

Dear Clients and Friends:

We hope that your 2010 has shown signs of improvement. As always, we have enjoyed the opportunity to help you with your personal and business needs. We think there will be even more opportunities for our clients in 2011 and hope to assist you in any way we can.

On the tax side of things, Congress passed and President Obama signed into law a two-year extension of soon-to-have-expired Bush-era tax cuts, including extension of current individual tax rates and capital gains/dividend tax rates. The new law also provides a temporary across-the-board payroll tax cut for wage earners, a retroactive AMT "patch," estate tax relief, education incentives, energy incentives, and many valuable incentives for businesses, including 100 percent bonus depreciation and extension of many temporary tax breaks.

Because of the frequency of changes enacted by congress we are planning on mailing a seasonal update to keep you informed of changes that may affect you.

Important to know for 2011:

- **The IRS has delayed the processing of most tax returns until at least mid-February, e-filing returns will still be the most efficient way.**

- ***Employee FICA withholding reduced*** – Effective for calendar year 2011, the employee portion of the Social Security taxes has been reduced from 6.2 % to 4.2% up to the taxable wage base of \$106,800. Self-employed individuals will pay 10.4% on self-employment income up to the wage based (reduced from the normal 12.4% rate). Be sure to change withholding for your employees or make sure your software does.

- ***Form 1099*** - Owners of rentals must issue 1099's beginning in 2011. Remember to get the name, address, and social security number or FEIN from all vendors before making payments to them in 2011. Contact us for a form W-9 to request this information from your vendor **or go to our website www.mpmsco.com/resources to access one.**

Important to know for preparing your 2010 return:

Individuals

- ***Tax Rates*** - Among the most valuable tax breaks for individuals in the new law are a two-year extension of individual income tax rate

reductions retaining the current 10, 15, 25, 28, 33, and 35 percent individual tax rates, through December 31, 2012, and the extension of the repeal of the limitation on itemized deductions and the personal exemption phase-out for two years. Married couples filing jointly will also benefit from extended provisions reducing or eliminating the so-called marriage penalty.

- **Capital gains/dividends** - The new law also extends the reduced capital gains and dividend tax rates. Individuals in the 10 and 15 percent rate brackets can take advantage of a zero percent capital gains and dividend tax rate for 2011 and 2012.
- **Alternative Minimum Tax (AMT)** - As you may know, the AMT was intended to ensure that very wealthy individuals did not evade taxation. Because the AMT was not indexed for inflation, and for other reasons, the AMT today encroaches on many moderate-income taxpayers, especially two-income married couples. The new law provides higher exemption amounts and other targeted relief for the coming years.
- **Credits for purchasing a personal residence.** A taxpayer who is a first-time homebuyer of a principal residence may claim a refundable credit equal to 10 percent of the purchase price of the residence (with a maximum credit of \$8,000 (\$4,000 for married couples filing separately). The Worker, Homeownership and Business Assistance Act of 2009, signed into law on November 6, extend the credit for qualified taxpayers purchasing principal residences on or before April 30, 2010. A taxpayer is eligible if they enter into a binding contract before May 1, 2010, to close on the purchase of a principal residence before September 30, 2010.

The new law also expands the credit to "long-time homeowners" who are buying replacement property but at a reduced amount of the credit. Individuals who have owned and used the same residence as their principal residence for any five consecutive year period during the eight year period ending on the date of the purchase of a subsequent principal residence, may be eligible for a reduced credit of \$6,500 (\$3,250 for married couples filing separately).

Congress has also made the credit available to more individuals by increasing the modified adjusted gross income (MAGI) phase outs for the credit. For purchases made after November 6, 2009, the credit begins to phase out for individuals with MAGI between \$125,000 and \$145,000, and for married couples filing joint returns with MAGI between \$225,000 and \$245,000.

