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TAX AND BUSINESS ADVISOR

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TAX AND BUSINESS Alert™

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Qualified Charitable Distributions

IRA owners and beneficiaries who have reached age 70½ are permitted to make cash donations to IRS-approved public charities directly out of their IRAs. These so-called qualified charitable distributions, or QCDs, are federal-income-tax-free to you, but you get no itemized charitable write-off on your tax return. But, that's okay because the tax-free treatment of QCDs equates to an immediate 100% deduction without having to worry about restrictions that can delay itemized charitable write-offs. QCDs have other tax advantages, too.

A QCD is a cash payment of an otherwise taxable distribution, by your IRA trustee, directly to a qualified public charity. The funds must be transferred directly from your IRA trustee to the charity. You cannot receive the funds yourself and then make the contribution to the charity. However, the IRA trustee can give you a check made out to the charity that you then deliver to the charity. You cannot arrange for more than $100,000 of QCDs in any one year. If your spouse has IRAs, he or she has a separate $100,000 limitation. If you are the beneficiary of an IRA (as opposed to an account owner), you too are eligible for the QCD deal if you are at least age 70½.

You must keep substantiation of the contribution from the charity. Also, you must not have received any benefit in return for making the contribution.

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QCDs are not included in your adjusted gross income (AGI) on your federal tax return. This lowers the odds that you'll be affected by various unfavorable AGI-based phase-out rules. In addition, you don't have to worry about the 50%-of-AGI limitation that can delay itemized deductions for garden-variety cash donations to public charities. QCDs also count as payouts for purposes of the Required Minimum Distribution (RMD) rules. Therefore, you can donate all or part of your 2011 RMD amount (up to the $100,000 limit on QCDs) and thereby convert taxable RMDs into tax-free QCDs.

The QCD privilege is generally beneficial for seniors in the following circumstances:

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Deducting Job Search Expenses

In this economy, many individuals are looking for jobs and may incur some expenses along the way. While it may seem unfair, you can only deduct expenses to search for a job that's in the same occupation as the last one you had (or the one you still have if you're looking for a better position). If you pass this "same occupation test," you can potentially deduct the expenses (subject to the 2%-of-AGI miscellaneous itemized deduction limitation). You can also deduct expenses to look for a new job in the same occupation even if you're temporarily working in another field. And you can deduct expenses to look for full-time work in your existing occupation while you're working part-time or sporadically in the same line of work.


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Some examples of deductible job-hunting expenses include employment agency or headhunter fees, travel costs, resume preparation, copying, postage, and long-distance calls (but only if you have to pay extra for them). If you drive in connection with your search, you can deduct the IRS business mileage allowance. But keep this in mind: transportation expenses to go out of town are only deductible if the primary reason for your trip is the job search. You can't deduct expenses that are reimbursed by a prospective employer or a future or past employer.

Qualified Dividend Income

You may have heard that qualified dividends are taxed at the favorable long-term capital gain rates (maximum 15% rate). While that's great news for investors, there are a few exceptions you should watch out for before you assume all your dividend income will qualify for the reduced tax rate.

First, you must hold the stock for at least 61 days (91 days for certain preferred stock) during a certain time period around the dividend. While this is usually not a problem, some transactions (like selling the stock short or acquiring or selling options on the stock) may cause some of the days you own the stock not to count toward the required holding period. This required holding period also applies to shares in a mutual fund. In addition, if you are under an obligation to make related payments with respect to a dividend you receive, that dividend will not qualify for the preferential rate. This could be the case if you have both a long and short position in the dividend-paying stock.

Qualified Charitable Distributions

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1. You don't itemize deductions. Under the "normal" rules, only itemizers get any income tax benefit from charitable donations. Making QCDs will save taxes whether you itemize or not because neither you nor your heirs will ever have to pay income taxes on the donated amounts.

2. Your itemized charitable donations would be delayed by the 50%-of-AGI limitation. Making QCDs will avoid this unfavorable limitation.

3. You want to avoid being taxed on RMDs that you are forced to take from your IRAs. The QCD strategy does the trick while also allowing you to satisfy your charitable inclinations.

Which Is Best for Your Business: Section 179 or 100% Bonus Depreciation?

Taxpayers who acquire assets for use in their trade or business activity have a very good chance of writing off the entire cost, thanks to 100% bonus depreciation plus very generous Section 179 deduction limits. If there is a choice between them, this article will help determine which of these options is most beneficial. First, let's go over the basic rules for asset purchases.

