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SPECIAL EDITION ON THE 2010 TAX ACT

This past December, Congress passed and the President signed the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the “2010 Tax Act”). This long overdue legislation resolves significant tax issues pending for many years. Important changes to income tax rates, capital gains rates, taxes on dividends, and gift and estate taxes took effect on January 1, 2001, with a ten-year term, including repeal of the estate tax in 2010. The 2010 Tax Act revisits many of the issues addressed ten years ago and reinstates the estate tax, but with new limits and features. Due to the importance of the 2010 Tax Act, we are devoting most of this newsletter to a discussion of aspects of the new law.

Quick Guide to Gift, Estate, and Business Income Taxes

	2010	2011	2012
Federal Annual Gifting Exclusion	\$13,000 per recipient	\$13,000 per recipient	\$13,000 per recipient ¹
Federal Gift Tax Exemption	\$1,000,000	\$5,000,000	\$5,000,000 ²
Federal Gift Tax Rate	35%	35%	35%
Federal Estate Tax Exemption	\$5,000,000 (Estates of persons dying in 2010 can “opt out” and take carryover basis subject to limited basis adjustments)	\$5,000,000	\$5,000,000 ³
Federal Estate Tax Rate	35%	35%	35%
Basis on Death	Step up to fair market value on date of death	Step up to fair market value on date of death	Step up to fair market value on date of death
Generation-Skipping Transfer (“GST”) Tax Exemption	\$5,000,000	\$5,000,000	\$5,000,000 ⁴
GST Tax Rate	0	35%	35%
Minnesota Estate Tax Exemption	\$1,000,000	\$1,000,000	\$1,000,000
Maximum Minnesota Estate Tax Rate	16%	16%	16%
Bonus Depreciation	100% for new property placed in service after 9/8/10	100%	50%
Section 179 Expense Limit	\$500,000	\$500,000	\$25,000
S-Corp Built-in Gains Tax Period	7 Years	5 Years	10 Years
Employee Social Security Tax Rate	6.2%	4.2%	6.2%

1 Will be indexed for inflation in increments of \$1,000 thereafter.
 2 Will be indexed for inflation in increments of \$10,000 thereafter.
 3 Will be indexed for inflation in increments of \$10,000 thereafter. In 2011 and 2012, the unused federal estate tax exemption of first spouse to die is portable to surviving spouse.
 4 Will be indexed for inflation in increments of \$10,000 thereafter.



By Dave F. Senger
and Nancy M. Kiskis



Dave Senger is a member of our business law and wealth preservation and estate planning practice areas. He works extensively with individuals and businesses in connection with their estate, business, and succession planning.

He also spends considerable time negotiating business acquisitions and sales and other commercial contracts. Dave can be reached at 612.877.5262 or SengerD@moss-barnett.com.



Nancy Kiskis is a member of our wealth preservation and estate planning practice area. Her practice includes planning for death and disability, health care planning, charitable giving, and income, gift, and estate tax planning. She has personal and professional experience in working with families affected by Alzheimer's and dementia. Nancy can be reached at 612.877.5385 or KiskisN@moss-barnett.com.

REPEAL OF THE REPEAL - MAJOR CHANGES TO THE FEDERAL ESTATE TAX LAWS

The 2010 Tax Act provides some certainty as to the estate tax laws for the next two years and provides tax planning opportunities through 2012.

Increase in Federal Estate Tax Exemption to \$5 Million

A significant change under the 2010 Tax Act was an increase in the federal estate tax exemption to \$5 million. The exemption had been \$3.5 million in 2009, and, until the 2010 Tax Act, the exemption was scheduled to drop to \$1 million in 2011. In addition, the exemption will be adjusted by the rate of inflation for years after 2012 in \$10,000 increments.

Portability of Federal Estate Tax Exemption Between Spouses

The 2010 Tax Act introduces an entirely new provision that allows "portability" of the federal estate tax exemption between spouses. Upon the death of the first spouse, the decedent's unused exemption can be transferred to the surviving spouse. A surviving spouse is limited to the unused exemption of his or her last deceased spouse. For the exemption to be portable, a federal estate tax return must be filed following the death of the first spouse to die. The generation-skipping transfer tax exemption is not portable.

