Arkansas Public Accountant

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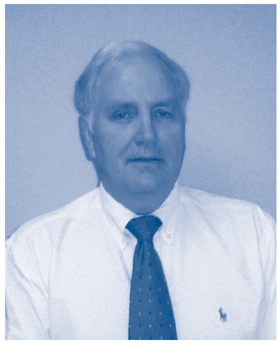
• FROM YOUR PRESIDENT'S PEN •



Dear Members:

Is bigger really better? There must be those in our world that are believers in that theory. This past week two giants merged so that they could use their buying power to compete with another mega retailer. Everywhere we turn we are faced with the decision of whether or not bigger is better.

Topics Covered in this Newsletter

- SOCIAL SECURITY BENEFITS
- EARNED INCOME CREDIT FOR NEICES AND NEPHEWS
- IRS WEBCASTS
- VALUABLE TAX RELIEFS ON VANS AND LIGHT TRUCKS
- LIFE INSURANCE LOOPHOLES

The two big decisions that involve our use of software both for write-up work and tax work cross this subject in a big way. The crazy thing about where we are today with these decisions is that much of the time it is not really a decision that we get to make. I am speaking from past experience. Two times my tax software provider has sold out to a larger (and better I am sure) provider. Many of you are using long time providers that are small. Hopefully you can put off the decision of bigger and better. However, you may not be able to put off this decision much longer.

Our write-up options are shrinking as well. The choices for write-up software are getting tougher and tougher. Not only are we faced with the bigger-better decision but also pricing is a big issue for all of us. It is with the tax software as well. The fact that most of us have small offices makes price almost as much an issue as quality of the software itself.

You might be asking yourself, why are we having this discussion anyway. Well our society is facing the bigger-better decision. A few weeks ago a letter came over the fax from our write-up provider-The Thompson Company—you know- Creative Solutions. It seems that the people who have been providing our CPE for years had been purchased by The Thompson Company.

On the surface, this news didn't really sink in until a few days later when the rest of the story became known. Thompson Company has made assurances to us that they are retaining the Gear-Up speakers and that we will continue to receive a great seminar for the price that we are spending. Your society is working hard to make sure that their promise will be good. We know how important your CPE provider is and we also know that you have options as well. You have our promise that we will do whatever is necessary to provide you with quality CPE at competitive prices.

Hopefully, you have attended the 1040 tax seminar by the time you read this. It is just a few days until we start the madness all over again. I wish that each of you has a joyous holiday season and have a great new year. May each of you be blessed.

Respectfully yours,

Tom Simmons, President
Arkansas Society of Accountants

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SOCIAL SECURITY tax wage base goes up to $90,000 in 2005. This is an increase of $2,100 from $87,900 in 2004. About 10 million individuals will pay higher Social Security taxes as a result. *Flip side:* Social Security benefits will increase by 2.7% in 2005 for 52 million recipients.

SURPRISINGLY HIGH TAXES ON SOCIAL SECURITY BENEFITS----------

Social Security recipients now can incur the highest tax rates of anybody. While the normal top bracket rate has been reduced to 35%, Social Security Recipients may face effective marginal tax rates of 50% or more.

WHY? Up to 50% of Social Security benefits become subject to income tax when adjusted gross income (AGI) exceeds $25,000 on a single return and $32,000 on other returns, and up to 85% of benefits are taxed when AGI exceeds $34,000 on a single return or $44,000 on other returns.

EXAMPLE: A single individual with AGI over $34,000 will an income range where every extra dollar of regular income causes $0.85 of Social Security benefits to be taxes as well – so tax becomes due on $1.85. If the individual is in the 28% bracket at that range, the extra dollar of income will generate 52 cents of tax (1.85 x .28 = 0.518) an effective marginal tax rate of 52%. The rate may be higher when state taxes are counted. (some states do tax SS benefits)

TWIST: Interest on tax-exempt bonds is counted in AGI for this purpose – so even tax-free interest can cause Social Security benefits to be taxed.

