

# 2010 Mutual Fund Tax Guide





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## Purpose of This Tax Guide

This tax guide provides some basic information about the tax forms you have received or that may be mailed to you later this year. The information on pages 7-14 lists the various tax forms, who will receive them, and when the forms are required to be mailed. We have included a detailed explanation of each tax form, frequently asked questions and answers, and where to go for further information.

**Although this guide may assist you in preparing your tax return, it is not designed to provide specific tax advice or guidance. Given the scope and complexity of our tax laws, you should consult your tax or financial advisor who may have knowledge of your personal financial history and who can best assist you in preparing your tax return.**

## Tax Items of Interest

### ***The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (“the Act”)***

Signed in December 2010, this Act extended several tax provisions beneficial to mutual fund shareholders.

The current, reduced tax rates on long-term capital gains and qualified dividend income have been extended through December 31, 2012.

<b>2011 – 2012</b>		
<b>Ordinary Income Tax Rate</b>	<b>Ordinary Dividend Tax Rate</b>	<b>Qualified Dividend Tax Rate (QDI)</b>
10%	10%	0%
15%	15%	0%
25%	25%	15%
28%	28%	15%
33%	33%	15%
35%	35%	15%

Furthermore, the exemption from NRA withholding on qualified interest income and short-term capital gains paid to certified foreign shareholders has been extended through all fiscal tax years for mutual funds which begin prior to January 1, 2012.

Section 3406(b) of the Internal Revenue Code requires backup withholding to occur upon certain payments being made to a mutual fund shareholder, including dividends, short-term and long-term capital gains, and redemptions/exchanges. The backup withholding rate was scheduled to rise to 31% on January 1, 2011 but instead will remain at 28%.

The Pension Protection Act provision allowing an income exclusion of up to \$100,000 for qualified charitable distributions from IRAs which were paid directly to certain charitable organizations after the IRA owner attained the age of 70 ½ expired at the end of 2009. This provision is now extended through December 31, 2011. A transition provision does exist allowing IRA owners to elect to have qualified charitable distributions made in January 2011 only to be treated as having been made on December 31, 2010. Therefore that distribution must be recorded on their 2010 federal tax returns, even though that distribution event will be reported to the IRA owner and the IRS on the 2011 tax year Form 1099-R.

The tax benefits of Coverdell education savings accounts were slated to expire on December 31, 2010, however, the Act extended such provisions for two years, through December 31, 2012, to include but not limited to the following: \$2,000 annual contribution amount, tax-free status of distributions when used for qualified higher, secondary, and elementary expenses, age rules for special needs beneficiaries, and the extended time frame during which contributions can be made and excess contributions removed without additional tax.

The American Opportunity Tax Credit, previously known as the Hope Credit, was modified to make the credit available to

a broader range of taxpayers to assist with payment of qualified tuition and related education expenses and is now available through December 31, 2012 to qualified taxpayers based upon their modified AGI. For more information regarding this credit, please see the IRS Publication 970, Tax Benefits for Education.

The Act allows for an estate tax exclusion amount of \$5 million in 2011 and will be indexed for inflation for decedents dying January 1, 2012 and forward with a maximum estate tax rate of 35 percent. The same thresholds apply to gifts made after December 31, 2010. These annual exclusion amounts and tax rates are scheduled to expire after December 31, 2012.

Federal Insurance Contributions Act (FICA) tax applicable to employees is reduced by the Act from 6.2 percent of total covered wages to 4.2 percent for the 2011 tax year only.

**Maximum Contribution Limits** – Taxpayers can contribute up to the amounts listed below for the 2010 and 2011 tax years. “Catch-up” contributions, for those shareholders age 50 or over on December 31 of each year 9 are also provided below.

<u>2010 &amp; 2011</u>	<u>Contribution</u>	
		<u>“Catch-Up”</u>
Traditional IRA	\$5,000	\$1,000
Roth IRA	\$5,000	\$1,000
SEP IRA	\$49,000*	\$5,500
SIMPLE IRA	\$11,500	\$2,500
Coverdell Education Savings (CESA)	\$2,000	N/A

\*or the lesser of 25% of your 2010 or 2011 compensation

### **Savers Credit**

If you make eligible contributions to an employer-sponsored retirement plan or to an IRA, you may be able to take a tax credit. To be eligible for the credit you must be at least 18 years of age, not a full-time student, and cannot be claimed as a dependent on another person's federal tax return. The tax credit may be up to \$1,000 or up to \$2,000 if married filing jointly. Please review IRS Publication 590 and IRS Form 8880 for more details.

