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The Essential Tax & Wealth Planning Guide for 2007

Including year-end tips for 2006

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This guide was developed by the Deloitte Tax Private Client Advisors practice under the direction of Katy Hollister, Partner and National Leader of the Private Client Advisors practice, Deloitte Tax LLP.

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Table of Contents

Introduction	**5**
The Current Environment	**7**
Rules and Regulations Designed to Curtail Abuses	7
Congressional Agenda	8
The American Jobs Creation Act of 2004, The Working Families Tax Relief Act of 2004, And The Jobs And Growth Tax Relief Reconciliation Act of 2003	11
Individual Income Tax Rates	11
Marriage Penalty Relief	11
Child Tax Credit	11
Alternative Minimum Tax (AMT) Relief	12
Reduced Capital Gain Rates	13
Reduced Dividend Rates	13
Increased Section 179 Expensing	14
Deducting Attorney Fees	15
Deducting State Sales Taxes	15
Charitable Contribution Deductions	16
Limits Imposed on Exclusion of Principal Residence Gain	16
Qualified Roth IRA Contribution Program	16
Foreign Tax Credit Reform	17
S Corporation Reform	17
Executive Compensation Changes	17
Individual Expatriation	18
Longer Write-off Period for Start-Up and Organization Costs	18
Tax Shelter Disclosures and Penalties	18
Year-End Tax Planning	**19**
Perform Multi-Year Alternative Minimum Tax Calculations	19
Avoid Underpayment Penalties	20
Avoid Overpaying Estimated Taxes	21
Evaluate Recognition of Compensation Income	21
Evaluate "Extraordinary" Dividend Income	21
Examine Capital Gains and Capital Losses	21
Manage the Timing of Itemized Deductions	22

Revisit Stock Option Planning	23
Time the Payment of Medical Expenses	23
Contribute to a Medical Savings Account	24
Establish a Health Savings Account	24
Review Flexible Spending and Pre-Tax Transportation Account Balances	25
Review Estate Plans	27
Make Gifts to Charities	27
Review Investments in Retirement Accounts	29
Consider Converting Your Traditional IRA to a Roth IRA in 2006	31
Review Investment Plans	31
Examine Distributions from Tax-Preferred Retirement Savings	32
Establish Education Savings Accounts	33
Examine State Planning Opportunities	34
Manage Passive Gains and Losses – Individuals	34
Review Split-Dollar Insurance Arrangements	35
Review Disability Insurance Options	35
Obtain Taxpayer Identification Numbers for Dependents	36
Use Low Interest Rates to Optimize Family Wealth Planning	36
Tax Shelter Disclosure Requirements	**38**
Year-End Planning Checklist	**40**
Yearly Tax Planning Calendar	**46**
Deduction Limitations Of Outright Charitable Gifts	**48**
2007 Individual Income Tax Rate Tables (Projected)	**49**
Deloitte Tax Private Client Advisors	**50**
Investment Consulting Services	**52**

Introduction

It is difficult to plan ahead. We are all consumed by our day-to-day lives and responsibilities, and it is often difficult to devote time to things that will not happen for months or even years. However, there are advantages to planning ahead, including the peace of mind that comes from knowing that you are prepared for your financial future.

As you plan for 2007, a number of uncertainties must be taken into consideration, not the least of which is the possible overhaul of the current tax system. President Bush has made tax reform one of the top priorities for his second term, yet little substantive change has been made to the overall federal tax system. The Tax Increase Prevention and Reconciliation Act that was signed into law in May 2006 extended many valuable provisions originally enacted earlier in the decade, such as the fifteen percent tax on dividends and capital gain, and temporarily held back the Alternative Minimum Tax from affecting millions of middle class Americans. In August of 2006, the Pension Protection Act of 2006 was enacted in an attempt to shore up the pension systems of private employers, in the wake of the economic crisis faced by the airline and auto industries. The Pension Act also included substantial charitable reforms for both exempt organizations and their donors. The House of Representatives passed, but the Senate failed to pass, substantive reforms to the federal estate and gift tax system. The failed bill had included the extension of many pro-taxpayer provisions.

The value of year-end tax planning cannot be overstated. When the clock strikes midnight on December 31, 2006, many 2006 tax savings opportunities will be lost forever. Without year-end planning, these potential opportunities will be discovered only when your tax return is being prepared... often when it is too late to act. A little time well-spent now can result in significant tax savings later.

In this guide, we invite you to walk through the steps necessary to review your current personal tax situation and to consider any appropriate actions to reduce your tax liability before year-end. In leading you through these steps, this guide covers the following topics:

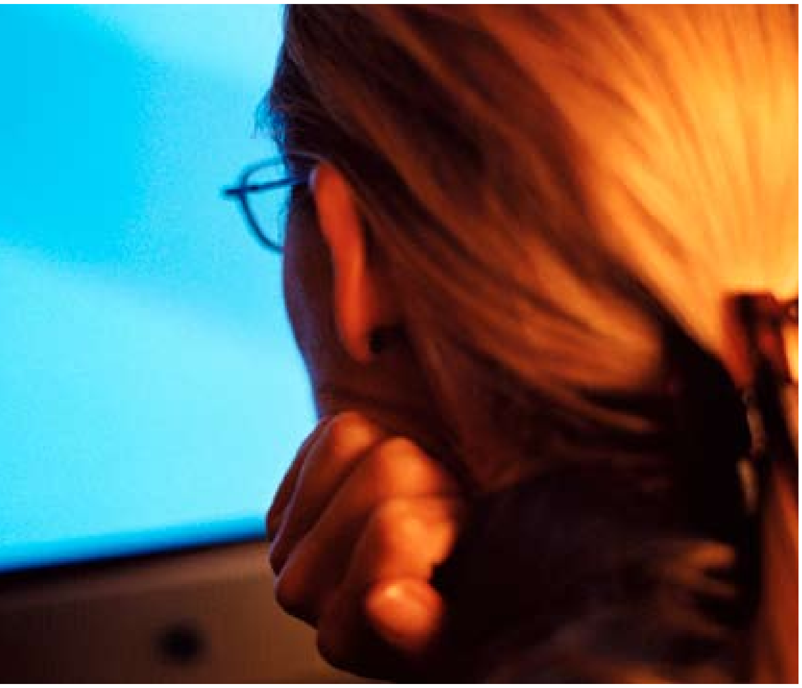
- An overview of the current tax environment, including recent regulatory changes that affect the way we do business and how you should handle your tax planning in the future.
- Recent tax changes that may affect your tax situation this year and beyond.
- How to assess your current tax position and any immediate planning strategies you should consider, including (but not limited to) planning the timing of income and deductions.
- Steps to take before year-end to reduce your tax liability.
- Tax planning related to a low interest rate environment.
- General financial planning tips to consider at year-end.
- A calendar of important dates.

Planning for 2007 will also be affected by other uncertainties. For example: Will interest rates remain relatively low? The Federal Reserve has increased interest rates regularly since June of 2004. The Fed has paused during the summer of 2006, but will the next move be up or back down? Will the stock market continue its multi-year bull run or will the sharp decline felt in May 2006 be a precursor for things to come? What will be the state of the economy and the job outlook? Will another tax cut or increase occur? Will Congress fix the AMT system? Will the estate tax be repealed? Will the mid-term elections in November 2006 result in progress or stalemate in tax policy? No one knows with certainty what will happen in the future. Given this uncertainty, a good plan is necessary to provide you with maximum flexibility in meeting financial goals.

A map for success will integrate your financial, investment, wealth transfer, and tax planning objectives into a comprehensive plan. We hope this guide provides you with many insights into your tax and overall financial planning.

Deloitte Tax LLP is pleased to provide our clients and others with this 2007 Planning Guide. We hope you find this guide useful, and we encourage you to consult with your Deloitte Tax advisor to help plan your financial future.

The Current Environment



Rules and Regulations Designed to Curtail Abuses

The compliance environment for taxpayers and their advisors has changed significantly over the last five years as a result of legislative and regulatory actions taken to curb the use of tax shelters, strengthen corporate governance, and improve oversight of public accounting firms.

The enactment of new disclosure and penalty provisions in the American Jobs Creation Act of 2004 (AJCA) gave the IRS many tools to uncover and shut down abusive tax schemes quickly. The AJCA strengthened disclosure requirements under which taxpayers are required to provide the Internal Revenue Service with details concerning their participation in certain potentially abusive transactions. However, the broad definition of a potentially abusive transaction means that the disclosure requirements are far-reaching and apply to a wide range of transactions that may not be abusive. There can be severe consequences for failing to comply with the disclosure requirement. In addition to a substantial penalty for failure to file disclosure forms, taxpayers could also be subject to a higher penalty on any tax understatement attributable to the transaction, loss of the reasonable cause defense against the understatement penalty, and extension of the time period in which the IRS could assess and collect taxes related to an undisclosed transaction. Taxpayers who do not make the required disclosures will find that the IRS can obtain information concerning their participation in potentially abusive transactions from other sources because the AJCA also modified prior rules requiring that promoters register potentially abusive transactions and maintain lists of the investors in those transactions. The AJCA expanded the application of the rules to persons who may not have been directly involved in promoting or organizing these transactions. Under the new rules, virtually anyone retained by the taxpayer to provide tax advice concerning a potentially abusive transaction, including lawyers, accountants, bankers, and insurers, may be obligated to reveal information concerning the taxpayer's participation in the transaction to the IRS. Thus, taxpayers must consider that if they do not make the required disclosures concerning a transaction, their advisors may nonetheless have an obligation to reveal their participation in the transaction to the IRS.

Additional details regarding the disclosure regime are provided on pages 38-39.

In addition, the Treasury Department has amended "Circular 230," which governs the practice of attorneys, certified public accountants, and others who practice before the IRS. The revised rules affect the manner in which taxpayers receive advice from their tax advisors. Tax advisors must carefully consider the numerous requirements and options under Circular 230 before they provide any written tax advice to clients because running afoul of the rules could result in sanctions for the tax advisor and the tax advisor's firm.

The Public Company Accounting Oversight Board (PCAOB) is a private-sector, nonprofit corporation created by the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley) to oversee accounting professionals who provide independent audit reports for publicly traded companies. The PCAOB was created by Congress and is overseen by the SEC. Responsibilities of the PCAOB include the following:

- registering public accounting firms;
- establishing auditing, quality control, ethics, independence, and other standards relating to public company audits;
- conducting inspections, investigations, and disciplinary proceedings of registered accounting firms; and
- enforcing compliance with Sarbanes-Oxley.

On July 26, 2005, the PCAOB finalized their ethics and independence rules concerning independence, tax services, and contingent fees. These rules, which went into effect in 2006, provide that an audit firm is not independent if the firm, or any affiliate of the firm, provides any tax services to a person in a financial reporting oversight role or to an immediate family member of such person.

The above rules and regulations may affect the way you invest as well as the way you hire and transact with professional advisors. These rules and regulations are complex. Deloitte Tax professionals can assist you with determining whether these rules affect your tax reporting and/or disclosure obligations.

Congressional Agenda

With the contentious mid-term elections behind them, lawmakers will turn their attention to several pressing tax policy issues. One of those issues is likely to be the individual alternative minimum tax (AMT) problem. The Tax Increase Prevention and Reconciliation Act extended the temporary increase in AMT exemption amounts for 2006 but, without a change in the law or another extension, an estimated 20 million additional taxpayers will owe AMT liabilities in 2007. Solutions to the AMT problem are costly. Extending AMT relief through 2007 costs roughly $30 billion and repealing it, without offsets, costs more than $1 trillion, if the current tax cuts are extended.

Estate tax reform could also make it onto the legislative agenda in 2007. Under the 2001 tax cuts, the estate tax is being gradually reduced through 2009. It will be completely repealed for 2010 and revert to its pre-2001 status in 2011. While the House has repeatedly passed permanent estate tax repeal, the legislation has failed to garner sufficient support in the Senate. Recognizing that a permanent reduction in the estate tax -- rather than outright repeal -- may be the best hope for reform, Republican leaders pushed two bills through the House during 2006 that would increase the estate tax exemption and lower estate tax rates. Senate Finance Committee member Jon Kyl, R-Ariz., and Senate Finance Committee ranking Democrat Max Baucus of Montana appeared close to completing their draft of similar legislation that they hoped would receive sufficient support to pass the Senate. However, due to time constraints no additional action was taken on this issue in the Senate. Because a compromise may already be within reach, estate tax reform could be one of the few opportunities Republicans and Democrats have in 2007 to produce legislation for the President's signature.

Lawmakers are likely to continue looking for ways to deal with the so-called tax gap, the difference between the amount of taxes owed and the amount that is timely paid to the government, which is currently estimated to be $345 billion annually. With federal budget deficits expected to continue well into the next decade, there is increased pressure on lawmakers to offset the cost of future tax cuts. Measures that reduce the tax gap can serve the dual purpose of improving compliance and raising much needed revenue.

In 2006, Congress' Joint Committee on Taxation (JCT), at the request of Senate Finance Committee Chairman Charles Grassley, R-Iowa, and ranking Democrat Max Baucus of Montana, added new proposals to its 2005 recommendations for reducing the tax gap. Seven of the eight new JCT proposals could have a substantial impact on non-corporate taxpayers. They would:

- Require that brokers report a customer's adjusted basis in publicly traded securities sold during the preceding taxable year to the Internal Revenue Service. Every broker would be required to provide its customers with information statements showing the same basis information that is included for those customers in returns filed with the IRS.
- Expand third-party information reporting relating to the mortgage interest deduction. Mortgage holders would have to include additional information on the annual interest statement provided to taxpayers. This information would include whether the underlying loan was a financing or refinancing, whether the debt proceeds exceed the $100,000 home equity limit, and the amount by which the refinancing loan amount exceeds the balance of the loan being refinanced.
- Require reporting of real estate taxes. The JCT described two options for implementing this proposal. One option is to require that state and local taxing jurisdictions report to the IRS and taxpayers the amount of taxes paid (excluding nondeductible amounts). The other option is to require that mortgage lenders report to the IRS and taxpayers the amount of real estate taxes paid by taxpayers through escrow accounts.
- Require that brokers report proceeds of auction sales. Broker information reporting requirements would be expanded to include proceeds from property sold at auction, including collectibles or motor vehicles.
- Establish new reporting requirements for individuals with an interest in offshore bank accounts and offshore trusts. Tax return preparers would be subject to a due diligence requirement in determining whether a client must submit a return to the IRS reporting transactions with foreign trusts and receipts of foreign gifts.
- Modify the determination of amounts subject to self-employment tax for partners and S corporation shareholders in personal service businesses. The present-law rule that a general partner's distributive share is subject to employment taxes would be applied to all types of partners and S corporation shareholders with income from service businesses. The proposal also would include members of a limited liability company or other entity that is treated as a partnership for federal income tax purposes.
- Deny deductions and credits for untimely returns of nonresident aliens and foreign corporations. The JCT presents two options for implementing this proposal. One option is to specify by statute a fixed date or event after which a foreign person's deductions or credits will be denied. The other option is to specify by statute that a foreign person's deductions or credits will be denied when tax returns are not timely filed, and delegate to Treasury the authority to define what is meant by "timely."

Grassley and Baucus have been successful in getting several of the JCT's 2005 proposals enacted in recent legislation, including the Tax Increase Prevention and Reconciliation Act of 2005. They have indicated that the Finance Committee will review the new proposals in 2007 and decide whether to act on any of them.

Although one focus of this guide will be on year-end planning for 2006, that focus is always taken with an eye to the future. Year-end planning is just the starting point for setting the course for many years to come. While no one can predict what will happen next year, five years from now, or twenty years from now, one thing is certain: a sound financial plan requires an integrated, comprehensive examination of your financial picture over multiple years. Plan now for your future.

Tax Increase Prevention and Reconciliation Act

President Bush signed into law May 17 the five-year, $70 billion reconciliation tax cut bill that was authorized by last year's budget resolution. At a White House signing ceremony, the president called the new law "a victory for the American taxpayers and…a strong lift for our economy." The Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA) did not include new tax cuts: it largely extended the cuts put in place earlier in Bush's presidency. The Act includes a two-year extension of reduced capital gains and dividends rates (through 2010) and a two-year extension of enhanced section 179 expensing (through 2009). It extends the increased exemption for AMT that had expired at the end of 2005 for one year. Fixing the AMT for 2007 is expected to cost an additional $35 billion.

In addition to the extension of many favorable tax provisions, the Act extended the imposition of the "kiddie tax" to children under 18 years old and required tax exempt municipal bond interest to be reported on a Form 1099. The Act also created an opportunity for taxpayers with IRAs to convert them to Roth IRAs beginning in 2010, regardless of income level.

> ☑ **Planning Tip No. 1:** The IRA to Roth IRA conversion in 2010 can be planned for in 2006. If a taxpayer is not eligible to contribute to a Roth IRA due to the income thresholds, the taxpayer should consider contributing to a regular IRA or non-deductible IRA beginning in 2006 so those amounts can be eventually be converted to a Roth in 2010. Contributions to a non-deductible IRA build basis in the plan, which will be non-taxable at the subsequent conversion in 2010.

To the detriment of many Americans abroad, TIPRA amended the rules relating to the foreign earned income exclusion, also known as the "Section 911 exclusion." This amendment increased the tax bills of many individuals working abroad and was included in TIPRA to help offset the cost of the other taxpayer favorable provisions.

The Act does not address the numerous other expired or expiring tax provisions, including the research and experimentation tax credit, the work opportunity tax credit, the welfare-to-work credit, the state and local sales tax deduction, and the 15-year recovery period for leasehold improvements and restaurant property. At the time of printing of this guide, Congress has yet to enact legislation which would extend these and other expired or expiring provisions.

Pension Protection Act of 2006

President Bush on August 17, 2006 signed into law comprehensive pension reform legislation that will transform rules governing defined benefit plans, clarify rules for hybrid plans, make permanent retirement savings provisions set to expire in 2010, and strengthen rights and information requirements for participants of defined contribution plans. In addition to pension reforms, the Pension Protection Act of 2006 also includes a handful of tax incentives to promote charitable giving and provisions to curb abuses among tax-exempt organizations.

The Joint Committee on Taxation staff estimates that the pension bill will cost $7.7 billion over five years and $73.2 billion over ten years.

The most significant developments for individuals concern the charitable giving provisions included in the Act. The Act contained many charitable provisions, but the following will likely have the broadest applicability:

Limitation on Deductions for Clothing and Household Items

Deductions are no longer allowed for charitable contributions of clothing and household items unless such items are in "good" used condition or better. In addition, the IRS is given discretion to deny a deduction for any item with minimal monetary value.

Household items include furniture, furnishings, electronics, appliances, linens, and other similar items. Food, paintings, antiques, and other objects of art, jewelry and gems, and collections are excluded from the provision (and therefore continue to be governed by existing law).

IRA Withdrawals for Charity

A withdrawal of up to $100,000 per year from a traditional individual retirement account (IRA) or a Roth IRA, which would otherwise be included in income, are excluded from income if the distribution is made to charity. To qualify for this special provision, the IRA owner must be older than 70 1/2 on the date of distribution and the charitable distribution must be made directly to a tax-exempt organization to which tax deductible contributions are ordinarily deductible. Individuals may not take an itemized deduction for the contribution, and the amounts contributed by the IRA are not included for purposes of total charitable contributions for purposes of applying the annual AGI limitations. The charitable distribution will be taken into account for purposes of the minimum distribution rules. This provision does not apply to employer sponsored plans such as 401(k)s, SEP or SIMPLE plans. The provision is effective for tax years 2006 and 2007.

