ARKANSAS SOCIETY OF ACCOUNTANTS

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RESPECTED ACCOUNTING PROFESSIONALS SERVING OUR COMMUNITIES

Monthly Newsletter
May 2006

Depreciation Limits for 2006 business cars
Information on IRS audits
"Client Loyalty" advice
Defering Taxes on Real Estate Sales

• FROM YOUR PRESIDENT'S PEN •

Dear Members,

The first leg of the tax filing season has finally drawn to a close. Without an August 15th deadline this year, our firm will have to stay on top of our extended return filings, or we will be in trouble come October 15th.

Our firm will spend the next three or four weeks catching up on our monthly accounting engagements that we have somehow gotten behind on completing. We will also spend some time on all of the other projects that we have put off until after tax season.

This is also the time of year that many firms give their tax preparation software a performance review. If you think a software change is in your future, now is an excellent time to begin testing new software on some of your extended 2005 tax returns.

Most of us are also formalizing our plans for our continuing professional education needs for the upcoming seminar season. Visit the Arkansas Society of Accountants website at arspa.org for a complete list of the seminars we will be sponsoring for 2006.

The first of these seminars is coming up in Little Rock on May 26th at the Holiday Inn Select. It will be presented by GearUp and the topic will be fraud detection. This seminar is a new topic for a lot of us. It will be nice to start the year with something we haven't had in the past, which is very relevant in all of our practices in this post Enron/WorldCom environment. The early bird registration ends on May 12th, so if you have not received your registration form, visit the ASA website today for a downloadable copy of the registration form.

If you are not a member of the National Society of Accountants, now would be an excellent time to join. The NSA provides its members with too many benefits to mention in this letter, so visit the NSA's website at nsacct.org for information about becoming a member.

I look forward to seeing each of you at the fraud detection seminar in Little Rock later this month.

Sincerely,

Bryan K. Johnston. CPA
President, Arkansas Society of Accountants

NEWLY RELEASED depreciation limits for business cars purchased in 2006 and used 100% for business are $2,960 in 2006, $4,800 in 2007, $2,850 in 2008 and $1,775 in subsequent years. Using these limits, it would take more that 19 years to fully depreciate a car costing $40,000.

WHAT THE IRS doesn't want us to know about audits. In recent months, and especially as the tax return filing deadline approached, the IRS has been publicizing its renewed emphasis on tax law enforcement and how it is auditing an increasing number of tax returns.

But just released data on IRS audit rates during 2005 (examining returns filed in 2004) reveal that IRS enforcement levels remain at or near historic lows in many critical areas.

IRS claims of increasing audit rates are misleading in some cases, and even where audit rates have increased as the IRS says, it has only been from recent all-time lows, leaving the rates very low overall.

The face-to-face audit rate has reached new lows, especially for highest income returns. It's true, as the IRS highlights, that the audit rate for personal tax returns is increasing, and that the IRS is giving special audit scrutiny to returns of high income taxpayers. (Those with income over $100,000).

The audit rate for all individual tax returns increased to 0.93% for tax returns examined in 2005 from a low of 0.49% in 2000, a 90% increase.

The audit rate for "high-income" tax returns was 1.19% in 2005, up from a low of 0.69% in 2001, an increase of 72%.

April 26, 2006

From Jim's Desk:
A message from your District VIII Governor

Now that we have tax season behind us and everyone has had a chance to rest up some and catch their breath, some of you are probably slowly sifting through your files wondering why this or that client didn't come back this year. Well, here's a thought. It might sound silly, stupid or unrealistic to you, but I assure you it really is working for me.

Challenge. Make yourself indispensable in the mind of your client. You are THE most important professional person your client comes in contact with the exception of perhaps his/her doctor because you not only keep them out of trouble with the dreaded IRS, but you also provide them with a myriad of other financial and sometimes personal advice to make their lives easier and better. You are a true professional in every sense of the word, but still, every year there are those for seemly no reason, don't come back. It's not that they no longer have enough personal deductions to itemize so they are in essence "short formers" now and don't need your additional expertise to file an "A" or "EZ" form. They left for some other reason.

Well, here's some "client loyalty" advice for you- GET A DOG. That's right, get a dog and bring it to your office every day. I did that two years ago really to protect my wallet. You see we had just gotten a new 9 month old Cocker in late November and boy
Did that dog chew! We keep the dogs (total of three) in our garage when we are not at home and at night to sleep. This new dog, Zoë, was chewing everything in the garage, I mean everything. Not just a couple of throw

rugs we have out there, not just their beds (she chewed all three of them at one point or another), but she even started chewing the sheet rock on the walls!!! Zoë had chew toys, pull toys, every kind of toy you can buy a dog, but left alone, she preferred "other" things – anything but her toys.