### **Gift Tax Exclusion**

Gift tax is a tax on the transfer of property by one individual to another while receiving nothing, or less than full value, in return. The tax applies whether the donor intends the transfer to be a gift or not. The annual exclusion for gifts made to a donee during the calendar year has increased to \$13,000, for the 2009 and future tax years.

### **Mandatory Cost Basis Reporting**

The Emergency Economic Stabilization Act of 2008 requires mutual funds to report cost basis information for shares purchased on or after January 1, 2012. Shareholders will generally be required to use the cost basis information provided by the mutual fund for shares purchased on or after that effective date. Eligible accounts currently have their cost basis tracked using the IRS single-category

average cost method. The long-term or short-term designation of a gain/loss associated with a redemption (or exchange) of mutual fund shares is also required under the Act, beginning with the 2012 tax year. For your benefit, that gain/loss information will be incorporated into the Average Cost statement you receive in conjunction with your 2010 1099-B tax form, if applicable.



## TAX FORMS

### Form 1099-DIV

**Purpose** - Reports all dividend and capital gain earned from distributions (cash or reinvested) on non-retirement accounts. If there were no taxable capital gain or dividend distributions, you will not receive a 1099-DIV. 1099-DIV information is reported on either IRS Form 1040, Schedule B or Form 1040A, Schedule 1. Your capital gain may be reported on Schedule D. See the instructions for filing Schedule D. You will not receive a Form 1099-DIV if your total dividends for a fund are less than \$0. Even if you do not receive Form 1099-DIV, you must still report all of your taxable dividend income on your tax return.

**Who Will Receive It?** - Individuals, trusts, estates, partnerships and certain other institutions. Retirement plan accounts will NOT receive this form.

**Required Mailing Date** - February 15, 2011

**Box 1a:** Reports total ordinary dividends, including short-term capital gains (will include amount from box 1b)

**Box 1b:** Reports qualified dividend income that may be taxed at a reduced rate depending on your tax bracket

**Box 2a:** Reports total long-term capital gains

**Box 3:** Reports non-taxable portion of a dividend distribution

**Box 4:** Reports backup withholding to include on your tax return as taxes withheld

**Box 6:** Reports foreign tax paid

## **Form 1099-B**

**Purpose** - If you have made any redemptions, exchanges, or payments from non-retirement or non-money market accounts, a Form 1099-B will be sent. The information from the 1099-B is reported on the IRS Form 1040, Schedule D. Sales of municipal income fund shares are taxable and are reported on IRS Form 1040, Schedule D.

**Who Will Receive It?** - All accounts which had redemptions during 2010 except for retirement plan, corporate, and certain institutional accounts.

**Required Mailing Date** - February 15, 2011

**Box 1a:** Trade date fund shares were sold

**Box 2:** Reports gross proceeds from sale, is reported on Schedule D

**Box 4:** Reports backup withholding to include on your tax return as taxes withheld

**Box 5:** Reports number of shares that were sold

**Box 7:** Description, including share price and number of shares of transaction

## **Form 1099-R**

**Purpose** - Reports distributions from a Traditional IRA, Roth IRA, SEP IRA, SIMPLE IRA and certain Qualified Plans. This information must be reported on IRS Form 1040 or Form 1040A, and may be reported on Form 8606.

**Who Will Receive It?** - Individuals who took a distribution in 2010. Any IRA trustee to trustee transfers are not reportable.

**Required Mailing Date** - January 31, 2011

**Box 1:** Gross distributions including rollovers or transfer conversions to a Roth IRA or a recharacterized IRA contribution

**Box 2a:** The taxable amount for distributions from IRAs is generally not computed

**Box 4:** Federal withholding

**Box 7:** Codes that identify the type of distribution made. See the reverse side of Form 1099-R for detailed descriptions of the codes

**Box 10:** State withholding

## **Form 1099-Q**

**Purpose** - Reports distributions from Coverdell ESA accounts.

**Who Will Receive It?** - Individuals who took a distribution in 2010. Trustee to trustee transfers are considered reportable on this form.

**Required Mailing Date** - January 31, 2011

**Box 1:** Gross distributions including rollovers and transfers

**Box 2:** Only displays earnings made on excess contributions, otherwise not applicable for 2010

**Box 3:** N/A

**Box 4:** Reports if the distribution in Box 1 was a trustee to trustee transfer

## **Form 1099-INT**

**Purpose** - Reports tax-exempt interest dividends on non-retirement accounts. See the appropriate 1040 tax return instructions to determine the proper manner in which to report this information to the IRS.

