THE WEALTH FACTOR

BY MIKE SLOTOPOLSKY

MANY IN THE TOP TAX BRACKET HAVE BEEN HIT HARD IN THE POCKETBOOK AND PRESIDENT OBAMA'S TAX PROPOSALS AIM TO TAKE A BIGGER BITE. OUR FINANCIAL COLUMNIST HAS SOME ADVICE.

CERTAINLY THE ÜBER-RICH have come under attack lately in a sort of *Let them eat cake/Off with their heads* back and forth between the haves and have nots. Between Bernie Madoff and those AIG bonuses, it's a wonder there hasn't been a call for public guillotining.

But what about the folks who are seen by most of America as wealthy, and, more importantly, are viewed by the government as rich but who don't necessarily feel all that rich. You know who I'm talking about because, quite possibly, you fit this demographic. Those of us on the coasts in or close to a major metropolis, where the high cost of living coupled with pricey mortgages makes us feel like we're struggling to keep up with the Joneses despite six figure incomes.

And there's no life preserver in sight. By 2011, President Obama's tax proposals would increase taxes for those making more than $250,000, raise the top tax rate from 35% to 39.6%, and limit itemized deductions on charitable donations, mortgage interest, and state and local taxes. It's enough to make the *mass affluent* – a term the banks use – feel fairly shaken and pretty beat up.

Despite the fact that the Obama tax proposals basically return tax levels to 1993 levels, what they were under Clinton's tenure, there's more outcry because so many *mass affluents* have lost so much in their paper portfolios. If you're a *mass affluent*, there are a number of steps you can take to keep your hard-earned dollars in your own pocket.

- There's plenty of time to figure out how to decrease your tax bill. Small business owners especially can benefit from acting early by paying themselves a qualified dividend which reduces the value of their company and is taxed as capital gains, not ordinary income. You can also sell all or part of your business to an ESOP – employee share ownership plan – which takes money out of the company and gives an ownership stake to employees. What you get is taxed at a capital gains rate which increases to 20% from 15% in 2011. Shareholders can also sell concentrated stock positions purchased at a low value, a good idea since concentrated stock positions would have to outperform the broader index by 5% to be worth holding.
- Buy municipal bonds which offer positive returns and tax-exempt status. While the Dow lost 25% last year, munis returned 3% to 5%. An added benefit is these bonds are exempt from federal tax and if you're a resident of the state where the bond was issued they're also exempt from local taxes.
- Deferring compensation is a smart tax idea. Execs often put income into a company-sponsored deferred-compensation plan and pull it out when they retire at a lower tax bracket. If your company has this plan it could be a good strategy, provided your company doesn't go bust. If it does, there goes your plan. There's also another possible problem. The tax rate at your retirement could be higher than today. If taxes remain constant, deferring is a prudent move. But if federal taxes rise to 15% (which, incidentally, would still below 1970's levels) deferring income over 15 years wouldn't be smart. Always run the numbers.
- Next year was supposed to be the best year for a wealthy person to die. Under the current tax code, the estate tax is zero for 2010 and increases to $1 million in 2011. President Obama's tax proposals would preserve the estate tax at 2009 levels, a $3.5 million individual exemption at a 45% top rate. The plan leaves a loophole though. Current tax codes exclude single people earning more than $105,000 a year from putting post-tax money into a Roth IRA, accounts that pay out tax-free gains upon retirement. In 2010, however, this limit is set to disappear for one year so anyone can convert a traditional IRA to a Roth IRA. Taxes would have to be paid now because the money went into the traditional IRA tax-free, but those taxes would be paid on depressed assets and all the appreciation would be tax-free.
- Heed Warren Buffet's advice: buy during a recession. Buffett has always been a buy-and-hold investor, genius advice which has made him one of the world's wealthiest men. But most folks don't have the chutzpah to buy as the market keeps tumbling although it might be a smart time to follow Buffett's lead. There are huge discounts available; the trick is choosing the companies that will survive and thrive.

Whether we're in economic tempests or opulent times, there are always steps that can be taken to make the most of your money and keep it in your wallet where it belongs. ❑

Michael Slotopolsky, CPA, is the managing partner of Vision Financial Group CPAs, LLP, an accounting, tax, and consulting firm. He is also a member of the American Institute of CPAs.