WHAT TO DO: Before you retire, learn the amount of your expected Social Security benefit and project your other income. Next, project your tax bracket situation. Then you can plan steps to reduce your future tax rate as your situation dictates.

POSSIBILITIES:

…If you will keep working after your full retirement age, defer receiving you Social Security benefit to take a proportionately increased benefit later.

…Reduce AGI by taking capital losses and incurring business expenses.

…Defer cashing in investments and taking distributions from IRAs and retirement accounts until you need the money or are required to take minimum distributions.

…Invest in appreciating assets rather than income producing assets, and in tax-efficient mutual funds that pay minimal taxable distributions.

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EARNED INCOME CREDIT AVAILABLE FOR NIECES AND NEPHEWS. Matthew Gilmore was 19 years old and lived in an apartment with his mother, three sisters and two children of one of his sisters. He had a job, helped support the family, and cared for his nieces, for whom he claimed an earned income credit. But the IRS denied the credit. *Tax Court:* To qualify Matthew for the EIC, the children must meet age, residence, and relationship tests. As minors who lived with him, they met the first two. As nieces, they met the relationship test if he "cared for them as his own children." *Ruling:* As the oldest male of the family who both cared for and worked to support them, he did so and thus gets the credit. *Matthew D. Gilmore,* TC Summary Opinion 2004- 38.

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IRS WEBCASTS ON FREE TAX EVENTS AND POLICY INFO

Tax Talk Today is a free Internet video broadcast in which top IRS officials and private-sector tax experts discuss a key subject of tax practice and IRS policy.

During the monthly, live program, you can send questions to the panelists by E-mail, telephone or fax.

Scheduled web cast topics…..

December 14, 2004, "Get ready for Filing Season 2005 (Part 1 – Individuals)."
January 11, 2005, "Get Ready for Filing Season 2005 (Part 2 – Business)."

All live web casts are on Tuesdays, from 2pm – 3 pm Eastern Standard Time. You can also review an archive of past discussions at any time.

Subjects of recent web casts available in the archives…..

- Executive Compensation
- IRS Collection – The Times Are a'Changing.
- A Professional Responsibility for Tax Practitioners
- Everything's Electronic
- What Business Entity Are You? – Oh, the Difference It Makes

For more information about the web casts, details about scheduled discussions, and to view archived shows, visit www.taxtalktoday.tv.

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American workers spend more of their day working to pay taxes than they do to feed, clothe, and house their families.

The Tax Foundation

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That most delicious of all privileges – Spending other people's money.

John Randolph, US Senator
1825 – 1827

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VALUABLE NEW TAX RELIEF
ON VANS & LIGHT TRUCKS

Thousands of businesses, from neighborhood handy-men to big companies with fleets of vehicles – may be able to claim more generous depreciation on vans and light trucks than they previously could, thanks to regulations issued earlier this year by IRS.

Like temporary regulations issued last year (TD 9069), the final regulations (TD 9133) apply to property placed in Service on or after July 7, 2003. However, the final regulations are more generous, offering retroactive relief as well. Taxpayers may choose to apply the pertinent sections [Code Section 1.280F-6©(3)(iii)] to property placed in service before that date by filing amended returns for all open tax years – 2001, 2002, and 2003 – or by treating the matter as a change in accounting method and filing IRS Form 3115, *Application for Change in Accounting Method.*

While no tradesperson dressed in coveralls and driving a van outfitted with tools and supplies is likely to harbor the illusion that he/she is driving a luxury automobile, luxury automobiles are the heart of the matter.

Until the temporary regulations were issued last year, there were severe limitations in the depreciation that could be claimed on trade vehicles because of the rules limiting depreciation on luxury automobiles.

Despite the term "luxury," for years, these rules affected vehicles used 100% in business and costing more than $15, 300. and for 2004, they affect vehicles costing more than $14,800. The regulations noted that the purpose of the rules was "to discourage overspending on passenger automobiles purchased for use in business."

