

TAX NEWS

Fall 2012

TAX CLIENT NEWSLETTER

INTRODUCTION

Everyone in Washington is complaining about the uncertainty of the reduced tax rates which expire at the end of the year but no one seems to be able to do anything about it. With a deadlocked Congress focused only on the election, we will have to wait until after November 6th to find out if Congress will head off automatic tax increases and spending cuts before the end of the year. The tax platforms of the two candidates in this issue offer you a preview of what may come. The IRS updates in this issue offer guidance on reporting of tips, the limitation on meal and entertainment deductions, the tanning excise tax, and business use of an aircraft. A brief review of recent court opinions includes an important ruling that severance pay is not subject to social security taxes. This ruling only applies to certain taxpayers, so read my analysis in the Court Opinion section. Other court cases address inherited IRAs, the mortgage interest deduction limit, and income from cancellation of credit card debt. I also offer you some pointers on deciding whether to do a Roth IRA rollover, and, finally, I explain the higher Medicare tax for upper-income taxpayers which is set to go into effect in January 2013. I hope you find this information useful as the tax year winds down.

CONGRESSIONAL UPDATE

SENATE COMMITTEE CLEARS TAX EXTENSIONS BUT FINAL ACTION WILL HAVE TO WAIT UNTIL AFTER ELECTIONS

The Senate Finance Committee has approved a bill to extend the many tax breaks that expired at the end of 2011. The measure, the Family and Business Tax Cut Certainty Act of 2012, is the first major action this year addressing only the most pressing expiring tax provisions. The bill does not include an extension of the Bush tax cuts which expire at the end of this year. (See discussion below.) The bill also includes a statement supporting "comprehensive tax reform." Included in the \$200 billion package are the research and development credit, the tuition deduction, the state and local sales tax deduction, the mortgage debt forgiveness exclusion, the deduction for mortgage insurance, and alternative minimum tax relief. The bill also includes higher expensing limitations for investments in depreciable property.

The legislation gathered Republican support by limiting the extenders included in the measure. Instead of potentially extending 73 tax provisions, the Finance Committee only addressed 54, representing about a 25 percent reduction. Senator Orrin Hatch (R-Utah), ranking member of the Senate Finance Committee, praised the Committee action as "a step towards the ultimate goal of comprehensive tax reform." Six out of 11 Republicans

on the Finance Committee voted in favor of the legislation, setting the stage for a bipartisan effort to enact the bill.

Lame Duck Session and the Bush Tax Cuts

Key tax writers in the House of Representatives are working on their own legislation to extend expired tax provisions. However, a House tax subcommittee Chairman, Patrick J. Tiberi, R-Ohio, has indicated that his Committee will not move it to a vote until after the November elections. After the elections, Congress will come back in a so-called "lame-duck" session to address unfinished business. Many observers believe that Congress will take up not only the expired 2011 tax breaks listed above, but it also may consider an extension of the Bush tax cuts which are set to expire December 31, 2012, in an event that has been dubbed "Taxmageddon." Even if Congress acts quickly during the lame-duck session to extend the Bush tax cuts for a short time, the IRS has warned that the uncertainty from last-minute Congressional action is likely to make for a very difficult filing season.

IRS WARNS OF DELAYED FILING SEASON FROM TAX UNCERTAINTY

With the upcoming election and the uncertainty regarding what the lame-duck Congress will do with expired and expiring provisions, the IRS has begun warning of another difficult filing season with filing and refund delays. It takes the IRS at least six to eight weeks to make changes to its forms, tables, and other documents when tax changes occur. The timing of so many provisions expiring or expired at once means that Congress may be approving extensions at the very last minute and some extensions will be retroactive to the beginning of 2012. According to the IRS Oversight Board, this scenario will put billions of dollars in refunds on hold. Last year, the IRS had to delay return processing by a month because of last-minute tax changes. This year could be worse.