Persons Dying in 2010

Prior to the enactment of the 2010 Tax Act, there was no federal estate tax for persons dying in 2010. Under the 2010 Tax Act, the federal estate tax was reinstated retroactive to January 1, 2010. However, purportedly to head off any challenge of this retroactive reinstatement of the federal estate tax (which challenge had been anticipated on behalf of estates of the mega-wealthy who died in 2010, such as George Steinbrenner), the 2010 Tax Act provides that the decedent's estate can "opt out" of the federal estate tax for 2010.

There are advantages and disadvantages to "opting out" of the new federal estate tax for 2010. If the estate of a decedent who died in 2010 takes the default position and is subject to the federal estate tax (whether or not any tax is actually due), most assets in the decedent's estate receive a step up in basis equal to fair market value of the assets on the decedent's date of death. Alternatively, if a decedent's estate elects to "opt out" of the federal estate tax, no part of the estate will be subject to the federal estate tax, but the decedent's assets receive a carryover basis equal to the decedent's basis in the assets during life, subject to a special basis adjustment of \$1.3 million and a \$3 million marital basis adjustment.

No Changes to Minnesota Law

It is important to note that there have been no changes to Minnesota estate tax law. The estate tax exemption in Minnesota remains at \$1 million. Thus far, Minnesota has not adopted the changes enacted under the 2010 Tax Act, such as portability of the estate tax exemption to a surviving spouse.

Changes Effective Through 2012

The estate tax law changes enacted by the 2010 Tax Act are effective through 2012. Although it appears that many of the provisions were written with permanent enactment in mind, no one can predict what will happen after 2012. We encourage you to contact your attorney at Moss & Barnett to discuss how the new tax laws may benefit you and your family.

ALERTS:

Property Tax Relief for Owners of Contaminated Property in Minnesota

To encourage property owners to clean up contaminated property, Minnesota law provides an opportunity to reduce property taxes on those properties for the duration of the clean-up. This is accomplished through the application of a contamination tax. At last, a tax that you may want to pay!

Property owners who have a cleanup plan approved by the State of Minnesota benefit through a reduction in the assessed market value of the property. The assessed market value is the value used to determine the applicable taxes payable each year. If the assessed market value of the property is reduced due to contamination, the amount of the reduction becomes the “contamination valuation.” The property owner’s tax bill is lower because the assessed market value is decreased by the amount of the contamination valuation. The amount of the contamination valuation remains subject to taxation, but the applicable tax rate is substantially less than the standard commercial/industrial tax rate.

If a property owner has an approved cleanup plan and the property owner is the responsible party, the tax rate on the contamination valuation is 50% of the standard rate. A property owner who has an approved cleanup plan but is not responsible for the contamination pays at a tax rate of 12.5% of the standard rate. For large, highly valued properties, the tax savings may be significant.

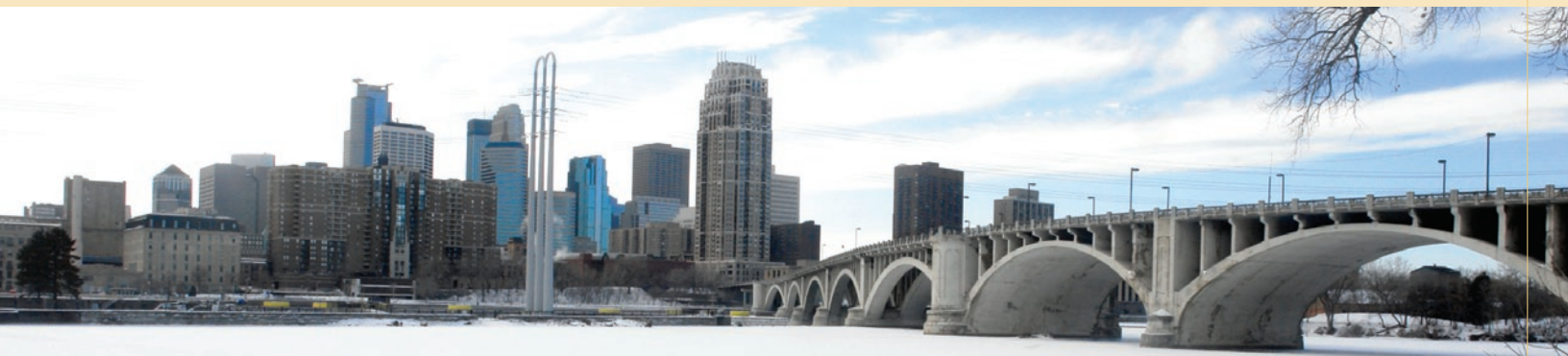
Thousands of properties across the state have been affected by contamination and have been cleaned up. The Minnesota Department of Revenue, however, acknowledges that only a few eligible property owners have actually sought property tax relief afforded by the contamination tax.

