

# TAX UPDATE

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CERTIFIED PUBLIC ACCOUNTANTS AND ADVISORS

DENVER | HOUSTON | DALLAS | ORANGE COUNTY

# AGENDA

- Business Tax Update And Planning Ideas
- Retirement Planning
- State Tax Considerations
- AICPA Update
- Final Items of Note

# BUSINESS TAX UPDATE AND PLANNING IDEAS

- How do you plan when:
  - Expiration of Bush-era tax cuts loom
  - Expirations of various provisions are imminent
  - Upcoming elections will have an impact
  - New tax legislation will impact businesses and individuals
  - Tried and true thought processes of deferred income and accelerated expenses will not always be the best answer
  - Implementation may take time (don't leave to the last minute)
  - Business and economic constraints must be considered
  - Crystal balls are undependable

# SMALL BUSINESS EXPENSING DECLINES AFTER 2011

- The increased Code Section 179 deduction allows a business to expense up to \$500,000 of the cost of qualifying property acquired in 2011
- The ceiling for the total cost of qualifying property is increased to \$2M
- The definition of qualifying property is expanded to include up to \$250,000 of certain real property
  - Qualified leasehold improvement property
  - Qualified restaurant property
  - Qualified retail improvement property
- For 2012, the annual dollar limit is set to fall to \$125,000 (\$139,000 indexed for inflation), and the qualifying property limit will fall to \$500,000 (\$560,000 indexed for inflation); \$25,000 for 2013 and thereafter

# BONUS DEPRECIATION

- The additional first year depreciation deduction equal to 100% of an asset's cost is available for qualified property acquired after 9/10/10 but before 1/1/12
  - Asset must be placed in service before 1/1/12
  - Original use must begin with the taxpayer - new property
  - In 2012, bonus depreciation will be reduced back to 50% of the asset's cost
  - 100% will still apply in cases of certain longer-lived production and transportation property

# SMALL BUSINESS HEALTH INSURANCE TAX CREDIT

- Small businesses that provide healthcare coverage to their employees are eligible
  - Must have fewer than 25 employees
  - Average annual wages for employees must be less than \$50,000 per employee
  - Premiums must be paid by the employer under a qualifying arrangement
- Amount of the Credit:
  - 35% of the employer's premium expense
  - 25% if the employer is a tax-exempt employer
- Phase-Out of the Credit:
  - Full-time employees >10 and average annual wages per employee >\$25,000

# PARTNERS AND S CORPORATION SHAREHOLDERS

- Owners of interests in partnerships and “S” corporations can only deduct losses to the extent that they have basis in the entity
- For Partnerships:
  - Consider making a loan to the partnership
  - Consider making capital contributions to the partnership
  - Increases partner’s basis and allows more losses to be deducted

## PARTNERS AND S CORPORATION SHAREHOLDERS (cont.)

- For “S” corporations, consider making capital contributions to increase the amount of losses allowed - loans to the corporation do not increase basis for “S” corporation shareholders but direct loans from shareholders do
  - Watch reasonable salaries for shareholders
  - Medical premiums – If the policy is held in the name of the shareholder, the “S” corporation must pay premiums or reimburse the shareholder by 12/31 and properly report the premiums on the W-2 in order to qualify for the “above-the-line” deduction.

# EXPIRING BUSINESS INCENTIVES

- Incentives scheduled to expire after 12/31/11:
  - Indian employment tax credit
  - Railroad track maintenance tax credit
  - Mine rescue team training tax credit
  - Grants for specified energy property in lieu of tax credits
  - Seven-year recovery period for motorsports entertainment complexes
  - Special expensing for film and television production costs
  - Expensing of brownfields remediation costs
  - Exceptions under Subpart F for active financing income
  - Percentage depletion for oil and gas from marginal wells
- Do special interests and lobbying affect the Internal Revenue Code?

# EMPLOYER PROVIDED CELL PHONES

- **IRS Clarifies New Rules**
  - Employer provides cell phone to employee primarily for non-compensatory business reasons
  - Employee has no income for business or personal use
  - No recordkeeping is required
  - If employee provides the cell phone for bona-fide employment related use which is reimbursed by the employer – not taxable to the employee. Employee no longer has to itemize deductions to offset income.
  - No longer considered listed property
  - Applicable after 12/31/09
- **Land Lines**
  - Must be a designated second line to deduct
  - Cannot “allocate” usage to determine business portion

# SELF EMPLOYMENT TAX FOR 2011

- Self employment tax deduction for 2011
  - For 2011, the OASDI portion of SE tax is reduced 2% from 12.4% to 10.4%
  - For 2011, the deduction for SE tax is computed at 59.6% of the OASDI tax paid and 50% of the HI tax paid (2.9%)
  - The above rules were extended.

