



# Special Tax Issue

*There is temporary stability in the tax law* – stability that is not likely to last through 2013. It's relatively clear that 2013 will bring some major changes. That's when the current tax rules are scheduled to expire, more of the health care reform law is scheduled for implementation, and automatic spending cuts will go into effect if Congress has not yet passed legislation to cut the deficit. Tax increases are likely to be included in the big changes that lie ahead. This *Donnelly-Boland Special Tax Issue* should remind you of the value of consulting with us as soon as possible to discuss how to minimize your 2011 taxes, and, more importantly, how to plan what you can do to minimize your tax position in light of coming tax changes. Please call if you have questions or if you would like to get together to discuss your tax planning options. And please share this issue with friends or associates who might be interested in this information. Here's a look at what's covered in this issue of *Client Connection*:

## Still Time To Save, Still Time To Plan

Overall, there's less uncertainty about the short-term outlook for tax law than we had at the end of last year. With this temporary clarity comes the opportunity to create a sound tax-saving plan – and the time to put your plan into action. Here are several strategies to consider.

■ **Reap tax benefits with retirement savings.** Rule #1 in retirement saving is to contribute the maximum amount allowed every year. (Cont'd. page 2)

*"The temporary stability in the law is just that -- TEMPORARY. This is the perfect year to meet with us to know where you stand so you can adjust to your advantage when the law changes."*  
—Jamie Scherich, CPA, Branch Manager, Glassport

## Learn What You Did in 2011 That We Should Know About

Whether you are an employed individual tax client, a business owner or a retiree, you should be aware of certain events and transactions that could favorably affect how much tax you owe. Take a minute to review this section to make sure our professionals have all the information we need to help you. (Cont'd. page 3)

## Learn the Secret of Tax Rate Planning

The secret of effective tax planning efforts lies in understanding tax rates. Do you know your marginal tax rate? More importantly, do you know your real tax rate (also called your effective tax rate)? They are not the same, and knowing the difference can be critical to how much money you pay in taxes. (Cont'd. page 4)

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Donnelly-Boland Tax Services operates in the Tri-State Area from offices in Baldwin, Brentwood, Glassport, and Waynesburg. The firm provides strategic tax planning, with registered representatives who provide investment and retirement planning services, for individuals and any organization offering retirement benefits.

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For 2011, the IRA contribution limit is \$5,000, and those 50 and older can contribute \$6,000. Participants in a 401(k) plan can contribute as much as \$16,500 (\$22,000 if 50 or older).

Did you know you can make IRA contributions for your spouse when you're working and your spouse is not? For 2011, the maximum spousal IRA contribution is the lesser of \$5,000 or your combined earned income. You can add an additional \$1,000 when your spouse is over age 50.

If you're self-employed, establishing a retirement plan such as a SEP or a SIMPLE means a current-year tax deduction in addition to tax-deferred growth. For 2011, you can contribute 25% of your salary to a SEP plan, up to a maximum contribution of \$49,000. The maximum SIMPLE contribution is \$11,500, plus an additional \$2,500 as a catch-up contribution if you're over age 50. A federal tax credit may also be available – up to \$500 for each of the first three years of your new plan. Remember, credits reduce your tax bill dollar for dollar.

■ **Roth conversions affect taxes.** Roth conversions were included in tax planning last year, in part due to the one-time opportunity to defer paying federal income tax on the conversion. If you made the election, remember you'll report half the income on this year's return. Current or prior-year net operating losses, unused tax credits, and deductions that lower

Are you already taking required withdrawals from your retirement accounts? Then you know required minimum distributions from traditional IRAs increase your adjusted gross income (AGI). In turn, your AGI affects how much of your social security benefits are taxable. One option for reducing the impact is to take only the minimum from your traditional IRA. Use nontaxable Roth distributions or capital gain / loss harvesting in taxable accounts to supplement your income.