The contamination valuation cannot exceed the market value of the property, and the costs of the approved cleanup plan are considered in the contamination valuation. A formal appraisal may be required to determine the impact of the contamination on the value of the property. Any refund created by the decrease in assessed market value is set off by any contamination tax. As long as cleanup measures are in place, a party may be eligible for tax relief.

Red Flag Program Clarification Act of 2010

In several issues of this newsletter, we have told you about the impending and then delayed enforcement of the Red Flag Rules, which would require “creditors” to implement a program to detect and prevent identity theft involving credit accounts. As initially drafted, the Rules could have been interpreted to include businesses that extend credit to other businesses or individuals. Congress responded to the concerns of the business community, and President Obama signed the Red Flag Program Clarification Act of 2010, on December 18, 2010. The term “creditor” now has been limited to a creditor that obtains or uses consumer reports in relation to a credit transaction, furnishes information to consumer reporting agencies in connection with a credit transaction, or advances funds based on an obligation of repayment. Service providers who advance funds to cover expenses associated with the service are not considered “creditors.”

If you would like assistance in assuring best practices in any of these areas, please contact your attorney at Moss & Barnett.





Moss & Barnett is committed to strengthening our law firm through the addition of professionals and staff reflecting the increasing diversity of our region. Recognizing the need to take action on this important initiative, our firm became one of the early members of the following two organizations:

Minnesota Women Lawyers

Minnesota Women Lawyers (“MWL”) is an association made up of more than 1,200 attorneys, judges, law students, legal employers, and legal professionals who are all dedicated to advancing the success of women attorneys and striving for a just society. Since 1972, MWL has played an active role in Minnesota’s legal community. MWL provides unique opportunities for members to learn, develop as leaders, network with other attorneys, and have an impact on their communities by fostering a greater satisfaction within the profession. Many of our women attorneys are involved with MWL, including Jennifer Reussé, our 2010 Paul Van Valkenburg Service Award Recipient, who is a mentor in MWL’s attorney-law student program. You can learn more about MWL at mwlawyers.org.



*MWL’s 2011 Winter Celebration (February 15, 2011)
 Back Row (from left to right): Moss & Barnett Attorney Terese West, Elizabeth Lambrecht (Vice President-SBA, Park Midway Bank), Moss & Barnett Attorneys Jennifer Reussé and Caroline Bussey, Lucas Dawson (law student) Front Row (from left to right): Moss & Barnett Attorney Miggie Cramblit, Sarah Thompson (law student), Moss & Barnett Attorneys Betsy Kiernat and Kim Bonuomo*

Twin Cities Diversity In Practice

Twin Cities Diversity In Practice is an association of 24 law firms and 12 corporate legal departments with a well-defined mission: to attract, recruit, advance, and retain attorneys of color in the Twin Cities legal community. On January 25, 2011, Paul Zisla, an attorney in our real estate practice area, represented Moss & Barnett at the Twin Cities Diversity in Practice “Mapping Your Legal Pathways” event. Mapping Your Legal Pathways is an opportunity for first-year law students of color to explore legal career opportunities in the Twin Cities market. This unique program lets students learn about the kinds of careers available to them through firsthand perspectives and gain a better understanding of the local legal landscape. You can learn more about Twin Cities Diversity In Practice at diversityinpractice.org.