Modification of Record-Keeping Requirements for Certain Charitable Contributions

The Act amends a taxpayer's record-keeping requirements by requiring that in the case of a charitable contribution of money, regardless of the amount, the donor must maintain a cancelled check, bank record, or receipt from the donee organization showing the name of the donee organization, the date of the contribution, and the amount of the contribution.

Non-Spousal IRA Rollovers

Beginning in 2007, an individual receiving an inherited qualified retirement plan from a decedent other than their spouse may rollover the inherited account into their own IRA. The rollover must executed by a trustee-to-trustee transfer, and may be done anytime after the owner's death. The inherited amounts transferred to the IRA will be treated as an inherited IRA subject to the IRA minimum distribution rules. Thus, beneficiaries will now have the option to take payments over their life expectancy.

The American Jobs Creation Act of 2004, The Working Families Tax Relief Act of 2004, And The Jobs And Growth Tax Relief Reconciliation Act of 2003

The American Jobs Creation Act (AJCA) of 2004, providing $137 billion of primarily business tax relief, was signed into law on October 22, 2004. It contains individual tax cuts and excise tax reforms, in addition to tax relief for U.S.-based manufacturing activities, reforms in the taxation of multinational businesses, and general business income tax relief. Among other provisions, AJCA permits individuals the choice of deducting the greater of their state sales taxes or state income taxes, extends the section 179 expensing limits established by the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA) for two additional years, and permits the deduction of certain attorney fees in full rather than as an itemized deduction.

The Working Families Tax Relief Act of 2004 (“Working Families Act”), signed into law on October 4, 2004, extended the availability of many of the relief measures included in JGTRRA. In addition, several business incentives (such as the research credit, work opportunity tax credit, above-the-line deduction for teachers’ classroom expenses, and credit for electricity from renewable resources) were retroactively extended.

JGTRRA was signed into law on May 28, 2003, by President Bush. The $330 billion tax cut package accelerated many of the provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). Among other provisions, JGTRRA retroactively dropped individual income tax rates, reduced the tax rate on dividends and capital gains, expanded the child tax credit, and provided marriage penalty relief. Certain provisions for business owners were also enacted.

This chapter presents an overview of the changes made by the AJCA, Working Families Act, and JGTRRA, and contains certain planning tips related to the changes. Many of the items are discussed only briefly as they relate to the change in tax law, and are expanded upon in the chapter focusing on year-end planning.

An overview of the changes that affect individuals enacted by the Working Families Act and JGTRRA can be found in the chart on page 18.

Individual Income Tax Rates

JGTRRA reduced individual income tax rates. It brought the top tax bracket down from 38.6 percent to 35 percent. The 10 percent tax bracket for 2006 applies to the first $7,550 of taxable income for single filers and the first $15,100 of taxable income for married couples filing jointly. These amounts are adjusted for inflation after 2005. Please refer to pages 49 of this guide, 2006 and 2007 Individual Income Tax Rate Tables, for a full list of 2006 and 2007 income tax rate brackets.

> ☑ **Planning Tip:** Taxpayers should revisit their estimated tax/withholding strategy. If you have overpaid estimated taxes (or are expecting a refund because withholdings have been too high during the year), reducing withholdings for the remainder of the year will put more money in your pocket now, instead of waiting for a refund. However, certain limitations apply as to the number of exemptions that may be claimed, which affects the amount that can be withheld; therefore, you are encouraged to discuss your particular situation with your tax advisor prior to filing a new Form W-4 to adjust your withholding.

Because of the changes under the Working Families Act, the 10 percent bracket, in its expanded form, is now available through 2010.

Marriage Penalty Relief

Two provisions of JGTRRA provide some relief from the “marriage penalty.” The standard deduction for married couples was increased to twice the amount for single taxpayers. The range of the 15 percent tax bracket for married couples was changed to equal twice the amount for single taxpayers. Because of changes made by the Working Families Act, both provisions are now available through 2010.

Child Tax Credit

The child tax credit for 2006 is $1,000 per child. The credit will phase out for higher income taxpayers. For example, a family with two qualifying children will receive no benefit from the increased credit if the couple’s modified AGI exceeds $150,000. The Working Families Act provides that the $1,000 child tax credit is available through 2010.

Alternative Minimum Tax (AMT) Relief

The AMT exemption for 2006 is $62,550 for married couples filing jointly and $42,500 for single filers. As with the regular income tax, high income taxpayers may not be able to take advantage of the exemption due to phase out provisions. While the increased exemption amount will help some taxpayers, the reduction of marginal rates will dramatically increase the number of taxpayers subject to AMT, especially high earners who will not benefit from the exemption. In 2007, the AMT exemption is scheduled to decrease to $45,000 for married couples filing jointly and to $33,750 for single filers, if the higher exemption amounts are not re-extended by Congress.

The Working Families Act extended the rule allowing nonrefundable personal credits, such as the dependent care credit, to offset AMT for 2004 and 2005. This tax break was again extended through 2006 by TIPRA. It was previously scheduled to end in 2003.

☑ **Planning Tip No. 1:** If you expect to be in AMT in 2006 and a "regular" bracket next year, consider accelerating ordinary and short–term capital gain income and deferring certain 2006 deductions to 2007 (especially the deductions not deductible for AMT, such as state and local income taxes, real estate taxes, and investment advisory expenses). This is contrary to typical planning techniques, but may lower your ultimate tax bill.

☑ **Planning Tip No. 2:** If you are not subject to AMT in 2006, but expect to be in 2007, accelerate expenses that are not deductible for AMT into 2006. Consider paying off home equity debt if the interest expense is not deductible for AMT purposes.

☑ **Planning Tip No. 3:** Some of the differences between the AMT and regular tax systems are merely matters of timing. For instance, AMT generally requires slower depreciation than is permitted for regular tax purposes. Other differences are permanent; for example, state income or sales taxes can never be deducted under the AMT system, while under the regular system they are deductible when paid. Paying AMT in one year may generate a credit against a future year's regular tax when adjustments are due to timing differences. Overall, the taxpayer may be better off if AMT is paid in a previous year in order to gain a credit in a later year. Perform a multi-year analysis to anticipate the effect in future years of planning techniques used in 2006.

☑ **Planning Tip No. 4:** Consider whether any exercised incentive stock options should be disqualified before year-end to minimize AMT liability if the stock has dropped in value. A disqualifying disposition will limit compensation income to the difference between the exercise price and the lower value of the stock at sale. However, if there is a wash sale (i.e., you repurchase the same stock within 30 days of the disqualifying disposition), compensation will be computed at the spread at exercise (at the old, higher value).

☑ **Planning Tip No. 5:** Perform an AMT "self diagnosis." Falling victim to AMT has many possible causes, but you may be particularly prone to AMT if you have any of the following circumstances:

- Large state and local income or sales tax or property tax deductions
- Large long-term capital gains or qualified dividends
- Large deductions for accelerated depreciation
- Large miscellaneous itemized deductions
- Mineral investments generating percentage depletion and intangible drilling costs
- Research and development expenses
- An exercise of incentive stock options
- Large amounts of tax-exempt income that are not exempt for state tax purposes
- Tax-exempt income from private activity bonds

If you are affected by one or more of these circumstances, you should discuss your AMT situation with your tax advisor.

Watch out for other AMT traps. Income from private activity (municipal) bonds is taxable for AMT purposes. Certain mortgage interest, such as from a home equity loan, is not deductible for AMT purposes as home mortgage interest if the funds from the loan are not used to buy, build, or substantially improve a primary or second home. However, be sure to tell your tax advisor if you used the funds in your business or to make investments, since the interest may be deductible.

Taking advantage of special tax rules can produce AMT implications under several situations, so carefully consider your overall tax situation before taking any action. For example, the bargain element associated with the exercise of an incentive stock option is not subject to ordinary tax, but is subject to AMT. Similarly, any large capital gain may raise your state and local taxes to a level that would trigger AMT. The resulting AMT could wipe out some or all of the benefit you anticipate from the lower capital gains rate. This makes it particularly important to plan on a multi-year basis for transactions that could trigger AMT.

Reduced Capital Gain Rates

Long-term capital gain rates were decreased in 2003 for all individual taxpayers. For taxpayers in the highest four tax brackets, the long-term capital gain rate was decreased from 20 percent to 15 percent for sales or exchanges that occur after May 5, 2003, and before January 1, 2009. For taxpayers in the lowest two tax brackets, the rate dropped from 10 percent to 5 percent for sales or exchanges that occur after May 5, 2003, and before January 1, 2008. It drops to zero percent for sales or exchanges that occur in 2008. The lower rates also apply to installment sales payments that are received after May 5, 2003, even if the installment sale occurred prior to May 6, 2003.

The Tax Increase Prevention and Reconciliation Act enacted in May 2006 extended the reduced capital gain structure through 2010.

☑ **Planning Tip No. 1:** Taxpayers interested in family wealth planning should consider gifting appreciated assets (or those that are expected to appreciate) to their children who are over the age of 17 and in the lowest two tax brackets. Since taxpayers in the highest four tax brackets are taxed at a 15 percent long-term capital gain rate versus a 5 percent rate for taxpayers in the lowest two tax brackets, an immediate 10 percent tax savings may be realized. If the recipient child remains in the lowest two tax brackets and the assets are sold between 2008-2010, no capital gains tax will be due. Combining utilization of the gift tax annual exclusion with a gift of appreciating assets can be a powerful wealth transfer planning tool.

☑ **Planning Tip No. 2:** Taxpayers who are considering selling a business should attempt to structure the transaction as a sale of the company's stock, rather than a sale of the company's assets. In most circumstances, a sale of the company's stock will constitute a sale of a capital asset, eligible for the lower capital gains rates, as opposed to a sale of the assets, which would be subject to tax as ordinary income. The buyer will typically want to structure the transaction as a sale of assets in order to take advantage of certain depreciation rules; therefore, some negotiation is to be expected.

☑ **Planning Tip No. 3:** Taxpayers in the technology industry should consider selling patents, rather than licensing patents. Generally, the sale of a patent will generate capital gains, whereas income from the licensing of a patent will generate ordinary income.

☑ **Planning Tip No. 4:** When a taxpayer expects to be in a higher tax bracket in future years or tax rates are expected to increase significantly in the taxpayer's retirement years, it may be more advantageous for individuals approaching retirement to invest in equities outside of their retirement accounts. By doing so they can obtain the favorable capital gains rate when they "cash in" their investment. They should also invest in taxable bonds in their retirement accounts where the ordinary income generated can be deferred. Retirement plan distributions are generally taxed at ordinary income tax rates, which can be as high as 35 percent. Taxpayers should run a multi-year tax projection to determine the best method of investing for retirement, while keeping taxes to a minimum.

Certain sales of capital assets do not qualify for the lower capital gain rate. Collectibles remain subject to a 28 percent maximum rate; unrecaptured "section 1250" gain on real estate is subject to a 25 percent maximum rate; and small business stock is still subject to the 50 percent exclusion and the net taxed at 28 percent.

Reduced Dividend Rates

A lower rate of tax also applies to qualified dividends. Prior to the changes enacted by JGTRRA, dividends were taxed at the taxpayer's ordinary income tax rate. For taxpayers in the highest four tax brackets, the tax rate was decreased to 15 percent for qualified dividends received after December 31, 2002, and before January 1, 2009. For taxpayers in the lowest two tax brackets, the rate will be 5 percent until January 1, 2008, and will drop to zero percent for qualified dividends received in 2008.

The Tax Increase Prevention and Reconciliation Act enacted in May 2006 extended the reduced capital gain and dividend structure through 2010.

☑ **Planning Tip No. 1:** Investment interest expense is only deductible to the extent of current year net investment income. Dividends that are taxed at the 15 percent (or 5 percent) reduced rate are not treated as investment income for purposes of this calculation; therefore, taxpayers should consider electing to tax a portion of qualified dividends (or capital gains) at ordinary income rates to maximize use of the investment interest deduction. Taxpayers may elect to recognize just enough of the qualified dividends to be taxed at ordinary income tax rates to offset investment interest expense, and allow the remainder of qualified dividends to be taxed at the lower 15 percent rate (or 5 percent rate for lower income taxpayers). In the alternative, taxpayers should consider whether carrying over an investment interest expense into a future year is more advantageous than electing to recognize qualified dividend income (and/or capital gains) as ordinary income for a current year offset. If you have paid investment interest expense and received dividend income in 2006, you should discuss the possibility of making this election with your tax advisor.

☑ **Planning Tip No. 2:** Taxpayers interested in family wealth planning should consider gifting assets that are expected to pay dividends to family members who are in lower tax brackets. As noted above, taxpayers in the highest four tax brackets are currently taxed at 15 percent on qualified dividends, whereas taxpayers in the lowest two brackets are taxed at 5 percent – a 10 percent tax difference. If the recipient taxpayer remains in the lowest two tax brackets, qualified dividends received in 2008-2010 are expected to be taxed at a zero percent rate. Taxpayers should remain mindful of the kiddie tax rules, which provide that children under the age of 18 who have investment income greater than $1,700 may be subject to tax based upon their parents' top marginal tax rate.

☑ **Planning Tip No. 3:** In order to qualify for the reduced rate, the underlying stock upon which a dividend is paid must be held for at least 61 days during the 121-day period beginning 60 days before the ex-dividend date (91 days of the 181-day period for preferred stock). The shares must be unhedged during this time period in order to qualify; therefore, taxpayers who regularly engage in hedging transactions or other derivative transactions may want to consider more complicated investment techniques, such as selling a qualified covered call, in order to take advantage of the lower rates.

In the past, the Internal Revenue Service has challenged shareholder compensation in C corporations on the grounds that the compensation was excessive. As a result, the excess amount was disallowed as a deduction to the corporation, and recharacterized as a constructive dividend to the shareholder. Shareholders should be aware that this recharacterization is not automatic; therefore, strategies to purposely create excess compensation in the hopes that the shareholder will be taxed at the lower dividend rates should be approached with caution. Alternatively, corporations that plan to decrease salaries to low levels and raise dividends should be aware that they may be establishing a new salary history if the lower dividend rate finally expires in 2010 as planned, and salaries are again raised to original levels. Corporations may then be under fire for excess salaries, given the history of lower salaries established. The level of compensation provided to an employee should be determined by reasonableness in light of all of the facts and circumstances, rather than upon the tax effect.

Some margin accounts allow the broker to borrow shares held in the margin account, and return the shares at a later date. In practice, the broker borrows shares from a pool of investors in order to lend the shares to another investor to execute a short sale. For tax purposes, payments that are made while the shares are borrowed out are considered "payments in lieu of dividends," rather than dividends, and thus will not qualify for the lower rate. Investors should consult with their brokers to see whether it is their policy to borrow shares from non-institutional investors. In certain cases, an investor may want to transfer dividend-paying shares into a cash account or place a restriction on the broker's ability to borrow the shares. Alternatively, the investor may want to ensure that he has the ability to call back shares of stock before the dividend date, so that he will be the owner of the shares on the dividend record date. In most cases, however, no action will be needed because most brokers have already considered the impact of these rules and have notified their customers accordingly.

Increased Section 179 Expensing

Section 179 of the Internal Revenue Code allows taxpayers, other than estates, trusts, or certain non-corporate lessors, to treat the cost of qualifying property as an expense rather than a capital expenditure. This provides an immediate tax deduction rather than a need to depreciate the asset over a number of years. For 2006, the maximum dollar amount that may be deducted under section 179 is $108,000 ($112,000 in 2007). However, the section 179 deduction is limited for sport utility vehicles ("SUVs") placed in service after October 22, 2004. Certain vehicles are excluded from the definition of an SUV, such as pickup trucks, delivery vehicles, and large passenger vans. For SUVs placed in service after October 22, 2004, and for all other qualifying property placed in service in tax years beginning in 2010 or later, the section 179 limit drops to $25,000 per year.

The election has a "use it or lose it" nature. If the election is not used in whole or in part in one year, the opportunity to use the election is lost in that year. In other words, if a taxpayer did not use the section 179 election at all in 2005, the taxpayer is still limited to the $108,000 threshold limitation in 2006 – the opportunity that was available to deduct up to $105,000 in 2005 is not added on to the $108,000 that may be deducted in 2006. The deduction may be limited by business income (including wages). If the election is made but the deduction is limited because business income is low, the rest of the deduction will carry forward into the next year. Therefore, even if the deductible amount is limited in the current year, it may be worthwhile to make the election.

☑ **Planning Tip No. 1:** Taxpayers who have been considering making a purchase of capital assets that would be considered a qualified expense should consider making the purchase prior to December 31 to utilize the section 179 election.

☑ **Planning Tip No. 2:** If taxpayers have qualifying expenses in excess of $108,000, the section 179 expensing election should be used against those qualified assets with the longest recovery period (depreciable life). By picking and choosing which assets to expense, the cost of the property will be recovered in the shortest period of time possible.

☑ **Planning Tip No. 3:** The expensing election under section 179 does not affect the ability of a business owner to deduct ordinary business expenses. If a purchase qualifies as an ordinary business expense, rather than as a capital asset with a useful life of more than one year, the entire purchase price would be deductible in the year of purchase without the need to elect expensing under section 179 and use up part of the $108,000 limitation. Taxpayers should analyze the nature of their business expenses to take maximum advantage of all expensing elections.

☑ **Planning Tip No. 4:** The definition of "qualified property," for purposes of section 179 expensing, has been expanded to include off-the-shelf computer software. However, if the software has a useful life of one year or less, the cost may also qualify for expensing under section 167(f) of the Internal Revenue Code. If the section 179 threshold has already been met (or exceeded), this may be an additional method for the business owner to expense the cost of the software.

☑ **Planning Tip No. 5:** Utilizing the section 179 expensing election will reduce the taxpayer's adjusted gross income (AGI), which may allow the taxpayer to use additional itemized deductions, convert a traditional IRA to a Roth IRA, or qualify for otherwise disallowed credits (e.g., child tax credit, IRA contribution deductibility, personal exemptions, and Hope Scholarship and Lifetime Learning credits). Nevertheless, taxpayers may want to forego the section 179 expensing election in one year in order to be able to take depreciation deductions in years when income is higher and more deductions are beneficial.

Deducting Attorney Fees

Attorney fees and court costs for some lawsuits will be fully deductible against income (i.e., are "above the line" and not classified as itemized deductions) if the settlement or judgment occurs after October 22, 2004, and the fees are paid after that date. These fees and costs will also be deductible for AMT. The deduction may not exceed the amount includible in gross income resulting from the claim. For settlements occurring before October 23, 2004, many individual taxpayers must include the gross amount of any settlement or judgment in their gross income and claim any deduction for legal fees on Schedule A as a Miscellaneous Itemized Deduction subject to the 2 percent floor; such items are not deductible for AMT.

Taxpayers affected by this change are those involved in an action regarding:

- A claim of unlawful discrimination;
- Certain claims for personal injury and property damage against the federal government; and
- Certain claims covering health benefits provided to employees who are eligible for Medicare.