My Recommendation

As your tax professional, I will be watching events in Washington closely, and I will take steps to expedite your return processing in any way that I can. I recommend that you start assembling your tax information early this year so we will be ready to move on your tax filings as soon as the IRS is ready to begin processing.

GOVERNMENT STUDY FINDS HEALTHCARE CREDIT NOT BEING USED BY SMALL BUSINESSES

A congressional agency, the Government Accountability Office (GAO), has reported that the healthcare tax credit provided to small business employers was barely used in 2010. One factor limiting the credit's use is that most very small employers, 83 percent by one esti-

mate, do not offer health insurance. The report also concluded that the complexity of the tax credit contributed to its low use. Many comments sent to the GAO stated that it was too much of an administrative burden for a business to supply the IRS with additional worksheets to support the application for the tax credit. The GAO recommended that the IRS improve the instructions for the credit to encourage employers to apply. Although the fate of the credit is uncertain pending the elections and the promised repeal of the health care law by Presidential candidate Romney, I can help you analyze your eligibility and file the necessary information with the IRS to get approval for the credit, if you have an insurance plan for your employees.

6.6 MILLION YOUNG ADULTS NOW ON PARENT'S HEALTH INSURANCE PLAN

A new report by the Commonwealth Fund says that about half of the 13.7 million young adults insured under their parents' health plans in 2011 were made eligible by President Obama's health care law. The group, which supports the President's plan, got its numbers from a health insurance tracking survey of more than 1,800 young adults aged 19 to 25 between late 2010 and late 2011. More than one in ten 19-to-29-year-olds told the Commonwealth Fund they were unemployed.

PRESIDENTIAL CANDIDATES' TAX PLATFORMS

This year's Presidential election comes in the midst of a potential fiscal crisis that could occur just weeks after the November 6, 2012 vote—the expiration of the Bush tax cuts, which have now been in place for almost 12 years. The Congressional Budget Office has warned that if taxes on all Americans are allowed to go up suddenly, when the lower rates expire on December 31, 2012, it could trigger another economic crisis in the United States, when combined with deep spending cuts which also will automatically take place without Congressional action.

The Presidential candidates' tax platforms, outlined below, show the key elements in the debate over which tax plan would successfully move the economy in the right direction. This side-by-side comparison gives you a preview of what tax changes to expect within the coming months, depending on who wins the election. I also hope this information will give you a basis for comparing the different candidates so you can make an informed decision when you vote. For further information, see the links below to the two parties' platforms.