Paul Zisla

Kevin Busch and Susan Rhode Re-elected to Board of Directors

Kevin Busch and **Susan Rhode** were recently re-elected to three-year terms as members of the firm's board of directors. Kevin is chair of our commercial department and banking and commercial transactions practice area. He also serves as the firm's Chief Operating Officer. Susan is co-chair of the firm's family law practice area. They will each continue practicing law on a full-time basis in addition to handling their management responsibilities. Kevin and Susan join returning directors, **Brian Grogan, Rick Johnson, Dave Senger, and Tom Shroyer.**



Kevin Busch and Susan Rhode

Tim Gustin Appointed Adjunct Director

Tim Gustin, a member of our real estate practice area, has been appointed as an adjunct director for 2011. Adjunct directors are shareholders who serve as non-voting members on our board of directors for one year. The adjunct director program is intended to train future leaders of the firm. Past adjunct directors include, **Mike Nixt, Cecilia Ray, John Rossman, Betsy Kiernat, Joe Maternowski, and Mark Peterson**



Tim Gustin

Best Wishes to Bob Lukes

Bob Lukes retired from the practice of law at year's end, following a career that spanned four decades. He began practicing law in Chicago, working for a *pro bono* legal service, before going to work for Chicago Title Insurance. Working for the title company meant that Bob became one of the rare experts in title standards – a skill that served him well as he went into private practice with a heavy emphasis on real estate transactions. In 1985, Bob joined Moss & Barnett along with other attorneys from the Wiese & Cox law firm. Bob's service to the firm expanded with his election to the board of directors and culminated with his service as our Director of Administration from 2005 to 2010. Bob will be missed around the office for his droll wit, his unfailing good faith, and for the keen sense of what it took to get real estate deals closed for our clients.

We wish Bob many long and happy years of his well-deserved retirement!



CEO Tom Shroyer and Bob Lukes





By *Cindy J. Ackerman*
and *Richard J. Kelber*



Cindy Ackerman is a member of our wealth preservation and estate planning practice area. She represents clients in the areas of estate planning, charitable gift planning, tax strategy planning and compliance, tax-exempt organizations, probate and trust administration, and guardianships and conservatorships. Cindy can be reached at 612.877.5330 or AckermanC@moss-barnett.com.



Rick Kelber is a member of our business law and wealth preservation and estate planning practice areas. He represents clients in buying and selling businesses, financial transactions, and estate and succession planning. Having also worked in a corporate setting, he brings a financial and business approach to those various areas. Rick can be reached at 612.877.5433 or KelberR@moss-barnett.com.

GIFT TAX HOLIDAY

Introduction

We celebrate the start of the year 2011 with dramatically expanded federal gift tax exemptions. The 2010 Tax Act provides a \$5 million exemption until January 1, 2013, from the following federal transfer taxes:

- Gift tax on transfers during lifetime;
- Estate tax on transfers upon death; and
- Generation-skipping transfer tax on transfers to grandchildren and younger generations during lifetime or upon the death of the transferor.

These changes present new opportunities for lifetime transfers of wealth to children and grandchildren. A national commentator recently noted that “a surge in gifting” is expected in 2011 as a result.

Annual Exclusion Gifts

Gifts to children and grandchildren equal to the annual gift tax exclusion amount continue to be an effective method for transferring wealth to children and grandchildren. The annual exclusion amount for the year 2011 is \$13,000 per recipient. A married couple may give each recipient \$26,000 without the need to file gift tax returns.

Gifts for Tuition or Medical Expenses

In addition to the annual exclusion gifts, a parent or grandparent may pay tuition or medical expenses for a child or grandchild free from gift tax. To qualify for this exception from the gift tax, the tuition check must be payable directly to the educational institution and the medical expense check must be payable directly to the medical provider.