If you are involved in a lawsuit and may receive a judgment or settlement, discuss this with your tax advisor to determine if your legal fees may be deductible "above the line."

Deducting State Sales Taxes

Individuals who itemize deductions may deduct the greater of their state and local income or sales taxes. This provision will likely provide the most benefit to persons residing in states that do not levy income taxes, (e.g., Alaska, Florida, Nevada, South Dakota, Texas, Washington, and Wyoming). Individuals in states that tax only dividends (e.g., New Hampshire and Tennessee) may have larger sales tax than income tax expense.

Individuals may determine their deductible state and local sales tax by using (1) actual receipts on all purchases, or (2) tables published by the IRS. Those using the tables may also deduct sales tax paid on the purchase of motor vehicles, boats, and other items specified by the Treasury Department.

As originally enacted, the provision was only available for 2004 and 2005 tax years. If not extended by Congress, the state and local sales tax deduction expires after 2005. Contact your Deloitte Tax adviser for an update on the status of this, and many other expiring provisions, that may be extended by Congress in the coming months.

Charitable Contribution Deductions

Under the AJCA, the charitable deduction available for donations of vehicles after December 31, 2004 (including cars, boats, and airplanes) with a claimed value exceeding $500 is, in most cases, limited to the gross proceeds received by the charity upon subsequent sale of the donated vehicle. The new law also requires that charitable organizations provide the donor with a written contemporaneous acknowledgement of the donation.

The AJCA also requires increased reporting for certain charitable donations of property by corporations. When property other than cash, inventory, and publicly traded securities is donated to charity after June 3, 2004, and such property is valued above $5,000, the property must be appraised in order for a corporation to claim a charitable deduction (this previously applied only to non-corporate taxpayers). If the value exceeds $500,000, the appraisal must be attached to the donor's income tax return, whether the donor is an individual, partnership, or corporation.

The AJCA also modifies the treatment of charitable deductions for donations of intellectual property. If a donor contributes a patent or other intellectual property (other than certain copyrights or inventory) to a charity after June 3, 2004, the donor's initial charitable deduction is limited to the lesser of basis or fair market value. If the donated property provides income to the charity, the donor may deduct certain additional amounts in the year of contribution or subsequent years, based on a specified percentage of the income received by the charity.

Limits Imposed on Exclusion of Principal Residence Gain

Individuals are permitted to exclude from income up to $250,000 of gain on the sale of a principal residence ($500,000 for married couples filing jointly). In order to qualify for this exclusion, the property must have been used as a principal residence for at least two out of the five years immediately preceding the sale. The exclusion is available once every two years. If an individual has not used the property as a principal residence for the required two years, and the sale is due to employment, health, or unforeseen circumstances, a prorated exclusion may be permitted.

After October 22, 2004, gain on the sale of a principal residence cannot be excluded if the home was acquired in a like-kind exchange within five years from the date of sale. The date of sale for this purpose is the closing date. Therefore, individuals who own property which was originally acquired in a like-kind exchange and which is currently used as a principal residence must wait until the five-year anniversary of the property's acquisition date has passed before selling the property in order to exclude all or a portion of the gain.

Qualified Roth IRA Contribution Program

Beginning in 2006, employees who elect to contribute to a 401(k) plan may designate some or all of these contributions as Roth IRA contributions ("designated Roth contributions"), if their particular 401(k) plan permits such treatment. Designated Roth contributions are taxable to the employee in the contribution year; however, distributions from the designated Roth portion of the 401(k) plan after the employee reaches age 59 1/2 will be tax-free. Designated Roth contributions must be separately accounted for within the 401(k) plan. The maximum amount an employee may contribute to all 401(k) plans, including designated Roth contributions, is $15,000 in 2006. Beginning in 2007, the $15,000 limit will be indexed for inflation. The maximum amount an employee may contribute in 2007 is $15,500. In addition to these amounts, taxpayers over age 50 by the end of the year can make additional contributions of $5,000 thereby making the maximum contributions for these individuals $20,000 in 2006 and $20,500 in 2007.

Foreign Tax Credit Reform

The AJCA made significant changes to the rules regarding foreign tax credits. Prior law permitted individual taxpayers with unused foreign tax credits to carry the credits back two years and forward five years. For credits generated in 2005 and later years, any unused foreign tax credits may be carried back only one year. Also, for credits being carried forward into 2004 and later years, the credit may be carried forward for ten years.

The AJCA provides that the AMT foreign tax credit may be fully applied against the AMT in 2005 and later years. Prior to 2005, the AMT foreign tax credit was limited to 90 percent of the tentative minimum tax; therefore, even if a taxpayer had a significant amount of AMT foreign tax credit, they were unable to use this credit to fully offset their AMT liability. Any excess over the 90 percent was carried forward to future years. This sometimes resulted in a taxpayer with no regular tax liability (because the regular tax foreign tax credit would fully offset regular tax) but who had an AMT liability. Beginning in 2005, the 90 percent limitation no longer applies and taxpayers may use their AMT foreign tax credit to fully offset AMT.

The AJCA also modified the rules regarding categories or "baskets" of income for foreign tax credit purposes. For 2006 and earlier tax years, there are nine separate foreign tax credit income baskets: (1) passive income; (2) high withholding tax interest; (3) financial services income; (4) shipping income; (5) dividends from certain noncontrolled corporations; (6) dividends from a domestic international sales corporation ("DISC") or former DISC that are treated as foreign source income; (7) taxable income attributable to foreign trade income; (8) distributions from a foreign sales corporation ("FSC") or former FSC; and (9) income not mentioned in any of these categories. The foreign tax credit is computed separately for each basket of income; therefore, foreign tax credits generated from one basket of income may not be credited against income in another basket. This prevents high-rate foreign taxes that are generally imposed on income such as active business income from being credited against U.S. tax on passive income, which may be imposed at a lower rate.

The AJCA provides that beginning in 2007, there will be only two baskets: (1) general income and (2) passive income. Having fewer baskets of income may result in more foreign tax credit being allowed in the year in which the tax is paid or accrued, and less being carried back to prior tax years and/or forward to future tax years.

If you pay foreign taxes and/or have carried over foreign tax credits from a prior year, you should discuss with your tax advisor how the new rules may affect you. Certain types of foreign taxes may either be deducted or taken as a credit for federal tax purposes. You should discuss the appropriate treatment with your tax advisor. Note that if foreign taxes are equal to or less than $300 ($600 for married couples filing jointly), you can take a foreign tax credit without completing any additional tax forms.

S Corporation Reform

The AJCA updated and simplified the rules applicable to S corporations, and expanded the eligibility rules for using these entities. These and other S corporation provisions were further modified in the Gulf Opportunity Zone Act of 2005 and the Pension Protection Act of 2006.

The S corporation rules are outside the scope of this publication. However, if you own an interest in an S corporation, your tax advisor can explain how the new rules may affect you.

Executive Compensation Changes

The AJCA made significant changes to the rules governing deferred compensation arrangements. The changes generally broaden the definition of deferred compensation, restrict the availability of assets held by plans, and would prohibit use of some offshore trusts.

For amounts earned or vested after December 31, 2004, the timing and method of distribution must be fixed before amounts are considered earned, and can only be changed in limited circumstances. In addition, any modification to plans or arrangements after October 3, 2004, may cause previously deferred amounts to be subject to the new rules. Violation of the new rules could result in a 20 percent penalty tax. Individuals will now have to more carefully review expected cash flow in making deferral elections and may decide less deferred compensation is the prudent approach.

The AJCA limits deductions attributable to personal use by an executive of company-owned aircraft for expenses incurred after October 22, 2004. The deduction cannot exceed the amount recognized in the executive's income. The change generally applies to officers, directors, or more than 10 percent owners of the company.

Individual Expatriation

The AJCA adopted more objective tests for determining whether an expatriating individual falls under alternative tax rules. These rules apply to individuals who expatriate after June 3, 2004.

Longer Write-off Period for Start-Up and Organization Costs

Under prior law, business start-up and organization costs could be amortized over 60 months. The AJCA changes the amortization period to 15 years and allows a partial deduction in the first year of business of up to $5,000 each of start-up and organizational costs. However, each $5,000 expense is reduced if the total start-up or organization costs exceed $50,000; once the total start-up or organization costs equal or exceed $55,000, the $5,000 initial year deduction will be reduced to zero. These rules apply to start-up and organization costs paid or incurred after October 22, 2004.

Tax Shelter Disclosures and Penalties

The AJCA requires greater tax shelter disclosure, increases penalties related to tax-shelter activity, targets specific tax-avoidance transactions, and strengthens IRS administrative processes. For more information on how these provisions apply to individuals, see pages 38-39.

Summary of Changes Made by JGTRRA & the Working Families Act Affecting Individual Taxpayers

<table>
<tr><th colspan="10">Changes Affecting Individuals</th></tr>
<tr><th>Provision</th><th>2003</th><th>2004</th><th>2005</th><th>2006</th><th>2007</th><th>2008</th><th>2009</th><th>2010</th><th>2011</th></tr>
<tr><td>Marginal Income Tax Rates</td><td colspan="8">35%
33%
28%
25%
15%
10%</td><td>39.6%
36%
31%
28%
15%
(no 10% bracket)</td></tr>
<tr><td>Child Tax Credit</td><td colspan="8">$1,000</td><td>$500</td></tr>
<tr><td>Marriage Penalty Relief
Standard Deduction
Percent Bracket</td><td colspan="8">
Twice single
Twice single</td><td>
N/A
N/A</td></tr>
<tr><td>Capital Gains* & Dividend Rate (High Brackets/Low Brackets)</td><td colspan="5">15% – top four brackets
5% – lowest two brackets</td><td colspan="3">15% – top four brackets
0% – lowest two brackets</td><td>Capital gains: 20% / 10% Dividends: Ordinary income rate</td></tr>
<tr><td>AMT Exemption
Single Filers
Married Filing Joint</td><td colspan="3">
$40,250
$58,000</td><td>
$42,500
$62,550</td><td colspan="5">
$33,750
$45,000</td></tr>
</table>

* The lower capital gain rates apply to sales or exchanges (or installment payments received) on or after May 6, 2003.

Year-End Tax Planning

Although active steps should be taken throughout the year to achieve your financial and personal goals, there are actions that can be taken before year-end to potentially minimize your tax burden. The discussion below provides a broad range of topics to consider before year-end, and a checklist of items to assist in your year-end planning.

Perform Multi-Year Alternative Minimum Tax Calculations

The individual alternative minimum tax (AMT) system was originally designed in 1969 to prevent the "very wealthy" from using a variety of special tax incentives to avoid paying income tax. However, AMT has evolved into an unwieldy system that will ensnare millions of unsuspecting taxpayers in coming years. Current forecasts by the Congressional Budget Office (CBO) estimate that nearly 30 million taxpayers will be subject to AMT in 2010 (up from 2 million in 2002). Those living in states with high income taxes (such as California, New York, Montana, Oregon, and Vermont), high property taxes (such as New York, Illinois, and New Jersey), and deductible personal exemptions are more likely to be affected.

Think you are immune? The CBO estimates that about two-thirds of households with incomes between $50,000 and $100,000 and over 85 percent with incomes between $100,000 and $500,000 will be subject to AMT before the end of the decade. The CBO also estimates that if the current system remains in place, by 2050, 70 percent of taxpayers will be affected by AMT and that total AMT revenues will account for 20% of personal income taxes collected by the federal government.

Planning for the AMT has become increasingly difficult for taxpayers. Taxpayers must be especially mindful of year-end cash payments, such as fourth quarter state income taxes, pre-payment of investment and tax advisor fees, and charitable contributions. In addition, tax projections from hedge funds and managing private activity bonds take on special significance. Current year planning around timing of the payment of expenses that constitute itemized deductions not deductible under the AMT system is certainly important, but it may not be enough. More than ever, multiple year scenarios must be examined to engage in any meaningful AMT planning.

See the AMT discussion in the section above on the AJCA, Working Families Act and JGTRRA for planning tips (page 12).

Avoid Underpayment Penalties

Federal law requires the payment of income taxes throughout the year as the income is earned. This obligation may be met through withholding, making quarterly estimated tax payments, or both. The penalty for underpayment is calculated as interest on the underpaid balance until it is paid, or until April 15, 2007, whichever occurs first.

For 2006, individuals will not be subject to an underpayment penalty if the balance due on their federal tax return (total tax liability for the year, less withholdings) is $1,000 or less. If the balance due is more than $1,000, the taxpayer will be subject to a penalty unless 2006 withholdings and estimated tax payments equal 90 percent of the 2006 tax liability; 100 percent of the 2005 tax liability (110 percent if 2005 Adjusted Gross Income (AGI) exceeds $150,000); or 90 percent of 2006 tax liability, based on quarterly annualization of year-to-date income. Individuals also must consider any underpayment rules imposed by their state(s) of residency and/or local tax authorities.

The following table illustrates the amount required to be paid (cumulatively) for 2006 taxes under each method by each date for calendar year taxpayers.

Cumulative Amount of Estimated Taxes To Be Paid				
Due Date				
2006 Tax Payment Method	April 17, 2006	June 15, 2006	Sept. 15, 2006	Jan. 16, 2007
Current year's tax or annualized income method	22.5%	45%	67.5%	90%
Prior year's tax – safe harbor for AGI of $150,000 or less	25%	50%	75%	100%
Prior year's tax – safe harbor for AGI over $150,000	27.5%	55%	82.5%	110%

☑ **Planning Tip No. 1:** Income tax withholdings are considered paid equally throughout the year, even if the withholdings are made near the end of the year. If you anticipate that you have underpaid your estimated taxes for 2006, consider adjusting withholdings for the remainder of the year to avoid penalties for underpayment of estimated taxes.

☑ **Planning Tip No. 2:** In certain circumstances, supplemental wages (e.g., bonuses, commissions, overtime pay, etc.) may be subject to a flat 25 percent withholding rate. If this rate is different from your "normal" withholding rate, be sure to factor the different rate into your estimated tax calculations. Similar to withholding on regular wages, taxpayers may increase the withholding amount on their supplemental wages to avoid penalties for underpayment of estimated taxes. Beginning in 2005, supplemental wages in excess of $1,000,000 are subject to a 35 percent withholding rate.

☑ **Planning Tip No. 3:** A taxpayer who anticipates being liable for underpayment penalties on estimated tax should consider taking a distribution from a traditional or Roth IRA account during the year of underpayment. The trustee of the IRA is required to withhold 20 percent of the funds distributed as a pre-payment of federal income. By triggering sufficient withholding tax, the taxpayer can "cure" prior underpayments of estimated tax and avoid or reduce penalties. As long as the taxpayer re-deposits the gross amount of the IRA distribution to another IRA within 60 days, no adverse tax consequences result from the rollover, provided the taxpayer meets the once-per-year rollover limitation.

Avoid Overpaying Estimated Taxes

Just as a taxpayer should avoid underpaying estimated taxes and incurring a penalty, a taxpayer should avoid overpaying estimated taxes. Overpaying taxes is the equivalent of providing an interest-free loan to the government. You may receive a refund eventually, but you have lost the opportunity to have the money working for you.

☑ **Planning Tip:** If you anticipate that estimated taxes have been overpaid (or withholdings have been too high during the year), consider reducing withholdings during the remainder of the year to create an early refund. Certain restrictions apply with respect to the number of exemptions that may be claimed, which will affect the minimum amount that can be withheld; therefore, check with your tax advisor before submitting a new W-4 to adjust your withholdings for 2006. Also, estimate your withholding for 2007, and file a new W-4 with your employer, if necessary.

Evaluate Recognition of Compensation Income

Depending on your situation, you may be able to time the receipt of commissions, bonuses, or billings. Income recognition timing isn't easy, however. You need to consider the time value of money and the impact acceleration might have on various deductions, credits, and other nontax financial factors. However, several income recognition techniques should be considered.

☑ **Planning Tip No 1:** Income is usually taxable to individuals in the year of receipt. Therefore, in most cases, deferring income into 2007 will defer the associated tax. Consider delaying the receipt of an annual bonus until after December 31, or waiting until January to bill for services. However, check with your tax advisor prior to engaging in this type of planning to be sure you are not running afoul of constructive receipt rules which treat income as received even though you do not have cash in hand, or subjecting the income deferred to the very stringent rules imposed on nonqualified deferred compensation pursuant to the AJCA. Also check with your tax advisor to determine whether you are expected to be subject to AMT in either year, which may affect your ability to benefit from such a deferral strategy.

☑ **Planning Tip No 2:** Analyze opportunities around making a "section 83(b) election" on restricted stock to convert ordinary income to capital gains. Section 83 of the Internal Revenue Code imposes ordinary income tax on property received as compensation for services as soon as the property becomes vested and transferable. If you receive eligible property (such as restricted stock), you can elect under section 83(b) to recognize immediately as income the value of the property received and convert all future appreciation to capital gains income, and all future dividends on the stock to dividends qualifying for the reduced 15 percent rate. However, keep in mind that making the election comes with a risk – if you make the election and the stock never vests or it depreciates in value, you cannot "undo" the election at a later date, and your choice to recognize the income immediately may not provide the anticipated benefit. Careful planning is required to make sure you comply with strict rules and are able to properly weigh the benefits against the risks; therefore, you should consult with your financial advisor before making this election.

Evaluate "Extraordinary" Dividend Income

The receipt of "extraordinary" dividends may cause unexpected tax results. Extraordinary dividends are typically the result of larger-than-normal dividends and/or a very low basis in the stock.

Dividends are considered "extraordinary" if the amount of the dividend exceeds 10 percent of the shareholder's adjusted basis in the stock (5 percent if the shares are preferred). All dividends with an ex-dividend date within the same 85 consecutive days are aggregated for purposes of computing whether this threshold is met. Individuals who receive extraordinary dividends and later sell the stock on which the dividends were paid must classify any loss on the sale, to the extent of such dividends, as a long-term capital loss, regardless of how long the stock was held. Thus, for the investor who anticipated receiving short-term capital loss treatment on the sale, presumably to be able to offset short-term capital gains, unexpected tax consequences may result. Absent this rule, taxpayers who had already realized short-term capital gain could buy a stock that was expected to pay out large dividends, hold the stock only long enough to receive the dividend, then sell the stock at a loss to offset the short-term capital gains while enjoying favorable tax rates on qualified dividends.

Examine Capital Gains and Capital Losses

The decision to sell capital assets should be based on economic fundamentals together with your investment goals; however, tax aspects should also be considered. For taxpayers in the highest four tax brackets (35-, 33-, 28-, and 25- percent), current law generally provides a 15 percent rate on assets held for more than one year and sold after May 5, 2003. Thus, for those in the highest tax bracket, a 20 percent rate differential exists between short-term capital gains (which are taxed at ordinary income rates) and long-term capital gains. Pay attention to the holding periods of assets to take full advantage of the long-term capital gain rates available for assets held more than one year. However, as discussed earlier, taxpayers should perform hypothetical calculations prior to making a sale to avoid unexpected tax consequences.

☑ **Planning Tip No. 1:** If you anticipate being in a lower tax bracket in 2007, or if significant amounts of capital losses are anticipated in 2007, consideration should be given to recognizing capital gains in 2006, but deferring tax recognition until 2007. This can be accomplished by using such strategies as entering into an installment sales agreement or implementing other investment techniques. Consult your tax advisor for planning techniques for your specific situation.