# ACCOUNTING METHODS

- Generally, businesses calculate income based upon either the accrual method or the cash method of accounting. Once elected, the method must be used until a change is requested by filing a request with the IRS.
- Accrual Method Considerations
  - 2½ month compensation payments
  - Pension plan contributions
- Cash Method Considerations
  - Manage cash receipts to defer revenue
  - Credit cards – date charged equals payment, so deductible when charged

# NET OPERATING LOSSES

- Applies to “C” Corporations (and Individuals)
  - Consider foregoing carryback period
    - Will the corporation be in a higher tax bracket in the future?
  - Need to consider if there is any risk to not having the NOL available to carryback in case of IRS adjustment
  - If there is no benefit to carryback – i.e., no taxable income in the carryback years, don’t make the election

# NET OPERATING LOSSES

- Applies to “C” Corporations
  - New developments under Section 382
    - Enacted to prevent/limit the trafficking of NOLs
    - Example – A loss company is sold for \$10,000,000 with \$25,000,000 in NOLs when the LT tax exempt rate is 2%. The utilization of the NOLs is limited to \$200,000 annually.
  - Applies when an ownership change occurs – a greater than 50% change in the ultimate ownership of the lost company
    - Less than 5% owners are generally treated as a single “hypothetical” public group, so most transactions other than transactions among the <5% owners generally affect the equity ownership
    - Proposed regulations to address these small shareholders and ease the administrative procedures

# STOCK TRANSACTIONS

- For 2011, there is a new form – Form 8949 replaces Schedule D-1
  - Reports gains/losses from sale of capital assets
  - Gains/losses from involuntary conversions
  - Non-business bad debts
  - The Schedule D calculates the overall gain/loss and picks up capital gain distributions
  - Effective 1/1/11, brokers are required to report gross proceeds AND adjusted basis of “covered securities” and whether the gain is LT or ST. Applies to stock in corporations acquired after 1/1/11, mutual funds acquired after 1/1/12, and other securities acquired after 1/1/13.

# STOCK TRANSACTIONS (cont.)

- Incentive Stock Option Planning
  - Consider exercising options and holding the stock for the required holding period to lock in post-exercise appreciation at long-term capital gain rates
    - Meet the required holding period if ISO stock is held for two years after grant or one year after exercise
    - Watch AMT – Difference between FMV and option price is added back for AMT. RESULT – different basis in shares for regular tax and AMT that needs to be considered when shares are sold
  - If close to retirement or considering leaving your job, consider exercising any ISOs since retirees only have 90 days after separating from service to exercise
  
- Nonqualified Stock Option Planning
  - Typically taxpayers have waited until late in the year to exercise to delay the tax consequences – is this the best strategy based on rate changes?
  - NQSOs generate taxable income when exercised

# ALTERNATIVE MINIMUM TAX PLANNING (cont.)

- Planning has become increasingly difficult – things to consider include:
  - Year-end state tax payments
  - Pre-payment of investment and tax advisor fees
  - Charitable contributions
  - Projecting AMT adjustments from flow-through investments
  - Due to complex regular tax and AMT rules, it is important to look at multiple-year scenarios that consider the most tax advantageous timing for the deduction.

# RETIREMENT PLANNING

- **Sole-Proprietorships and Partnerships:**
  - Establish defined contribution plan before end of the year
  - Have until the extended due date to fund
  - May contribute the lesser of 20% of self-employment income or \$49,000 for 2011; \$50,000 for 2012
  - Limit is applied to SE income after the deduction for the contribution and half of SE tax
  - More mature individuals may want a defined benefit plan since they can contribute more

# RETIREMENT PLANNING (cont.)

- “S” Corporation Shareholders/Employees
  - If no other employees, consider a defined benefit plan
  - Allows larger contributions
  - Can make contributions even in years with no compensation
  - Alternatively, defined contribution plan contributions are limited to \$49,000 or 100% of compensation, or \$50,000 for 2012
- Consider a solo 401(k) or SEP IRA
  - Solo 401(k) must be established before end of year
  - SEP IRAs may be set up and funded as late as the extended due date

# RETIREMENT PLANNING (cont.)

- Maximize Annual Plan Contributions
  - Consider making contributions early in the year to take advantage of compounding
  - 401(k) annual limit is \$16,500 (\$17,000 for 2012)
  - If over age 50, catch-up is an additional \$5,500 for 401(k), \$1,000 for ROTH and traditional IRAs, and \$2,500 for SIMPLE plans
  - Take advantage of employer match!
  - If AGI limit allows, consider contributing \$5,000 to ROTH IRA
    - Non-deductible
    - Distributions are non-taxable
  - Set up a spousal IRA
    - Spouse cannot be an active participant in another plan
    - Maximum annual contribution is \$5,000 or combined taxable compensation of both spouses
    - Watch AGI phase-out limit: begins to be phased-out when MFJ AGI = \$173,000 for 2012, \$169,000 for contribution to be deductible; consider a non-deductible contribution

# STATE TAX CONSIDERATIONS

- Business Considerations
  - Does your state have Enterprise Zones? New rules apply regarding timing for certifications.
  - Does the Colorado capital gain exclusion apply?
  - What states are you required to file in?
    - Nexus issues
    - Any structuring to minimize overall state burden

# AICPA UPDATE

## ISSUES OF CURRENT IMPACT

- Tax Preparer Registration
  1. CPAs are exempt from CPE and testing
    - Non-signing staff of CPAs are exempt from testing and CPE
  2. Overall goals are to enhance compliance and elevate ethical conduct
  3. Major elements:
    - PTIN
    - Circular 230
    - CPE
    - Testing
  4. Database will distinguish between CPAs and non-CPAs