■ **Review support provided for relatives.** While planning to maximize deductions, remember to take into account the financial support you provide for relatives. Potential tax breaks include dependency exemptions, head-of-household filing status, medical deductions, and the dependent care tax credit. Generally, you'll need to provide over half of the living expenses for your relative. What if you don't provide more than 50% of support for your relative? You could enter into an arrangement with other family members

(Cont'd on page 4)



your adjusted gross income can help reduce the resulting tax bill.

Haven't converted to a Roth yet? You still have time to decide if a full or partial Roth conversion makes sense for you this year. A potential tax-reducing suggestion: Transfer investments from your traditional IRA to a Roth during a market dip. You'll capture after-conversion growth without owing additional tax.

*NOTE: This newsletter is issued to provide you with information about minimizing your taxes. Do not apply this general information to your specific situation without additional details. Be aware that the tax laws contain varying effective dates and numerous limitations and exceptions that cannot be summarized easily. For details and guidance in applying the tax rules to your individual circumstances, please contact us.*

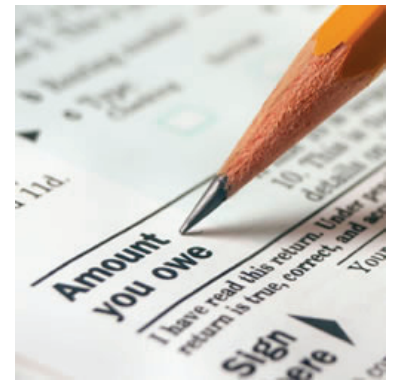
# WHAT WE SHOULD KNOW TO LOWER WHAT YOU OWE? (Cont'd from page 1)

## *Let's begin with advice that applies to virtually all of our clients:*

Bring all your documentation when you come to your appointment . . . not just tax documents like W2s and 1099s, but also receipts, *particularly for any charitable deduction you plan to take*. You risk losing your deductions if you don't have proper documentation for all your 2011 charitable contributions. Even gifts under \$250 require a bank record or a receipt from the charity.

**Did you install certain energy-efficient property in your home?** This could be your last chance to claim the last of the residential energy credit (a federal tax credit of up to \$500) if you installed enhancements such as insulation, doors, and windows. That's the aggregate total credit, including amounts you claimed in prior years. The credit expired December 2011.

**Bring investment statements because any losses in your investment or retirement portfolio matter.** Maximizing losses by increasing your participation in passive activities, taking steps to write off worthless securities and bad debts, and harvesting capital losses from poorly performing securities are activities that should be brought to our attention when you drop off your return.



## BUSINESS OWNERS, JUST A FEW QUESTIONS

### ■ **Did you gather tax identification numbers your business will need in order to issue year-end reporting statements?**

Though two reporting requirements were repealed (the one for rental property owners and the one for payments to corporations), the old rules live on. In addition, penalties for failure to file have increased.

■ **Did you assess equipment needs for your business and make tax-saving purchases?** For business owners, 2011 offered what may be a last-chance opportunity for an enhanced deduction: 100% bonus depreciation, which was scheduled to expire December 31, 2011. The increased Section 179 expensing of up to \$500,000 was also slated to shrink after the end of the year. If you bought new assets in 2011, we may be able to

synchronize these two tax benefits with an asset purchase plan to make the most of 2011 deductions. For instance, the Section 179 deduction could be applied to used property, then the bonus depreciation could be used only for new assets you bought and placed in service in 2011. One caution: Some states do not follow federal bonus depreciation rules, so savings would be to Federal taxes alone.

■ **Did you start a retirement plan for the benefit of your employees?** If not, it's not too late to set up a newly available SIMPLE cafeteria plan for your business. The plus: pre-tax employee benefits without the need for discrimination testing.

■ **Did you employ a child this year?** If your child is interested in what goes on in the family business, there

are unintended benefits to giving them the opportunity to work with you. If you hire your child under the age of 18 to do legitimate work in your business, you get a business tax deduction, and your child can earn up to \$5,800 without paying income tax. Bonus: When your business is a sole

proprietorship, you don't have to pay FICA taxes. Double bonus: The kiddie tax does not apply to wages.

