



Business records are vital

Many business owners assign low priority to recordkeeping, at least until their first tax audit. Then they find legitimate deductions have been disallowed or revenues overestimated, solely because of inadequate documentation. Without supporting evidence, tax auditors create their own estimates of income and expenses, often resulting in inflated tax assessments.

- **Tax audits.** The normal statute of limitations for an IRS audit is three years, but that period may be extended to six years if the agency suspects gross income has been understated by more than 25 percent. It's wise to keep most records for seven years. Certain types of records, such as loan papers, asset purchase contracts, or long-term investment documents, should be kept for the life of the loan or asset plus seven years. Partnership agreements, articles of incorporation, operating agreements, and similar documents should be kept permanently.

- **Management information.** Operating without keeping records is a little like driving blindfolded. Besides saving tax dollars, proper records can help business people identify and evaluate trends in earnings and expenditures and thereby plan more intelligently. They also facilitate preparation of financial statements, which are required when applying for financing or reporting to regulatory agencies.

For a review of your business's recordkeeping needs, give us a call. ♦

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client alert

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Nine tax moves you should consider before year-end



Don't overlook tax moves you can still make before year-end that could lower your 2011 taxes. Here are some possibilities.

- 1) Do what you can to delay income until 2012 and accelerate deductions into 2011. That may enable you to claim larger deductions, credits, and other tax breaks for 2011 that are phased out based upon adjusted gross income.
- 2) If you believe that you will owe state or local taxes, consider prepaying them before the end of the year in order to claim the deduction in 2011.
- 3) If you are a homeowner, consider making energy-saving improvements to your residence in order to qualify for energy tax credits.
- 4) Consider accelerating certain big ticket purchases into 2011 in order to generate a deduction for sales taxes if you can claim the general sales tax deduction rather than a state income tax deduction.
- 5) Use your credit card to purchase deductible items in 2011. Remember that using a credit card allows for a deduction when the purchase is made, not when the card is paid.
- 6) Review your stock portfolio and offset gains and losses. Consider taking additional losses (up to \$3,000) to be deducted in 2011.
- 7) If you are a business owner and need additional furniture, fixtures, equipment, etc. to operate your business, consider making that purchase before the end of the year in order to qualify for the Section 179 expensing deduction and/or 100% bonus depreciation.
- 8) If you believe that a Roth IRA is better for you than a traditional IRA, consider converting stock from an IRA to a Roth IRA while the market is down. While that will be a taxable transaction, you'll be trading taxes paid today for tax-free income in the future, with a potential for profit in a market recovery.
- 9) Consider prepaying eligible education expenses in 2011 since the \$4,000 above-the-line education deduction is scheduled to expire at the end of this year. ♦



Answers to your estate and gift tax questions

The estate tax rules were changed by the *2010 Tax Relief Act*, and these rules are scheduled to be in effect through 2012. You may have some questions about how these rules could affect you. Here are a few answers you might find helpful.

Q. Will my estate pay tax under current rules?

A. As before, the answer depends on the total amount of assets you own, adjusted for allowable deductions and certain gifts.

For 2011 and 2012, estates with a net fair market value of less than \$5 million will owe no federal estate tax, though a return may need to be filed.

Estates greater than \$5 million can be taxed at a maximum rate of 35%.

Q. How do the current rules affect married couples?

A. The \$5 million estate tax exemption is per person; thus a couple's exemption is \$10 million. Also notable in the law is the new portability of the unused portion of an individual's exemption. Under prior law, married couples frequently performed complex estate planning to take full advantage of both spouses' exemptions. Now the law allows a deceased spouse's estate to transfer any unused exemption amount to the surviving spouse without all the complex planning.

Q. Does the \$5 million exclusion apply to taxable lifetime gifts?

A. Yes. The \$5 million exclusion is also available for gifts – over and above the amount you can give tax-free each year.

The result: Up to \$5 million of assets, in any combination of gifts during your lifetime and bequests through your will and other planning documents, can be transferred to heirs during 2011 and 2012, free of federal estate and gift taxes. (If you're married, you can shelter up to \$10 million of assets.)

The exemption for “generation-skipping” transfers – gifts and bequests that skip a generation, such as those you make to grandchildren – is \$5 million as well.

Q. What's the effect of current rules on estates of those who died in 2010?

A. Estates of those who died in 2010 can choose to use the rules for 2011 and 2012, as described above. That is, you can opt to apply the \$5 million exclusion and the appropriate tax rate.

Alternatively, you can take advantage of the no-estate-tax rules that were in effect for 2010. Making this election means an estate is not taxed, no matter the value of the assets. Instead, beneficiaries generally inherit the same cost basis as the decedent and may have to pay more tax when they sell or dispose of the assets they inherit. There are exceptions to the general rule that allow a basis increase for some assets.

With either choice, filing an estate return or other forms may be required to establish the value of assets and take advantage of tax-saving elections.

Q. What estate planning techniques should I consider?

A. Strategies include making gifts to family members and/or charitable organizations. You can also set up and fund trusts to transfer future appreciation of your home and other assets.

Reviewing your will and existing trust documents, as well as life insurance policies and beneficiary designations for retirement accounts, is another smart move.

Whether you're safeguarding wealth or family security, it's wise to do some planning. Give us a call. We're here to answer your estate tax questions and help you create a plan to preserve the value of what's important to you. ♦

Should you borrow from your 401(k)?