Democratic Party: http://www.democrats.org/about/party_platform

Republican Party: http://www.gop.com/2012-republican-platform_home/

INDIVIDUAL TAX PROVISIONS	DEMOCRAT: OBAMA	REPUBLICAN: ROMNEY
<p>TAX RATES and BUSH TAX CUTS: Currently 6 brackets: 10%, 15%, 25%, 28%, 33% and 35%.</p> <p>Long-Term Capital Gains Rate: Now, 0% for taxpayers in the 15% bracket and 15% for individuals in the 25% bracket and higher. Increases to 20% in 2013.</p> <p>Dividend Rate: Now, 0% for taxpayers in the 15% bracket, 15% for individuals in the 25% bracket and higher. Expires in 2013 when dividends will be taxed in regular brackets up to 39.6%.</p>	<p>End Bush Tax cuts for individuals with income above \$200,000 and married couples with income above \$250,000. Top rate would be 39.6% and lowest rate would be 10%. Households with income over \$1 million would have a minimum tax rate of 30%.</p> <p>Allow the current reduced tax rates on dividends and capital gains to expire as scheduled for upper-income taxpayers..</p> <p>The maximum dividend and capital gains tax rate for upper-income taxpayers (\$200,000/\$250,000) would increase from 15% to 20%. Other taxpayers would keep existing lower rates</p>	<p>Extend Bush tax cuts for all income levels pending tax reform.</p> <p>Enact tax reform to reduce each bracket by 20%. The top bracket would be 28% and the lowest bracket would be 8%.</p> <p>Keep 15% long-term capital gains and dividend rate; Eliminate tax on capital gains, dividends, and interest for taxpayers with yearly income under \$200,000.</p>
<p>ESTATE and GIFT TAXES: Current estate and gift tax exemption is \$5 million per person with a tax rate of 35%. These numbers will revert to a \$1 million exclusion with a 55% tax rate in 2013.</p>	<p>Set permanent estate tax rate at 45% with an exclusion of \$3.5 million per person. Make permanent the ability of a surviving spouse to use any unused estate and gift tax exclusion of the deceased spouse (portability).</p>	<p>Completely repeal the estate tax.</p>
<p>HEALTHCARE TAX INCENTIVES and FUNDING PROVISIONS: Net Investment Tax and Increased Medicare tax set to take effect in 2013</p>	<p>Supports health insurance premium tax credits of up to 35% for individuals and small businesses; penalties on large employers that do not offer insurance to their employees; and increased Medicare tax on high-income individuals (from 2.9% to 3.8%). New Medicare tax on net investment income would be 3.8% for singles with income above \$200,000 and married couples with more than \$250,000 in income. Investment income includes flow-through business income, interest, dividends and capital gains.</p>	<p>Repeal the Affordable Care Act, including the 0.9% additional Medicare tax on wages and the 3.8% tax on net investment income of high-income individuals.</p>
<p>ALTERNATIVE MINIMUM TAX (AMT)</p>	<p>Index the AMT exemption amount to inflation.</p>	<p>Repeal the AMT.</p>
BUSINESS TAX PROVISIONS	DEMOCRAT: OBAMA	REPUBLICAN: ROMNEY
<p>CORPORATE TAX RATE:</p>	<p>Lower the top corporate tax rate to 28% from the current 35%.</p>	<p>Lower the corporate tax rate from 35% to 25%. Eliminate the corporate Alternative Minimum Tax.</p>
<p>INTERNATIONAL TAX PROVISIONS:</p>	<p>Eliminate deductions for outsourcing operations; make companies pay an international minimum tax on overseas profits. Create a tax credit of 20% for U.S. companies moving their overseas operations back to the U.S.</p>	<p>Move the U.S. from a worldwide tax system to a territorial system, where income is taxed only in the country where it is earned; allow a "tax holiday" for U.S. corporations bringing overseas profits back to the U.S.</p>
<p>DEPRECIATION AND CAPITAL RECOVERY:</p> <p>Job-related tax credits:</p>	<p>Extend for 1 year the full expensing of capital costs. Increase expensing deduction limits to \$250,000 for capital investment in business property with an \$800,000 purchase limit.</p> <p>New tax credit in 2012 through 2014 for companies investing in new factories, equipment, or production in depressed areas; 10% tax credit for companies that increase their payrolls, up to \$500,000.</p>	<p>Extend for 1 year the full expensing of capital costs.</p> <p>No specific job tax benefits but favors reduced regulations on businesses.</p>
<p>RESEARCH & DEVELOPMENT TAX CREDIT:</p>	<p>Make the R&D credit permanent and increase the rate of the Alternative Simplified Credit (ASC) from 14% to 17 %.</p>	<p>Make the R&D credit permanent.</p>
<p>ENERGY TAX INCENTIVES:</p>	<p>Supports numerous alternative or "clean energy" tax credits.</p>	<p>No specific tax provisions but backs increased drilling in the U.S. for oil and natural gas.</p>

IRS UPDATE

IRS OFFERS NEW DETAILS ON FICA TAXATION OF TIPS, AUTOMATIC GRATUITIES

The IRS has updated its guidance on FICA taxation of tips to explain in detail both employer and employee responsibilities for reporting and paying the tax. Employees who received \$20 or more in cash tips in a single calendar month must furnish written documentation of the tips to employer. If this is not done, then the employee is liable for the employee portion of the FICA taxes and is subject to penalties. In this situation, the employer is only liable for the employer portion of FICA taxes after IRS issues a "notice and demand." The employer is not liable to withhold and pay the employee share of FICA taxes on the unreported tips. Cash tips include tips received from customers, charged tips (e.g., credit and debit card charges) distributed to the employee by the employer, and tips received from other employees under any tip-sharing arrangement. On the other hand, automatic gratuities are not tips and are not used in computing the hourly tip rate or the tip tax credit.