**Who Will Receive It?** - Individuals, trusts, estates, partnerships and certain other institutions. Retirement plan accounts will NOT receive this form.

**Required Mailing Date** - February 15, 2011

**Box 1:** Reports interest income

**Box 4:** Reports backup withholding to include on your tax return as taxes withheld

**Box 8:** Reports tax-exempt interest dividends - Reportable on line 8b of Form 1040 or 1040A

**Box 9:** If applicable, reports tax-exempt interest AMT dividends – See the Instructions for Form 6251, Alternative Minimum Tax - Individuals

## **Form 1042-S**

**Purpose** - Used to report dividends (including short term capital gains) subject to withholding paid to nonresident aliens.

**Who Will Receive It?** - Foreign investors who are not U.S. citizens.

**Required Mailing Date** - March 15, 2011

**Box 1:** Income code

**Box 2 :** Gross income paid

**Box 5:** Country withholding rate

**Box 6:** Exemption code

**Box 7:** Federal tax withheld

**Box 13b:** Type of Recipient

**Box 16:** Country code

**Box 17-20:** Non-Qualified Intermediary information

## **Form 5498**

**Purpose** - Reports IRA contributions, rollovers, conversions, and recharacterizations. These amounts are reported on one of the IRS Forms 1040, 1040A or Form 8606.

**Who Will Receive It?** - Individuals who contributed to a Traditional, Roth, SEP, or SIMPLE IRA for 2010. Assets transferred between like arrangements from one custodian or trustee to another will not generate this form.

**Required Mailing Date** - May 31, 2011 (except for fair market value information which is supplied via an annual statement by January 31, 2011)

**Box 1:** Traditional IRA contributions made in 2010 and through April 15, 2011 for 2010

**Box 2:** Rollover contributions

**Box 3:** Amount converted or reconverted to a Roth IRA from a Traditional, SEP or SIMPLE IRA

**Box 4:** Amount recharacterized from one IRA type to another

**Box 5:** Fair market value at year end

**Box 7:** Type of IRA

**Box 8:** SEP contributions made in 2010

**Box 9:** SIMPLE contributions made in 2010

**Box 10:** Roth IRA contributions made in 2010 and through April 15, 2011 for 2010

**Box 11:** Reports to the IRS if a Required Minimum Distribution is required to be taken for the tax year of 2011

## **Form 5498-ESA**

**Purpose** - Reports Coverdell ESA contributions, rollovers, and transfers.

**Who Will Receive It?** - Individuals who contributed to a Coverdell ESA account on behalf of a beneficiary for the tax year of 2010. A shareholder who transferred assets from one custodian or trustee to another will also receive this form.

**Required Mailing Date** - May 2, 2011

**Box 1:** Coverdell ESA contributions made in 2010 and through April 15, 2011 for 2010

**Box 2:** Rollovers and transfers made during 2010



## Special Tax Considerations

### Cost Basis Statements

Shareholders who took a distribution from their mutual fund accounts may receive an Average Cost Basis Statement. Retirement plan accounts or those accounts which have had a change of ownership or control will not receive an Average Cost Basis Statement.

In addition to fund and shareholder registration information, your statement will show:

- Trade date
- Number of shares redeemed
- Redemption price
- Redemption proceeds
- Average cost basis
- Gain (loss)

The dollar amount of your gain (loss) is calculated by using the IRS approved "Average Cost Single Category" method of accounting. Cost basis is a way of measuring the dollar amount of your investment for tax purposes. The basis of stocks, bonds and mutual fund shares includes acquisition cost, commissions and fees paid, as well as other adjustments. The Average Cost Single Category method uses an average basis of shares you own, taking into consideration those shares acquired at different times with different prices. For example, a shareholder makes three share purchases: 100 shares on 1/2/10 at \$10.00 per share, 100 shares on 6/1/10 at \$12.00 per share and 100 shares on 12/1/10 at \$20.00 per share. The 300 shares purchased cost a total of \$4,200. The average cost per share is \$14.00 (\$4,200 divided by 300 shares.) If you sell 150 shares, the basis of those

shares sold is \$2,100 (150 shares multiplied by \$14.00 average cost per share) A wash sale transaction occurs when you sell shares at a loss and purchase new shares (including reinvested dividends) in the same fund within a 61 day period, beginning 30 days prior to the sale and ending 30 days after the sale. With wash sales, you may not be able to claim some or all of the capital loss immediately. The amount of any postponed loss is added back to the cost basis of the remaining shares you own. When you eventually sell those shares, your average cost will reflect the postponed loss amount.