\$5 Million Gift Tax Exemption

Beyond the existing annual exclusion gifts and gifts for tuition and medical expenses, each person now has a \$5 million lifetime cumulative gift tax exemption (\$10 million for couples), a dramatic increase from the prior \$1 million exemption. The 2010 Tax Act unified the gift and estate taxes. Thus, each person may give up to a maximum of \$5 million during his or her lifetime or upon death free from gift and estate taxes. Any portion of the \$5 million not given away during lifetime will pass free from estate tax after death.

Generation-Skipping Transfer Tax Exemption

Each person also has a \$5 million generation-skipping transfer (“GST”) tax exemption (\$10 million for couples). The GST exemption enables a grandparent, during his or her lifetime or upon death, to make significant gifts to grandchildren free from GST. This exemption is co-extensive with the gift tax exemption and not in addition to it.

Valuation Discounts

Discounts are often applied in determining the fair market value of closely-held stock, limited partnership units, or limited liability company membership units to reflect the lack of control and lack of marketability of such ownership interests. Bills have been introduced in Congress that would restrict or eliminate the

use of valuation discounts in determining fair market value for gift tax purposes. The 2010 Tax Act does not include any restrictions on the use of valuation discounts. For now, valuation discounts remain an important tool to be used with the \$5 million exemption to leverage gifts of closely-held business ownership interests.

Minnesota Gift and Estate Tax

Currently, Minnesota does not have a gift tax. Minnesota has an estate tax with a maximum estate tax rate of 16% for gross estates of \$10 million or more. The filing requirement for the Minnesota estate tax is \$1 million.

Opportunities and Advantages of Gifting

The dramatic increase in the gift tax exemption was unexpected and presents new opportunities to transfer wealth to children or future generations. Advantages of gifting include the following:

1. A gift removes future appreciation on the property from the estate and, thus, is more effective than a transfer at death.
2. A transfer is more tax-efficient if made during lifetime due to differences in the way the gift tax and the estate tax are computed.
3. Transfers can be made in trust as well as outright. Transfers in trust during lifetime allow a parent or grandparent the opportunity to guide the recipient on the wise use of the assets transferred.

Disadvantages of Gifting

Lifetime gifts have the following disadvantages:

1. To make a completed gift, the donor must relinquish all control over the property given.
2. The recipient of the gift must use the donor's basis ("carryover basis") in determining gain or loss on a subsequent sale of the property. If the recipient received the property as a result of the death of the donor, the recipient's basis in the property is "stepped-up" to fair market value as of the donor's death. Gifting leads to higher taxes than transfer upon death if the value of the property appreciates in the hands of the recipient.
3. The 2010 Tax Act expires on December 31, 2012. Thereafter, the gift and estate tax exemptions will be \$1 million unless Congress takes further action. One action Congress could take is to lower the gift and estate tax exemptions to something between \$1 million and \$5 million. If the estate tax exemption is less than \$5 million at the time of a donor's death, there is a risk of additional estate taxes being imposed on the donor's estate as a "clawback" of the tax benefits of utilizing the higher gift tax exemption.

The dramatic change in the gift tax exemption is available for only two years. Further, Minnesota could enact a gift tax in the coming years. Those who see opportunities in the current law should act soon.



HOLIDAY GIVING

Moss & Barnett is committed to giving back to the community, and this year we were honored to participate once again in **Sponsor-A-Family**, a holiday project of Catholic Charities of St. Paul and Minneapolis. This was Moss & Barnett's 20th year participating in this important community outreach program. Sponsor-A-Family helps low-income families and individuals in the Twin Cities area celebrate the holiday season. Participating family members prepare a list of desired items (e.g., clothing, household items, toys), and Moss & Barnett employees donate time and money to purchase the listed items, as well as a grocery store gift certificate to provide a holiday meal for the family. You can learn more about Sponsor-A-Family at sponsorafamily.org.



Julie Donaldson, Personnel Administrator, and Lori O'Donnell, Facilities Manager, with gifts for this year's family





JENNIFER REUSSÉ NAMED PAUL VAN VALKENBURG SERVICE AWARD RECIPIENT

Moss & Barnett established the Paul Van Valkenburg Service Award* in 2001. It is awarded annually to a Moss & Barnett team member in recognition of his or her outstanding volunteer contributions to the community. The award is named after our retired colleague, Paul Van Valkenburg, whose volunteer career set an example of the spirit of service and dedication that we seek to promote and recognize within our firm.