☑ **Planning Tip No. 2:** If you have short-term capital gains (which are taxed at ordinary income tax rates), consider selling capital assets that will generate a capital loss, in order to offset the short-term capital gain. Taxpayers are allowed to deduct up to $3,000 of net capital losses against ordinary income each year. Any net capital losses in excess of $3,000 are carried over to future years.

☑ **Planning Tip No. 3:** Under the "wash sale" rule, if securities are sold at a loss and the same – or substantially the same – securities are purchased within 30 days before or after sale of the original securities, the loss cannot be recognized until the replacement securities are sold. There is, however, often a satisfactory alternative. To realize the loss and maintain the ability to benefit from the market's upside, consider selling a stock or mutual fund to realize a loss, and replacing it in your portfolio with one of similar characteristics in the same industry or style group.

Manage the Timing of Itemized Deductions

Explore opportunities to time deductions for charitable contributions, state and local taxes, and other payments whose timing is in your control. If you are accelerating a substantial amount of income into the current year, it may be better to take deductions currently. However, some timing decisions, such as prepaying state income tax, may subject you to the AMT. Before making any decisions, consult your advisor.

Individuals whose AGI is greater than an "applicable amount" are subject to an overall limitation of their itemized deductions. This limitation requires that such individuals reduce their allowable itemized deductions by the lesser of (1) 3 percent of AGI over the applicable amount or (2) 80 percent of the amount of itemized deductions that would otherwise be allowable. For 2006, the applicable amount is $75,250 for married persons filing separately and $150,500 for all other persons. For 2007, the applicable amount is $78,200 for married persons filing separately and $156,400 for all other persons. Beginning in 2006, this limit on itemized deductions will be phased out until it is fully repealed effective for tax years beginning after 2009. In 2006-2007, the reduction will be limited to 2/3 of the amount computed under the formula above; for 2007-2008, the reduction will be limited to 1/3 of this amount. Discuss the timing of itemized deductions with your tax advisor in order to minimize your exposure to the 3 percent limitation and the AMT.

☑ **Planning Tip No. 1:** If you are not subject to AMT in 2006, consider paying real estate and property taxes before December 31, 2006, even though payments are not due until early in 2007. Also, consider paying the balance of 2006 state and local estimated income tax payments before the end of the year. By making these payments before the end of the year, taxpayers will be able to include the deduction in their 2006 tax return. However, state and local taxes are not deductible for AMT purposes; therefore, AMT consequences should be taken into consideration before these payments are made.

☑ **Planning Tip No. 2:** Accelerate mortgage payments. In most cases, cash-basis taxpayers can deduct expenses in the year paid. Mortgage payments are usually due on the first of the month. Prepayment of your January 1, 2007 mortgage payment in 2006 provides a deduction for interest related to 2006.

☑ **Planning Tip No. 3:** If you would like to make payments that qualify as itemized deductions prior to year end, but do not have the cash flow available, consider making the payments with your credit card. Some payees may add an additional charge for credit card payments, and the credit card agency will charge interest on any outstanding balances remaining beyond the grace period; therefore, analyze this option carefully before moving forward. If the payee does not charge an additional fee and you are able to fully pay off your credit card obligation before finance charges accrue, this strategy is a method of receiving a short-term interest-free loan to manage the timing of your itemized deductions; and take advantage of any reward programs offered by your credit card agency (e.g., frequent flier miles).

Revisit Stock Option Planning

Traditionally, a favorite form of performance compensation for corporate executives was the granting of stock options. Why? Executives had the flexibility to determine when they wanted to exercise the options and, therefore, controlled the timing of the tax event. However, the AJCA dramatically changed the tax rules applicable to some stock options; specifically, options other than those to purchase employer stock with an exercise price equal to the fair market value of the stock on the date of grant. The new rules will result in significant changes to equity compensation. Discuss the impact of the changes with your tax advisor in order to avoid the negative tax consequences of noncompliance.

Two types of options exist: nonstatutory (also known as nonqualified) options and statutory options (also known as incentive stock options or employee stock purchase plan options). Generally, nonqualified options (NQSOs) generate compensation income when exercised, provided that the stock is not restricted. At exercise, the taxpayer pays tax at ordinary income tax rates on the "spread" between the fair market value of the property received and the exercise price. Historically, taxpayers waited until near the end of the exercise period to delay the tax consequences as long as possible.

Incentive stock options (ISOs) have a different tax consequence, which is not affected by the AJCA. An ISO cannot be granted with an exercise period longer than 10 years, but it can be shorter if the company so chooses. The exercise of an ISO does not affect a taxpayer's regular taxable income; however, the exercise may affect the taxpayer's AMT. Therefore, taxpayers must plan for and control the timing and exercise of ISOs.

☑ **Planning Tip No 1:** Consider exercising incentive stock options (ISOs) and holding the stock for the required holding period to lock in post-exercise appreciation at long-term capital gain rates. A taxpayer is eligible to use the lower capital gain rates if ISO stock is held for two years after the option was granted and more than one year after the option is exercised. The lower capital gain rate makes exercising ISOs more attractive. In some cases, exercising ISOs could trigger AMT, but with careful planning, the AMT may be avoided. Under the AJCA, an eligible person who, in order to comply with federal conflict of interest requirements, sells shares of stock after October 22, 2004 that were acquired pursuant to the exercise of an ISO will be treated as satisfying the statutory holding period requirements for capital gain treatment, regardless of how long the stock was actually held.

☑ **Planning Tip No. 2:** Many taxpayers continue to hold ISOs at retirement. As a general rule, retirees only have 90 days after retirement to exercise the options as ISOs. If you are approaching retirement, determine whether the exercise of any remaining ISOs is beneficial.

Time the Payment of Medical Expenses

Medical expenses are deductible only to the extent they exceed 7.5 percent of AGI. Therefore, grouping or bunching medical costs may allow you to take better advantage of this deduction.

☑ **Planning Tip No. 1:** Many taxpayers do not track the cost of their medical expenses because they do not believe such expenses will exceed 7.5 percent of their AGI. While in general this seems to be a high threshold, there are numerous medical expenses that many taxpayers may forget to consider that may be taken into account in meeting the threshold. A non-exhaustive list of such expenses includes: over-the-counter medical supplies that are not merely for beneficial health (e.g., bandages, aspirin, blood sugar test kits, batteries for a hearing aid), dental treatment, chiropractic treatment, drug treatment programs, psychiatric care, smoking cessation programs, weight-loss programs as a treatment for obesity, laser eye surgery, wheelchairs, and costs to renovate a home for handicap access. A more extensive list of deductible medical expenses can be found in IRS Publication 502, Medical and Dental Expenses.

☑ **Planning Tip No. 2:** If your 2006 medical expenses are approaching the threshold, accelerate any foreseeable medical costs (e.g., expenses for eyeglasses, contact lenses, routine dental work, periodic medical examinations) into 2006. Conversely, if your medical expenses are minimal in 2006, try to defer any additional medical costs into 2007 to be bunched with other 2007 medical costs for deduction purposes and/or flexible spending account purposes. Remember that the amounts reimbursed through a flexible spending account cannot be used in calculating expenses for purposes of the 7.5 percent of AGI threshold. Also, medical expenses below 10 percent of AGI are not deductible for AMT purposes; therefore, AMT consequences should be taken into consideration before these payments are made.

☑ **Planning Tip No. 3:** Generally, if a taxpayer is not self-employed, the payment of health insurance premiums, including long-term care insurance premiums (subject to certain limitations based on age), is a qualified expense that may be included in the calculation to reach the 7.5 percent threshold amount (as long as such premiums are paid directly by the individual and not paid by the individual's employer or reimbursed by a flexible spending account). If you have flexibility in when to pay your premiums, determine whether it is more advantageous to pay the premiums in 2006 or 2007.

☑ **Planning Tip No. 4:** Self-employed individuals who are not eligible to participate in a subsidized health plan (either directly or through a spouse's employer) may deduct 100 percent of their health insurance payments from AGI. Therefore, it may be advisable to accelerate payment of health insurance premiums into 2006 in order to take the deduction in the current year.

Contribute to a Medical Savings Account

A medical savings account (MSA) otherwise known as an Archer MSA, is a tax-exempt trust or custodial account established for the purpose of paying qualified medical expenses in conjunction with a high-deductible health plan (HDHP). Over the past several years, the cost to employers of insuring their employees has sky-rocketed, many times resulting in the employers passing a portion of the costs to their employees in the form of higher deductibles. Employee contributions to an MSA are deductible in computing AGI, and contributions to the employee's MSA by the employer are excludable from gross income. Contributions to an MSA cannot be deducted as a medical itemized deduction. Contributions can only be made to accounts established before 2006.

For 2006, qualifying high deductible insurance must have a deductible for self-only coverage that is not less than $1,800 or more than $2,700, and a ceiling on annual out-of-pocket expenses for covered benefits that does not exceed $3,650. For family coverage, the deductible must not be less than $3,650 or more than $5,450, and the ceiling on out-of-pocket expenses must not exceed $6,650.

For 2007, qualifying high deductible insurance must have a deductible for self-only coverage that is not less than $1,900 or more than $2,850, and a ceiling on annual out-of-pocket expenses for covered benefits that does not exceed $3,750. For family coverage, the deductible must not be less than $3,750 or more than $5,650, and the ceiling on out-of-pocket expenses must not exceed $6,900.

Once the MSA is established, contributions may be made as late as the filing date for the participant's tax return (without extensions). The maximum annual contribution that may be made to a MSA for a year is 65 percent of the deductible under the HDHP in the case of individual coverage and 75 percent of the deductible in the case of family coverage. Excess contributions to MSAs are subject to a 6 percent excise tax.

See IRS Publication 969 for more general information on Medical Savings Accounts.

☑ **Planning Tip:** Unlike flexible spending accounts (discussed below), balances in MSAs may be carried over indefinitely. Upon death, an MSA may be passed on to a surviving spouse without federal tax liability; otherwise, it is included in the gross income of the beneficiary or on the decedent's final tax return.

Establish a Health Savings Account

A health savings account (HSA) is a tax-exempt trust or custodial account established for the purpose of paying qualified medical expenses. It can only be used by those participants in a high-deductible health plan (HDHP).

Both individuals and employers can contribute to HSAs. In general, the definition of a HDHP is less restrictive under the HSA rules than under the MSA rules. Therefore, HSAs may be a good alternative to establishing an MSA. An HDHP is defined as a plan that provides for a minimum deductible of at least $1,050 ($1,100 for 2007) for individual coverage and $2,100 ($2,200 for 2007) for family coverage, and that caps out-of-pocket expenses at $5,250 ($5,500 for 2007) for an individual and $10,500 ($11,000 for 2007) for a family. Individuals must be covered by an HDHP and not covered by another health plan in order to contribute to an HSA; for example, individuals enrolled in Medicare or a non-HDHP employer plan (including a flexible spending account) may not contribute to an HSA. Note that contributions made to MSAs reduce the allowable contributions to HSAs.

Individual contributions to HSAs are deductible for income tax purposes even if the contributor does not itemize. Employer contributions are not subject to income or employment taxes. Distributions from HSAs used to pay medical expenses are tax free. Earnings within the HSA are also tax free. However, distributions used for anything other than medical costs are subject to income tax as well as a 10 percent penalty, unless distributions are made after an individual dies, becomes disabled, or becomes eligible for Medicare.

Both employers and individuals can contribute to an HSA, up to annual limits, in 2006, of $2,700 ($2,850 in 2007) for individuals and $5,450 ($5,650 for 2007) for families. HSA owners between ages 55 and 65 may make larger "catchup" contributions. The maximum contribution to an HSA is computed on a monthly basis. Excess contributions to HSAs are subject to a 6 percent excise tax.

☑ **Planning Tip No. 1:** Consider naming your spouse as beneficiary of your HSA. Upon an HSA owner's death, the HSA passes to the individual named as beneficiary on the account. If the surviving spouse is the beneficiary, he/she is not subject to income tax on distributions so long as they are used for medical expenses. However, if the beneficiary is anyone other than the surviving spouse, the HSA will cease to be an HSA, and the beneficiary will be taxed on the value remaining in the HSA upon the original owner's death.

☑ **Planning Tip No. 2:** There is no deadline by which HSA funds must be spent. The only requirement in order to avoid income taxation and penalties is that HSA funds be used for medical expenses. If there is a balance in an HSA near the end of the year which the account owner does not need, he or she may either leave the funds in the account to pay medical expenses expected in future years or have the HSA make distributions in the current year to cover medical expenses of the account owner's spouse and/or dependents.

☑ **Planning Tip No. 3:** If excess contributions were made to an HSA, distribute the excess contribution and income attributed to such excess contributions to the HSA's owner before the owner's income tax return is due for the year of the excess contributions. Only the income attributable to the excess contribution will be included in the owner's taxable income. The excess contribution will not be subject to income tax or the 6 percent excise tax.

Review Flexible Spending and Pre-Tax Transportation Account Balances

Flexible spending accounts (FSAs) allow pre-tax payments of:

(I) medical and dental costs that are not covered by insurance, and

(II) dependent-care expenses up to $5,000 per year.

(III) Pre-tax transportation programs allow pre-tax payments of certain commuting costs: $105 per month for mass transit ($110 for 2007) and $205 in per month for qualified parking in 2006 ($215 for 2007).

Reimbursements from such plans are not included in gross income; therefore, they escape federal income tax. Although employers may set limits on reimbursable expenses and contributions to FSAs and pre-tax transportation programs lower than the maximum allowed by federal law, most employer plans allow reimbursement for many types of expenses and permit employees to contribute the maximum amount. The enrollment period for these plans typically falls in the last months of the calendar year; therefore, careful planning at the end of 2006 may reap great benefits in 2007.

☑ **Planning Tip No. 1:** The value of flexible spending accounts and pre-tax transportation programs is often underestimated. Assume a family of four has (i) medical costs that are not covered by insurance in an amount of $5,000 per year; (ii) qualified daycare expenses of $5,000 per year; and (iii) commuting costs of $600 per year. If the family has a combined federal and state marginal tax rate of 40 percent, that family may be able to save up to $4,240 ($10,600 x 40 percent) in taxes by participating in a flexible spending account and pre-tax transportation program. Combine this with the fact that the money also escapes social security and Medicare tax, and the savings jump another $800.

Although the funds are deducted gradually throughout the year, the full amount set aside in an FSA for medical costs may be available in January, depending upon your employer's plan.

☑ **Planning Tip No. 2:** Amounts remaining in an FSA for medical costs and dependent care costs must be forfeited at the end of the year (or by March 15 after the close of the year if the employer adopts a grace period). Therefore, individuals should make every effort to use the remaining balance in the account on qualified expenses, such as eyeglasses, contact lenses, medications, hearing aids, medical supplies, and routine dental care, by either the end of the year or the end of the grace period, if applicable.

☑ **Planning Tip No. 3:** Over-the-counter medications (e.g., antacids, allergy medication, pain relievers, and cold medi-cine) that do not require a doctor's prescription may now be reimbursed by flexible spending accounts. However, amounts for dietary supplements (i.e., vitamins) that are merely bene-ficial to general health remain non-reimbursable. Check with your employer's benefit administrator to determine which costs are covered by your company's plan.

Review Miscellaneous Deductions

A defined group of miscellaneous expenses (e.g., unreimbursed employee business expenses, costs of business publications, certain legal and accounting fees, tax preparation fees, financial planning fees, costs of certain investment advice, charges for safe deposit boxes) are deductible to the extent they exceed 2 percent of adjusted gross income (AGI). As with medical expenses, taxpayers should consider bunching these expenses in a single year if they can meet the deduction threshold. Miscellaneous deductions subject to the 2 percent floor are not deductible at all for AMT purposes; therefore, taxpayers should analyze their AMT situation in conjunction with planning their miscellaneous deductions.

Make Gifts to Others

One of the most powerful estate planning techniques is also one of the most simple. Every individual may give up to $12,000 per year in 2006 (same in 2007) in "present interest" (outright) gifts to an unlimited number of donees without paying gift tax or using a portion of their lifetime exemption. Such gifts provide current tax benefits (future income is transferred to a taxpay-er who is, presumably, in a lower tax bracket) and help minimize taxes on the transferor's estate by removing the property from the estate (taxed at rates up to 46 percent in 2006, and 45 percent in 2007-2009). In addition, taxpayers in the lowest two marginal tax brackets pay a lower rate of tax on long-term capital gains (5 percent on sales or exchanges during 2004 – 2010, and zero percent in 2008) and qualified dividends (5 percent for 2004 – 2010, and zero percent in 2008).

To demonstrate the power of gifting, assume a couple has three children. In 2006, this couple can transfer up $24,000 per child or $72,000 to all three children. If each child has a spouse, the maximum amount that can be given to the children and their spouses is $144,000 without incurring a taxable gift. If the couple has grandchildren, their ability to further reduce their taxable estates increases through this gifting program.

Gifts must be made by year-end. If the couple fails to make these tax-free transfers by year-end, they cannot double-up on gifts in 2007 without incurring gift taxes or utilizing a portion of their lifetime exemption amount.

An annual gifting program can shift significant wealth down generational lines. This is especially true if the asset being transferred appreciates and/or generates income that will be excluded from the donors' estates. If a gifting program is desired, you should consider a trust vehicle as the recipient for these gifts. Certain types of trusts (irrevocable grantor trusts) are tax efficient vehicles for transferring wealth.

In addition to the $12,000 per year, per donee annual exclusion, each person has a gift tax exclusion amount of $1,000,000 for gifts made during life. By making lifetime gifts, either outright to children or grandchildren or in trust for their benefit, donors may save a significant amount of transfer tax. For many donors, it makes sense to use the entire gift tax exemption as early in life as possible. The reason is that as the gifted property appreciates, the post-gift appreciation is transferred to the donee and will not be included in the donor's estate. However, note that the beneficiaries will pay capital gains tax when they sell the appreciated assets, as their tax basis is the donor's cost. If the donees are in the lowest two tax brackets, these gains may be taxed at a 5 percent rate (or zero percent rate in 2008). This rate may be lower than the donor's marginal income tax rate.

☑ **Planning Tip No. 1:** If your child has earned income, consider making a cash gift to your child. Your child may use that gift to contribute $4,000 or the amount of the child's earned income, whichever is less, to a traditional IRA or Roth IRA. Funds contributed to a Roth IRA will grow tax-deferred, and qualified distributions will be tax-free for federal income tax purposes. Funds contributed to a traditional IRA may be deductible by your child.

☑ **Planning Tip No. 2:** Certain payments made directly to providers of medical and educational services are not treated as taxable gifts to the recipient of these services. For example, a grandmother who wishes to help pay for a granddaughter's education can write tuition checks directly to the school without making a taxable gift. If she writes the check to the granddaughter, however, she will have made a taxable gift of the amount exceeding the $12,000 annual exclusion. Direct payments to medical and educational institutions should be part of any plan, whether for year-end or throughout the year.