Businesses had complained that under the applicable depreciation limits they could not recover the costs of small vans or light trucks, a category that includes sport-utility vehicles, over a standard five-year period, even though they were using the vehicles for valid business purposes.

Bigger vans or trucks weighing more than 6000 pounds were not affected by the luxury automobile rules, but trades people such as cable installers, painters, carpenters, electricians, and many repair people, often use the smaller vans or trucks that were affected.

The new regulations note that vans and light trucks have been subject to greater price inflation than passenger cars since the annual dollar limits on depreciation were established in 1988.

The regulations raise the limits for the trucks and vans. For trucks and vans, the first year depreciation in 2004 is $3,260 (or $10,910 if you include the 50% bonus depreciation provided by the *Jobs and Growth Tax Relief Reconciliation Act of 2003)*, $5,300 in the second year, $3,150 in the third year, and $1,875 in each succeeding tax year.

In contrast, or ordinary cars placed in service in 2004, the depreciation limitations are $2,960 for the first year (or $10,610 under the 50% bonus depreciation), $4,800 in the second year, $2,850 in the third year, and $1,675 in each succeeding tax year.

In addition to raising the dollar limits, the regulations exclude vans and trucks from the luxury automobile dollar limitations, provided they have been modified to preclude the likelihood of anything but de minimus personal use.

Among the criteria listed in Code Section 1.274-5T(k)(7) for what are termed "qualified nonpersonal use vehicles" are delivery trucks with a seat for only the driver or for the driver and one passenger in a folding jump seat, the installation of permanent shelving and fixtures, and painting the name of the business or advertising on the exterior.

A tradesperson's van would likely qualify for exclusion from the luxury automobile depreciation limits. A comfortable passenger van used by a real estate person to drive clients to homes would not qualify, even if it the van is used solely for business – but it would qualify for the higher write-offs on vans instead of cars.

The matter is further complicated because, as the regulations note, both the *Job Creation and Worker Assistance Act of 2002 and the Jobs and Growth Tax Relief Reconciliation Act of 2003* provided temporary relief on depreciation of business assets.

A solo tradesperson who bought a van last year and took advantage of temporarily expanded Code Section 179 limits to depreciate it fully would have no need to act further. But a tradesperson who bought his van in 2001 or 2002 or a business with substantial depreciable assets that used Section 179 for other assets could benefit from the new regulations' retroactive provisions.

Whether you should amend returns for prior years or file for a change of accounting to take advantage of the new regulations will depend on when the business had the greatest income and thus when the depreciation deduction would be of greatest value.

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LIFE INSURANCE
LOOPHOLES

Smart insurance buyers can save a bundle in taxes, both in life and in the execution of their estates, if they look into these strategies….

Life insurance proceeds are income tax free. This is true even if only a few premium payments were made. However, life insurance premiums are not tax deductible.

Life insurance proceeds are partly or totally estate tax free if the policy or part of it is owned by the beneficiary, not the insured.

Better: Use an irrevocable life insurance trust (ILIT) as the policy owner. If children or other individuals own the policy, it becomes available to an ex-spouse or unintended strangers in the event of divorce or a lawsuit against the child. The proceeds are estate tax free if you have no control over the policy. *Caution:* Making your estate the beneficiary subjects the proceeds to tax.

Do not let your spouse own the policy. A policy owned by the decedent or his/her spouse is taxed in the estate if both due simultaneously. Instead use an ILIT as owner of the policy.

Do not name a former spouse as beneficiary. If you do, the proceeds will be included in your estate because the policy will have been owned by the decedent.

Better: Set up an ILIT as owner in accordance with your divorce agreement.

So-called "Crummey letters" make annual gifts to a trust to pay for life insurance premiums eligible for the $11,000 annual gift tax exclusion. (A Crummey letter notifies trust beneficiaries of their right to withdraw the amounts given to the trust.) If the beneficiaries do not waive their rights to their portion of the gift via a Crummey letter, the gift is subject to gift tax.

