SUMMER, 2011

NEWSLETTER

New law repeals expanded 1099 reporting rules

On April 14, 2011, President Obama signed legislation - the Comprehensive 1099 Taxpayer Protection and Replacement of Exchange Subsidy Overpayments Act of 2011 - repealing expanded reporting rules for businesses and landlords that had been created by laws passed in 2010.

Business reporting. The Form 1099 reporting rules were changed by the 2010 health care legislation. Under the Patient Protection and Affordable Care Act of 2010, every business, charitable organization, and governmental unit was required to file a Form 1099 for payments to any vendor or supplier of goods or services (other than a tax-exempt organization) totaling $600 or more for the year. Both the recipient and the IRS had to receive a copy of the Form 1099.

These rules were scheduled to take effect for payments made after December 31, 2011. Before the passage of the health care law, payments to corporations were generally exempt from the Form 1099 reporting requirements. The 1099 law just signed by President Obama completely repeals the expansion of business reporting requirements, and the reporting rules return to what they were before health care legislation.

Rental property reporting. Similarly, new Form 1099 reporting requirements were recently imposed on landlords. Under the Small Business Jobs Act of 2010, owners of rental properties were generally required to file a Form 1099 for rental-related payments to any provider for services totaling $600 or more for the year. These reporting rules were to apply to recipients who provided professional services, such as accountants, as well as workers

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Estate taxes might not affect you, but you still need a plan

There's good news if you're concerned about estate taxes. For the next two years (2011 and 2012), the value of your estate that's excluded from tax is set at $5 million. And the top rate on taxable estates is 35%.

The $5 million exemption is per person, thus a couple's exemption is $10 million. Also notable in the law is the new portability of unused exemptions. Under prior law, couples frequently performed complex estate planning to take full advantage of the then $7 million exemption for couples. Now the law allows a deceased spouse's estate to transfer any unused exemption to the surviving spouse without all the complex planning.

So what should a taxpayer do to take advantage of the current rules? First, estimate the size of your estate and if you may be subject to taxes, consult us and your attorney for planning options. For example, you might consider taking advantage of the favorable gifting and generation skipping tax exemptions by making tax-free gifts to planned beneficiaries now. It's important to realize that not only will planning for these events minimize potential estate tax, but also you will be preserving assets for your family.

If your estate is under the tax threshold, don't assume that you can just ignore estate planning. If you have a plan in place, you should review and update it at least annually. First, your financial situation might have changed. Or there could be changes among your heirs or beneficiaries. Think of all the births, marriages, deaths, and divorces in your extended family during the last year.

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New law repeals expanded 1099 reporting rules *(continued from page 1)*

like plumbers and electricians. They were to be effective for payments made after December 31, 2010.

The new law repeals these expanded Form 1099 reporting rules for landlords. As with the repeal for business reporting, it's like the requirements never existed.

Repeal of the expanded business and rental property expense reporting rules will eliminate a flood of paperwork for most small business and rental property owners.

Estate taxes *(continued from page 1)*

If you don't have an estate plan, establish one as soon as possible. A plan is not just about avoiding estate taxes. At a minimum you need the following:

* A will or trust to specify who will inherit your assets and to appoint a guardian for any minor children.

* A medical directive or "living will."

* Health care and financial powers of attorney.

* Updated beneficiary designations for insurance and pension assets.

For help calculating the value of your estate, or to learn more about how estate taxes might affect you, please contact our office.

Consider the time value of money in making business decisions

Suppose you're selling your business, and it's worth $400,000. You're offered $210,000 down and lump sums of $100,000 at the end of year one and year two. Should you take the offer?

Most people know that $1,000 now is worth more than $1,000 a year from now. Here's why:

1. Inflation: In a year, a dollar will buy less than it would today.

2. Risk: Over time, the risk increases that some of the money owed you will not be paid.

3. Opportunity loss: Funds on hand could be invested and earning more money.

Present value analysis attempts to quantify these variables. It discounts the value of future funds by estimating inflation rates, risks of loss, and rates of return from alternative investments.

Assume you could earn 2% by investing in a $100,000 CD. Disregarding compounding, in a year your investment would be worth $102,000. Conversely, if you postponed receipt of $100,000 for a year and inflation eroded the principal by 3%, you'd receive the equivalent of $97,000 in today's dollars. (Note that with 3% erosion, even the $102,000 CD proceeds would be worth only $98,940 in today's dollars.)

In the opening example, your proposed "investment" (a two-year $200,000 note receivable) would be far riskier than a CD. To compensate, you might decide not to accept anything less than an 8% return. A present value table indicates that at 8%, the discount factors for one and two years are .926 and .857, respectively. $100,000 times .926 is $92,600; $100,000 times .857 is $85,700.

Thus, in today's dollars, the buyer is offering $388,300 ($210,000 down payment plus $92,600 plus $85,700). Since your business is worth $400,000, you would be selling for $11,700 less than full value.

A similar analysis can be applied to any business transaction involving future payments. For help with the calculations or assistance with any of your business needs, call us for an appointment.

Tax breaks can help when disaster strikes

Recent events here and abroad are reminders that disasters can occur at any time - often with staggering human and financial costs. If you're an unlucky victim of a disaster, you may receive help from insurance and federal disaster aid. But the tax code also offers some relief. You may be able to take an itemized deduction for part of your loss. In tax terms, it's a "casualty loss," and it can also apply to events such as a car crash, a house fire, or theft. Here are the basics.

* The loss or damage must be due to an unexpected and sudden event. Losses due to slow deterioration over the years, such as rot, rust, or insect damage, don't qualify.