Review Estate Plans

As stated above, in addition to the $12,000 gift tax annual exclusion, every individual taxpayer can transfer a certain amount of property during his or her lifetime without paying gift tax. The amount of property that can pass tax-free is referred to as the exemption equivalent amount. The exemption equivalent amount is used to calculate the credit available to offset the gift tax. For gifts made after December 31, 2001, the exemption equivalent amount for lifetime gifts is $1,000,000. In addition, each taxpayer has a $2,000,000 generation-skipping transfer tax lifetime exemption that is scheduled to increase to $3,500,000 for 2009.

Transfers to a spouse who is a U.S. citizen are covered by the unlimited marital deduction. Therefore, such transfers may be made totally free of gift tax. If your spouse is not a U.S. citizen, there is no marital deduction; instead, the annual exclusion amount is increased for gifts to your spouse to $120,000 in 2006 and $125,000 for 2007. If your spouse is not a U.S. citizen, it is imperative that your estate planner be made aware of this fact.

☑ **Planning Tip No 1:** U.S. citizens and resident aliens are allowed a $1 million lifetime gift tax exclusion; however, nonresident aliens are not afforded the same treatment. Nonresident aliens are generally allowed a credit which exempts only $60,000 of U.S. situs assets from estate tax, but not gift tax. If you or your spouse are not U.S. citizens or resident aliens, check with your estate planning advisor to determine limitations on your gifting techniques.

☑ **Planning Tip No 2:** Review wills and trust agreements. Changes made by the Economic Growth and Tax Relief Reconciliation Act of 2001 may produce unwanted results if your documents were drafted prior to the change in law. For example, assume your net worth is $2 million and you die in 2006. If a credit shelter trust (also known as a bypass trust) is to be established and funded upon your death for the benefit of your minor children, and your will states that the trust should be funded up to the exemption equivalent amount, you could unwittingly leave your entire estate to your minor children and nothing to your surviving spouse. The exemption equivalent amount for estate tax purposes is $2 million for 2006. This amount is scheduled to increase to $3.5 million in 2009; therefore, you may want to consider putting a percentage limitation (or other limitation) on the amount you want to pass to children when the first spouse dies.

Make Gifts to Charities

If you are planning to make a gift to a charity in 2007, consider making the gift in 2006 to accelerate the tax benefit of the contribution. Gifts to qualified charities qualify for an unlimited deduction for gift tax purposes; therefore, the $12,000 limit that applies to gifts to others does not apply to gifts to charities. In other words, outright gifts in any amount can be made to a qualified charity without paying gift tax. Gifts in trust for charity and gifts of partial interests in property, however, may be subject to gift tax. It is also important to note that certain limitations exist with respect to income tax deductions for charitable contributions. See the Deduction Limitations of Outright Charitable Gifts chart on page 48 for more detail.

☑ **Planning Tip No. 1:** Taxpayers planning to make a contribution to a public charity should consider a gift of appreciated securities. By making such a contribution, a taxpayer may be able to deduct the full market value of the gift for both regular and AMT purposes (if the securities were held for more than one year), whereas if the securities are sold and the proceeds donated, both the charity and the taxpayer will receive a lesser benefit.

For example, if a taxpayer contributes an appreciated security that has a basis of $20,000 and a fair market value of $100,000, the taxpayer may take a deduction equal to $100,000 (subject to certain limitations) and the charity receives a gift worth $100,000. If the taxpayer sold the securities, and donated the proceeds (less capital gains tax), the charity would only receive $88,000 [$100,000 – (($100,000 - $20,000) x 15 percent)]. In addition, the taxpayer would receive a lesser tax benefit.

	Gift of Stock	Gift of Proceeds (net of capital gains tax)
Charitable Gift	$100,000	$88,000
Marginal Tax Rate	35%	35%
Net Tax	none	$12,000
Benefit of Gift	$35,000	$30,800

☑ **Planning Tip No. 2:** In addition to receiving a greater tax benefit from donating appreciated securities (rather than cash) to charity, the taxpayer can use the cash that would have been donated to charity to purchase new investments and "refresh" basis. For example, assume a taxpayer would like to provide a public charity with a $100 benefit, and the taxpayer is indifferent as to whether the donation is made in cash or other assets. If the taxpayer has XYZ stock in his portfolio, which has a cost basis of $10 and a fair market value of $100, donation of the stock to the charity will provide the taxpayer with a charitable deduction of $100, subject to certain limitations. The taxpayer can then use the $100 that he would have otherwise donated to charity to repurchase XYZ stock. The basis of the taxpayer's "new" XYZ stock is $100. In effect, the taxpayer received a step-up in basis of his XYZ stock from $10 to $100 in addition to meeting his charitable goals. Remember that the wash sale rules only apply to losses upon sale, not gains; therefore, the wash sale rules are inapplicable to this situation.

☑ **Planning Tip No. 3:** Gifts of $250 or more require a contemporaneous, written description of the contribution from the charity in order to qualify for the charitable contribution deduction. A cancelled check is not sufficient to support the deduction. Also, any gift in excess of $5,000, other than cash or stock in a publicly traded company, requires an appraisal from a qualified appraiser in order to qualify for the deduction.

In the case of gift of cash, you must maintain a cancelled check, bank record, or receipt from the donee organization showing the name of the donee organization, the date of the contribution, and the amount of the contribution. This new substantiation requirement was created by the Pension Protection Act of 2006 and applies to all gifts of money, regardless of the amount, made in years beginning with 2007.

If you donate a used vehicle, boat, or airplane worth more than $500, the deduction will equal the fair market value of the contribution only if the charity uses the property in its tax exempt function. If the charity sells the item, your deduction will generally be limited to the proceeds the charity actually receives. The charity will be required to furnish donors with a receipt that documents sales proceeds.

When making a non-cash donation, consider the following requirements:

Documentation of Charitable Deductions	
$250 to $500	A written acknowledgment from the charitable organization is required.
$501 to $5,000	In addition to a written acknowledgement, a taxpayer must show the means of acquisition, the date acquired, and the adjusted basis of the property.
More than $5,000	Most contributions over $5,000 require a written appraisal. (Publicly traded securities do not require written appraisals).
More than $500,000	Donors required to attach written appraisal to tax return, if appraisal is required.

☑ **Planning Tip No. 4:** Consider contributing to a donor-advised fund (DAF). A DAF is a fund that is managed under the tax umbrella of a public charity such as a community foundation. The donor makes an irrevocable gift of property (such as stock) to the host charity, and receives a fair market value tax deduction in the year of the gift. Assets are deposited into an investment account where they can grow tax-free. The donor retains the right to advise (but not to direct) the host charity in administering the affairs of the DAF.

Depending on the policies of the host charity, this advice may include naming the fund, managing investments, recommending grants, and selecting a replacement advisor at the death of the donor. DAF funds cannot benefit the donor or any other private interest.

☑ **Planning Tip No. 5:** If you are over 70 1/2, considering using assets in your IRA or Roth IRA to fund your charitable contributions during 2006 and 2007. The maximum amount of IRA funds that can be directed to charity is $100,000 per year and no itemized deduction is permitted. However, the distribution from the IRA is not included in income, and the distribution qualifies as part of the annual required minimum distribution.

Review Investments in Retirement Accounts

Successful retirement planning begins long before retirement. In fact, most of us should be accumulating capital throughout our working careers to sustain us in later years. Sound retirement planning involves reviewing your entire financial life. While taxes are obviously not the only issue, they are central to retirement planning. The tax-related decisions you make today, and at various points in your career, may have a marked effect on how you save for retirement and how much you will have down the road to support your goals. Many tax decisions you make about retirement are one-time choices that can be very costly to change, so it pays to plan.

☑ **Planning Tip No. 1:** Sole proprietors or partnerships may establish a Keogh plan for themselves and their employees. Although contributions do not have to be made until the due date of the tax return (including extensions), the plan must be established by year end. For 2006, self-employed individuals may contribute the lesser of $44,000 ($45,000 for 2007) or 100 percent of self-employment income to a defined contribution Keogh plan. However, any non-deductible amount (generally, any amount above the lesser of $44,000 ($45,000 for 2007) or in the case of plans for self-employed individuals with no employees, 20 percent of net self-employment income) is subject to a 10 percent excise tax; therefore, self-employed individuals generally contribute only the lesser of $44,000 ($45,000 for 2007) or 20 percent of their net self-employment income. Older individuals should consider establishing a defined benefit Keogh plan, which will likely allow a higher contribution amount.

☑ **Planning Tip No. 2:** An owner/employee of an S corporation without other employees should consider establishing a defined benefit plan. Generally, contribution amounts will be higher for the owner/employee through a defined benefit plan versus a defined contribution plan. In addition, contributions to the defined benefit plan may be made in a year in which the owner/employee does not receive any compensation (or earned income for persons considered self-employed). In contrast, contributions to a defined contribution plan are limited to the lesser of $44,000 ($45,000 in 2007) or 100 percent of compensation (or earned income for persons considered self-employed); therefore, if no compensation is received by the owner/employee, no contribution can be made to a defined contribution plan for that year.

☑ **Planning Tip No. 3:** In addition to Keogh plans, self-employed individuals are eligible to establish solo 401(k) plans and SEP IRAs. Solo 401(k) plans must be established prior to year-end, whereas a SEP IRA may be established and funded at the time of filing the individual income tax return (including extensions). Each plan has its advantages and disadvantages; therefore, self-employed individuals should discuss retirement plan options with their financial advisor to determine which plan works best for them.

☑ **Planning Tip No. 4:** Earning compensation for serving on a company's board of directors may qualify as self-employment income, and therefore, be subject to self-employment taxes. An individual earning self-employment income may qualify to invest in a Keogh or other self-employed retirement plan. Qualification as self-employment income may be possible even if the individual is an employee of the company, as long as the compensation is sufficiently segregated from wage income. The rules in this area are complex; individuals earning director fees should discuss this topic with their financial advisor.

☑ **Planning Tip No. 5:** Analyze contributions to employer-sponsored 401(k) plans. The maximum contribution to a 401(k) plan is $15,000 for 2006 and $15,500 for 2007. Many investors have considered stopping contributions to their 401(k) plans in favor of investing in currently taxable accounts due to the lower capital gain and dividend rates. However, the amounts contributed to a 401(k) plan are "pre-tax," which may lower your current tax bill, and affect AMT planning. Also, if the taxpayer's employer offers employer-matching contributions, the employee is giving up "free" money. Taxpayers are strongly encouraged to talk to their investment advisor to determine whether funds should be invested in a currently taxable account or tax-deferred account.

☑ **Planning Tip No. 6:** Consider making contributions to a Roth IRA. Although contributions to a Roth IRA are never deductible, any income earned within the Roth IRA may be free from federal income tax when the individual withdraws money from the account. For 2006-2007, the maximum annual contribution that may be made to Roth IRAs is $4,000. The maximum permitted annual contribution is phased out as income increases, so it is important to check with your tax advisor. Unlike traditional IRAs, individuals may continue to make contributions to a Roth IRA after reaching age 70 1/2.

☑ **Planning Tip No. 7:** Individuals who are age 50 or over by year-end may make additional "catch up" contributions to their retirement plans. For a 401(k) plan, an individual may make additional contributions of $5,000 in 2006 and 2007. Check with your plan administrator for the proper procedure to make catch up contributions to your 401(k) plan. For an IRA or Roth IRA, an individual may make additional contributions of $1,000 for 2006 and 2007. Participants in SIMPLE plans may make additional contributions of $2,500 in 2006 and 2007.

See the chart for more detailed information on the contribution amounts to retirement plans.

Contribution Limits to Retirement Plans	2006	2007
Individual Retirement Account (IRA)		
Under age 50	$4,000	$4,000
Age 50 or above	$5,000	$5,000
Roth IRA		
Under age 50	$4,000	$4,000
Age 50 or above	$5,000	$5,000
401(k) or 403(b) (Tax-Sheltered Annuity or "TSA")		
Under age 50	$15,000	$15,500
Age 50 or above	$20,000	$20,500
Simple retirement account (SIMPLE)		
Under age 50	$10,000	$10,500
Age 50 or above	$12,500	$13,000
Keogh or SEP-IRA		
(Limited to the lesser of the amount at right or 20% of net self-employed income)	$44,000	$45,000

☑ **Planning Tip No. 8:** Consider establishing a spousal IRA. A spouse who has little or no earned income, and who is not an active participant in an employer-sponsored retirement plan, can still have an individual retirement account (IRA). The maximum contribution to a spousal IRA is the lesser of $4,000 or the combined taxable compensation of both spouses. The deduction for such contribution is phased out for married taxpayers filing jointly who have adjusted gross income (AGI) between $150,000 and $160,000. After 2006, the contribution limits are indexed for inflation. The 2007 adjusted gross income limitation begins at $156,000. Although the contribution may not be deductible, the amounts contributed will still grow tax-deferred; therefore, this may still be a good retirement planning option.

☑ **Planning Tip No. 9:** Make contributions to your own IRA prior to year-end even though the contributions are not due until April 15. Making contributions earlier increases the effect of compounding on retirement account earnings. As with the spousal IRA, the contribution may not be deductible, but your contribution will grow tax-deferred. If your contribution is deductible, your AGI will be lower, possibly allowing you to take advantage of certain credits that are limited by AGI levels – take this into consideration when making year-end decisions. Taxpayers are allowed to contribute to both a 401(k) plan and an IRA in the same year; however, if you contribute to a 401(k) plan, your ability to deduct contributions to an IRA in the same year will be limited if your adjusted gross income exceeds $75,000 ($80,000 in 2007) for joint filers.

☑ **Planning Tip No. 10:** An excise tax is imposed on excess contributions to various savings vehicles. Generally, excess contributions to an IRA, medical savings account, health savings account, or Coverdell account (also known as an Education IRA) are subject to a 6 percent excise tax. Excess contributions to other qualified plans (e.g., 401(k)) are subject to a 10 percent excise tax. In addition, contributions to Keogh and pension plans in excess of the deductible amount are subject to a 10 percent excise tax. To avoid potential excise taxes, correct excess contributions before year-end.

Consider Converting Your Traditional IRA to a Roth IRA in 2006

In some cases, it may be advantageous to convert an IRA to a Roth IRA. Although the amount rolled-over or transferred from a traditional IRA to a Roth IRA generally must be included in gross income, qualified distributions from a Roth IRA are tax-free, including the income and appreciation components of such distributions. In order for a distribution to be a "qualified distribution," a five-year holding period must be satisfied, and one of the following four requirements must be met:

1. The distribution is made on or after the date on which the individual attains age 59 1/2;
2. The distribution is made to a beneficiary or the individual's estate after the individual's death;
3. The distribution is attributable to the individual's being disabled; or
4. The distribution is to pay for certain qualified first-time homebuyer expenses (up to $10,000).

The five-year holding period is separately determined for each conversion contribution.

Additional advantages of Roth IRAs are that contributions are permitted after the individual reaches age 70 1/2 and the mandatory distribution rules applicable to traditional IRAs during the lifetime of the owner do not apply.

Only individuals with modified adjusted gross income below $100,000 may convert their traditional IRAs to Roth IRAs. In years before 2005, required minimum distributions from IRAs were counted toward this $100,000 limitation, resulting in many individuals not qualifying for conversion. Beginning on January 1, 2005, required minimum distributions are not counted toward the $100,000 limitation. If you currently have IRA accounts, you should discuss the possibility of converting to a Roth IRA with your tax advisor. While income taxes would be due currently, you and your heirs may have more after-tax wealth as a result of the conversion.

Review Investment Plans

Achieving investment success in today's investment environment is challenging, but attainable. Investors have more choices and greater challenges than ever before: an unlimited number of investment products and strategies, more volatile markets, mutual fund shake-ups, greater personal responsibility for retirement security, changes to tax laws, and a flood of alarming and often conflicting statistics and predictions. Keeping your focus on the basic tenets of investing will increase your chances for success. With investment success comes the realization of your personal financial goals, the ultimate reason that you invest today.

Although tax consequences should not be the only consideration in making investment decisions, proper tax planning can help you meet your financial goals. Tax-aware asset allocation considers the tax efficiency of an investment, the type of vehicle holding the asset (e.g., taxable, tax-deferred, or tax-free growth), and its investment return potential to create the most tax-beneficial mix of investments in a portfolio. You must consider all of these factors, or work with a qualified investment advisor, to determine the best mix of assets and best placement of those assets for your situation.

Determine, quantify, and prioritize your financial goals. Design an asset allocation strategy. Prepare an investment policy statement. Implement the policy. Monitor and review performance. Rebalance your portfolio. These are the basic tenets of investing, and if followed, you will be well on your way to your financial goals.

☑ **Planning Tip No. 1:** As you are reviewing your investment portfolio for possible opportunities to offset capital gains with capital losses, perform an "x-ray" of your mutual funds to determine the holdings within each fund. If several of your mutual funds contain the same holdings, you may be incurring additional costs without the intended diversification.

☑ **Planning Tip No. 2:** Consider amortizing any taxable bond premiums to convert a deferred capital loss to a current ordinary loss. The election applies to all taxable bonds held during or after the taxable year for which the election is made and may not be revoked without IRS permission.

☑ **Planning Tip No. 3:** Reevaluate mutual funds with high expense ratios. The reduced tax on dividends results in a substantial increase in the after-tax cost to own these funds. In other words, a dollar of expense, offset by a dollar of dividend, will now save 15 cents instead of 35 cents.

☑ **Planning Tip No. 4:** Consider electing to use the "specific identification" method for computing cost basis on mutual funds. Volatile markets may allow for year-round tax loss harvesting if you dollar-cost average into a particular fund during the year. Additional record-keeping will be necessary; however, the extra benefit may be well worth the effort.

☑ **Planning Tip No. 5:** Consider tax implications when deciding where to place a particular asset class. Less tax efficient asset classes, such as REITs and taxable bonds, should be placed in a tax-deferred account, such as an IRA or 401(k). As a general rule, "buy and hold" growth-oriented strategies are more tax efficient than value strategies. Likewise, large-cap funds are generally more tax efficient than mid- and small-cap funds.

☑ **Planning Tip No. 6:** Consider ETFs (exchange traded funds) to take advantage of lower expense ratios, greater tax efficiency, and more trading flexibility. ETFs trade like stocks, which allows for intra-day purchase and sale, whereas mutual fund transactions are priced at the close of the market.

Examine Distributions from Tax-Preferred Retirement Savings

In general, a 10 percent early withdrawal penalty applies to distributions from qualified plans and IRAs for participants who have not yet reached age 59 1/2. Numerous exceptions exist to this general rule; therefore, if you have a need to withdraw funds prior to age 59 1/2, you are strongly encouraged to consult with your financial advisor.

Generally, taxpayers who have reached age 70 1/2 by December 31 must start receiving required minimum distributions from qualified plans or severe penalties will be assessed. Generally, minimum distributions must begin for the calendar year in which the taxpayer reaches age 70 1/2 (or when the taxpayer retires, if later) and must be paid no later than April 1 the following year. For every year thereafter, distributions must be made by the end of the year. Therefore, if the first distribution is delayed until the year following the individual reaching age 70 1/2, two distributions will be required in that year (one by April 1 and one by December 31). For subsequent years, only one distribution will be required by the end of the year. The rules differ between self-employed individuals and non-self-employed individuals, so check with your financial advisor to determine whether you are subject to special rules.