So rather than completely rebuild the inside of the garage when tax season was over, I decided to just bring her into work with me so I could keep an eye on her. After buying a cute hardwood gate for around $99 I had seen in a catalog to keep her in my office we started tax season.

I must admit I was a little apprehensive about how the clients would react to her being there. But my fears were vanquished with each client that came in. This was especially true with couples that came in. I'm sure this is true in your office as it is in mine. Once the interview begins one of the spouses becomes the dominant on interacting with me on their tax records. The other usually sits politely and quietly and says very little. Well this year that person almost without exception began playing with Zoë and periodically tapping the other spouse on the shoulder to call his/her attention to "how cute the little dog is".

Well, tax season finally ended and Zoë, thank goodness, had basically gotten all of her permanent teeth so chewing everything in sight was no longer her number one priority. As a result, I stopped bringing her to the office.

January 2006 rolls around and I'm out of the habit of being Zoë to the office. I'm not joking or exaggerating, five out of the first 6 tax clients that came in this year, before they ever sat down in their chair, turned around in the room and said "Where is the dog? You mean you didn't bring the dog! We liked that dog. Shame on you for leaving her at home!"

Well, sometimes I'm a little slow on the pick-up, but I got the hint. Zoë was back in my office the next day and everyone again played with her, petted her, fed her French fries they had with them – and all was well in Del City, America once again.

So, if you want true **CLIENT LOYALTY**, get a dog! No joke.

Upcoming NSA events, activities. April 19th I'll be off to once again participate in the budget meeting as chair of the Board's finance committee. This is where the final "tweaks" will be made to the 2006-07 NSA budget that Budget chair Donny Woods and the NSA staff have been working on so hard this past month. The budget will then be presented to the full Board of Governors at their May meeting for consideration. The meeting will be held in St. Augustine, FL the 19th through the 21st .

Upcoming NSA events to note: NSA's "Serving Aging America" Levels 1-3 in Las Vegas, NV June 5th through the 10th. Excellent CPE! And it's not too early to start planning to attend the NSA convention in Providence, RI, August 16th – 19th.

District VIII really stood out at last year's NSA Convention during the time allotted for contributions to the Foundation's Circle of Support portion of the business sessions. With the assistance of some generous non-resident members of some of the states in District VIII, we became the FIRST district to have all of its ASO's donate $1,000 each to the Circle of Support!

That's a tough act to follow, but I'm at it again. Please make plans to include in your budgets for the upcoming year your ASO's contribution to the circle of Support. These funds must be presented at the annual NSA convention to be included in this year's campaign. I'll be visiting with the various state presidents about this over the next month or two, but all members should encourage the ASO leadership to include the funding of the Circle of Support in every annual ASO budget. The Foundation trustees have made great strides this year to "lasso" him overhead, changing the way the foundation operates to make it measurably more cost effective. But there is and will always be overhead to pay for if we are to have a scholarship program. Get involved now to include a contribution from your ASO to the Circle of Support at this year's NSA Convention.

I am really looking forward to seeing many of you again this June and July at your state conventions in Louisiana, New Mexico, Oklahoma and Texas. (I'll have to wait until the NSA Convention to see my Arkansas friends as their state convention isn't until September.) This is truly the best part of being your Governor – getting to visit one on one with so many of you each year, not just at the NSA convention, but at your state convention as well.

JIM ALSO FORWARDED TO ME THE ARTICLE THAT HE REFERENCED IN HIS LAST LETTER. (APRIL PUB) AND I SENT THIS ON TO OUR WEB GUY TO POST ON THE WEBSITE. IF ANY OF YOU ARE INTERESTED YOU MAY ACCESS IT THERE. www.arspa.org.

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IRS loses. Can't set off firm's tax refund against pre-bankruptcy tax bill. Rocor Inc. was a trucking company that paid both heavy vehicle highway use (HVHU) tax and fuel tax, and that filed bankruptcy in the middle of a year. After filing, it came entitled to a $160,000 fuel tax refund. But the IRS offset that against HVHU tax payments that it didn't make after the filing. Key: The IRS could offset the post-filing refund only against taxes incurred post-filing not any incurred before the bankruptcy filing. Court: Although Rocor owed HBHU payments post-filing, the year's tax bill was determined before the filing by the number of trucks it owned at the start of the year. So, the IRS can't keep the refund. In re: Rocor International Inc., Bankr. WD Ok., No.02-17658-WV.

Roger Sherer didn't file a tax return for 1999, so the IRS properly mailed a deficiency notice to the address shown on his last-filed return.

But Sherer didn't live there anymore and the US Postal Service failed to deliver the notice to him, so he didn't learn about the tax assessment.

