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## DouglasBradley's MONEYWISE

Financial News and Insight from an Independent Advisor

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### Personal Notes

**Doug** - For the past twenty years, my brother, father and I have had a tradition of attending the NCAA Men's Lacrosse Championships on Memorial Day weekend. This year they returned to Baltimore's Raven's Stadium, so we spent the weekend watching five lacrosse games. Monday was an exciting championship game between Notre Dame and Duke - neither of whom have won a championship title in the past. Tied at 5 goals apiece at the end of the fourth quarter, we went into sudden death overtime. Duke won the face-off and immediately ran down the field to score the winning goal.

All around, it was another great weekend of memories with friends and family.

**Brad** - Work and other important projects are keeping me from putting my boat in its slip. Since the boat is getting a bit older now (it was new in 2000), I try to accomplish a big preventative maintenance task each year to ensure I don't have to be towed back to port. Last year it was the thermostats (it has two) and this year it is the low pressure fuel pumps (three of them) and a difficult to reach fuel filter. The new Ethanol-based fuel has wreaked havoc

### Hurry up and Wait - for Tax Law Changes

Many of the tax law changes that President Bush enacted in 2001 are scheduled to expire in 2011. Will Congress simply let them expire, extend them or make changes? With important mid-term elections coming this November, our guess is we won't know until the last 45 days of 2010.

As the great hockey player Wayne Gretzky replied when asked to explain his success, "I skate to where the puck is going to be, not where it has been." We believe it is a similar characteristic that distinguishes DouglasBradley. We are always looking ahead to see how changes in the economy, stock market, legislation, public attitude, etc... might impact our clients' personal finances.

Towards that end, we are going to look ahead to some very important tax changes that will affect all taxpayers in 2011 - only 6 months from now - and how we think these changes may skew the US economy.

On January 1, 2011, the tax cuts enacted by President Bush in 2001 are set to expire. If Congress does nothing, many taxes revert back to their higher pre-2001 levels. Considering the deficits the federal government is running up, it's unlikely Congress will extend the cuts.

Here are some of the tax cuts set to expire:

- The highest marginal income tax rate will jump from 35% to 39.6%.
- The special 15% tax rate for qualified dividends will disappear (mostly this is stock dividends).
- The lowest marginal income tax rate of 10% is eliminated - making 15% the new lowest.

on marine engines and fuel systems.

**Mahesh** - I just finished soccer season last weekend. My team went 7-0-1. This is the third straight season that our team has gone undefeated. Now with soccer season behind me, I'm looking forward to enjoying the rest of the summer with my two children. I have a fishing trip scheduled on the Chesapeake Bay in July. I'm hoping to catch a few Rockfish and have a barbecue with close friends and family the day after the trip. I've always talked about catching and grilling fish, but this will be the first time I'm actually able to do it.

- The long-term capital gains tax rate increases to 20% from 15% (this is the tax on profit from the sale of stocks and mutual funds held longer than 12 months).
- The Child Tax Credit is reduced to \$500 from \$1,000.
- The ability to deduct mortgage insurance premiums is removed.
- The federal estate tax (currently 0%) returns for estates in excess of \$1 million with a top rate of 50%.

These are a selection of the potential changes with the broadest impact. As you can see, they impact nearly all taxpayers. With only 6 months to go, you'd think our elected leaders would have carefully considered a course of action and started discussions. Why has the Capitol been so quiet? Mid-term elections are in November and no one wants to bring up higher taxes and risk the ire of the public.

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Higher federal taxes aren't the only thing to watch out for. State governments are facing huge budget shortfalls and are looking to raise revenue as well. A number of states have raised income tax rates already and more are sure to follow.

We know for a fact that taxpayers will alter their behavior and decision making to reduce their tax burdens. This will have its own impact on the economy.

For example, higher income taxes will make certain investments less attractive. Might investors be less interested in the stocks of utility companies and their high dividends if the tax on those dividends more than doubles from 15% to 39.6%?

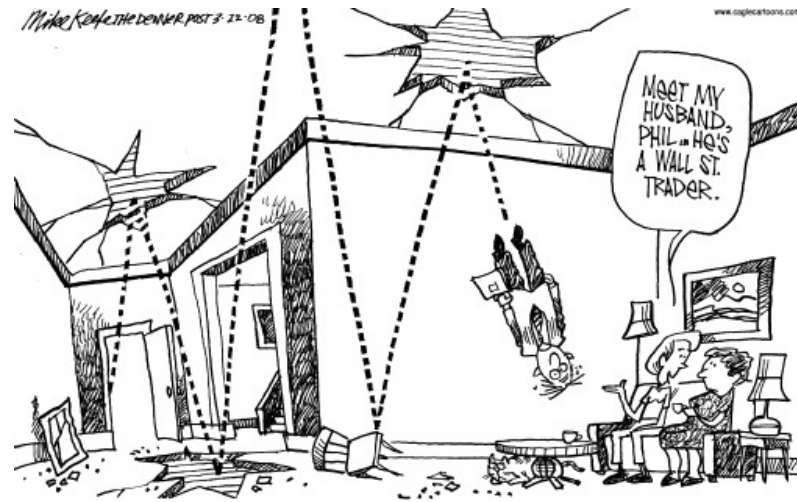
If taxpayers fear income taxes will be higher in 2011, they will certainly try to shift income and spending to minimize their liability. We saw this with the "Cash-for-Clunkers" program last year. It had the intended effect of increasing new automobile purchases - but it essentially "stole" those sales from the future. The result was a drastic drop in car sales once the program ended. We're seeing a similar situation with the just-ending home buyer's credit.

Looking ahead, we think it's reasonable to assume taxpayers, to the extent possible, will shift as much income as possible to 2010. Similarly, they will shift expenses and production into 2011 and beyond when those deductions will have a greater impact.

Small business owners have perhaps the most control over their taxable income and should plan on reviewing their finances in the fall. Employees have little to no flexibility with their taxable income - making planning frustrating. Executives with stock

options or restricted stock might consider exercising/selling in 2010 versus 2011.

Planning will be challenging considering it is unknown what changes will be made. But you certainly want to be aware of what things to look at once the new laws take shape.



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