☑ **Planning Tip No. 1:** In general, a penalty is imposed on withdrawals from a qualified plan or IRA prior to age 59 1/2. Ideally, funds will not need to be withdrawn prior to retirement; however, where funds are withdrawn from a qualified plan or IRA prior to age 59 1/2, the withdrawal may take place without penalty if the participant dies or suffers a qualified disability. In addition, funds may be withdrawn without penalty under the following circumstances: (1) the payments are made following separation from service after attaining age 55 (not applicable to IRAs), (2) the payments are made in a series of substantially equal payments over the life of the participant (or joint lives of the participant and beneficiary); (3) distributions are used to pay qualified medical expenses that exceed 7.5 percent of AGI; (4) distributions are made to a nonparticipant under a qualified domestic relations order; or (5) for certain distributions made by employee stock option plans ("ESOPs") of dividends on employer securities.

Separate exceptions apply to distributions from other tax-deferred plans (such as SEP IRAs, SIMPLE plans, Keoghs, and 401(k) plans), as well as IRAs and Roth IRAs; therefore, you are encouraged to discuss your options with a qualified financial advisor.

☑ **Planning Tip No. 2:** Although the first required minimum distribution does not need to be paid until April 1 of the year following the year the taxpayer reaches age 70 1/2, postponement of the initial payment will result in "doubling up" on payments in the following year. For example, if a taxpayer reaches age 70 1/2 in 2006, the first required minimum distribution does not need to be paid out until April 1, 2007. However, the required minimum distribution for 2007 must be received by December 31, 2007, resulting in two payments in 2007. This may push the taxpayer into a higher tax bracket in 2007 and affect other tax planning strategies.

☑ **Planning Tip No. 3:** If you are over 70 1/2, considering using assets in your IRA or Roth IRA to fund your charitable contributions during 2006 and 2007. The maximum amount of IRA funds that can be directed to charity is $100,000 per year and no itemized deduction is permitted. However, the distribution from the IRA is not included in income, and the distribution qualifies as part of the annual required minimum distribution.

☑ **Planning Tip No. 4:** The required minimum distribution rules do not apply to Roth IRAs during the lifetime of the owner. Distributions from Roth IRAs are required after the death of the participant if the spouse is not the beneficiary. When the spouse is the beneficiary of a Roth IRA, the Roth IRA may be treated as owned by the surviving spouse after the death of the first spouse. For traditional IRAs, required minimum distributions must be made by April 1 of the year following the year the taxpayer reaches age 70 1/2, even if the taxpayer has not retired.

☑ **Planning Tip No. 5:** In certain situations, an individual may receive a distribution of employer securities out of a qualified retirement plan while deferring taxation on unrealized gain until the securities are subsequently sold. At that point, realized long-term capital gains will be eligible for the lower rates and can be offset by capital losses from other investments. Check with your financial advisor if you currently own employer securities inside of a qualified plan and anticipate a distribution, in order to create a favorable tax strategy.

An excess accumulation is any amount of a required minimum distribution that is not timely distributed. A hefty 50 percent excise tax is imposed for each year the excess is not distributed. Although penalties may be waived under certain circumstances, taxpayers should make every effort to comply with the required minimum distribution rules.

Establish Education Savings Accounts

With the ever-increasing cost of college tuition, planning early for your children's education has never been more important. However, even if your children (or grandchildren) are only one year away from starting college, some planning is still better than no planning.

Utilizing qualified tuition programs (QTPs, otherwise known as section 529 plans) and Coverdell accounts (formerly known as Education IRAs) are two methods of saving for educational costs. Contributions to a Coverdell account are limited to $2,000, and may be made as late as April 15 of the year following the year to which the contribution applies. The ability to contribute to a Coverdell account phases out for joint filers with AGI between $190,000-$220,000. In contrast, there is no AGI limitation for contributors to a 529 plan, and contributions may be over $200,000, depending upon the particular plan limitations.

In general, all funds in a Coverdell account must be distributed by the time the beneficiary reaches age 30 or taxes and penalties will apply. Although each 529 plan has its own rules, generally, there is no age limitation on when funds must be distributed, and any unused funds may be rolled over to a plan for another member of the beneficiary's family.

In most cases, qualified distributions from Coverdell accounts and 529 plans are tax free for federal purposes. Tax treatment for state purposes varies from state to state. To the extent a distribution from a Coverdell or 529 plan is excluded from income, the excluded amount must reduce the amount of tuition paid for purposes of taking the Hope Scholarship and Lifetime Learning Credits. Check with your financial advisor for specific advice regarding the tax treatment of distributions from educational savings accounts.

☑ **Planning Tip No. 1:** Taxpayers are allowed to contribute to both a 529 plan and Coverdell account in the same year. Education credits (e.g., the Hope Scholarship Credit and Lifetime Learning Credit) may also be used in conjunction with a 529 plan and/or Coverdell account, provided that sufficient qualified expenses are incurred to cover all three benefits and all other requirements are met.

☑ **Planning Tip No. 2:** Taxpayers who make gifts to section 529 plans may be able to take advantage of a provision that allows the value of the gift to be taken into account ratably over five years. This allows the taxpayer to "frontload" contributions by making a $60,000 ($120,000 in the case of a married couple) contribution to a section 529 plan without gift tax consequences. The taxpayer must make an election (by filing a gift tax return) to utilize five years worth of annual exclusions in order to obtain this treatment. For example, if a taxpayer makes an election to treat a $60,000 transfer made to a 529 plan in 2006 as having been made ratably over five years, they will be deemed to have utilized annual exclusions for the years 2006 through 2010 for the beneficiary of the 529 plan. In the event of an increase in the annual exclusion between the contribution year and the end of the five year period, the taxpayer may make an additional gift to the beneficiary of the 529 plan for the 2007-2010 years without paying gift tax or utilizing lifetime exemption as long as the additional gift is less than or equal to the annual exclusion available in that year less the $12,000 deemed utilized by virtue of the election made in 2006. The ability to make the five-year election is scheduled to expire on December 31, 2010 under current law.

☑ **Planning Tip No. 3:** If your state allows a state tax deduction for contributions to section 529 plans, consider making the contribution prior to year-end in order to take advantage of the deduction on your 2006 tax return. However, taxpayers subject to state AMT may not be able to take advantage of the deduction. Investigate other state plans that may provide lower expenses and more investment options as these attributes may outweigh the state income tax savings.

☑ **Planning Tip No. 4:** Section 529 plans may only be used to pay for qualified higher education expenses (i.e., college or graduate school tuition, fees, books, supplies, and room and board) for college or graduate school. However, Coverdell accounts may be used to pay for elementary and secondary education expenses as well as college or graduate school expenses. Eligible Coverdell covered expenses include tuition, fees, books, supplies, equipment, room and board, tutoring, uniforms, transportation, and even computer equipment, subject to certain limitations.

☑ **Planning Tip No. 5:** Due to recent state budget crises, soaring tuition, and poor investment returns, some states are halting new enrollment in some 529 prepaid tuition plans or are prohibiting current participants from making contributions in 2007. Check the plans you are currently invested in (or are planning to invest in) to determine whether contributions can and should be made in 2006.

☑ **Planning Tip No. 6:** Even if you do not plan to establish an education savings account for yourself or others, keep in mind that certain educational expenses, such as interest on an education loan and tuition and fees required for the enrollment or attendance at an eligible educational institution, are deductible (subject to certain limitations).

Examine State Planning Opportunities

Most tax planning focuses on saving federal taxes. However, state tax planning, especially for individuals living, working, or holding property in states with high tax rates, is equally important. Some individuals work and earn income in more than one state, requiring an analysis of the tax laws of several states as well as the possibility of filing several different state income tax returns. State laws vary widely, and the interaction between laws can be complicated. This guide cannot possibly cover all aspects of state tax planning; therefore, we encourage you to consult with your local tax advisor for more detailed state tax planning techniques.

☑ **Planning Tip No. 1:** Many states offer special business incentives to those who work in or operate a business in that state. For example, multiple states offer an enterprise zone credit that may offset sales tax or provide significant hiring credits. Businesses located in the New York Liberty Zone (NYLZ) or those that relocated from the NYLZ to another part of New York City due to the September 11 attacks may also be eligible for significant federal tax benefits.

☑ **Planning Tip No. 2:** Certain states may allow a discount for early payment of taxes. For example, some Florida counties provide a discount of up to four percent for early payment of property taxes. However, these discounts should be examined in conjunction with AMT planning.

☑ **Planning Tip No. 3:** Taxpayers (including trusts) who have a sufficient "nexus" with more than one state may owe taxes and have reporting requirements in multiple states. Nexus may be created through a variety of contacts; however, the most common are working in another state, owning property in another state, or engaging in a business activity in another state. Trusts may have "nexus" due to the residency of the beneficiary or the trustee. To complicate matters, each state may have its own definition of nexus, residence, and domicile. Credits may be available in your resident state to offset taxes paid to other states; therefore, you are strongly encouraged to check with your local tax advisor to determine where taxes may be due, what credits may be available, and whether a return must be filed in more than one state.

In addition to a separate income tax, many states have their own gift, estate, and inheritance taxes. In other words, you may be liable for not only federal taxes in these areas, but also state taxes. Individuals living in states that have decoupled from the federal estate tax may end up paying more in overall estate taxes even as the federal estate tax rate drops. Consideration of state taxes must be part of any taxpayer's overall financial planning, especially individuals who are considering moving to another state upon retirement. Although income taxes may be saved by the move, total taxes in the new locale may create an unexpected tax burden.

Manage Passive Gains and Losses – Individuals

Net losses from passive activities cannot be deducted currently against income from other sources. Instead, these losses are suspended, to be deducted when the activity that generated the loss is disposed of in a taxable transaction or when the taxpayer's passive activities begin generating taxable income. Credits arising from passive activities are subject to similar rules. In addition, donations (either to family members or charity) do not permit the use of suspended passive losses.

The tax law treats two types of activities as passive activities. The first is any business activity in which the investor does not materially participate. The second is most rental activities, regardless of the investor's level of participation (subject to special rules for real estate professionals).

Individuals who own rental properties and are actively involved in the management decisions of such property are able to deduct up to $25,000 of losses per year against other income. The deduction is phased out for AGI between $100,000 and $150,000.

☑ **Planning Tip No. 1:** Increase your participation in what would otherwise be treated as a "passive activity" or dispose of passive activities with suspended losses or credits. This could allow you to currently use passive activity losses or credits that otherwise would be deferred. Alternatively, ask your tax advisor whether decreasing your participation in a profitable business activity will make the income passive so that it can be sheltered by losses from other passive activities.

☑ **Planning Tip No. 2:** Passive losses that are "freed up" (generally, through disposition of the activity) may be used to offset ordinary income. In addition, any applicable capital gains generated by the disposition may be eligible for the lower 15 percent rate and will be treated as passive income to allow utilization of suspended passive losses from other activities. Timing of the disposition of a passive activity should be carefully coordinated with other activities throughout the year in order to provide the best overall results.

☑ **Planning Tip No. 3:** Remember that generally, a disposition must be part of a taxable transaction to "free up" any suspended losses. If the activity that generated the passive losses is disposed of in a transaction other than a taxable sale, the suspended losses may be lost to the original holder. For example, if the activity is transferred by gift, suspended passive losses are added to the donee's (recipient's) basis and are not deductible by the donor. If by divorce, the suspended passive losses are added to the basis of the spouse who receives the property, and the spouse who gives up the property loses the suspended losses. If by sale to a related party, the suspended losses remain as suspended losses to the seller – when the related party sells the property to an unrelated party in a taxable transaction, the original seller may be able to deduct any remaining suspended losses. If a decedent holds a suspended passive loss upon death, the passive loss is reduced to the extent of any stepped-up basis, and the remainder is deductible on the decedent's final return. This is a complicated area of the law, and taxpayers are encouraged to discuss passive activity planning with their tax advisor.

☑ **Planning Tip No. 4:** Each passive activity may also have a suspended AMT loss. Suspended AMT losses are generally smaller than their regular tax counterparts because each passive activity's AMT preferences and adjustments are "added back." The difference between the regular tax and AMT suspended passive loss is recognized as a separate AMT adjustment in the year of disposition. If the difference is significant, any regular tax benefit may be lost in increased AMT. Further compounding the problem is that the AMT basis of the disposed passive activity will be greater than regular tax basis in an amount roughly equal to the difference between the regular and AMT suspended losses. The result is reduced AMT capital gain (thus decreasing the applicability of preferential capital gain rates), or worse, creation of an AMT capital loss, which will be deductible only up to the capital loss limitation of $3,000. Obviously, this is a very complicated area, and you are strongly encouraged to discuss AMT issues with your tax advisor.

Review Split-Dollar Insurance Arrangements

The Internal Revenue Service has released guidance regarding the taxation of split-dollar life insurance arrangements. Split-dollar arrangements split the costs and benefits of a life insurance policy between a sponsor (employer/donor) and a benefited party (employee/irrevocable life insurance trust or other donee). The arrangements have been a popular method of providing supplemental retirement income to employees and making tax leveraged gifts of life insurance policies within estate plans.

Rules governing the taxation of split-dollar life insurance arrangements are complex and extremely dependent on the specific terms of a given arrangement. The tax consequences can be costly, especially in agreements involving irrevocable life insurance trusts where policy cash values are inaccessible and taxes must be paid from the employee's personal assets.

Review Disability Insurance Options

If a taxpayer pays the disability insurance premium on his or her own policy (versus the employer paying the premium) or pays amounts for employer-provided coverage with after-tax dollars, any disability benefits paid to that taxpayer will not be taxable. This would mean that less coverage is needed than under a policy the premiums of which are being paid by the employer. It is important to understand how compensation is defined for purposes of a particular disability policy. For example, if bonuses are not included in the definition of income, coverage under the policy may be lower than expected.

Obtain Taxpayer Identification Numbers for Dependents

The IRS may deny both the personal exemption and the dependent care credit if a tax return does not include a taxpayer identification number (usually, a social security number) for each dependent. Failure to provide a taxpayer identification number is treated as a clerical error, which allows the IRS to assess tax without conducting an audit.

Use Low Interest Rates to Optimize Family Wealth Planning

Although interest rates have risen from their historic lows in mid-2003, rates are still much lower than in years past. Many taxpayers have already taken advantage of low interest rates by refinancing their homes, utilizing home equity lines, and purchasing assets at low rates. However, perhaps the most powerful use of the low interest rates involves various gift and estate planning strategies that will optimize family wealth.

The value of annuities (other than commercial annuities), life estates, term interests, remainders and reversions for estate, gift, and income tax purposes is determined by tables issued under section 7520 of the Internal Revenue Code. The rate changes monthly; however, the Internal Revenue Service generally releases the rate for the following month approximately 2 weeks prior to the beginning of that month. Therefore, taxpayers have the advantage of limited foresight – for example, they will know in mid-November whether rates will rise or fall in December.

Following is a brief list of family wealth planning strategies that work well in a low interest rate environment.

Grantor Retained Annuity Trust (GRAT). A GRAT is an irrevocable trust into which the taxpayer (the Grantor) transfers appreciating assets and retains an annuity for a term of years (generally, a minimum of 2 years). The GRAT is a statutory technique that allows a taxpayer to move future appreciation of an asset to another person free of gift tax. At the end of the annuity term, the remaining assets can either be retained in trust for the taxpayer's beneficiary(ies) or distributed outright to such beneficiary(ies). The ideal assets for funding a GRAT would include: publicly traded stock that is depressed in value and has reasonable prospects of rebounding within the next 2 or more years; stock in a company planning an IPO, sale, or other merger or acquisition in the near future; or, any other asset that is expected to rise in value more than the federal interest rate (Section 7520 Rate).

Intra-Family Loan. An effective estate planning technique is available in this current low interest rate environment. A taxpayer may loan funds to children (or other family members) under a promissory note that bears an interest rate that is not less than the AFR for the term of the note. Although the AFR is usually lower than the commercial rates, the difference in rates is not a gift. The loaned funds can be used by the taxpayer's children to acquire assets that appreciate faster than the rate on the borrowed funds. Thus, the appreciation in excess of the loan and interest rate inures to the benefit of the children. This transaction will have the benefit of: 1) removing appreciating assets from the taxpayer's estate (in other words, freeze the value of the estate at the value of the note, plus the interest); 2) transferring wealth in excess of the note and interest free of gift tax.

The note may also be structured with flexible terms. For example, the note may be structured as an interest only note with a balloon payment at the end of the term. This loan arrangement may also be used to provide current income to the lenders. For example, assume the taxpayer's child is interested in purchasing a home, but does not have sufficient cash. The taxpayer may loan the necessary amount to the child at the AFR. If this rate is lower than commercial rates, the child saves on the rate differential. The rate may also be higher than rate the taxpayers receive through a savings account, for example. Thus, the taxpayer benefits through higher interest income.

Consideration should be given as to whether the loan term should be long term or short term. Short term loans will have lower AFR rates; however, the borrower is at risk of rate increases to the extent the loan is still outstanding.

There are transfer tax risks involved in intra-family loans. The loan arrangement must not appear to be a disguised gift. The lender should document the borrower's ability to repay the note, and the lenders must intend to enforce and collect the note. Disclose intra-family transactions (including intra-family loans) on a gift tax return to start the statute of limitations.

Taxpayers are encouraged to consult with their financial advisors to discuss the advantages and disadvantages of intra-family loans.

Installment sales. Installment sales allow a taxpayer to sell an interest in property to other family members for a combination of cash and an installment obligation. As long as the sale is for the property's fair market value, no adverse gift or estate tax consequences arise on the transfer or sale. The installment debt is included in the taxpayer's estate at its face value, and future appreciation may pass to heirs free of gift, estate, and generation-skipping transfer taxes. The income tax consequences are the same as if the sale were to a third party; taxable income will be recognized as payments are made on the note. There may be disadvantages to installment sales, so be sure to review any potential sale with a tax advisor.

Self-Canceling Installment Note. Another option is for a taxpayer to sell assets in exchange for a self-canceling installment note. The note is designed to automatically extinguish at the seller's death. The note term should not be longer than the expected life of the seller. A self canceling installment note ("SCIN") will provide that upon the death of the seller, no further payments (of principal or interest) will be payable; notwithstanding that the full amount of principal has not been paid. There is a premium assigned to the installment note interest rate which establishes that the parties "bargained for" the SCIN provision. If the taxpayer dies before the end of the installment sale term, there may be taxable gain to report on the estate's first income tax return. However, any note balance remaining upon the taxpayer-seller's death is excluded from the seller's taxable estate. As with the private annuity, as long as an appropriate interest rate is charged and the note represents fair market value of the asset purchased, no gift tax will be due, and the seller is able to remove assets from his or her estate. However, the seller should disclose the intra-family sale on a gift tax return to start the statute of limitations. If the sale is not disclosed, the IRS may dispute the value of the property sold, and attempt to assess a gift tax up to four years after the death of the seller.

