Halcolm Bard
Certified Public
Accountant
& Consultants

TAX AND BUSINESS
ADVISOR

Visit our web page at www.halcolm.com

TAX AND BUSINESS Alert™

November 2007

Once Again, It's Time for Year-end Tax Planning

There is still plenty of time to lower your 2007 tax bill, add to your tax-advantaged retirement accounts, and do a little planning for next year. Here are a few ideas to get you started.

IRAs. You can contribute up to $4,000 ($5,000 if you are age 50 or older by year-end) to your IRA for 2007 if certain conditions are met. For married couples, the combined contribution limits are $8,000 ($4,000 each) and $10,000 ($5,000 each if both are age 50 by year-end) when a joint return is filed, provided one or both spouses had at least that much earned income. The IRA contribution amount is scheduled to increase to $5,000 for 2008, creating an even better opportunity to increase your tax-deferred savings. And keep in mind that contributions to traditional IRAs may be tax deductible subject to specific limitations.

Capital Gains Tax Rates. It may be a good time to consider selling capital assets (e.g., common stock) with a low cost basis. The maximum capital gains tax rate is 15% for gains from the sale of qualifying assets held more than one year. The 15% maximum tax rate is available for both the regular and alternative minimum tax (AMT). In addition, qualifying dividends individuals receive during 2007 will generally be taxed at the 15% (or less) capital gains rate.

Elective Deferrals. The 2007 annual deferral limit for qualified retirement plans is $15,500. If you are at least age 50 by year-end, you can contribute an additional $5,000 to 401(k), 403(b), and 457 plans in 2007.

Photos.com

Section 179 Expensing. For your business, the Section 179 (election to expense otherwise depreciable assets) limit is $125,000 for eligible property placed in service during 2007 and includes qualifying property placed in service as late as December 31, 2007. However, the Section 179 deduction phases out, dollar-for-dollar, after eligible equipment purchases reach $500,000. So, the $125,000 deduction amount for 2007 is completely phased-out when eligible equipment purchases reach $625,000.

Disability Insurance for Business Owners and Professionals

As you probably know, it's wise to have disability insurance coverage to protect you and your family from loss of earnings if you become unable to work. Studies show that the possibility of permanent disability is far greater than death during a person's working lifetime. Total and permanent disability is not only statistically more common than premature death, but can also have a much greater financial impact on the family. Both death and disability can remove a source of income, but with disability, family expenditures might actually increase. The disabled person must be fed, clothed, and sheltered, and the family is faced with large, ongoing medical expenditures.

Disability insurance needs are usually based on the level of wages that would be lost if you were disabled. However, a more precise method may be needed to measure the gap between anticipated expenditures and continuing income. This method considers other sources of income and special funding needs, such as unfunded education costs.

The benefits paid under a disability insurance policy can be totally tax-free to you, 100% taxable, or partially taxable depending on the type of policy, who pays the premiums, and whether or not they are paid with pre-tax dollars.

Reporting Poker Tournament Winnings

Photos.com

The IRS has issued a new procedure requiring poker tournament sponsors (including casinos) to withhold from and report payments to tournament participants to whom they pay winnings exceeding the winner's tournament entrance fees by at least $5,000.

This new procedure is effective for payments made on or after March 4, 2008 and covers all payments made to a winning payee in a single tax year by filing an information return for each payee. Specifically, the tournament sponsor must furnish a copy of the information return(s) to the IRS by February 28th (March 31st if filed electronically) of the year following the calendar year in which the payment was made.

Observation: Earlier this year, the Tax Court held that tournament poker is a wagering activity for tax loss limitation purposes.

IRS Warns Taxpayers of a New *Phishing* Scam

The IRS recently warned taxpayers of a new phishing scam in which a phony IRS email tells recipients they can receive $80 by filling out an online customer satisfaction survey. *Phishing* is the term used to describe the practice of tricking victims into revealing private personal or financial information over the Internet, telephone, or by other means. In this case, the email notifies the recipient that he or she has been randomly selected to participate in a survey. They are told that, in return for filling out the survey, they will receive an $80 credit from the IRS. In addition to standard customer satisfaction survey questions, the survey requests the name and phone number of the participant and also asks for credit card information.

Taxpayers should note that the IRS does not initiate contact with taxpayers via email and they can send information about suspicious emails claiming to come from the IRS to *phishing@irs.gov*. Since establishing this email box last year, the IRS has received more than 30,000 emails reporting almost 400 separate phishing incidents.