Before you elect to use the average cost basis statement for reporting purposes, you should consider the several ways to calculate the cost basis of shares sold. Please consult with your tax advisor to determine whether or not the average cost basis method is the most advantageous method for your specific financial situation.

### **Dividends from U.S. Government Obligations**

Some states do not tax their residents on mutual fund income received that is earned directly from U.S. Government obligations. Short-term capital gain distributions, although treated as ordinary income are generally not eligible for state tax-exemption. A statement may accompany your Form 1099-DIV indicating the percentage of income your fund earned that was attributable directly to U.S. Government obligations.

## **Alternative Minimum Tax**

The Alternative Minimum Tax (AMT) was created to prevent excessive use of tax deductions and credits. Its goal is to ensure that individuals who benefit from these deductions pay a minimum amount of federal income tax. Refer to the instructions for Form 1040 or Form 6251 to determine if this tax applies to you. The AMT calculation begins with your regular taxable income and adjusts for certain "tax-preference" items. One of these "tax-preference" items that would be added back to your regular taxable income is tax-exempt interest from private activity bonds. Private activity bonds are municipal bonds issued to benefit private, for-profit operations. If you own shares of a fund that invests in private activity bonds, you must include that portion of the funds distributions that are attributable to private activity bonds as a "tax-preference" item in your AMT calculation. If a fund invests in private activity bonds, a letter will generally be sent that reports to its shareholders the amount of distributions subject to the AMT.

## **Capital Losses**

Taxpayers who redeemed mutual fund shares at a capital loss during the year may be able to use those losses to offset other capital gains or in some cases ordinary income. The IRS has created several rules in order to discourage loss-oriented selling. Two of these rules are:

## **Wash Sales**

If you purchase shares of a mutual fund (including reinvested dividends) within 30 days before or after you redeemed shares of the same mutual fund for a loss, the redemption will be considered

a “wash sale” and some or all of your capital loss will be deferred. The amount of your deferred loss increases the cost basis of the shares purchased which created the wash sale. When those shares are subsequently sold the deferred loss is then allowed. Please consult your tax advisor for more information about wash sale rules.

### **Long-Term Capital Gain Distributions**

Capital gain distributions from a mutual fund are generally reported as long-term capital gains regardless of how long you owned shares in a fund. However, if you owned shares for less than six months, received a capital gain on these shares, and sold them at a loss, part or all of the loss on the sale of the shares (which would normally be short-term based on the holding period) may be recharacterized as long term instead. The amount of the loss equal to or less than the capital gain distribution is the amount which will be recharacterized as long term. The amount of the loss greater than the capital gain distribution remains short term. See IRS Publication 564 or consult a tax advisor before making this calculation.

## QUESTIONS AND ANSWERS

### **Q - How can I request duplicate tax forms?**

A - After February 15, 2011, you can contact U.S. Bancorp Fund Services, LLC to receive duplicate copies of your tax forms.

### **Q - Will I receive a Cost Basis Statement?**

A - You should receive a cost basis statement, using the IRS Average Cost Single Category Method, if you redeemed shares from a taxable account during 2010 and received Form 1099-B. A cost basis statement is mailed by February 15, 2011, in conjunction with Form 1099-B. There are certain situations, such as a transfer of shares, which may prevent you from receiving a cost basis statement. Please consult IRS Publication 564 Mutual Fund Distributions for additional information regarding cost basis for your mutual fund account.

### **Q - Can I spread the taxable portion of a conversion to a Roth IRA over future tax years?**

A - Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA) only allowed that option for conversions which occurred during the 2010 calendar year. Beginning with 2011, the taxable portion of a conversion to a Roth IRA must be included in your taxable income for the year in which the conversion was performed.

### **Q - At what point can I no longer recharacterize a Roth IRA for the 2010 tax year?**

A - A Roth IRA can be recharacterized through October 17, 2011.

**Q - What is a capital gain distribution and how is that different from a capital gain that is incurred when shares of my account are sold?**

A - A Fund Capital Gain Distribution can occur when a fund buys and sells stocks and other securities within the fund's portfolio. This activity may create a net capital gain for the fund. This capital gain distribution is taxable for non-retirement accounts. A Shareholder Capital Gain occurs when the shareholder sells shares for a gain in a taxable, non-retirement, non-money market account.