■ **Did you start a retirement account for a child who works in the family business?** Boost the tax savings you

get from paying your child to work in your business by gifting the child money for a deductible, traditional IRA contribution. The maximum basic contribution for 2011 is \$5,000, a benefit for you and your business in the short-term, and a long-term benefit for your child.

## Don't Stop Thinking About Tomorrow . . .



Regardless of what time of year – or what time of life –  
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# The Secret to Tax Rate Planning Revealed

The U.S. individual income tax system is based on six tiers of rates: 10%, 15%, 25%, 28%, 33%, and 35%. A common misconception is that a taxpayer falls into just one of these

brackets, but actually if someone's income is high enough, their tax bill could be affected by all six. This is because the tax system is graduated,

meaning the first taxable dollars are taxed at the lowest rates first, then up the scale until the marginal rate is reached. Your marginal rate is the rate you will pay on your next dollar of taxable income. Your real tax rate (also called your effective tax rate) is the actual percent of tax you pay on your taxable income.

For example, the 10% rate is assessed on taxable income from \$1 to \$8,500 (if filing as single in 2011). The 15% bracket covers income from \$8,501 to \$34,500. If your taxable income is \$30,000, your marginal (i.e., top tier) tax rate is 15%, but your real tax rate will be less because the first \$8,500 of income is taxed at 10%.

## Other Factors Affect Your Rate

There are other factors that can affect real tax rate. Personal

exemptions and itemized or standard deductions can lower taxable income and thereby lower one's overall rate.

Conversely, unearned income, such as interest and dividends, might raise a taxpayer to a higher bracket. And some types of income are taxed differently from earned income.

Long-term capital gains are taxed at 15% unless your ordinary income tax bracket is 10% or 15%, in which case long-term capital gains are not taxed at all.

### Here's the Point

Knowing where your income is in relation to the six brackets can make a big difference in keeping your real tax rate as low as possible.

Say, for example, your taxable income is \$83,600, which is the top of the single 25% tax bracket. The next dollar you earn above that figure (up to \$174,400) will be taxed at your marginal rate of 28%. So if the timing of a future receipt of income is within your control, such as from a pending business contract, consider deferring the income to next year. Another strategy might be to reduce taxable interest income by keeping money in a tax-exempt investment instead of a taxable one.

Or consider moving savings into Series EE savings bonds, where tax on the interest is deferred. You might also invest in longer-term CDs which can pay interest next tax year. Or defer taking short-term capital gains until next year.

On the other hand if your income is just above a certain tax bracket, your strategy might be to look for deductions that will bring your income back down into the lower bracket. Options include such steps as contributing the maximum allowed to your 401(k) plan,

your SEP, or your SIMPLE retirement plan. Another possibility is making a deductible IRA contribution for you and your spouse.

With the economy causing many household incomes to vary significantly from year to year, "watching your marginal tax bracket is more important than ever – and so is your retirement security." Let us know if you would like more information or a complete analysis of where you stand.



## Still Time To Plan *(Cont'd from page 2)*

who provide help, or you could shift assets you would dispose of anyway to pay for the support. You would then be shifting the related income and tax to your relative.

Here's an illustration of asset and income shifting. Instead of selling stock at a gain and using the proceeds to pay for a parent's living expenses, gift the stock to your parent and let him or her make the sale. Long-term gains could qualify for a zero-percent tax rate if your parent is in the lower tax brackets.

### ■ Gather your tax documents and prepare to file early.

Here are just a few of the reasons filing early is beneficial to you:

- You can use any refund to pay down holiday spending and other debt, or use the refund to make a last-minute IRA contribution.
- You have more time to execute tax-minimizing transactions that affect your short-and long-term tax consequences.
- You can adjust your spending to reflect your new tax plan, financial goals, and to budget for what you hope to achieve in light of your tax position.