular investing discipline of using qualified dividends and long-term capital gains to produce tax-advantaged cash flow should continue to be an attractive option for the next two years. Remember that simply holding an asset for a year and a day will convert short-term capital gain on sale – taxed as ordinary income – to long-term capital gain.

ITEMIZED DEDUCTION AND PERSONAL EXEMPTION LIMITATIONS

Expiring Law	2010 Tax Relief Act
<p>The itemized deduction limitation reduced the amount of allowable deductions for taxpayers who reported gross income over \$169,550 in 2011 (projected amount as increased for inflation). Essentially, taxpayers lose the benefit of up to 3% of their adjusted gross income over this amount subject to an overall cap of 80% of certain itemized deductions. This impact of this limitation had been reduced over the last few years and was completely repealed for 2010.</p> <p>The personal exemption phase-out was also calculated using a taxpayer's income over a threshold amount of gross income. Unlike the itemized deduction limitation, it was possible for higher income taxpayers to completely lose the benefit of their personal exemptions. This provision was also scaled back over the course of the last few years and was repealed for 2010.</p> <p>In 2010, every taxpayer, regardless of their income, received full benefit of their itemized deductions and personal exemptions.</p>	<p>The repeal of the itemized deduction and personal exemption limitations will be extended through 2012. For those taxpayers with higher income and large deductions, the itemized deduction and personal exemption limitations created a stealth surtax on their normal tax rate, effectively raising their marginal tax rate by a percentage point or more.</p>

Key Takeaways: Because these limitations are tied to income, most of the benefits of this provision will be received by the class of taxpayers that have income in excess of the \$250,000 threshold. While bundling deductions (such as charitable donations) into any one tax year may still make sense, the sense of urgency seems to have passed.

ALTERNATIVE MINIMUM TAX (AMT)

Expiring Law	2010 Tax Relief Act
<p>Under the scheduled law, the 2011 AMT exemption would have dropped to \$33,750 for single filers and \$45,000 for joint filers. This would have captured a significant number of middle-income taxpayers.</p>	<p>For 2011, the AMT exemption amount has been increased to \$48,450 for single filers and \$74,450 for married filing jointly. This represents approximately a 44% increase for single filers, and a 65% increase for married filing jointly, over the previously scheduled 2011 exemption amount.</p>

Key Takeaways: This is one of the provisions that so many taxpayers were waiting for. The increasing reach of the AMT has raised the effective tax rate for a number of middle-income taxpayers. Most taxpayers are subject to the AMT for one or more of a few different reasons, such as high capital gain and dividend income relative to their ordinary income, high deductions for medical expenses, taxes and investment management fees, or having larger families. Others are subject to AMT as a result of stock option exercise or investments in private activity municipal bonds. But many are impacted by the AMT solely because the AMT exemption is not automatically indexed for inflation. Despite the temporary patch, this stealth tax system should still be monitored by upper-income taxpayers.

INDIVIDUAL CHARITABLE CONTRIBUTION INCENTIVES

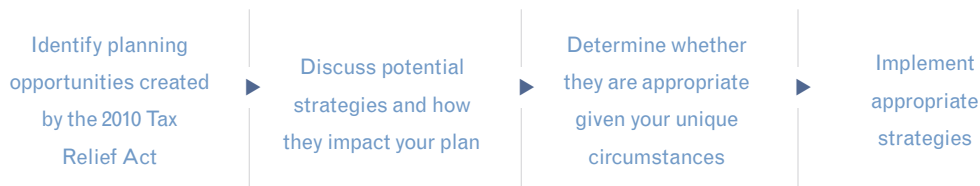
Expiring Law	2010 Tax Relief Act
<p>IRA account owners who had attained the age of 70 ½ were allowed to direct their IRA custodian or trustee to pay a distribution of up to \$100,000 directly to their favorite qualified charity. If the amount of the qualified charitable distribution (QCD) met or exceeded the investor's required minimum distribution (RMD) for the tax year, he will be considered to have met his RMD requirement, but not be subject to income tax (and the contribution would not be deductible).</p>	<p>This provision was extended through the end of 2011.</p>

Key Takeaways: This is a useful provision for individuals who have large IRAs and charitable intentions. Making a qualified charitable distribution from an IRA will lower the IRA asset value thereby decreasing the amount of future RMDs.

WORK WITH YOUR FINANCIAL ADVISOR

Tax planning is an important and complicated part of a comprehensive financial plan. Lower tax bills may be important, but they are not the only important consideration. To maximize overall portfolio performance and tax results, review short- and long-term objectives, portfolio asset allocation, and investment diversification before taking action.

You should work closely with your financial advisor as well as other relevant tax professionals to:



Any information is not a complete summary or statement of all available data necessary for making an investment decision and does not constitute a recommendation. Investors are urged to consult with their own tax advisors with regard to their specific situation prior to making any investment decisions with tax consequences.

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880 CARILLON PARKWAY // ST. PETERSBURG, FL 33716 // 800.248.8863

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