**Q - Do I have to report reinvested capital gains & dividends on a non-retirement account?**

A - Yes, capital gain and dividend distributions are considered income in the year they are distributed regardless whether they are paid in cash or reinvested. The amount of the reinvested dividends and capital gains are then added to the cost basis when a redemption occurs. This is to avoid being taxed twice on the same dollars.

**Q - Why are SEP and SIMPLE contributions that were made in 2011 for the 2010 tax year NOT on Form 5498?**

A - IRS rules state that only contributions made to a SEP and SIMPLE IRA during the calendar year are to be reported on Form 5498. Only contributions made during the 2010 calendar year will be reported on the 2010 Form 5498, regardless of which tax year those contributions were directed.

**Q - What happens if I make an excess contribution?**

A - You will receive Form 5498 (Form 5498-ESA for a Coverdell ESA account) that details the total amount of your contribution. If the excess contribution is removed, you will receive Form 1099-R (Form 1099-Q for a Coverdell ESA account) detailing the removal of that excess, including any earnings. Please consult IRS Publications 590 and 970 for more information regarding the IRS penalties associated with excess contributions.

**Q - Why was there backup withholding on my taxable account?**

A - Generally, backup withholding applies when the Fund did not have either a properly completed application or IRS Form W-9 on file or the IRS has instructed the Fund to withhold due to a TIN/Name mismatch on your account or due to your failure to pay federal taxes.

**Q - Do I have to report capital gains and dividends on an IRA account?**

A - No, if they were reinvested in the same IRA. Yes, if taken as a cash distribution.

**Q - What tax forms are mailed to nonresident aliens?**

A - Form 1042-S is mailed to nonresident aliens who received Fund capital gain or dividend distributions on their taxable account or liquidated assets from a retirement account. A nonresident alien is not a U.S. citizen.

**Q - Where can I get more information on completing my tax return?**

A - Please refer to the Additional Resources section in this tax guide for more information, or consult a tax advisor.

## Additional Resources

**IRS Web Site** - Download forms, instructions, and publications: [www.irs.gov](http://www.irs.gov)

**IRS Tele Tax Topics** - Touch tone service on topics, 24 hours/day, 7 days/week (rotary service will vary) 1-800-829-4477

**\* See the IRS Form 1040 instructions or IRS Publication 910 for a complete list of Tele Tax Topics**

### \*Topic

<u>Number</u>	<u>Subject</u>
155	Forms/Publications
307	Backup Withholding
309	Roth IRA Contributions
310	Coverdell Education Savings Accounts
404	Dividends
409	Capital Gains & Losses
410	Pensions and Annuities
412	Lump-Sum Distributions
413	Rollovers from Retirement Plans
424	401(k) Plans
451	IRAs
553	Tax on a Child's Investment Income
556	Alternative Minimum Tax
557	Tax on Early Distributions from Traditional and Roth IRA's
558	Tax on Early Distributions from Retirement Plans
610	Retirement Savings Contribution Credit
652	Notice of Underreported Income

**Tax Forms** - Forms, instructions, and publications can be found at your local IRS office, bank, post office, library, or by calling the IRS Forms Distribution Center at 1-800-TAX-FORM.



**IRS General Information** - 1-800-829-1040

**\*\*Key IRS Publications** - Please see IRS Publication 17 or 910 for a complete list.

<u>Number</u>	<u>**Title</u>
3	Armed Forces' Tax Guide
17	Your Federal Income Tax (For Individuals)
54	Tax Guide for US Citizens and Resident Aliens Abroad
505	Tax Withholding & Estimated Tax
514	Foreign Tax Credit for Individuals
515	Withholding of Tax on Nonresident Aliens and Foreign Entities
525	Taxable and Nontaxable Income
526	Charitable Contributions
530	Tax Information for Homeowners
550	Investment Income and Expenses
552	Recordkeeping for Individuals
553	Highlights of Tax Changes
554	Tax Guide for Seniors
560	SEP, SIMPLE, and Qualified Plans
564	Mutual Fund Distributions
590	IRAs
593	Tax Highlights for U.S. Citizens and Residents Going Aboard
907	Tax Highlights for Persons with Disabilities
929	Tax Rules for Children & Dependents
970	Tax Benefits for Education

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