Tip v. Service Charge

The IRS explained the difference in tips and service charges, which are reported as non-tip wages. The following criteria apply to tips:

- The payment must be made free from compulsion.
- The customer must be able to determine the amount of the payment.
- The payment should not be negotiated or be dictated by the employer.
- The customer should have the right to decide who receives the payment.

For example, if a restaurant charges a set amount for parties of six or more, the charge is not a tip, but rather is a service charge.

The IRS is granting extra time for businesses not currently in compliance to revise their business practices and make needed system changes to comply with the new rules.

NEW RULES MAKE IT EASIER FOR SHAREHOLDERS TO INCREASE BASIS ON LOANS TO S CORPORATIONS

Under current law, S Corporation shareholders can only take losses and deductions into account if they have sufficient "basis" in the entity. A shareholder's basis reflects the shareholder's economic investment in the corporation and includes the adjusted basis of the shareholder's stock in the corporation as well as the basis of any debt the corporation owes the shareholder. In the past, the IRS and the courts have typically denied a basis increase to shareholders who borrow funds from a related entity (instead of a third-party lender) that are then loaned to the S Corporation, referred to as a "back-to-back loan." New proposed regulations relax the IRS position and allow a basis increase for legitimate loans to the S corporation. The loan must run directly to the shareholder, meaning that there must be a bona fide creditor/debtor relationship between the shareholder and the S Corporation. This is an important development that I will be glad to discuss with you because basis computations are key to your ability to deduct any losses you incur on your investment in an S Corporation.

PROPOSED RULES CLARIFY HOW 50% LIMIT ON MEALS AND ENTERTAINMENT DEDUCTION APPLIES TO MULTIPLE PARTIES

The IRS has issued proposed regulations that explain how the 50% deduction limitation on meals and entertainment expenses applies when multiple parties are involved. The rules are designed to impose the deduction limit on only one party. The new regulations explain how the limitation applies when a taxpayer is performing services for another person under a reimbursement arrangement. In the case of independent contractors, the parties can enter into their own agreement as to who will be subject to the 50% deduction limitation. If no agreement is reached, the limit will be applied to the independent contractor if the contractor does not substantiate the expense or to the client or customer if the contractor properly substantiates the expense. Anyone who reimburses an employee is subject to the deduction limitation if the payment is not treated as compensation or wages to the employee.

INDOOR TANNING EXCISE TAX FOR SINGLE-OWNER ENTITIES

New IRS regulations explain the responsibility of disregarded entities for the indoor tanning excise tax. A "disregarded entity" is an entity that elects to be disregarded as an entity separate from its owner." For example, if a "disregarded entity" is owned by an individual, it is treated as a sole proprietor. If the "disregarded entity" is owned by any other entity, it is treated as a branch or division of its owner. Under the new rules, for taxes imposed on amounts paid on or after July 1, 2012, the excise tax form must be filed under the name and employer identification number of the entity instead of the owner. This rule affects excise tax returns due on or after October 31, 2012. For taxes imposed on amounts paid before July 1, 2012, the IRS will treat payments made by a disregarded entity as having been made by the owner of that entity.