Jennifer Reussé, an attorney in our real estate practice area, was the 2010 recipient of the Paul Van Valkenburg Service Award. Jennifer was given this award based on her work with a wide range of charitable organizations, including:

Junior League of Minneapolis (“JLM”) - JLM is an organization of women committed to promoting voluntarism, developing the potential of women, and improving communities through the effective action and leadership of trained volunteers. Established in 1923, JLM continues to develop projects to fill needs within the Minneapolis community. Past projects include helping to found the Greater Minneapolis Crisis Nursery, Free Arts Minnesota, and the Jeremiah Program. Current projects address issues from hunger to literacy. Jennifer has been an active member of JLM since 2006. Last year, she was the legal advisor on the board of directors, attending board meetings and negotiating over 30 contracts on behalf of JLM. She also prepared a Leadership Handbook and a Member Handbook, rewriting and reorganizing many of JLM’s policies and procedures. This year, she is on the Backpack Buddies Committee, which provides backpacks of food every Friday of the school year to very low-income students at Anderson Open Elementary School in Minneapolis who would not otherwise have enough food to eat over the weekend.

Adaptive Recreation and Learning Exchange (“ARL&E”) – ARL&E is a cooperative among the Cities of Bloomington, Eden Prairie, Richfield, and Edina that provides recreation, leisure, and community education opportunities for people with disabilities. The past two winters, Jennifer took training to become a volunteer ski instructor for ARL&E and taught the fundamentals of downhill skiing to students with developmental disabilities.

Guthrie Theatre – For three years, Jennifer was an active member of the Business Circle Committee of the Guthrie Theater, a nationally-recognized regional theater. The committee is comprised of executives and emerging business leaders who volunteer their time and energy to help the Guthrie to cultivate and engage corporate donors.



Jennifer Reussé, Paul Van Valkenburg Service Award Recipient

Minnesota Women Lawyers (“MWL”) – For five years, Jennifer has been a mentor in the MWL attorney-law student mentor program. Moss & Barnett’s involvement with MWL is discussed further in this newsletter at page 4.

Fund for Legal Aid One Hour of Sharing – Jennifer is one of our firm’s liaisons for an important fundraising campaign for the Legal Aid Society of Minneapolis.

Past recipients of the Paul Van Valkenburg Service Award include **Chuck Parsons, Tom Keller, Adrienne Summerfield, Kevin Busch, Cheryl Riggs, Marcy Frost, and Bill Haug**. We are proud to recognize Jennifer and our other award recipients for their willingness to be part of organizations focused on improving the lives of others.

**The Paul Van Valkenburg Service Award includes a cash donation by the firm to the recipient’s chosen charity, a special recognition ceremony, and a commemorative piece of pottery created by Minnesota artist, Steve Hemmingway. For 2010, the firm’s donation was made to the Junior League of Minneapolis.*

MIGGIE CRAMBLIT JOINS MOSS & BARNETT

Miggie E. Cramblit has joined our regulated entities practice area. Miggie received her law degree from Hamline University School of Law in 1980. Following graduation, she clerked for former Associate Justice James C. Otis of the Minnesota Supreme Court. After completing her clerkship, she entered private practice as a litigation associate and public defender. For most of her 30-year career she has served as inside counsel to natural gas and electric utilities. She is the former general counsel for NorthWestern Energy (Sioux Falls, South Dakota, and Butte, Montana), The Dayton Power & Light Company (Dayton, Ohio), and Minnegasco (now the Minnesota division of CenterPoint Energy, Minneapolis, Minnesota). As an adjunct professor at William Mitchell College of Law, she taught legal writing for over ten years, as well as a course on negotiation and mediation. Miggie also served on the William Mitchell Board of Trustees and was Chair of the Board. She was one of the founders of the Public Utility Section of the Minnesota State Bar Association. She is licensed to practice law in Minnesota, Montana, Nebraska, and South Dakota.



Miggie Cramblit

Welcome to the team, Miggie!