If you need money, you may decide to borrow funds from your 401(k) account, assuming the plan permits it. However, be aware of these key requirements:

- ▶ The loan is exempt from federal income tax, plus the 10% tax penalty on early withdrawals, but it generally can't exceed the lesser of \$50,000 or 50% of the vested amount in your account. The loan proceeds are taxable if you default on the loan.
- ▶ Most plans require a minimum loan amount of \$500 or \$1,000 to discourage participants from using their 401(k) for minor cash needs.
- ▶ The loan must bear a "reasonable" rate of interest comparable to the rate that would be charged by other lenders.
- ▶ The loan must be adequately secured. You may use up to 50% of the account balance to secure a loan.
- ▶ The terms of the loan must require repayment within five years. Exception: A longer repayment period is allowed if the funds are used to acquire a principal residence.
- ▶ The loan is usually repaid in equal installments deducted from your paycheck. Once a loan is issued, you generally can't change the payment terms, but some plans allow you to pay off the loan early.

There are several pluses and minuses to a 401(k) loan. On the plus side, there's little paperwork to fill out, and you don't have to demonstrate a dire financial need. As opposed to a more traditional loan, you're effectively paying yourself back with interest.

On the minus side, you're eroding the nest egg you've set aside for retirement by foregoing investment opportunities on the borrowed funds. Depending on market conditions, the timing of withdrawals could create additional losses. Finally, the plan may charge certain fees for taking out a loan.

Bottom line: Investigate other options before you tap into your 401(k). For most retirement-savers, a 401(k) loan should be a last resort. ♦

financial alert

A survivor's guide: Dealing with the financial and tax issues

The death of a spouse is a stressful event. In addition to the emotional turmoil, the surviving spouse must deal with a number of financial and tax issues, some of them mundane and some quite complex. Here's a quick guide to help you through this difficult time.



- **Locate important documents.** These include wills, insurance policies, deeds, investment certificates, powers of attorney, birth and marriage certificates, bank statements, and vehicle titles. You'll need these documents to change beneficiaries, revise asset titles, and verify account balances.
- **Check survivor benefits.** Contact the Social Security Administration to learn about survivor benefits. Also call your spouse's former employer to find out about employee benefits, such as payouts of unpaid salary, unused vacation, and pensions.
- **Make decisions on life insurance.** Benefits may be paid in a lump sum or an annuity. If you take proceeds in a lump sum, you'll want to consider placing them in short-term, interest-paying investments to ensure that the money is readily available.

- **Hold off on major decisions.**

Now is not the time to relocate, overhaul your investment portfolio, or make luxury purchases. Think twice about paying off your mortgage. If at all possible, don't withdraw money from IRAs or 401(k) plans. Wait until you've had time to develop a long-term financial plan.

- **Get legal and financial advice.**

Seek out qualified and trusted professionals to help you through the process of probate, taxes, and planning for your financial future. All too often, the surviving spouse makes irrevocable financial decisions or unnecessary purchases in the days and weeks following a partner's death.

Unfortunately, widows and widowers are easy prey for con artists. Someone may call with a great deal on a "sure fire" investment, or attempt to capitalize on your grief by offering unnecessary goods or services. A trusted professional advisor can provide objectivity when such "opportunities" are presented. If you need assistance, give us a call. ♦

Thank You

for giving us the opportunity to serve you this past year. Your business is appreciated, and your referrals are welcome.

We wish you a happy holiday season and a prosperous 2012!



IRS asks for volunteers

The IRS is asking employers to step forward and admit to erring about the employment status of workers. The reward? A low-cost way to satisfy tax obligations and obtain future audit protection on the issue.

Under the new “Voluntary Worker Classification Settlement Program” (VWCSP), an employer that previously misclassified employees as independent contractors agrees to pay a minimal amount to settle its tax debt. To qualify, employers must have consistently treated the workers as non-employees and issued 1099s to them for the past three years. The employer also promises to treat these workers as employees in the future.

If an employer is accepted into the VWCSP, the maximum penalty equals 1.068% of the wages paid to the reclassified worker in the prior year.

This program is strictly voluntary, but the IRS has been turning up the heat on employment tax disputes in recent months.

IRS keys in on cell use

Previously, the *Small Business Jobs Act of 2010* eliminated strict substantiation requirements for business use of employer-provided cell phones. Now the IRS has issued new guidance on the tax treatment for employees.

The IRS explains that the value of cell phones, where use may be both business and personal, can be excluded from an employee’s income if there are substantial business reasons for the arrangement. Substantial reasons include requiring the employee to be available at all times for client contact or for work-related emergencies. ♦

This newsletter is issued quarterly to provide you with an informative summary of current business, financial, and tax planning news and opportunities. Do not apply this general information to your specific situation without additional details. Be aware that the tax laws contain varying effective dates and numerous limitations and exceptions that cannot be summarized easily. For details and guidance in applying the tax rules to your individual circumstances, please contact us.

■ January 17, 2012

Due date for the fourth installment of 2011 individual estimated tax.

■ January 31

Employers must furnish W-2 statements to employees. 1099 information statements must be furnished by payers. (Deadline for 1099B and consolidated statements is February 15.)

■ January 31

Employers must file 2011 federal unemployment tax returns and pay any tax due.

■ February 28

Payers must file information returns (such as 1099s) with the IRS.*

■ February 29

Employers must send W-2 copies to the Social Security Administration.*

■ March 1

Farmers and fishermen who did not make 2011 estimated tax payments must file 2011 tax returns and pay taxes in full. ♦

*April 2 if filing electronically.