# AICPA UPDATE

## ISSUES OF CURRENT IMPACT (cont.)

- 10,000 Letters
  1. Purpose of the program is unclear
  2. CPAs have a right to know why they were chosen
  3. Inspecting client files is not appropriate
- Accounting Software
  1. Requests from IRS to have access to software
  2. May violate confidentiality and be beyond scope of pertinent information
  3. Right of redaction

# AICPA UPDATE

## ISSUES OF CURRENT IMPACT (cont.)

- FBAR & FAAR

1. Foreign bank assets and foreign asset accounts need substantially more information for reporting
  - Under Foreign Account Tax Compliance Act, must now report interests in specified foreign financial assets

# AICPA UPDATE ISSUES TO BE AWARE OF

- Uncertain Tax Positions
  1. UTP schedule released in Fall 2011
  2. There is an AICPA task force monitoring implementation – M-3 Schedule
  3. Still a push on threshold

# AICPA UPDATE

## ISSUES TO BE AWARE OF (cont.)

- Due Date of Tax Returns

1. Problems with late arriving K-1s and trying to look at big picture

2. Proposed:

Partnership	–	3/15 or 9/15
“S” Corporation	–	3/31 or 9/30
Trust	–	4/15 or 9/30
Corporation	–	4/15 or 10/15
Individual	–	4/15 or 10/15
FBAR	–	6/30 or 10/15
Employee Benefit	–	7/31 or 11/15

# AICPA UPDATE

## ISSUES TO BE AWARE OF (cont.)

- Legislation Moving Forward
  1. Trust administrative fees – Supreme Court had a subjective determination
  2. 3% withholding on government payments went away
  3. Revenue raisers:
    - Carried interest rules
    - “S” Corp and SE tax

# 12 FEDERAL TAX DEVELOPMENTS OF 2011

1. Joint Select Committee on deficit reduction would address the Bush tax cuts in a deficit reduction package. It failed to reach an agreement and disbanded.
2. Rollback of certain 1099 reporting requirements and withholding
3. The FATCA (Foreign Account Tax Compliance Act) was implemented. Requires taxpayers holding specified foreign financial assets to report that information. Guidance issued 12/11 about a new Form 8938.

# 12 FEDERAL TAX DEVELOPMENTS OF 2011

(cont.)

4. February 2011 – The Fresh Start Program was implemented allowing easier installment agreements and more flexibility.
5. September 2011 – Allows reduced penalties for employers who voluntarily reclass their workers for employment tax purposes.
6. September 2011 – Supreme Court agreed to a statute case regarding overstatement of basis.
7. Mileage rate increased in July 2011 to 55.5¢ a mile from 51¢ a mile. Stayed 55.5 ¢ for 2012 (Notice 2012-1).

# 12 FEDERAL TAX DEVELOPMENTS OF 2011

(cont.)

8. Return preparer oversight – PTIN process
9. January 2011 – Beginning in 2012, firms must compute the number of covered returns in the aggregate that they reasonably expect to file as a firm. If it is 11 or more, all members of the firm must electronically file those returns.
10. Updated PAL rules – Regulations were issued updating the definition of an interest in a limited partnership as a limited partner for purposes of the 469 rules. Also, an interest in a limited liability company is treated as a limited partnership interest for PAL rules.

# 12 FEDERAL TAX DEVELOPMENTS OF 2011

(cont.)

11. New “repairs” regulations issued December 2011
12. Voluntary classification settlement program – September 2011 – eligible taxpayers are allowed to voluntarily reclassify their workers as employees for federal employment allowing relief for other classification.

# FINAL ITEMS OF NOTE

- On December 16, 2011, the House passed HR2055 spending bill, which includes \$12.2 billion in funding for the Treasury Department and \$11.8 billion for the IRS – \$305 million less than FYI 2011
  - \$5.3 billion for enforcement activities
  - \$3.9 billion for operations of the agency
  - \$2.2 billion for taxpayer services
- The IRS' business systems modernization program will be funded at \$320 million for FY2012



## **THANK YOU!**

For additional information, please contact:

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# 2011 the Tax Year that's not!

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January 2012



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# Biggest tax story of 2011

- 1. Super committee bust
- 2. No Grand tax compromise
- 3. Puny 2 month payroll tax cut
- 4. No new reform on the horizon. No new anything.
- 5. Both **Democrats and Republicans** remain convinced that a majority of voters will support **their** position on taxes.

# Tax Reform talking point: Buffett tax plan

- Warren Buffett pays only 17.4% of Federal Income taxes
- Most of his income is from investments, capital gains and dividends.
- Proposes that taxpayers marking >\$1 million taxable income should pay more taxes
- And to top his wealth is that Berkshire Hathaway does not pay dividends.

## Tax Gap now 14.5% of taxes owed but not paid.

- IRS estimate that Americans underpaid their taxes by \$385 billion for 2006.
- The largest single element of noncompliance was unreported income from small businesses.
- The tax gap for individuals is \$235 billion was attributable to undeclared income by businesses reported on Schedule C and F

# One billion Served! Not McDonalds!

- On June 10, 2011, The Internal Revenue Service has announced that it has now passed the one billion mark for individual tax returns processed through its electronic filing (or e-filing) program.

# Colorado Billionaire loses appeal

- Our own Colorado Philip Anschutz lost his appeal.
- Position was the deals were pending not final sales. Thus tax deferred.
- Anschutz argued his “transactions followed the IRS guidance so tax could be deferred until the stock was sold.: Two courts, Tax Court and 10<sup>th</sup> Circuit of Appeals have ruled the transactions were sales.
- Key fact, stock was actually sold shortly after Anschutz transferred it to a securities firm.
- Zing, he owes \$94 million in taxes!