* Your tax deduction won't equal your total loss. You must subtract any insurance or other reimbursement. Then you must also deduct $100 for each loss and 10% of your adjusted gross income.

* Your loss may also be limited by your adjusted basis in the property. That's generally what you paid for it, plus or minus any improvements or previous losses.

* In a widespread disaster, the area may be classified a "Presidentially declared disaster area." If that happens, you have a special option. You can claim your casualty loss against the current year's taxes. Or you can amend the previous year's return and claim your loss against that year's taxes. That usually generates a faster refund, but it may change the amount of your deduction.

If you suffer a casualty loss, please contact us. We'll explain the rules and help you claim the maximum possible tax benefit.

Tax tips for your vacation home

Planning to rent out your vacation getaway? When it comes to taking advantage of the tax benefits, timing is an important factor. Here are two points to remember.

* The fourteen-day-or-ten-percent test. The IRS applies this test to determine if you use your vacation home as a personal residence. If you stay in the home more than 14 days or 10% of the total days it's rented in a calendar year (whichever is greater), the general rule is you're using it as your home.

Why does it matter? Because treating a vacation home as your personal residence affects your rental deductions. You'd include all the rent you receive as income on your tax return. But related expenses are generally limited to the amount of that income, meaning you can't offset other income with a loss. Note that time spent in your vacation home by family members and certain others can count as personal use.

* The less-than-fifteen exception. Rent out your vacation home for less than 15 days during the taxable year, and the income is yours, tax-free. You don't even have to report it on your return. Just be aware that any expenses related to the rental are nondeductible. If you itemize, you can still deduct qualified mortgage interest and real estate taxes on your vacation home.

Other tax rules, such as passive activity and capital gains reporting, can also impact the decision to rent out your vacation home. Give us a call before you put up that "For Rent" sign. We'll be happy to review your options under the tax rules.

"Tax Freedom Day" came later in 2011

"Tax Freedom Day" fell on April 12 in 2011, three days later than in 2010. According to the Tax Foundation, all the money earned by taxpayers in the first 102 days of 2011 will go to pay their federal, state, and local taxes.

Another statistic from the Tax Foundation: If the government were to collect enough taxes to fund all spending for 2011 (with no deficit), Tax Freedom Day would be May 23, 2011. That's 41 more days of work to provide the additional $1.48 trillion of revenue needed.

IRS raises threshold for imposing tax liens

The IRS recently announced that it will adjust its use of tax liens to collect back taxes. A federal tax lien gives the IRS a claim on a delinquent taxpayer's property for unpaid taxes.
This change means the IRS won't use a tax lien unless at least $10,000 in back taxes is owed; the previous threshold had been $5,000.

In addition, the IRS says it will "withdraw" more tax liens once the back taxes have been paid. A withdrawal removes the lien from the taxpayer's credit record, whereas a lien "release" as previously used left the lien on the credit record for at least seven years. Having a tax lien on a taxpayer's credit record can knock 100 points off the individual's credit score.

The IRS estimates that the new rules mean that "tens of thousands of people won't be burdened by liens."

Summertime tax tips

Summertime fun can be made even more enjoyable by adding tax savings. Here are some tax-saving ideas to consider.

* If you have summer travel plans and the primary purpose of your trip is business, you can deduct all the travel costs to and from your business destination and all other business-related costs even if you add on a few extra days for pleasure. You can't deduct costs related to the pleasure portion. Including a spouse or friend on your trip is permissible, but you can't deduct the additional costs for that person.

* If you itemize your deductions, you can deduct the mortgage interest and property taxes paid for your vacation home. A boat or RV can qualify as a vacation home if it has sleeping quarters, cooking facilities, and a bathroom. If a retreat also serves as rental property, you can control your tax deductions by changing the number of days you use it for vacation.

* If you and your spouse work, the cost of sending your children to a summer day camp may qualify for the child care credit.

* If you own a business, consider hiring your child for the summer. Your child can earn up to $5,800 tax-free this year, and your business is entitled to a deduction for the wages paid. You must pay your child a reasonable wage for the work performed. If your business isn't incorporated, a child under 18 is not subject to FICA taxes.

Put midyear tax planning on your summer schedule

Don't forget to put a little tax planning on your busy summer agenda. A midyear tax review is a great way to save tax dollars and time. To get together for a check of your 2011 tax situation, give us a call.

Look into the benefits of a solo 401(k)

Have you heard about solo 401(k) plans? The traditional type of 401(k) retirement plan is now available for self-employed individuals. And it lets you save more than other types of plans.

In the past, 401(k) plans were typically offered by larger corporations. Employees could make pre-tax contributions by payroll deduction. The company would then usually match a percentage of those contributions. Investments grew tax-free until withdrawn at retirement. One advantage of a 401(k) plan is the relatively large amount you can contribute each year - $16,500 in 2011 with an extra $5,500 catch-up if you're 50 years old or older.

Now you can establish the same type of plan if you're self-employed or run an "owner only" business. That's a business with just you and possibly your spouse, but no employees. You can save more with a solo 401(k) than with the traditional SEP, SIMPLE, or Keogh plans. That's because you are able to make two types of tax-deductible contributions. First you make the usual employer contribution as owner of the business. Then you can make an additional salary deferral as an employee. As a result, you could potentially shelter up to $49,000 of your 2011 self-employment earnings from tax. If you're eligible for the over-50 catch-up, that rises to $54,500.

The solo 401(k) plans are flexible and relatively simple to administer. If you think this plan might be right for you, please contact our office. We can tell you more about it and help show you how much you could save.

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