IRS TIGHTENS RULES FOR ISSUING TAX NUMBERS TO NONCITIZENS

Reacting to criticism, the IRS has changed its procedures for issuing Individual Taxpayer Identification Numbers (ITINs) to noncitizens, including illegal aliens. The IRS issues ITINs to people who are required to pay taxes but who are not eligible to obtain a Social Security Number. ITINs are issued regardless of immigration status because both resident and nonresident aliens may have a U.S. filing or reporting requirement. The number has nine-digits and always begins with the number 9 and has a 7 or 8 in the fourth digit, for example, 9XX-7X-XXXX.

The new rules are stricter on the documentation requirements. Now the IRS will only accept documents from an issuing agency including: passports, birth certificates, or certified documents. Notarized documents are no longer accepted to support applications. Spouses and dependents of U.S. military personnel who need ITINs are not subject to these changes.

DEDUCTION RULES FOR ENTERTAINMENT USE OF BUSINESS AIRCRAFT

The IRS has finalized rules on the deduction limitation for entertainment use of business aircraft. The final rules continue the policy established in 2007 that companies must allocate expenses between business and personal use on the basis of occupied seat hours or occupied seat miles, calculated as the yearly total hours or total miles flown by passengers multiplied by the number of occupied passenger seats. The total aircraft operating costs for the year are divided by occupied seat hours or occupied seat miles to arrive at cost per occupied seat hour or

occupied seat mile. Taxpayers also may allocate costs on a flight-by-flight basis which divides the total aircraft operating costs for the year by the number of flight hours or flight miles for the year to determine cost per hour or cost per mile. The cost per flight is then allocated to its passengers on a per capita basis.

IRS HAS PLAN TO HELP U.S. CITIZENS OVERSEAS CATCH UP WITH TAX FILINGS

The IRS has developed a plan to help U.S. citizens residing overseas, including those claiming to be dual citizens, to catch up with tax filing obligations and to provide assistance for people with foreign retirement plan issues. A new option that went into effect on September 1, 2012 allows U.S. citizens and others living abroad who have not been filing tax returns to come into compliance without paying penalties. Eligible taxpayers are those who have simple tax returns and owe \$1,500 or less in tax for any of the covered years. The new streamlined procedures also will allow resolution of issues related to foreign retirement plans, such as Canadian Registered Retirement Savings Plans. These taxpayers must file three years of delinquent returns and six years of foreign financial account reports.

AMERICAN FAMILIES' NET WORTH DROPS 40 PERCENT

If you own a home or have an IRA, no one needs to tell you something's awry. We hear every day that housing prices have plummeted to levels that left many homeowners underwater. The other side of most American family wealth has been in IRAs, and the lost value in these accounts is just beginning to be fully understood. Every three years, the Federal Reserve issues a report, the "Survey of Consumer Finances." The most recent report revealed that the median family had a net worth of \$77,300 in 2010, compared with \$126,400 in 2007, a reduction of about 40 percent. Seventy-five percent of the drop was blamed on the housing mess, but most of the rest was lost in quickly dwindling IRAs, where close to a trillion dollars disappeared from the family balance sheets.

TAX PLANNING

THINGS TO CONSIDER FOR ROTH CONVERSIONS

If you are thinking of converting your traditional IRA into a Roth IRA, you need to consider the possible changes to the tax code that could be coming after the elections. To convert your regular IRA into a Roth, you will have to pay income tax on the amount of the account that reflects any deductible contributions you made to the IRA as well as any untaxed earnings in the account. If you are in a high tax bracket now, it may make sense to wait until retirement age to withdraw your funds from a traditional IRA when your tax rate is likely to be lower. On the other hand, with the Bush tax cuts fully in effect, individual tax rates, especially those on upper-income taxpayers, are at an all-time low. You can take advantage of these low rates by converting your traditional IRA into a Roth before the end of the year.