# 2011 DUE DATES

- DUE DATES!!!!
- NOW APRIL 15<sup>TH</sup> IS NOT APRIL 15<sup>TH</sup>, IT IS NOT APRIL 16<sup>TH</sup>, IT IS APRIL 17<sup>TH</sup> FOR 2012!
- FEDERAL & COLORADO BOTH!
- And what about estimate dates? It is not 1/15, or 1/16 but 1/17/2012!

# Accounting jobs to grow!

- According to Department of Labor the number of accounting jobs is projected to grow 22 percent by 2018. “It is a career that will allow remunerative and stable employment. Both the demand for accountants and their salaries are expected to grow. Forget the green eyeshades stereotype. Accountants do everything from audits and budgets to financial planning and analysis to advising companies as they create new products and services.”

# KPMG set to hire 75,000 graduates

- KPMG international member firms plan to hire 75,000 graduates worldwide over the next 3 years.
- That is a 25% increase in the firm's historical staffing target
- New hires will be for all of the functional areas: audit, tax, advisory and internal firm services.
- KPMG currently has 138,000 employees

# AICPA launches new career site

- Dedicated to college students interested in becoming CPA
- Has all the state requirements
- [www.thiswaytocpa.com](http://www.thiswaytocpa.com)

# Amazon...state sales taxes

- Lawsuits and states need their money!
- Amazon and California struck a deal and Amazon will start collecting sales tax in July 2012.
- Now Amazon and Indiana Governor Daniels unveiled an agreement on Monday that has Amazon to start collecting sales tax in Indiana in 2014.
- Amazon and many states are pushing for Federal action on the sales tax issue.

# Colorado Tax Amnesty Program Closed

- Gov. John Hickenlooper signed into law a tax amnesty period
- From October 1 to November 15, 2011.
- It allowed Colorado taxpayers to catch up on overdue taxes.
- Hopes of raising about \$9.7 million for the State Education Fund, no news if program met goal.
- First amnesty period in Colorado since 2003.

# Establishing Evidence of Delivery to IRS

- IRS issued final regulations on how taxpayers can prove the timely delivery of physical documents to the IRS or Tax Court
- Prima facie evidence of delivery will be established
  - Register or certified U.S. mail
  - Not priority and delivery confirmation
  - Not first-class mail
  - Private delivery service
  - Specific criteria to be established in future
- Not so final then.

# New IRS Transcript Delivery System

- Effective 1/9/2011 Updated new and better system
- Allow Users to set a tax year range with a beginning and ending year.
- Allow Multiple Tax forms in one request
- Allow to submit more than one taxpayer in the same request

# Same-Sex Couple Filings

- More states passing legislation on same-sex marriage
- Same-sex couples do not qualify for federal tax benefits
- Complexities of how couple files depend on the relevant state law's and its reliance on federal tax laws
- If start with federal AGI, couple has to prepare a “mock” federal return as if filing joint and then file the state return as filing joint.
- Hassle of preparing 2 federal returns

# Tax Troubles for Small Businesses Increase

- Small companies are skipping their federal payroll taxes in wobbly economy.
- IRS gotten more aggressive penalizing executives, officers, accountants or other individuals related to the small company
- Once the IRS adds its penalties, the debts snowball
- Missing payment date by 2 ½ days can trigger fines that can go as high as 25% of tax due
- The best plan: meet the deadline, pay payroll taxes first!

# Accountant cannot deduct bathroom as Home Office

- Tax Accountant has home office
- Personal Residence has 2 bathrooms
- Taxpayer used one bedrooms exclusively as office for his accounting business.
- Taxpayer also claimed hallway and bathroom as exclusively for his accounting business.
- Taxpayer testified that his children and other personal guest occasionally used the bathroom.
- Accordingly, the hallway and the bathroom were not used exclusively for business purposes.

# Home Office Deduction

- Your home office must be used in a trade or business activity.
  - Home office not available for managing personal investments.
- Your home office must be used regularly and exclusively for business.
  - An area used for both business and personal does not qualify
- Home office must be one of the following:
  - Principal place of business
  - Place to meet patients, clients or customers in the normal course of business
  - Separate structure not attached to dwelling unit used for trade or business purposes.

# Home Office Deduction

- If an employee, home office must be for the convenience of your employer.
  - If employer does not require the employee to work from home and provides an office elsewhere, a home office is likely to be considered a matter of the employee's convenience and therefore not deductible.
- Even if taxpayer's home office meets the above rules, the deduction may be limited.
  - Expenses that you could otherwise deduct, such as real estate tax and mortgage interest. Otherwise, home office expenses limited by income limitation

# Audit: IRS Erroneously Gave Out \$151 Million In Auto Tax Breaks

- The Internal Revenue Service stumbled in handling a tax incentive designed to promote automobile sales, handing out more than \$151 million in erroneous deductions, as well as 473 credits given to people who were imprisoned, dead or underage.
- The IRS missed 4,257 individuals who claimed more than \$151 million, average of \$35,470 per taxpayer in undeserved tax deductions as part of the 2009 stimulus package program designed to boost automobile sales, according to an audit released Wednesday from the Treasury inspector general for tax administration.