Charitable Lead Trusts. In a charitable lead trust, a taxpayer (the grantor) transfers assets to an irrevocable trust, which provides that a charity will receive payments for the life of the trust. At the end of the term, the assets are transferred to the named remainder man of the trust, often the grantor's children or grandchildren. The grantor removes the asset from his or her estate, provides benefit to the named beneficiaries, and may enjoy a charitable contribution deduction in the year the assets are transferred to the trust. Lower section 7520 rates result in lower gift tax values and higher charitable contribution deductions in the year of transfer. The income tax ramifications to the grantor vary greatly, depending upon whether the trust is classified as a "grantor trust" or a "non-grantor trust"; therefore, consult with your tax advisor prior to establishing this type of trust to ensure you fully understand the potential tax consequences.

Tax Shelter Disclosure Requirements

This summary is designed to help you better understand the tax shelter disclosure requirements so that you can provide your tax advisor with the information necessary to evaluate your tax shelter disclosure obligations, if any. Due to the complicated nature of these rules, this summary cannot comprehensively cover all of the complex issues presented by this subject. Therefore, we encourage you to discuss this matter further with your tax advisor if this overview prompts any questions or concerns.

Failure to properly disclose any transactions or arrangements in which you directly or indirectly participated that are deemed to be reportable transactions may result in the imposition of significant penalties.

The regulations describe five categories of transactions that are deemed "reportable transactions." Reportable transactions must be disclosed in your tax return as well as separately filed with the IRS Office of Tax Shelter Analysis. A brief description of the five categories follows:

1. Listed Transactions. A "listed transaction" is a transaction that is the same as or substantially similar to a transaction that the IRS has determined to be a tax avoidance transaction. Currently, the IRS has identified more than 30 listed transactions, which can be viewed in more detail at www.irs.gov/businesses/corporations by clicking on "Abusive Tax Shelters and Transactions." A transaction that was not considered a reportable transaction at the time you entered into it may nonetheless become subject to the reporting requirements if the IRS subsequently classifies the transaction as a "listed" transaction as further described below.

2. Confidential Transactions. "Confidential transactions" are those offered under conditions of confidentiality. A transaction is considered offered under such conditions if the taxpayer's disclosure of the tax treatment or tax structure of the transaction is limited in any manner by an express or implied agreement with or for the benefit of any person who makes or provides a statement, oral or written, as to the potential tax consequences that may result from the transaction. The determination of whether a transaction has been offered under a condition of confidentiality is based on the facts and circumstances surrounding the offering or transaction, including the prior conduct of the parties.

3. Transactions with Contractual Protections. A transaction is deemed to have contractual protections if the taxpayer has obtained or been provided with contractual protection against the possibility that part or all of the intended consequences will not be sustained (i.e., contingent fee transactions).

4. Loss Transactions. Certain loss transactions, generally resulting from the sale or other disposition of assets, are considered "loss transactions" for disclosure purposes if they meet certain definitional requirements and if they result in, or are reasonably expected to result in, a loss in an amount that is at least: For corporations or partnerships with only corporations as partners – $10 million in a single year/$20 million in a combination of years;

   For other partnerships, S Corporations, individuals, and trusts – $2 million in a single year/$4 million in a combination of years;

   For individuals and trusts where the loss arises from certain foreign currency transactions (whether or not the loss flows through from an S corporation or partnership) – $50,000 in a single year.

   A full description of the types of loss transactions that are subject to the reporting requirements is beyond the scope of this discussion. Also note that there are numerous published exceptions for many common transactions. Therefore, you are encouraged to discuss any loss transactions that meet or exceed the threshold requirements listed above with your tax advisor.

5. Transactions Generating a Tax Credit if the Underlying Asset is Held For Less Than 45 Days. A transaction falls within this category if it results in, or is reasonably expected to result in, a tax credit in excess of $250,000 and the asset giving rise to the credit is held by the taxpayer for less than 45 days.

The disclosure requirements discussed above are for federal tax purposes only. In addition California, Connecticut, Illinois, New York, and several other states have adopted either legislation or administrative rules that impose state reporting requirements.

It may be difficult to identify potential reportable transactions that originate from pass-through entities (e.g., partnerships, S corporations, LLCs, trusts, etc.). If the necessary information regarding the particular pass-through entity in which you have invested is supplied to your tax advisor and/or you permit your tax advisor to make inquiries of the pass-through entity regarding these matters, your tax advisor can assist you in making this determination.

The AJCA imposes penalties on taxpayers who do not disclose the required information concerning a reportable transaction on a tax return due after October 22, 2004. For individuals, the penalty is $100,000 for a listed transaction and $10,000 for a reportable transaction other than a listed transaction. The Act permits the IRS the discretion to abate or rescind the $10,000 penalty in order to promote compliance and effective tax administration. However, the IRS has no authority to abate or rescind the $100,000 penalty. In addition to the $100,000 and $10,000 penalties for failure to disclose, the AJCA created a separate penalty equal to 30 percent of tax understatements related to undisclosed listed transactions or other reportable transactions with a significant tax-avoidance purpose. If a listed transaction or other reportable transaction with a significant tax-avoidance purpose was disclosed, a lower penalty of 20 percent of the understatement applies. The 30 percent penalty may not be waived by the IRS. The 20 percent penalty may be waived by the IRS in certain circumstances. Each of the states noted above has also enacted significant penalties for failing to comply with their disclosure rules.

Year-End Planning Checklist

The checklist below is intended to provide you with a starting point for your year-end planning. Since each individual's situation is different, no single checklist can possibly apply to, or adequately address, every situation. However, if you and your financial advisor apply a comprehensive approach to year-end planning and multi-year planning, you are well on your way to financial success.

Financial Plan

- Do you have a comprehensive financial plan (i.e., retirement plan, estate plan, education funding plan, investment plan, contingency plans for death, disability, liability, or casualty)? When was it last updated?
- Have you determined your short- and long-term financial goals?
- Are you saving and investing sufficient sums to fund your short- and long-term goals?
- Do you know how much you need to retire or to be financially independent?
- Do you have a durable power of attorney for managing your assets if you are unable to manage your own affairs?
- Do you have an emergency fund that will provide you with cash to weather a squall or two without having to disturb your investment portfolio or sell off any other assets? Many experts recommend keeping the equivalent of three to six months' take-home pay in a liquid account; however, it may be wiser to keep at least eight months of pay available.

Income Tax

Each individual should take six steps to assess his or her tax situation:

1. Estimate your income, deductions, credits, and exemptions for 2006 and 2007.
2. Identify items of income you can shift from 2006 to 2007 or beyond, or vice versa.
3. Determine your marginal tax rate – the rate at which your next dollar of income will be taxed – for 2006 and 2007.
4. Determine how much tax you owe and when you must pay it to avoid underpayment penalties for federal, state, and local tax purposes.
5. Determine whether you are subject to the alternative minimum tax (AMT).
6. Consult with your tax advisor, then take actions needed to make the best of your situation.

Following is a checklist of items to consider related to your year-end income tax planning:

- Should you make up for underpayments retroactively by increasing your withholding?
- Should you take a 60-day-or-less "loan" from your IRA to avoid underpayment penalties?
- If you have overpaid estimated taxes or had too much withheld, are you eligible to reduce the amount withheld for the remainder of the year?
- Should you accelerate (or defer) payment of certain expenses (e.g., medical and dental, professional fees, unreimbursed business expenses, or management fees) to obtain some tax benefit?
- Should you elect to amortize any taxable bond premiums to convert a deferred capital loss to a current ordinary loss?
- Have you "harvested" your capital losses to minimize your overall tax liability?
- Have you performed a hypothetical calculation on your capital gains and losses to determine whether any capital losses will produce unexpected tax consequences?
- Have you avoided the "wash sale rule," which will prevent you from recognizing a loss on a sale if you purchased a substantially identical security within 30 days before or after the sale?
- Have you taken advantage of the worthless stock deduction where there is a cessation of business, foreclosure, or commencement of liquidation? Remember that the stock must truly be worthless to be able to take the deduction – if there is a chance that a shareholder will receive any value from a pending litigation, the stock is not worthless.
- If you have a margin account, you should consult with your broker to determine whether the broker makes a practice of borrowing shares from individual investors' accounts; if such borrowing does occur, it may cause some or all of your dividend income to be ineligible for the favorable rate applicable to qualified dividend income.
- If you work, have an office, or have a residence in multiple states, have you paid the correct tax to the applicable states? Is a credit available in your resident state for taxes paid to other states? Do you need to file a tax return in more than one state?

Employees

- Are you maximizing contributions to qualified retirement plans (e.g., 401(k) plans) and other deferred compensation plans where company matching contributions are available?
- If you are age 50 or over by year-end, have you made "catch up" contributions to your 401(k), IRA or SIMPLE plan?
- Are you utilizing pre-tax dollars in your flexible spending accounts to pay for medical, dental, transportation, and dependent-care expenses?
- Do you and your family have sufficient life, disability, medical, and long-term care insurance coverages? For individuals between the ages of 25 and 55, the risk of becoming disabled for 90 days or more before the age of 65 is at least twice the risk of dying before age 65.
- Are your savings or retirement plans subject to forfeiture in the event of your employer's insolvency?
- Have you considered the changes to your nonqualified deferred compensation arrangements that the AJCA mandates?

Self-Employed Individuals

- Do you have a profit-sharing or money purchase plan?
- Should you establish a profit-sharing plan or defined benefit pension plan (e.g., Keogh, solo 401(k), SEP-IRA, or SIMPLE plan)? If so, which one is best suited for your needs?
- Are you eligible to take advantage of the section 179 expensing election for qualified assets used in your business?

Company Stock and Stock Option Planning

- Are you subject to any SEC restrictions or reporting requirements on any sales or transfers of company stock?
- Have you considered the tax effects the AJCA will have on your stock options?

Restricted Stock

- Should you make a section 83(b) election for grants of restricted stock?

Stock Options

- Should you consider exercising nonqualified options (NQSOs) or incentive stock options (ISOs) before the end of the year?
- Should you exercise and sell, or exercise and hold?
- Should you consider disqualifying any ISO exercises before the end of the year to avoid being subject to the alternative minimum tax (e.g., has the stock price declined substantially since the exercise date)?

Investment Planning

- Do you have a tax-aware asset allocation strategy?
- Does your asset allocation need to be re-balanced?
- How are your mutual funds and money managers performing compared to the appropriate benchmarks and their peers?
- Perform an "x-ray" of your mutual funds to determine the major holdings within each fund. If several funds contain the same holdings, have you considered selling one or more of the funds to diversify your portfolio and save management fees?
- How much of your investment return is being depleted by fees?

Education Planning

- Do you have an education fund to cover the costs for primary, secondary, college, and graduate school for yourself or your children?
- Do you qualify for a Coverdell Education Savings Account?
- Should you consider contributing to a qualified tuition plan (529 plan)?
- Does your home state offer tax deductions for contributions to its 529 plan(s)?
- Should you consider transferring your 529 plan to another state?
- Should you consider converting your Coverdell or UGMA/UTMA account to a custodial 529 plan? Have you considered certain fiduciary issues if you do?
- Should you front-load your child's or grandchild's education savings by contributing up to $60,000 ($120,000 if married) to a 529 savings plan?
- Can either you or your children in college use the Hope Scholarship or Lifetime Learning Credit?
- What education expenses, including interest expense, are deductible?

Estate Planning

- Do you have a will? Remember that a will not only directs where your property will go after your death, but also allows you to name a guardian for your minor children. If you do not name a guardian, your state laws may determine guardianship, which may be inconsistent with your desires. Note that some of your property may pass outside of your will (i.e., by operation of law), such as property you own with someone else as joint tenants with rights of survivorship.
- Do you have a living will or other health care directive?
- Have you told family members or trusted friends where they can find your important documents (i.e., will, trust, birth certificate, powers of attorney, insurance policies, etc.)?
- Do you have a letter of instruction setting forth your desired funeral arrangements?
- Probate can be costly in some states, both in terms of time and expenses. If you own real estate in more than one state, have you discussed with an estate attorney the possibility of transferring all real property to a trust or other entity in order to avoid probate in multiple states?
- Have you and your spouse maximized the use of your annual gift tax exclusions? (Each spouse can gift up to $12,000 to any individual during 2006 and 2007 and, in addition, pay tuition and medical expenses for any individual directly to the institution).
- Should you utilize your remaining $1 million exemption from federal gift taxes? (Your spouse also has a $1 million exemption).
- Should you utilize your remaining $2 million exemption from federal generation-skipping transfer tax? (Your spouse also has a $2 million exemption).
- Have you considered making gifts to an irrevocable grantor trust?
- Have you determined whether your state has decoupled from the federal estate tax laws, which may affect your state liability for estate and gift taxes?
- Do you have ownership rights in life insurance on your own life or the lives of others? If so, the face value of the policy may be included in your estate upon your death. Have you considered establishing a life insurance trust?
- Have you checked the beneficiary designations on your life insurance policies, retirement accounts, and any other instruments where you are able to designate a beneficiary? If you have recently experienced a marriage, divorce, birth, or death in your family, your beneficiary designations may need updating. In addition, you can maximize the time over which your retirement plan distributions are paid (which results in more time for tax-deferred growth) by selecting the right primary and contingent beneficiaries for your retirement accounts. Remember that beneficiary designations take precedence over will provisions, so choose your beneficiaries wisely.

Insurance Planning

- Do you have split-dollar life insurance? Have you contacted your tax advisor to understand the tax implications of the arrangement in light of the IRS pronouncements in this area?
- Do you have enough insurance to protect your family if you die unexpectedly?
- Given the increasing amount that will be exempt from estate tax in future years, do you have too much life insurance?
- Are you adequately insured if your spouse dies? If you are the sole breadwinner in your family and your spouse is a stay-at-home parent, how will you pay for child care if your spouse dies?
- Should you reconsider your mix of universal, term, and variable life insurance?
- Do you have adequate disability or long-term illness insurance if you and/or your spouse could not work for an extended period of time?
- Are you adequately insured in the event of a need for elder care (for instance, if your parents need in-home care or need to be moved into an assisted-living facility)?
- Does your employer offer a lower-cost life insurance alternative than you could obtain outside of your employer?
- How are you managing the risks related to your personal property (auto, boat, home) in the event of liability, loss of use, or disaster? Do you need an umbrella policy?
- Do you need renters' insurance? If you have children away at college, your homeowners' policy may cover their possessions if they live in a dorm, but likely does not cover their belongings if they live off-campus.
- Do you need directors' or officers' liability insurance?
- Do you have sufficient workers compensation insurance and/or other insurance for household employees, such as nannies and housekeepers?

Charitable Giving

- Do you have appreciated stock available to fund charitable contributions?
- Have you considered a charitable lead trust to take advantage of the current low interest rate environment?
- Have you considered using your IRA to fund your charitable donations this year? The Pension Protection Act of 2006 allows taxpayers over 70 1/2 to contribute $100,000 per year in 2006 and 2007 from their IRAs to charity. See page 10 for more information.
- Have you considered a donor-advised fund that is sponsored by a bank or brokerage company or a community foundation (i.e., a public charity that acts as a holding account for future charitable transfers, sometimes referred to as a "foundation for everyone") to obtain the charitable contribution deduction this year while still maintaining substantial input over what charities receive the funds in future years?

Alternative Minimum Tax

- If you are subject to the AMT, what tax-planning strategies are available?
- See page 12 for a detailed discussion of AMT issues

Debt Management

- If you have not refinanced your home within the past few years and do not plan to move in the near future, have you considered refinancing to get a lower interest rate?
- Do you have a home equity line of credit? No payments are due unless you actually use your line of credit. However, if you wait until you really need that line of credit (such as if you lose your job), you may no longer be considered a good credit risk, and be unable to get the credit when you need it.
- If you have a good credit rating, but are paying a high interest rate on your credit cards, have you called the customer service center to request a lower rate? Again, the time to request a lower rate is when your credit risk is low.
- If you have not reviewed your credit report in the last several years, consider checking it now. Errors on your credit report can impact your ability to obtain credit and the rate at which you can borrow funds as well as the cost of insurance, etc. It is good practice to review your credit report at least once every few years. Also, some states have instituted rules permitting individuals to "freeze" their credit reports and to therefore restrict others' access to their personal information; check your individual state's rules for details.

Special Situations

Sale of a Principal Residence - $250,000 per person exclusion; $500,000 for married couples

- Have you used the residence for two of the five years immediately preceding the sale?
  - Is the sale due to employment, health, or unforeseen circumstances? If so, you may be able to prorate the exclusion if you have not used the residence for two of the last five years.
- Was the residence originally obtained in a like-kind exchange?
  - Did the exchange pursuant to which you acquired the residence occur more than 5 years before the sale?
- Have you used the exclusion within the past two years?
  - If the sale of your current residence produces a larger gain than sale of the residence for which you used the exclusion within the past two years, have you considered amending your past tax return to recognize the full gain on the past sale in order to use the exclusion for the current sale?
- Have you properly computed the basis of your home? The basis of a one-family home that you live in will generally be equal to purchase price plus the cost of capital improvements. Your tax advisor can assist you with this computation.

Adjusted Gross Income of Less than $100,000 (AGI does not include required minimum distributions from an IRA for this purpose)

- Should you convert your traditional IRA to a Roth IRA?

Real Estate Investors

- Should you consider a like-kind exchange?
- Do you qualify as a real estate professional?
- Should you consider selling property to free up passive losses?

Green Card Holders

- Should you consider terminating your green card status before the expatriation rules apply to you? Generally, an individual who qualifies as a long-term permanent resident (i.e., a person who has had a green card for all or part of at least 8 of the last 15 years) will be subject to the expatriation rules if the green card is surrendered. Note that the AJCA modified the tax rules for individuals who expatriate after June 3, 2004. Surrendering a green card may result in significant non-tax related issues. You should consult an immigration attorney before making any tax-related decisions involving the surrender of your green card.

Non-U.S. Citizens

- Where is your residence for U.S. estate and gift tax purposes? (Note that this may be different from your residence for income tax purposes).
- What assets (e.g., U.S. stocks and stock options, U.S. real estate, U.S. retirement accounts, or pension plans) do you have that will be subject to U.S. estate taxes in the event of your death?
- Do you have an estate plan in place to minimize U.S. estate taxes?
- How can you avoid making taxable gifts to your non-U.S. citizen spouse (i.e., gifts in excess of $120,000 during 2006 and $125,000 in 2007)?

Attaining Age 70 1/2 in 2006

- Should you take a distribution from your IRA or other retirement accounts this year or two distributions next year?

Retiring

- Have you considered what elections must be made before retirement, including termination of employment, for retirement account payouts (e.g., lump sum distributions)?
- If you move to a state without an income tax, will your retirement accounts still be taxable in your former state of residency? If so, what strategies (e.g., electing distributions over 10 years or life) are available to you to reduce or eliminate this tax?
- If you are a non-U.S. citizen and contribute to a foreign retirement account while living/working in the U.S., a portion of your distributions from the foreign retirement account may be subject to U.S. income tax, even if you are not living in the U.S. when you receive such distributions. Treaty relief may be available. Notify your advisor if you are not a U.S. citizen and are contributing to a retirement plan.

Marriage and Divorce

- If married, should you file jointly or separately?
- If filing separately and joint estimated tax payments were made, have you decided how the estimates will be allocated?
- Does it make a difference whether a payment is considered alimony or part of a property settlement?
- Who claims the children as dependents?
- Under what circumstances will you be considered "divorced" for tax purposes?
- Do any marital/divorce agreements (e.g., prenuptial, postnuptial, or divorce settlement) need to be coordinated with buy-sell agreements in which you have an interest?