Policies purchased by an irrevocable life insurance trust are not subject to a "waiting period." When existing policies are transferred to a trust, there is a three year waiting period before proceeds are tax exempt.

Strategy: When policies are transferred to new trusts, the clock starts ticking. If the insured dies within three years, the proceeds are subject to estate taxes. Buy an inexpensive three-year term policy to cover estate taxes.

Use income from life insurance proceeds to pay an "allowance" to children's guardians if both parents die. Establish the allowance provisions in the will or trust.

Avoid "transfer for value" taxation that applies when an owner sells the policy to the insured – a partner of the insured – a partnership in which the insured is a partner – or a corporation in which the insured is an officer or shareholder.

Trap: When the policy is sold to any of the buyers listed, the excess of the proceeds over the premiums paid is taxable income to the recipient of the death benefit.

Write an "apportionment" clause into your will. This designates that estate taxes attributable to inadvertently owned life insurance proceeds will be paid by the recipient, not the estate.

Employer-paid group term life insurance premiums are tax free up to $50,000 of life insurance. Premiums paid for policies over that are taxable at reduced rates determined by IRS tables.

Whole life insurance creates a tax-free build-up of cash value that offsets premiums in later years. When paid as part of the life insurance proceeds, it is not taxed ---- nor when borrowed from the policy… when withdrawn, it is tax free to the extent of total premiums paid.

THESE ARE JUST A FEW OF THE BENEFITS AVAILABLE THROUGH LIFE INSURANCE. BE SURE TO GO OVER THESE WITH YOUR CLIENTS AND OTHERS TO SEE WHAT THEY NEED IN THE WAY OF COVERAGE AT THE TIME OF DEATH.

APPLICATION FOR MEMBERSHIP IN THE ARKANSAS SOCIETY OF ACCOUNTANTS

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Newport, Arkansas 72112
longaspa@cox-internet.com
www.arspa.org

Last Name | First Name | Middle Initial | Business Phone | Home Phone

Business Address

How many years of accounting have you had?__________ Date of Birth__________

Sole Practitioner [ ] Partner [ ] Employee [ ] Corporate Officer [ ]

Name of Firm__________ Number of Employees__________

Name of Partner(s)__________

Are you a Licensed, Registered or Certified Public Accountant?__________ If yes, give License#__________

Are you an Accredited Public Accountant?__________ If yes, give Accreditation #__________

Are you an Enrolled Agent__________ If yes, give EA #__________

Do you hold an Associate or Baccalaureate degree with a minimum of 24 semester hours in Accounting? Yes____ No____

Are you engaged in any other trade or profession?__________ If yes, please describe__________

Please list other accounting organizations in which you hold membership:__________

I hereby state that the accompanying statements are correct to the best of my knowledge and belief. I further state that I will abide by the Constitution and By-Laws of the Society and will practice in strict conformity with the Code of Ethics and Rules of Professional conduct adopted by the Society.

Date__________ Signature of applicant __________

Annual dues are payable IN FULL in advance and are prorated for credit by ASPA on a monthly basis to August 31 - the end of ASPA's fiscal year.

[ ] Membership Annual Dues $85.00 [ ] Firm Annual Membership $50.00 [ ]Diamond State Annual Dues $15.00 (Non-Residents only)

Do Not Write Below This Line

State Member Approving Membership

Signature | Title | Date

Sponsor, If Any

FOR ASPA OFFICE USE ONLY

Amount	Date Received	Control Number

"State Society dues payments may be deductible as an ordinary and necessary business expense. However, they are not deductible as charitable contributions for Federal income tax purposes.

OFFICERS & GOVERNORS

FOR YOUR INFORMATION

The ARKANSAS PUBLIC ACCOUNTANT is the monthly publication of the ARKANSAS SOCIETY OF PUBLIC ACCOUNTANTS. We are a professional organization dedicated to the promotion of accountants and tax preparers in the State of Arkansas. We accept newsworthy articles and advertising. If you have either of these for publication, please contact the editor.

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