## More IRS Audits-up 23%

- Number of federal individual income tax returns examined over last 5 years up by 23%
- Still only 1% of individual taxpayers
- IRS Oversight Board poll cite 64% of taxpayers cite fear of audit as a factor influencing voluntary compliance
- Same poll reported 15% believe it is acceptable to cheat on their income taxes
- Most likely to get an audit by mail
- Only 1 out of every 503 actually got a F2F examination

## Millionaire IRS Audits rate is 12%

- Up from 3% in 2000.
- IRS says, “We base our audit decisions on tax issues and nothing else!”.
- Between 2004 and 2009 the % of millionaires audited ranged from 5% - 7%.

# More IRS Correspondence Audits

- IRS has expanded correspondence examinations in lieu of field examinations of individual income tax returns. Because of this expansion, IRS is collecting additional revenue more efficiently.
- It has caused difficulties for some taxpayers and CPAs representing them!
- The IRS has had problems in timely and properly responding to letters providing requested information or disagreeing with proposed adjustments
- Tax Practitioners should advise its clients to notify the practitioner if client receives any correspondence from a taxing authority.
- If assessment is incorrect, the practitioner should consider matter be transferred from a service center to local office, where it can be resolved by one auditor.
- IRS does not want to transfer cases because it will cause delays and it costs more.
- Practitioner may want to contact the local office of the Taxpayer Advocate Service and request assistance.

## Tax cheats: Single, young and male

- Surveys reveal that the typical American tax cheat is male, single and under the age of 45.
- 15% of Americans surveyed revealed that they fudged their tax returns. Of those over 68% are male, single and under the age of 45.
- Many cheaters try to justify their behavior. Far more tax cheats say that they are “overall better people” and that they are “special and deserve to be treated that way” compared to the other people who said they don’t cheat.
- Not surprising their willingness to cheat is not limited to their taxes but spans a wide range of situations.

# \$4.5M whistleblower award for CPA

- The IRS has paid an unidentified CPA \$4.5M as the first award under a newly whistleblower
- An in-house corporate accountant at one of the largest financial services firms in US.
- Discovered a tax liability of >\$20M that had been underreported
- The CPA was given the 3<sup>rd</sup> highest category of reward under the new law, 22% of the proceeds of whatever the IRS collects
- CPA had filed an IRS Form 211 without assistance of counsel and 2 years expired and no IRS response after numerous client inquires. Then contacted an experienced whistleblower attorney.
- The CPA continues to work as an in-house CPA and never wants to be known as the source. What about Ethics?

# Database of regulated tax preparers

- IRS to build database of regulated tax preparers
- May be available as soon as 2013
- Taxpayers will be able to examine qualifications of paid tax-return preparers
- Part of the Phased-In regulation of tax preparers that began in 2010
- Database will include names, addresses and professional qualification of tax preparers, along with any publicly disclosed professional disciplinary actions.

# Specified Tax Return Preparers

For 2011, a specified tax return preparer is a tax return preparer who reasonably expects to file 100 or more individual income tax returns during the year.

Starting in 2012, the 100 return limit will be reduced to 11 returns.

**Administrative exemptions include members of religious groups that are conscientiously opposed to electronic technology.**

**Other examples found in Final Regs.**

# Competency Exam by 2013

PTIN holders who are not CPAs attorneys or enrolled agents must pass a competency exam by 2013

These persons will also be subject to a continuing education requirement.

All tax return preparers will be subject to Circular 230 regulations. Thus all preparers will be subject to Circular 230 discipline. IE could be subject to severe economic consequences for the disbarred or suspended preparer.

Detail discussion in modified Circular 230.

# Prison inmates register with IRS as Tax Preparers

- 331 prison inmates serving prison terms received their PTIN from the IRS
- 43 of the prison applicants were serving life sentences.
- 962 applicants who had an incarceration date within the last 10 years got active or provisional tax preparer identification number.
- IRS is working on solution to suspend PTIN from prisoners and prevent future prison applicants from receiving a PTIN!

# 2011 PAYROLL TAX HOLIDAY

- 2011 The employee tax rate for social security is 4.2% down from 6.2%.
- The employer rate for social security remains unchanged.
- Self-employed individuals will pay Social Security payroll taxes at a rate of 10.4%, for a total of 13.3% down from 15.3%

# 2012 PAYROLL TAX NIGHTMARE

- The reduced payroll tax rate extended through February 29, 2012.
- Beware! There is a recapture provision. Applies to employees who receives more than \$18,350 in wages. Imposes an additional tax equal to 2% on these higher income taxpayers. This recapture will be payable in 2013!
- Unless Congress changes its mind!

# Too Good to Be True Case

- Tax Court disregarded for tax purposes a multi-level structure
- Colorado Psychiatry practice
- Formed LLC and 2 corporations.
- LLC was the Psychiatry practice. LLC had 2 members, the Dr and one of the corporations. The Dr's LLC ownership further split between 85% limited and 10% general partnership interest.
- One Corporation tracked expenses.
- Second corporation managed the psychiatry business and billed the LLC management fees.
- No self-employment taxes or salaries were paid.
- Dr. said the tax results were too good to be true!
- Tax court determined that the income was self-employment and assessed self-employment taxes and penalties!