Later, the IRS moved to impose a lien to collect the tax. At that point, Sherer requested an IRS Appeals "due process" hearing in which he tried to contest the tax bill on the merits. After the hearing, Appeals held against him.

Upon receiving the notice of determination from IRS Appeals upholding the tax lien, Sherer timely filed a Tax Court petition – but IRS said that he had forfeiting the right to do so when he didn't respond to the properly sent original deficiency notice.

Tax Court: Sherer had never had a chance to make his case on the merits because he had never received the deficiency notice, and the IRS Appeals later refused to consider the merits of the case.

Yet, he had cooperated with IRS Appeals, raised his argument at an Appeals hearing, and properly contested the hearing's determination, so his Tax Court filing is up-held (and in fact he won in court on the merits.) Roger L. Sherer, TC memo 2006-29.

Latest Way to Defer Taxes on Real Estate Sales. The long-running real estate boom has enticed many investors to buy rental properties. Most invest in relatively small properties—rental houses, modest apartment buildings, etc. By the time they factor in the cost of hiring a property manager or devoting their own time to operational details, many decide it's more lucrative and convenient to sell these properties and reinvest the proceeds in income-producing securities.

Trap: Doing so triggers capital gains tax.

With older properties in which the mortgage has been refinanced several times, the tax may be higher than the cash proceeds. (The depreciated basis will be low, increasing the taxable gain, while repayment of a large mortgage will cut down on cash to the seller.)

The above problem may be most severe for investors who have refinanced highly appreciated property.

Example: Joe Jones bought a professional office building in his hometown many years ago for $100,000. The building is now appraised at around $1 million.

Over the years, Joe has refinanced the building a few times as it went up in value. The mortgage has increased to $800,000.

Now Joe wants to sell the building so he won't have to deal with management responsibilities any longer.

Assuming that Joe has fully depreciated the building and nets $950,000 from the sale after expenses, he would have an $850,000 long-term gain. This gain would be taxed at the maximum long-term capital gains rate of 15%. The $100,000 worth of depreciation recapture would be taxed at 25%. Total tax: $152,500.

(Many states and even some cities would tax this income too. Which would add to Joe's obligation.

If Joe pocketed $950,000 from the sale and owed at lease $152,500 in tax, his after-tax profit would be less than $800,000.

Even if he hadn't refinanced the investment property this heavily, a sale still would likely generate a sizable tax bill.

Joe's solution: Use a like-kind exchange with ownership shared by other investors.

To qualify for an IRS safe harbor in this type transaction, replacement property must be identified within 45 days of selling the old property. The new property must be acquired within 180 days of the sale.

Since swapping one small property for another probably won't reduce Joe's management commitments substantially, he structured the exchange so that ownership is by tenants-in-common (TIC).

Instead of exchanging his property for another comparably valued one, he swapped for an interest in a larger property, a piece of a major office building or a regional mall, for example.

IRS guidelines allow up to 35 investors to hold TIC interests in such properties.

As owner of a TIC interest, Joe shares in the property's operating profits, pro rata. As one of 20 equal owners, for example, he would get 5% of any cash distributed to the owners.

At the same time, his fortunes aren't locked in to those of the co-owners. If Joe decides to sell (and pay the deferred tax bill of $152,500, plus tax on any current profits), he is allowed to dispose of him interest, even if co-owners prefer to hold onto the building. If Joe wants to sell his interest, it is up to him to find a buyer. The sponsor of the deal may be able to help him find a buyer.

How such an investment would save Joe money: Joe could sell his apartment building, receive $950,000, and pay off his $800,000 mortgage. The $150,000 net proceeds would be held by an unrelated third party, such as a real estate attorney or a trustee known as an accommodator. Recapture tax as well as capital gains would be deferred.

Then Joe could seek to invest his $150,000 in a TIC interest, which also has a mortgage, so the total purchase price of the property (among all investors) is at least $950,001.

(This is a hypothetical example. Some TIC programs have minimums of $250,000 or more.)

The same 45 and 180-day time constraints apply to a TIC exchange as described earlier.

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DON'T FORGET TO REGISTER FOR

THE GEAR UP FRAUD DETECTION

SEMINAR TO BE HELD MAY 26, 2006.

IF YOU NEED A REGISTRATION

FORM CALL 1-870-523-5329 OR FAX

870-217-0154.

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BOARD MEETING MAY 25, 2006

HOLIDAY INN SELECT 6:30 PM

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HAVE
A
NICE
DAY

APPLICATION FOR MEMBERSHIP IN THE ARKANSAS SOCIETY OF ACCOUNTANTS

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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

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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.

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The ARKANSAS PUBLIC ACCOUNTANT is the monthly publication of the ARKANSAS SOCIETY OF 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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