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Re: 2010 Mid-Year Tax Update

Dear Clients, Colleagues, and Friends:

Congress and the President have passed several tax bills this year and more are expected. Please see our web site at Paulhburgess.com for updates, including the recent Health Care Act. This newsletter alerts individuals and small businesses of some of the new potential tax traps and tax savings.

√ Starting in 2011 a new employee benefit cafeteria plan known as a Simple Cafeteria Plan will be available. Cafeteria plans, although good for larger employers, have been cost prohibitive for smaller employers.

√ The "Hire Act" passed in March of 2010 relieves a company from paying the social security tax (6.2%) on new hires that have not been employed full-time in the last 60 days.

√ The "Hire Act" also has an up to $1,000 credit per employee for retaining a new hire for 52 weeks or more. Contact our offices and we will provide you specific details of the "Hire Act", including the potential to hire your spouse for tax savings.

√ For 2011, Sec. 179 asset expensing is a measly $25,000. It may be increased before year-end. However, be prepared for it not to increase. Thus, if your business is soon planning larger asset purchases, 2010 purchases may be better than 2011, as the limit for 2010 is $250,000.

√ Penalties for failure to file a Partnership or S corporation tax return are now as high as $2,340 per partner and per shareholder. A few years ago there were not any penalties for failing to timely file an S corporation return and the partnership penalties were about 1/10th of what they are now.

√ Everyone can now convert their IRA to a Roth IRA in 2010. It makes sense in many circumstances, especially the ability to elect to include the conversion amount in income over two years. Here are some of the ideal circumstances:

- You currently have negative taxable income or are in a low tax bracket
- Your tax bracket will be higher in the future
- You have non retirement funds to pay the taxes on the conversion
- You can wait many years before you need the money or won't need it at all
- You are willing to pay taxes now so beneficiaries do not pay taxes later
- Your IRA has suffered a large loss and you anticipate the value to increase
- However, before converting, know the several tax traps to determine if they apply
- A good solution may be to convert part of your IRA to a Roth IRA

√ On June 24, 2010, a major tax bill did not pass the Senate. What the Senate majority leader did say was the bill is tabled for now while the Senate will turn their attention to a bill which would retroactively extend 50% bonus depreciation for 2010. The $8,000 increase in the first-year depreciation limit for passenger automobiles would also be extended for vehicles placed in service before 2011.

√ There have been a few recent tax developments of interest. They include:

- The Government Accounting Office (GOA) reports that S corporations have a high rate of noncompliance including calculating shareholder basis in taking losses and failure to pay shareholder employee adequate wage compensation. The recent tax bill that failed to pass the Senate addressed the inadequate wage compensation concerns.

- The Tax Court held that a nurse was entitled to deduct education expenses she incurred in connection with getting a master of business administration degree with a specialization in health care management.

- Watch out for surrendering whole life insurance policies. The Tax Court ruled a taxpayer had $136,000 of income when they only received $12,000 upon surrendering the policy. What happened is over the years the policy "paid" $124,000 of dividends that were in turn applied to annual premiums. The taxpayer had to include the $124,000 plus the $12,000 as ordinary income in the year of surrender.

- Credit card companies are issuing Form 1099s for cancellation of debt (COD) income. COD income is taxable, unless it is otherwise excludable from income. There are primarily two exclusions: (1) bankruptcy; and (2) insolvency. A taxpayer is insolvent for COD purposes if their debts exceed their assets. If a taxpayer meets one of the exclusions, the proper course of action is to report the COD as income and then take a deduction for the exclusion amount.

Of course the statements contained herein are basic overviews. They all have special rules, conditions, limitations, and exceptions. Thus, this newsletter is not to be viewed as legal, financial or tax advice for your circumstances. Instead, contact our offices. Our telephone number is 918.599.7755. You can also contact us via our web site at Paulhburgess.com. It contains additional information relating to taxation, business law, setting up a company, estate planning, and accounting.