# Estate Tax - New Law, New Options

- **2010: Carryover basis and limited step-up basis regime for inherited assets or new estate tax law**
- **2010, 2011, and 2012: \$5 million exemption, top rate of 35%**
- **For those who died in 2010, an election can be made to choose the estate tax provisions effective prior to the December 17, 2010 legislation**

# Gift Tax - New Law, New Options

- **No change in gift tax in 2011 annual exclusion –which is \$13,000**
- **In 2011, a person can make lifetime gifts of \$5,000,000.**
- **Much higher than historically and provides many opportunities for estate planning for the ultra-rich.**
- **Financial planners and estate planning attorneys for the high-net-worth clients are salivating.**

# Homebuyer Credit Anti-abuse not effective

- ✓ Homebuyers Credit expired in 2010.
- ✓ IRS implemented additional requirements to stop the Homebuyer credit abuse.
- ✓ However,
- ✓ 4,608 prisoners claimed the first-time homebuyer tax credit while incarcerated at the time they reported a home purchase
- ✓ 1,295 of the claims were processed resulting in \$9.1 million in tax credits.

# Mortgage Debt Forgiveness

- Mortgage liability post-foreclosure
- Tax-free debt discharge on/after Jan. 1, 2007, and before Jan. 1, 2013
- Primary resident requirement—means not second homes!
- \$2 million debt limit (\$1 million if married filing separately)

# Cancellation of Debt

- Form 982 must be filed with the return for the year of exclusion.
- Interest included in canceled debt is taxable if forgiven unless it would have been deductible when paid, i.e. mortgage interest
- Credit Card Debt Cancellation is taxable income if taxpayer is not insolvent or if taxpayer defaults on bankruptcy plan.

# IRS stepping up audits on employee classification.

## **GAO estimated that 38% of employers misclassified independent contractors**

- Both Wal-Mart and FedEx lost lawsuits/paid penalties
- No magic rules that “makes” the worker an employee or an independent contractor. The keys are to look at entire relationship
- Can file Form SS-8 with the IRS and they will make the determination.

## “It’s easier and quicker to audit small businesses.”

- Both IRS and state agencies redoubling efforts to uncover long term “temps” or independent contractors.
- Launched 3 year program to examine 6,000 companies
- In addition, President Obama’s proposed 2011 budget includes funding additional 100 IRS staffers to pursue such cases.
- The IRS and states are more able to share data on how companies classify employees
- Still no universal test.

# Small Businesses Fight IRS Over Data

- IRS is moving aggressively to collect more taxes from small business
  - When auditing, the IRS is asking that the exact copies of the electronic records kept in their business-software programs
  - This may force small business to turn over customer lists, personnel data, confidential client information and other unrelated information contained in the off-the-shelf software programs.
  - IRS's position is that small businesses are among the largest contributors to the tax gap.
  - The software that the IRS is looking at is QuickBooks and Peachtree.
  - So, beware that this may be requested with a client's audit.

# Small Businesses Fight IRS Over Data

- Taxpayers and CPA should fight this request.
  - Provide P &L and Balance Sheets only.
  - If IRS demands backup disks, use software to bridge client data to a trial balance. You want to only provide IRS with the year that is under audit. There are some software that take QuickBooks or Peachtree information and eliminates prior year information.
  - Like [www.dillners.com](http://www.dillners.com) and now Quickbooks 2012 Accountants Version.

# 2011 Tax Rates-Do Over from 2009 & 2010 &....

- 10%
- 15%
- 25%
- 28%
- 33%
- 35%

# Always More Tax!

- AMT exemption amounts for 2011 is \$74,450 for married couples filing jointly and surviving spouses, \$48,450 for single taxpayers and heads of households, and \$37,225 for married couples filing separately.

# American Opportunity Tax Credit

- Extended through 2012
- Applies to first four years of college/  
postsecondary school
- \$2,500 per student per year
- Increased tax incentives for higher education by  
over 90% or \$8.7 Billion in 2009!
- Average tax credit refund is over \$1,700

# Higher Education Tuition & Fees Deduction

- Extended for 2011 only!
- Deduct up to \$4,000
  - Modified AGI
    - Does not exceed \$65,000
    - Does not exceed \$130,000 (married/filing jointly)
- Deduct up to \$2,000
  - Phase-out limits apply\*
    - \$65,000 – \$80,000
    - \$130,000 – \$160,000 (married/filing jointly)

# Educator Deduction

- Educators can deduct up to \$250 for expenses they pay for classroom materials.
- This was extended for 2011 only.

# Health Savings Accounts

- Tax advantages – contributions, withdrawals and earnings
- Minimum annual HDHP deductible: \$1,200 (self only) and \$2,400 (family)
- Annual contribution \$3,050 (single) and \$6,150 (family) plus \$1,000 catch-up per individual age 55 or older.
- Maximum annual deductible/other out-of-pocket expenses: \$5,950 (self only) and \$11,900 (family)
- Additional tax on non qualified medical expense distributions was increased to 20%.