MOSS & BARNETT CONGRATULATES CINDY ACKERMAN

Moss & Barnett is pleased to congratulate **Cindy Ackerman**, a member of our wealth preservation and estate planning practice area, who was selected as a “FIVE-STAR Wealth Manager” for 2011. The “FIVE-STAR Wealth Manager” award is limited to less than five percent of all wealth manager professionals within the Twin Cities area. Wealth managers are rated by their clients and other financial service professionals on service, integrity, knowledge/expertise, communication, value for fees charged, meeting of financial objectives, quality of recommendations, and overall satisfaction. Cindy represents clients in a variety of matters, including wills and trust agreements, complex estate planning, charitable gift planning, tax strategy planning and compliance, tax-exempt organizations, and conservatorship and guardianship proceedings. Cindy understands that many of these issues can be difficult and strives to guide her clients through complicated situations with sensitivity and professional insight.

Congratulations, Cindy, from all of us at Moss & Barnett!



Cindy Ackerman





By Yuri B. Berndt and Joseph G. Socha



Yuri Berndt is a member of our business law and wealth preservation and estate planning practice areas. He represents individuals and business clients in the areas of business organization, structuring, and transactions. He also advises clients on tax planning issues. Yuri can be reached at 612.877.5267 or BerndtY@moss-barnett.com.



Joe Socha is a member of our wealth preservation and estate planning practice area. He represents individuals in the areas of estate planning and taxation, including the development and implementation of wealth transfer strategies and income, gift, and estate tax planning and compliance. Joe can be reached at 612.877.5283 or SochaJ@moss-barnett.com.

A FEW NEW TWISTS FOR BUSINESS TAXPAYERS

The 2010 Tax Act extends most, if not all, of the commonly called “Bush income tax cuts” through 2012. While many of the income tax provisions require no immediate action on the part of individual or business taxpayers (for example, the business and individual income tax rates and the 15% long-term capital gains and qualified dividends tax rates all remain the same through 2012), there are a few new or extended provisions that can be beneficial for businesses and their employees right away.

100% Bonus Depreciation in 2011

Businesses, including C-corporations, S-corporations, limited liability companies (LLCs), and sole proprietorships, can write off the entire purchase price of certain assets in 2011. These provisions must be considered when completing current-year budgets and developing long-term business growth strategies. Bonus depreciation on the purchase of qualified new business equipment now equals 100% if placed in service after September 8, 2010, and before January 1, 2012. The bonus depreciation rate declines to 50% for qualified property placed in service after December 31, 2011, and before January 1, 2013. In the simplest terms, a purchase of any new “qualified” property placed in service in 2011 (whether purchased on credit or with cash payment) will result in a tax deduction equal to its purchase price (a write-off of the entire purchase price). Even though we are at the start of 2011, you will want to make sure that you incorporate this deduction in your tax planning for 2011 and make sure qualified property is purchased and placed in service in 2011.

Section 179 Expensing

Section 179 expensing allows a taxpayer to take a tax deduction for the cost of qualified property purchased and placed in service in 2011, subject to certain taxable income and qualified purchase limitations. The Section 179 expensing limit continues to be \$500,000 for 2011 but will go down dramatically in 2012. You may ask why this is important given the 100% bonus depreciation. While bonus depreciation is limited to the purchase of “new” qualified property placed in service in 2011, Section 179 expensing is allowed on qualified property, including previously used property. This provision can be very beneficial when considering the purchase of assets of an existing business.

Reduction in S-corporation Built-in Gains Tax Period to Five Years

A corporation that elected to be an S-corporation more than five years ago may benefit from the reduction in the S-corporation built-in gains tax recognition period. Prior to 2010, an S-corporation that sold assets within ten years from the date of its S-corporation election was required to calculate and pay a built-in gains tax (a double tax). This built-in gains tax effectively taxes the gain on the sale of

an S-corporation's assets twice, just as gains are taxed on the sale of a C-corporation's assets (once at the corporation level and a second time when the proceeds are distributed to the C-corporation shareholders). For 2011, this built-in gains tax period has been reduced to five years. What does this mean? If your S-corporation election was made before 2006, you do not have to worry about paying the S-corporation built-in gains tax on the sale of your company's assets in 2011. This can be a significant tax benefit for any seller in 2011 and make more S-corporations open to selling assets.