Even if Mitt Romney wins the presidency and the Republicans take over Congress, it will take time for any longer-term tax reform plan with lower individual tax rates to be put in place. Thus, converting now could be a good compromise. The benefit of converting to a Roth IRA is that you will not have to pay tax on withdrawals later when you begin receiving distributions. Also, the earnings on your Roth IRA will never

be taxed if you hold any Roth IRA for 5 years and you delay receiving distributions until you are age 59 ½. Roths are more liquid than traditional IRAs, because you can withdraw rollover IRA contributions within 5 years after moving them into a Roth without a penalty. In short, this gives you better access to your savings without penalty while you still retain some of the benefits of a tax-qualified retirement plan. The rules are complex, though, and it is important to get the strategy right, depending on your individual financial goals. I will be glad to help you decide whether making a Roth rollover before the end of the year would be right for you.

COURT OPINION SUMMARIES

Court opinions in tax disputes are an important source of law that tax professionals use to advise their clients. What courts contribute to our understanding of tax law is an explanation of how the rules apply to different fact situations. Below I summarize several recent court cases that illustrate important tax rules.

ROLLOVER OF INHERITED IRA

A taxpayer's mother died leaving her daughter a traditional IRA managed by Citi Smith Barney. Citi made two death benefit distributions to the daughter with checks made out to her. The daughter kept some of the money and deposited the balance into a new inherited traditional IRA account at another institution. The taxpayer reported as income the portion she kept, but did not report the amount she put in the new IRA account. The IRS determined that all of the retirement income was taxable. The taxpayer said she intended to transfer the funds from the trustee of one account to the trustee of the second account, and argued that she had substantially complied with the rollover rules.

The Tax Court upheld the IRS assessment saying that because the funds were from an inherited IRA, the funds must be transferred directly from one account trustee to the other account trustee. If the taxpayer had control of the funds at any time, the distribution is taxable. The Court also noted that a taxpayer's "good intentions" do not determine the tax consequences of a transaction. The lesson here is that the rules for IRA rollovers are very strict and you should consult with a professional before making changes in your retirement accounts. (*Beech v. Commissioner*)

CANCELLATION OF CREDIT CARD DEBT

Gross income includes income from the discharge of indebtedness. In other words, if your debt is cancelled by a lender, you may have to pay tax on the amount of cancelled debt. The rationale is that the cancellation of debt gives the debtor an economic benefit that is equivalent to income. Financial institutions are required to send people 1099s when debt is discharged.

In a victory for taxpayers and those down on their luck, the Tax Court has decided that a taxpayer did not have cancellation of indebtedness income from unpaid credit card debt where the collection period had expired. Even though the debt collector issued a 1099-C for 2008, the Court found the debt was actually discharged much earlier. The Court looked at how long the debt had been outstanding and the creditor's efforts to collect the debt. It concluded that there was an "identifiable event" that indicated the debt would never be repaid. Note that even if you receive a Form 1099-C from a creditor, you do not necessarily owe tax on discharged debt because several exceptions apply. Please give me any Form 1099-C you receive for analysis. (*Stewart v. Commissioner*)

FEDERAL COURT SPLIT OVER WHETHER SEVERANCE PAYMENTS ARE SUBJECT TO FICA TAXES

The 6th Circuit Court of Appeals has ruled that severance payments are not subject to FICA taxes which include social security and Medicare taxes. The ruling allowed a refund of over \$1 million in employer and employee FICA taxes paid on severance benefits a company gave to its discharged workers. In 2008, another federal court came to the opposite conclusion in a different case when it found severance payments were subject to FICA.

When two federal appeals courts come to an opposite conclusion, taxpayers are left guessing which ruling their own Circuit court will follow. If a taxpayer is in the 6th Circuit, then the taxpayer can apply that Circuit's law. The 6th Circuit is made up of Michigan, Kentucky, Ohio, and Tennessee. However, other Circuits can make their own decisions, so taxpayers who reside in other circuits have an uncertain situation regarding the FICA taxation of severance payments. Thus, the IRS is likely to keep taxing severance pay until either Congress or the Supreme Court steps in to resolve the conflict. While some practitioners are recommending that employers consider filing refund claims, the legal situation is far from settled, and you need to have me, as your tax professional, carefully analyze your particular situation before any decision is made on how to treat severance payments. (*U.S. v. Quality Stores, Inc.*)