The Section 179 deduction limit is $500,000. This limit is reduced dollar for dollar (but not below zero) by the cost of qualifying property over $2 million. So, no Section 179 deduction is available if the total cost of qualifying property placed in service during the year is $2.5 million or more.

The 100% bonus depreciation provision effectively allows taxpayers to write off the entire cost of qualified assets placed in service during the year. However, specific deduction limitations apply for qualifying vehicles.

If both bonus depreciation and the Section 179 deduction are available, the taxpayer will have to choose one or the other. If that is the case, the following are some considerations to keep in mind.

The use of 100% bonus depreciation is mandatory. However, a business can elect not to deduct bonus depreciation for any class of property placed in service during the tax year. This election applies to all additions within a class placed in service that year. On the other hand, the Section 179 election is much more flexible. Not only is it available on an asset-by-asset basis, but taxpayers can also elect to expense less than the full amount of an asset's basis. In addition, the Section 179 deduction can be used for both new and used equipment; 100% bonus depreciation only applies for new equipment.

There is no limit on the amount of 100% bonus depreciation a business can claim for the year, nor is there a taxable income limit. This means that by claiming bonus depreciation, the taxpayer can create or increase a net operating loss (NOL) that can be carried back and possibly used immediately. On the other hand, the Section 179 deduction is limited to $500,000 (reduced dollar for dollar by qualifying asset purchases exceeding $2 million). It is also limited to the taxpayer's net trade or business income for the year, with any excess generally carried over to the following year.

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The Section 179 deduction claimed on qualified real property cannot be carried over past the 2011 tax year (unless this provision is extended). Disallowed deductions remaining at the end of the 2011 tax year are treated as if no Section 179 expensing election had been made for them. Amounts not carried over past the 2011 tax year are depreciated under the normal rules for real property.

To be eligible for the Section 179 deduction, the asset must be used more than 50% of the time for business. If the business usage later falls to 50% or less, the Section 179 deduction must be recaptured. Except in the case of listed property (e.g., passenger automobiles and computers), greater than 50% business usage is not a requirement for bonus depreciation. Therefore, bonus depreciation may be a better choice for an asset (other than listed property) currently used more than 50% for business if there's a chance that the business usage may later fall to 50% or less.

Finally, for taxpayers subject to alternative minimum tax, there is no adjustment for either bonus depreciation or Section 179 deductions.

The Importance of Updating Beneficiary Designations

Most of us have more than enough to do. We're on the go from early in the morning until well into the evening—six or seven days a week. Thus, it's no surprise that we may let some important things slide. We know we need to get to them, but it seems like they can just as easily wait until tomorrow, the next day, or whenever.

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A U.S. Supreme Court decision reminds us that sometimes "whenever" never gets here and the results can be tragic. The case involved a $400,000 employer-sponsored retirement account, owned by William, who had named his wife Liv as his beneficiary in 1974 shortly after they married. The couple divorced 20 years later. As part of the divorce decree, Liv waived her rights to benefits under William's employer-sponsored retirement plans. However, William never got around to changing his beneficiary designation form with his employer.

When William died, Liv was still listed as his beneficiary. So, the plan paid the $400,000 to Liv. William's estate sued the plan, saying that because of Liv's waiver in the divorce decree, the funds should have been paid to the estate. The Court disagreed, ruling that the plan documents (which called for the beneficiary to be designated and changed in a specific way) trumped the divorce decree. William's designation of Liv as his beneficiary was done in the way the plan required; Liv's waiver was not. Thus, the plan rightfully paid $400,000 to Liv.

The tragic outcome of this case was largely controlled by its unique facts. If the facts had been slightly different (such as the plan allowing a beneficiary to be designated on a document other than the plan's beneficiary form), the outcome could have been quite different and much less tragic. However, it still would have taken a lot of effort and expense to get there. This leads us to a couple of important points.

The first is that if you want to change the beneficiary for a life insurance policy, retirement plan, IRA, or other benefit, use the plan's official beneficiary form rather than depending on an indirect method such as a will or divorce decree. The second point is that it's important to keep your beneficiary designations up to date. Whether it is because of divorce or some other life-changing event, beneficiary designations made years ago can easily become outdated.

One final thought regarding beneficiary designations: while you're verifying that all of your beneficiary designations are current, make sure you've also designated secondary beneficiaries where appropriate.