- **S-corporation Tax Planning.** The five-year S-corporation built-in gains period creates a current opportunity to distribute business real estate (or other assets) from an S-corporation to its shareholders (or an LLC owned by the shareholders) in a potentially tax-neutral manner. A distribution of an appreciated asset from an S-corporation to its shareholders is subject to income tax on the asset's appreciation (the difference between its current fair market value and its tax basis). If the S-corporation built-in gains period has not expired, the S-corporation is subject to the built-in gains tax (a double whammy). With the depressed real estate market, the low capital gains tax rate, and bonus depreciation deductions, 2011 might be the right time to separate an S-corporation's real estate (or other lines of business) from the S-corporation structure. There are many business, legal, and tax reasons why this may be beneficial to an owner and to the business.
- **Corporate Conversions.** The new five-year S-corporation built-in gains period makes 2011 a good year to consider conversion of an S-corporation to a limited liability company. The details of this type of transaction are beyond the scope of this article, but Minnesota law allows a Minnesota corporation to convert to a limited liability company. A limited liability company, which is treated as a partnership for federal and Minnesota income tax purposes, has a number of advantages over an S-corporation,

including when considering expanding the company ownership to management (by using "profits interests") or selling ownership interests to management (with an IRC Section 754 asset step-up, which can produce current deductions for the buyer). An LLC is not the right choice in all situations, but advantageous opportunities may exist. A comprehensive review of the business and its objectives must be completed before undertaking a conversion transaction.

Employee Social Security Taxes

The 2010 Tax Act reduces the employee social security tax rate from 6.2% to 4.2% for 2011. Employees and self-employed individuals pay social security taxes on their earned income (up to a \$106,800 limit). The 2% rate reduction means an employee's tax bill, assuming wages of \$60,000, will be reduced by \$1,200 (\$60,000 of wages times the 2% reduction). Employers are still required to pay social security tax at a rate of 6.2% on its employees' compensation. Be sure to change your payroll processing to accommodate the lower withholding level.

In Conclusion

The 2010 Tax Act maintained the "Bush income tax cuts" for individuals, individually and as owners of LLCs and S-corporations. The 2010 Tax Act and the prior "Bush income tax cuts" did not affect federal corporate income tax rates, which continue to range from 15% on the first \$50,000 of corporate income to an effective rate of 35%. Likewise, there has been no change to Minnesota's corporate income tax rate of 9.8% or individual income tax rates ranging from 5.35% to 7.85%. The changes in the bonus depreciation, Section 179 expensing, and the built-in gains tax period, however, present significant opportunities for businesses and their owners this year. You should begin planning today to take advantage of these opportunities.






**Remember to tune in to WCCO 830AM Saturdays at Noon to listen to MINNESOTA LAW,
Presented by Moss & Barnett**

This one-hour program focuses on interesting law facts and important new developments in the law and features a different Moss & Barnett attorney and topic each week. Some of our recent programs featured Moss & Barnett attorneys Peter Koller, on “What to Expect When You Get Called for Jury Duty” (October 30, 2010); David Biek, on “Protecting Patents in Foreign Countries” (December 4, 2010); and Brian Grogan, on “Net Neutrality – What Does It Mean?” (January 30, 2011). Upcoming programs will feature Chief Justice Lorie Gildea, on the “State of Minnesota Courts” (April 9, 2011), and Robert Stein, Everett Fraser Professor of Law, University of Minnesota Law School, on the Uniform Law Commission (May 7, 2011), in addition to many of our Moss & Barnett attorneys discussing a variety of topics. To learn more about our upcoming programs and to listen to any of our past broadcasts, visit our web site at moss-barnett.com and click on the *MINNESOTA LAW* icon. Also, we are pleased to announce that podcasts of our *MINNESOTA LAW* shows are now available on iTunes, starting with our January 8, 2011 show.

IMPORTANT NOTICE

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