CONTRIBUTION OF RECEIVABLES TO AN S CORPORATION

The Tax Court was recently called upon to decide whether the distribution of one S corporation's accounts receivables to its shareholders, followed by their contribution of the receivables to a related S corporation, increased the shareholders' basis in the second S corporation's stock and allowed them to deduct its losses. The transfer involved an auto dealership and its related finance company. The finance company operated at a profit and the dealership operated at a loss. The shareholders did not have sufficient basis in the dealership to deduct its losses but had substantial basis in the finance company. The finance company distributed receivables to the shareholders who contributed them to the related dealership to allow the taxpayers to claim loss deductions on the dealership. The IRS disallowed the loss. The Tax Court held that the shareholders in the two related S corporations are not prohibited from receiving a distribution of assets from one S corporation and then contributing those assets to another of their S corporations to increase their basis. The Court made the point that while it is appropriate to scrutinize the validity of transactions between related parties in this situation, the fact that the corporations were related does not mean that there was not an honest shift in basis in the transaction. (*James Maguire v. Commissioner*)

MORTGAGE INTEREST DEDUCTION LIMIT FOR MARRIED FILING SEPARATE TAXPAYER

Taxpayers may take a deduction for mortgage interest on their principal residence for loans of up to \$1 million or \$500,000 for married taxpayers filing separate returns. The taxpayer in this case had obtained a \$1 million mortgage to help finance her purchase of a home owned by herself and her father-in-law. She and her father-in-law were liable on the mortgage. Although she was married, Petitioner paid the mortgage only with her own funds. On her tax return, she deducted the interest paid on the

entire \$1 million mortgage debt. The IRS disallowed the deduction and said she could only deduct the interest on \$500,000 of the debt. The Tax Court agreed with the IRS and ruled that the \$1 million limitation is only available to co-owners who are married and who file a joint return. In this case, the taxpayer's husband did not have joint ownership of the property and the couple did not file a joint return. Therefore, the full interest deduction was not available to them. (*Bronstein v. Commissioner*)

CLIENT ADVISORY

BRACE FOR INCREASED MEDICARE TAX ON HIGH INCOME EARNERS

Beginning in 2013, the Medicare tax rate for high wage earners will increase by 0.9%, from 1.45% to 2.35% for the employee's portion, on wages paid over \$200,000. The increase is only for the employee portion of the tax and will not be matched by employers. Specifically, an individual is liable for the additional Medicare tax if the individual's wages, other compensation, or self-employment income (together with that of a spouse if filing a joint return) exceed the threshold amount for the individual's filing status as follows:

Filing Status	Threshold Amount
Married filing jointly	\$250,000
Married filing separately	\$125,000
Single	\$200,000
Head of household (with qualifying person)	\$200,000
Qualifying widow(er) with dependent child	\$200,000

Married Couples May Overpay

The law requires an employer to withhold additional Medicare tax on compensation in excess of \$200,000 in a calendar year. This may cause an employee to overpay the Medicare tax if the employee is married filing a joint return and together the couple's income does not exceed \$250,000. Note that you may need to increase your withholding to avoid large tax liabilities at filing time, particularly if you are self-employed. I will be glad to evaluate your situation and make a recommendation.

THANK YOU FOR YOUR BUSINESS

As your tax professional, I will be carefully following any post-election tax legislation moving through Congress. I will apprise you of any delays I expect in the tax filing season when the tax rate situation becomes more clear. I will be happy to address any concerns and answer questions you have about any of the issues covered in this newsletter. Thank you for the opportunity and privilege of allowing me to serve as your tax professional.

Best regards,

QUOTATION

"I'm proud to be paying taxes in the United States. The only thing is - I could be just as proud for half the money."

--Arthur Godfrey, American television and radio personality.