Inheritance or Gifts Within the Past 9 Months

- Do you have time to disclaim any transfers so that the funds may be distributed to others without incurring negative gift tax consequences?

Terminal Illness

- Are additional funds needed? Have you considered a viatical settlement?

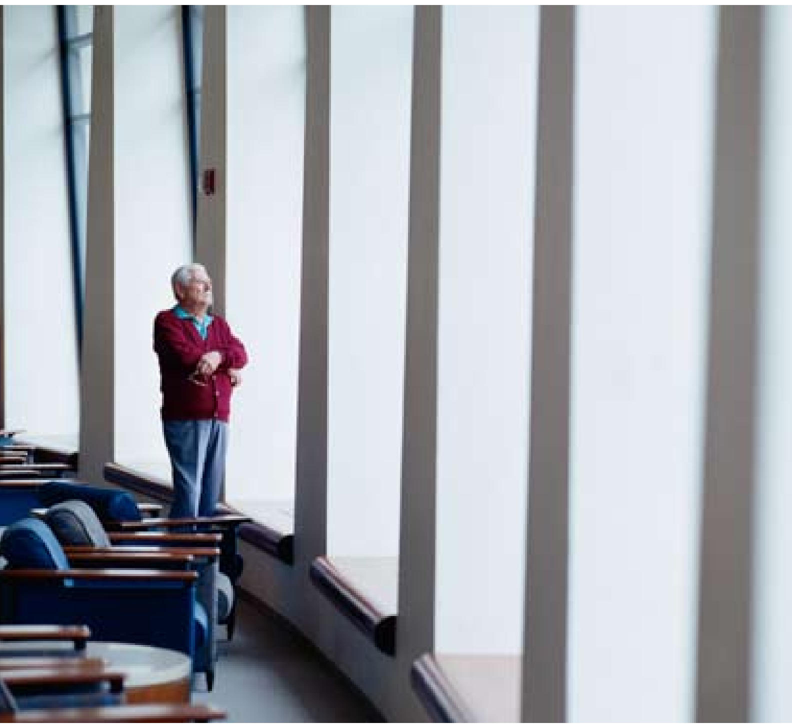
Passthrough Entities – S Corporations, LLCs and Partnerships

- The Pension Protection Act of 2006 allows special treatment of certain charitable contributions made by S Corporations in 2006 and 2007. If the S corporation makes charitable contributions of appreciated S corporation property in 2006 or 2007, shareholders will reduce their basis by their share of the adjusted basis of the contributed property instead of by their share of the market value of the property.
- Review your basis in the S Corporations, LLCs and Partnerships prior to year-end. If losses are expected, make sure that the partner/shareholder has adequate basis to absorb the loss. Consider making a capital contribution or a loan to the entity to generate basis to take the anticipated losses in 2006.
- Review the time dedicated to the entity during the year to determine whether the business is a passive or non-passive activity to the owner.
- Review suspended loss accounts at the time of any transfer, sale or other disposition to ensure all losses are properly deducted or transferred.
- S Corporation shareholders should consider whether they qualify to have the corporation close its books for purposes of allocation of tax items to them if such shareholders sold or transferred a certain number of shares of stock during the year.

Estates and Trusts

- With respect to estates, have you selected an appropriate tax year-end?
- Have you contacted a qualified professional advisor regarding any post-mortem elections that may significantly reduce or defer estate taxes?
- With respect to estates and trusts, have distributions been made to minimize overall income taxes?
- With respect to trusts and trust beneficiaries, have state income taxes been addressed? Some states tax trusts based on the residency of the beneficiaries or trustees. If any beneficiary, trustee, or the trust's grantor have moved since the trust was established, additional reporting requirements or state taxes may be due.
- In the case of a Qualified Subchapter S Trust, has the trust distributed all trust accounting income to the beneficiary? Further, if the QSST disposes of the stock, the income beneficiary may be able to consider suspended at-risk or passive losses.

Yearly Tax Planning Calendar



Tax and financial planning are activities best pursued year-round. The timing of some activities is critical; however, you should review all tax considerations from the perspective of your specific needs and establish an individualized planning calendar.

First Quarter

General:

- Complete Form W-4 and adjust withholding if needed.
- Apply for a Social Security number for any child who does not have one.
- Consider filing tax returns early in those states or jurisdictions where discounts are provided.
- Determine whether it is advantageous to pay any taxes with credit cards.

January 15:

- Pay fourth-quarter estimated taxes for the preceding tax year.
- Make quarterly defined benefit Keogh contribution for preceding year.

January 31

- Give domestic employees their copies of Form W-2, Wage and Tax Statement.

March 15

- If you are a U.S. owner of a foreign trust, ensure the trustee files Form 3520-A, Annual Information Return of Foreign Trust With a U.S. Owner, or applies for an extension to file on Form 2758. If the trustee fails to file, the U.S. owner may be subject to penalties.

Second Quarter

April 1

- Comply with minimum distributions rules for qualified plans by April 1 if you attained age 70 1/2 in the previous year.

April 15

- File individual and gift tax returns (or an application for an extension).
- File Schedule H (Form 1040) with your tax return if you paid cash wages of $1,500 or more in 2006 to a household employee.
- Report federal unemployment tax (FUTA) on Schedule H if you paid total cash wages of $1,000 or more in any calendar quarter of 2006 to household employees.
- Make first-quarter estimated tax payment.
- Make prior-year IRA and Coverdell Education Savings Account contributions.
- Make prior-year Keogh or SEP plan contributions. If you applied for an extension to file your tax return, these contributions are not due until you timely file your tax return.

- Make quarterly defined benefit Keogh contribution for the current year.
- If you have transacted with a foreign trust or person (e.g., you are the owner of a foreign trust, made a transfer to or received a distribution from a foreign trust, hold a qualified obligation of a foreign trust, or received certain gifts or bequests from a foreign person), file Form 3520.

June 15

- Pay second-quarter estimated taxes.
- If you filed for an extension to file Form 3520-A (originally due on March 15), file the form, or file a second extension request on Form 2758.

June 30

- File Form TD F 90-22.1, if necessary. Generally, each U.S. person who has a financial interest in, signature authority, or other authority over any financial accounts, including bank, securities, or other types of financial accounts in a foreign country, must report that relationship on Form TD 90-22.1. The requirement is only necessary where the aggregate value of the financial accounts exceeds $10,000 at any time during the calendar year. A $10,000 penalty may be imposed on individuals who fail to report an interest in a foreign financial account. Willful violations of this requirement can result in a penalty of $100,000 or more.

Third Quarter

July 15

- Make quarterly defined benefit Keogh contribution for the current year.

July 31

- File Form 5500, Annual Report of Employee Benefit Plan, if applicable.

September 15:

- Pay third-quarter estimated taxes.

Fourth Quarter

General:

- Begin your year-end tax planning:
- Project your current year and next year tax liabilities.
- Evaluate the applicability of the AMT and other taxes.
- Adjust withholding, if necessary.
- Evaluate year-end capital transactions.
- Establish a separate Keogh for self-employment income.
- Comply with minimum distribution rules for qualified plans.
- Evaluate before-tax and voluntary after-tax contributions to retirement plans.

October 15:

- File extended individual and gift tax returns.
- File Form 3520 (if necessary) if your individual income tax return was extended.
- Make quarterly defined benefit Keogh contributions for the current year.
- Recharacterize a Roth IRA conversion or change a prior year contribution from one type of IRA to another (if your individual returns were extended).

Throughout the Year

- Re-evaluate your long-term strategies.
- Evaluate your tax and financial strategy for receiving discretionary and mandatory retirement plan distributions.
- Evaluate investments on an after-tax basis.
- Rebalance your investment portfolio and re-evaluate your uses of debt.
- Consider income shifting to maximize family wealth by making gifts up to the annual exclusion amount or up to your lifetime exclusion amount.
- Evaluate passive loss exposure and potential investment shifts.
- If you have excess cash flow, consider how to invest those funds.
- Optimize mix of interest expense items.
- Consider making charitable contributions of property.
- Consider ways to fund your child's education.
- Evaluate your mix of portfolio and passive income.
- Review prior gifts to children under age 18 and their incomes to minimize the amount of income that will be taxed at your top marginal rate.
- Review the selection of your second residence and status of your vacation home.
- Be mindful of expiring credits, tax reductions, and exemptions.
- Review resident and non-resident filing requirements for federal and state income, estate, gift, and generation-skipping tax purposes.
- Be sure to inform your tax advisor of all transactions with friends and family during the year (such as sales between family members or trusts). It may be advisable to report such non-gift transactions on gift tax returns under the "adequate disclosure regulations."

Deduction Limitations Of Outright Charitable Gifts

Type of Property[1]	Public Charity or Community Trust	Support Organization	Private Foundation	Private Operating Foundation	Pass-Through Foundation
Cash[1] AGI Limitation	50%	50%	30%	50%	50%
Real Estate and Intangible Personal Property[2] Held More Than One Year	FMV	FMV	Cost Basis[4]	FMV	FMV[5]
Amount of AGI Limitation	30%[3]	30%[3]	20%	30%[3]	30%[3]
Tangible Personal Property Held More Than One Year	FMV[6]	FMV[6]	Cost Basis	FMV[6]	FMV[5,6]
Amount of AGI Limitation	30%[3]	30%[3]	20%	30%[3]	30%[3]
Real Estate and All Personal Property Held Less Than One Year	Cost Basis	Cost Basis	Cost Basis	Cost Basis	Cost Basis
Amount of AGI Limitation	50%	50%	30%	50%	50%
Ordinary Income Property	Cost Basis	Cost Basis	Cost Basis	Cost Basis	Cost Basis
Amount of AGI Limitation	50%	50%	30%	50%	50%

1. Special limits apply to donations of vehicles. See page 28.

2. Intangible personal property includes securities and partnership interests.

3. A 50 percent AGI limitation election is available when a cost basis deduction is taken.

4. If publicly traded stock held for more than one year was contributed, a fair market value (FMV) deduction is available.

5. If the foundation distributes an amount equal to 100 percent of the value of contributions made within two-and-one-half months of year-end, the FMV may be deducted.

6. If charity's use of property is related to its exempt purposes, a FMV deduction is available; Otherwise, only cost (or FMV if lower) may be deducted.

For all categories in the chart marked "Cost Basis," if the FMV is below cost, only the FMV may be deducted.

2007 Individual Income Tax Rate Tables (Projected)

For Married Taxpayers Filing Joint Returns and Surviving Spouses

Taxable Income

Over ($)	But Not Over ($)	Rate (%)
0	15,650	10
15,650	63,700	15
63,700	128,500	25
128,500	195,850	28
195,850	349,700	33
349,700	–	35

For Married Taxpayers Filing Separate Returns

Taxable Income

Over ($)	But Not Over ($)	Rate (%)
0	7,825	10
7,825	31,850	15
31,850	64,250	25
64,250	97,925	28
97,925	174,850	33
174,850	–	35

For Single Taxpayers

Taxable Income

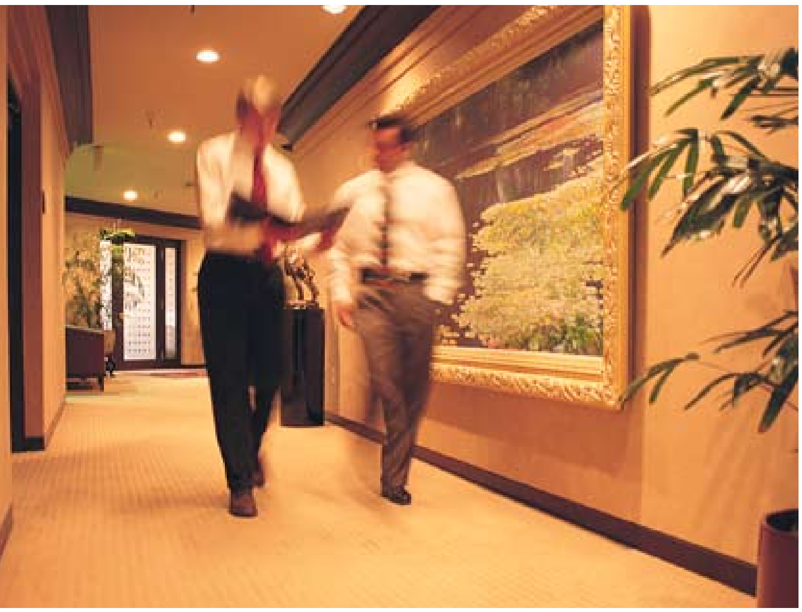
Over ($)	But Not Over ($)	Rate (%)
0	7,825	10
7,825	31,850	15
31,850	77,100	25
77,100	160,850	28
160,850	349,700	33
349,700	–	35

For Individuals Filing as Head of Household

Taxable Income

Over ($)	But Not Over ($)	Rate (%)
0	11,200	10
11,200	42,650	15
42,650	110,100	25
110,100	178,350	28
178,350	349,700	33
349,700	–	35

Deloitte Tax Private Client Services



Deloitte Tax provides comprehensive and objective wealth planning advice and services to affluent individuals and families, executives, and owners of closely held businesses, through hundreds of professionals nationwide. Our mission is to serve as our clients' most trusted advisor and to help them make informed and strategic decisions based upon their goals for personal financial comfort, business and investment needs, family legacy, and charitable giving during lifetime and at death.

We also offer a full range of personal tax and financial planning services through corporate employers who are aware of their executives' needs for tax and financial planning services from an advisor such as Deloitte Tax. In addition, we offer individual and group counseling sessions for executives or large groups of employees to address their financial planning needs when downsizing, restructuring, and significant benefit changes occur.

Comprehensive Financial Planning

Deloitte Tax takes a holistic approach to financial planning, incorporating investments, estate and retirement issues, insurance, income tax matters, education funding, compensation and benefits, and other issues that may potentially affect your financial goals or financial peace of mind.

Our multidisciplinary approach and understanding of interrelationships among components that build your net worth help us explore strategies that add value to your total financial position. We serve as your trusted advisor and can coordinate the activities of other advisors, ensuring that we all work toward your common goals.

Family Wealth Planning

Our wealth planning professionals have extensive experience working with affluent families to manage and sustain multigenerational wealth. These services address complex issues, including:

- Family legacies and liquidity needs of current and future generations
- Ownership and key decision-making, governance, and communication
- Business and investment assets
- Charitable objectives and future business and investment plans
- Insurance needs
- Income, gift, estate, and generation-skipping taxes

We work closely with families to assess whether their plans address the family's values, mission, philosophy, and long-term goals. For owners and operators of existing businesses, we also take into account the special challenges they face, such as ownership and management, succession planning, strategic development, and taxation of the business.

Individual Income Tax Planning and Compliance

Our dedicated income tax specialists guide clients through vital financial and individual income tax planning activities, helping them explore tax savings and focus on the changing tax and economic climate. Proficient in serving the complex needs of individuals, family members, and ventures, Deloitte Tax can help you evaluate the tax consequences of transactions and assist in structuring them so you address your tax objectives. We can also help address future tax impact by advising on the interplay of income tax planning strategies with other aspects of your wealth. Deloitte Tax has access to the world's largest network of tax professionals and deep experience in complex tax compliance matters. For those who work or live abroad, we can help with income tax residency and cross-border tax issues.

Business Succession Planning

Deloitte Tax provides objective and comprehensive advice to owners of privately held businesses on the complex and often emotional issues of succession planning. Our experienced specialists bring creativity, substance, and a strategic emphasis to a process that is often undocumented and uncommunicated. Focusing on your objectives and future vision, our systematic approach explores the most critical issues to managing your personal wealth, transitioning ownership, and ensuring business continuity and growth.

We work with you to define your strategic priorities and develop a comprehensive action plan that integrates:

- Goal articulation
- Business valuation
- Shareholder agreements
- Estate, gift, and investment planning
- Incentive compensation
- Exit strategy and retirement
- Business/family governance
- Insurance and disability planning
- Corporate structuring and finance
- Family information and communication

Estate, Gift, Trust, and Charitable Consulting

Our estate planning specialists can help you establish a plan to manage, administer, and distribute assets during your lifetime, at death, and after death. Our focus is to ensure that your wealth is allocated according to your family wealth and charitable intentions in a tax-efficient manner. We have in-depth experience in diverse planning vehicles, including trusts, partnerships, limited liability companies, charitable and family transfers, and financial instruments. Based on your personal goals, resources, and lifestyle decisions, we help you formulate a comprehensive estate management, gifting, and death transfer plan. We provide post-mortem consulting for estates that have significant tax exposure, non-traditional assets, or substantial litigious claims against them. In addition, our international estate planning specialists assist individuals and families with global assets and related tax issues.

Family Office Services

Affluent families often find themselves in need of more extensive family wealth planning and management services as the size and complexity of their assets increases. Deloitte Tax is the answer, providing full-service:

- Family office services, including income tax and wealth-transfer planning
- Family partnerships consulting
- Charitable planning, including private foundations
- Investment consulting
- Entity structuring consulting, including private business ventures

We serve as advisors to newly formed and mature family offices. We can help you create a plan to manage family wealth over multiple generations. We also serve the business and organizational needs of the family office. With access to an extensive global network of professionals, Deloitte Tax works closely with clients to tailor our services and approach to suit their unique needs.

Investment Consulting Services

Deloitte Tax provides investment consulting services under the supervision of Deloitte & Touche Investment Advisors (DTIA) LLC, an investment advisor registered with the Securities and Exchange Commission. Our investment consulting specialists provide fee-based advice that is comprehensive and tailored to your individual needs. Our research and knowledge enable us to create investment strategies for you that are innovative, tax efficient, and cost effective. We provide value by coordinating and integrating your investment strategies with your overall wealth management. We seek to develop long-term relationships through local, personalized service that combines proactive advice with ongoing monitoring to address your changing goals and needs. Our specialists are supported by the Center for Investment Consulting, which provides a comprehensive line of services, including in-depth fund and separate account research, extensive analysis of the financial markets, asset-class assumptions, and performance reporting.

Life Insurance Consulting Services[1]

Our life insurance specialists draw on their industry experience to explore innovative strategies to help you meet your individual, estate, and business life insurance needs. We do not sell products. You can benefit from our unbiased approach toward helping you address your needs, identify and manage risk, minimize costs, and maximize returns, whether you are:

- Reviewing current insurance policies
- Reviewing your options under split-dollar arrangements
- Assessing your funding options under executive benefit programs
- Evaluating insurance for closely held business operations
- Considering proposals for new insurance

From assessment and analysis through implementation and review, our life insurance specialists help you assess whether you have the right insurance within the right structure to help protect your assets, your family, and your business.

Partnership and Private Equity Services

As a leading provider of professional services to private equity investors, Deloitte Tax offers individuals and families a wide range of assistance with private equity. We understand the challenges and opportunities of structuring and managing a private equity fund successfully across the spectrum of business, personal tax, and management issues, and across funds of all sizes. We have the knowledge and experience to help partnerships with all aspects of operation, from initial set-up and day-to-day matters to investor issues and investment activities. Our services are designed to deliver high-quality work to funds and their investors.

[1] Certain insurance consulting services may be subject to state regulatory requirements and may not be available in all offices.

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