◇ Corporations◇LLCs◇Proprietorships◇Bookkeeping & Payroll◇Taxes◇Businesses & Individuals◇Financial Statements◇

Halcolm Bard CPA • 38 Fraley Street • Kane, Pennsylvania 16735 • (814) 837-9150 • Tax and Business Advisor

Tax Aspects of Refinancing Your Home Mortgage

Given all the turmoil in the residential lending market of late, it may be worthwhile or even necessary to refinance your mortgage. Refinancing your mortgage can be expensive, so you will want to avail yourself of any related tax breaks to offset your closing costs to the extent possible. Listed below are some of the tax implications of that refinancing decision.

Treatment of Points

Points paid to refinance a home mortgage are nothing more than prepaid interest on the new loan. As such, the tax rules for home mortgage interest apply, but with a few twists because the interest in question is being prepaid.

When the new mortgage simply replaces the old one on a principal residence (i.e., no additional debt is taken out), the points paid for the new mortgage are capitalized and then amortized ratably over the life of the new loan. The resulting amortization deductions are then written-off on your tax return as qualified residence interest for both regular tax and alternative minimum tax (AMT) purposes.

Under an exception to this general rule, homeowners can immediately deduct refinancing points allocable to additional mortgage debt if the debt is used to pay for additions or improvements to the homeowner's principal residence. In this case, the debt must be secured by the residence and there is generally an overall limit of $1 million on all debt qualifying as incurred to acquire, construct, or improve a qualified residence.

To claim an immediate deduction under this exception, cash-basis taxpayers must actually pay for the points out-of-pocket (they cannot be rolled over into the principal balance of the new loan). If the preceding conditions are satisfied, the allocable points can be deducted in full on your tax return in the year they are paid.

Other Refinancing Costs and Fees

In addition to points, mortgage lenders usually charge a variety of fees for obtaining the loan. These fees are not deductible. You may also incur attorney, appraisal, and title fees, and pay other incidental expenses associated with a home purchase, such as recording fees and transfer taxes. These fees and expenses are added to the home's basis (the cost used to determine gain or loss when the home is sold).


Photos.com

Interest Expense on the New Loan

Under both the regular tax and the AMT rules, interest expense is deductible to the extent the debt proceeds are used to (a) acquire, (b) construct, or (c) substantially improve your residence. Interest on a new mortgage taken out to refinance another mortgage is also qualified housing interest to the extent the principal of the original mortgage generated qualified housing interest. Thus, such a refinancing should have no effect on your ability to continue deducting the mortgage interest.

Unamortized Points from the Old Loan

That brings us to a potentially big deduction related to the refinancing. If you previously refinanced your mortgage and were amortizing the related points, the unamortized balance can be immediately deducted when the related loan is refinanced with a new lender (to the extent the points were amortizable in the first place under the regular tax and AMT rules explained above).

Please don't hesitate to contact us if you would like to discuss the tax ramifications of refinancing your home mortgage.

Halcolm Bard CPA • 38 Fraley Street • Kane, Pennsylvania 16735 • (814) 837-9150 • Tax and Business Advisor

Is an S Corporation Right for Your Business?

Photos.com

S corporations offer their shareholders many advantages. One major advantage of an S corporation, as opposed to a partnership, is that an S corporation offers liability protection to its shareholders. This means that as S corporation shareholders, you normally are not personally liable for corporate debts. In order to receive this protection, it is important that the corporation be adequately financed and that various state-required formalities be observed. These formalities include filing articles of incorporation, adopting by-laws, electing a board of directors, and holding organizational meetings.

If you expect the business to incur losses in its early years, an S corporation is preferable to a C corporation from a tax standpoint. Shareholders in a C corporation generally get no tax benefit from such losses. In contrast, S corporation shareholders generally can deduct their percentage share of these losses on their personal tax returns to the extent of their basis in the stock and in any loans they made to the entity. Losses that cannot be deducted because they exceed your basis are carried forward and can be deducted when there is sufficient basis.

When the S corporation earns profits, the income will be taxed directly to you whether or not it is distributed. It will be reported on your individual tax return and be aggregated with income from other sources. Distributions that you receive from the S corporation, however, are nontaxable to the extent of stock basis.

Keep in mind that a corporation must remain eligible for S corporation treatment. For example, the corporation could inadvertently lose its S status if stock is transferred to an ineligible shareholder such as another corporation, a partnership, or a nonresident alien. If the S election terminates, the corporation becomes a C corporation, which is a taxable entity. You would not be able to deduct any losses, and earnings could be subject to double taxation—once at the corporate level and again when distributed to you. In order to protect against this risk, we recommend that each shareholder sign an agreement promising not to make any transfers that would endanger the S election.

Please call us to cover these issues or any other important aspects of setting up and maintaining an S corporation.

❖ Corporations❖LLCs❖Proprietorships❖Bookkeeping & Payroll❖Taxes❖Businesses & Individuals❖Financial Statements❖
Halcolm Bard CPA • 38 Fraley Street • Kane, Pennsylvania 16735 • (814) 837-9150 • Tax and Business Advisor