- **Military personnel.** Individuals serving in the U.S. armed forces are eligible for a variety of tax incentives. For example, the Worker,

Homeownership and Business Assistance Act extends the homebuyer credit for members of the U.S. uniformed services, Foreign Service, and intelligence community on qualified official extended duty outside the U.S. to purchases made before May 1, 2011 (or July 1, 2011 for taxpayers with binding contracts). Additionally, there are special taxpayer-friendly rules for certain distributions from retirement accounts and for the treatment of differential pay. These provisions may be overlooked because they are not as well known as others. If you, a family member, or friend is serving in the armed forces, please contact our office for a complete review of all the tax incentives for service personnel.

Businesses

- ***Bonus depreciation*** - Bonus depreciation is intended to help businesses depreciate purchases faster against their taxable income. The new law makes 100 percent bonus depreciation available for qualified investments made after September 8, 2010, and before January 1, 2012. It also continues bonus depreciation, albeit at 50 percent, on property placed in service after December 31, 2011, and before January 1, 2013.
- ***Code Sec. 179 expensing*** - Along with bonus depreciation, the new law also provides for enhanced Code Sec. 179 expensing for 2012. Under current law, the Code Sec. 179 dollar and investment limits are \$500,000 and \$2 million, respectively, for tax years beginning in 2010 and 2011. The new law provides for a \$125,000 dollar limit (indexed for inflation) and a \$500,000 investment limit (indexed for inflation) for tax years beginning in 2012 (but not after).
- ***Employee healthcare*** - Certain eligible employers may receive a credit to be used against their taxes for employer provided healthcare. If you provide health insurance to 25 or fewer employees, please let us know.
- ***Other employee credits*** – The Work Opportunity Tax Credit Program has expanded its pool of eligible new hires available for this valuable credit (certain unemployed individuals, veterans and certain targeted youth). Please see us if you believe you may qualify for this credit in your business.

Energy

- ***Businesses*** - For businesses, one of the most valuable energy incentives is the Code Sec. 1603 cash grant in lieu of a tax credit program. This incentive encourages the development of alternative energy sources, such as wind solar or geothermal energy. Please contact our office regarding your options.

- **Green incentives.** When considering home improvements, do not forget a variety of federal tax incentives that can help you save money. One of the more popular tax breaks is the residential energy property credit. The credit is 30 percent of the sum of expenditures for qualified energy efficiency improvements, including windows, furnaces, water heaters, heat pumps, and more, which are placed in service in 2010. The credit is limited to \$1,500 for 2010. The improvement must meet strict energy efficiency standards. If it does not, you cannot claim a credit. This is a common error and it can be a costly one.

Estate and gift taxes

- The new law revives the estate tax, but with a maximum estate tax rate of 35 percent with a \$5 million exclusion. The revived estate tax is in place for decedents dying in 2011 and 2012. Oregon still has retained its exemption on estates whose value is one million or less. Please contact us to help amend or update your estate plans to take advantage of these provisions.

Mileage Rates

- For the 2010 tax year, the standard mileage rate for business miles was 50 cents a mile (it is 51 cents per mile in 2011)
- The standard mileage rate for charitable purposes will be 14 cents per mile for both 2010 and 2011.
- For 2010, the standard mileage rate for the cost of operating your car for medical reasons or as part of a deductible move is 16.5 cents per mile (it is 19 cents per mile in 2011).

Deduction for Production

- The tax deduction for a percentage of business income earned from manufacturing and certain other production activities occurring in the United States which became effective January 1, 2005, has increased to its full 9% for 2010.

Retirement contributions

- IRA contribution limits are \$5,000 for 2010 (\$6,000 if age 50+). These amounts may be limited in the event of participation in another retirement plan.
- For 2010 401k plan contribution limits are \$16,500 (\$22,000 if age 50+).

Oregon Minimum Wage

- Effective January 1, 2011, the Oregon minimum wage will remain the same at \$8.50 per hour.

Please note that we will continue to electronically file all eligible returns during the 2010 tax season. For specific forms or general information, please feel free to visit our website at www.mpmsco.com/resources.

If you have any questions at all, please feel free to contact us and we can meet with you personally. We sincerely appreciate and thank you for the opportunity to serve you and wish you a Happy New Year!

Sincerely,

Molatore, Scroggin, Peterson & Co. LLP