- Top tax rate of 15% for qualifying dividends
- 0% for taxpayers in 10% or 15% bracket
- Does not apply to interest payments
- Do not let tax considerations drive investment decisions

# Capital Gains Tax

- Maximum tax rate on net long-term gains is 15%
- 0% for taxpayers in 10% or 15% bracket
- Asset must be held more than one year
- 28% maximum tax rate for collectibles

# Capital Gain Tax-New Forms

- New forms for 2011
- A new Form 8949, Sales and Other Dispositions of Capital Assets
- A new schedule D for 2011

# Traditional IRA to Roth IRA

- No dollar limit on conversion amount
- No early-distribution penalty in certain circumstances
- No modified AGI requirement

# 2010 ROTH IRA CONVERSIONS

- If you converted or rolled over a Roth conversion and did not elect to report the taxable amount on 2010, then  $\frac{1}{2}$  of the conversion is reportable on your 2011 and the other  $\frac{1}{2}$  reportable in 2012.

# Charitable IRA Rollover

- 2010 and 2011 a taxpayer can direct up to \$100,000 of their distribution (per person limit) to qualified charities from an IRA.

- Standard Mileage
- Depreciation

# Standard Mileage Rates

**1/1-6/30 7/1-12/31**

**2011 2011**

<b>■ Business Miles</b>	<b>51.0</b>	<b>55.5</b>
<b>■ Charitable Miles</b>	<b>14.0</b>	<b>14.0</b>
<b>■ Medical/Moving</b>	<b>19.0</b>	<b>23.5</b>

# Standard Mileage Rates

	2012
■ Business Miles	55.5
■ Charitable Miles	14.0
■ Medical/Moving	23.0

# Luxury Auto 2011 Depreciation Limits

<u>Chassis</u>	<u>Autos</u>	<u>Truck</u>
Year 1*	\$3,060	\$3,260
Year 1	\$11,060	\$11,260
Year 2	\$4,900	\$5,200
Year 3	\$2,950	\$3,150
Year 4 & after	\$1,875	\$1,875

\* If bonus depreciation does not apply

# Depreciation What's the Number This Year

- 179 Extended
- Bonus Depreciation Extension thru 2011

# Section 179 Expense Maximum Amount

- **2002** \$ 24,000
- **2003** \$100,000
- **2004** \$102,000
- **2005** \$105,000
- **2006** \$108,000
- **2007** \$125,000
- **2008** \$250,000
- **2009** \$250,000
- **2010** \$500,000
- **2011** \$500,000
- **2012** \$125,000

# Section 179 Limited Small Business Investment Limitation

- **2002** **\$200,000**
- **2003** **\$400,000**
- **2004** **\$410,000**
- **2005** **\$420,000**
- **2006** **\$430,000**
- **2007** **\$500,000**
- **2008** **\$800,000**
- **2009** **\$800,000**
- **2010** **\$2,000,000**
- **2011** **\$2,000,000**
- **2012** **\$500,000**

## *Bonus first year depreciation*

- The Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 allows taxpayers to deduct **100%** of the cost of certain business property.
  - **The property must be eligible for MACRS and have a recovery period of 20 years or less and the original use of property must commence with taxpayer.**
  - **The qualified property must be acquired after September 8, 2010, and before January 1, 2012—**
  - **Property is acquired when the taxpayer pays or incurs the cost of the property.**

# *Leasehold Improvements Depreciation*

- **Sec. 168(e)(3)(E)(iv) Qualified leasehold improvement property treated as 15 year property.**
- **Thus such property is once again eligible for bonus depreciation**
- **For 2011 only can claim up to \$250,000 of Sec. 179 for qualified real property leasehold additions.**  
**Include:**
  - **Qualified leasehold improvement costs**
  - **Qualified restaurant property cost**
  - **Qualified retail improvement cost**

# THE MOST LITIGATED AREA WITH THE IRS- REPAIRS VS MAINTENANCE

- New IRS Audit Technique Guide
  - Provides useful insight into how cost will be categorized. But no conclusions!
- Based on factual determination with burden of proof rests with taxpayer.
- Practice recommendation-if taxpayer is a heavily asseted business, check this guide.

# SALES TAX DEDUCTION SET TO EXPIRE

- Individuals in states without income taxes should consider taking advantage of this deduction as it expires in 2011.
- Sales tax on purchases of motor vehicles, boats planes is deductible in addition to the sliding scale amount.

# Self Employed Issues

- Medicare Part B premiums qualify for the self employed health insurance.
- Net self-employed income is no longer reduced by the amount of self-employed health insurance deduction.

# 1099 Requirements

- Originally passed in March 2010 that all businesses required to report to the IRS any purchase from a vendor of goods or services worth \$600 or more during the calendar year to be effective for purchases in 2012.
- This expanded 1099 reporting requirements repealed on April 14, 2011.
- The 1099 reporting rules continue unchanged.
- \$600 or more payments in the course of such trade or business must report the amount, and the name and address of the recipient to the IRS.

# 1099 Requirements

- Increased penalties not repealed. The penalties are per information return.
  - **First-tier penalty ( file 30 days late)for failure to timely file an information return from \$15 to \$30 – yearly maximum from \$75,000 to \$250,000.**
  - **Second tier penalty ( file more than 30 days late but before August 1) was increased from \$30 to \$60--yearly maximum from \$150,000 to \$500,000.**
  - **Third tier penalty(file after August 1) was increased from \$50 to \$100 --yearly maximum from \$250,000 to \$1,500,000.**
  - **Intentional disregard increased from \$100 to \$250**

# New 1099 Requirements

- There remains a couple of new requirements effective for 2011
- As of 2011 brokers are required, when reporting the sale of securities to the IRS must also include the adjusted basis in the sold securities and classify any gain or loss as long or short term.
- Banks and other processors of merchant payment card transactions must report a merchant's annual gross payment card receipts to the IRS and the merchant. The reporting threshold is an aggregate value is \$20,000 and aggregate transactions of 200 or more. This is 1099-K.

# New Sneaky 1099 Requirements

- There is a new requirements effective for 2011
- On Partnership returns, page 3 question 18 asks, “Did you make any payment in 2011 that would require you to file Form(s) 1099? If “Yes” did you or will you file all required Form(s) 1099?”
- So how are you going to answer this question?

# S Corporation Issues

- **Corporate Issues but affect individual taxes**
- **Reasonable compensation**
  - **Boils down to payroll taxes. Several new cases shed guidance.**
  - **Check on your clients that have S Corporations and very little compensation.**
- **Basis records**
  - **Determine deductibility of losses, taxability of distributions**
  - **Lies with the shareholder but records are with the corporation**

# S Corporation Issues

- Recent case in Iowa
- A CPA took a \$24,000 salary
- His share of the S Corporation's profit was over \$200,000.
- IRS determined that pay was unreasonably low and ruled that the distributions are reclassified as salary
- Hit with payroll taxes and penalties

# IRS simplify election Reduced Research Tax Credit

- Taxpayers make a reduced credit election on Form 6765.
- Used to make the reduced credit on the original return
- Now can make the election whether or not they claim any amount of credit.
- Taxpayers should always consider making an intent-based election when filing an original return.

# What goes around, comes around !!

- Naples, Fla. couple made headlines for threatening to seize property from a Bank of America branch
- They purchased a home in 2009 for \$165,000. A year later, Bank of America tried to foreclose on it.
- One huge problem with the bank's actions. The couple didn't owe the bank a penny. They paid cash for the home. Still they had to go to court to prove the bank didn't have right to foreclose.
- Bank of America was ordered by judge to pay' \$2,500 attorney fees.
- After five months of calls and writing letters, the couple still hadn't seen their money from Bank of America.
- The couple sent their lawyer, the sheriff, and a moving company to a local Bank of America branch. They had court permission to seize branch assets.
- The couple was eventually given a check of more than \$5,700 to cover the court order and other expenses.

- Groupon Fuzzy Accounting
- Groupon had a NOL of \$420 million last year.
- Groupon thinks investors in its initial public offering should instead look at “adjusted consolidated segment operating income” or adjusted CSOI
- If you remove or ignore or strip out, marketing expenses, acquisition-related costs, stock compensation, interest expense and payments to the tax man, the start-up earned \$606 million!
- It's a miracle!

# New York court rules private lap dances not tax exempt

A Gentlemen's club near the state capital of Albany claimed the service was, "a tax free dramatic or musical art performance"

In New York state a sales tax must be paid on admission to or for the use of any place of amusement except for dramatic or musical arts performance.

The New York State Supreme Court Appellate Division ruled that the club had not provided enough evidence to support its argument that lap dances were a dramatic or musical art performance.

# Earned Income Credit

- Form 8867, Preparer's EIC Checklist must be submitted to the IRS.
- Paid preparers failing to meet their due diligence required face higher penalties for returns filed after December 31, 2011
- The penalty is raised to \$500.

# New Form 8938-Statement of Specified Foreign Financial Assets

- Taxpayers with foreign assets above certain thresholds may have to file this form.
- Unmarried taxpayers living in the US if the value of their foreign assets exceed \$50,000 on the last day of the tax year or more than \$75,000 at any time during the tax year.
- Married taxpayers living in the US if the value of their foreign assets exceed \$100,000 on the last day of the tax year or more than \$150,000 at any time during the tax year.
- This filing is separate from the disclosures of foreign accounts over \$10,000 required on Form TDF 90-22.

# IRS allowed \$4.2 billion in credits to undocumented workers

- Undocumented workers received \$4.2 billion in refundable tax credits.
- A dramatic rise from less than \$1 billion in 2005.
- IRS says it lacks authority to disallow claims
- Refunds based on earned income called the additional child tax credit.
- Returns filed with individual taxpayer identification numbers.

# Where O, where should you go?

- Sixth Circuit upheld the IRS's application of individual's tax overpayment.
  - Individual requested the year to apply the overpayment
  - IRS applied overpayment to tax liability for a discharged tax year.
  - IRS possess statutory discretion to credit overpayment to any tax year.

# New Hire Credit

- Qualified Employees hired during 2010,
- Hired after 2/3/10 and employed for at least 52 weeks.
- Credit is either \$1000 for each qualifying worker or 6.2% of wages paid over 52 week period.
- Credit may not be carried back and is non refundable.
- Form 5884-B

# Health Benefits reporting requirements 2013

- Employee's W-2 will need to show the health benefit coverage for the tax year 2012.
- Companies need to start gathering that information now so that they won't have to play catch-up next January.
- The benefits are not subject to tax. This disclosure is for informational purposes only!
- Smaller companies that filed 250 or fewer Forms W-2 the prior year, in this case the 2011 tax year, do not have to comply with this requirement.

# TAX LAW RULES!

- It's not Fair!  
It doesn't make sense!  
We're talking about Tax Law!



## **THANK YOU!**

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