Online Advisor – October 2010

Major Tax Deadlines
For October 2010

* October 1 - Generally, the deadline for self-employeds and small businesses to establish a SIMPLE retirement plan for 2010.

* October 15 - Deadline for filing 2009 individual tax returns on automatic extension of the April 15 filing deadline.

* October 15 - If you converted a regular IRA to a Roth IRA in 2009 and now want to switch back to a regular IRA, you have until October 15, 2010, to do so without penalty.

* October 15 - Extended deadline for 2007, 2008, and 2009 returns required of nonprofit organizations.

NOTE: Businesses are required to make federal tax deposits on dates determined by various factors that differ from business to business.

Payroll tax deposits: Employers generally must deposit Form 941 payroll taxes (income tax withheld from employees' pay and both the employer's and employees' share of social security taxes) on either a monthly or semiweekly deposit schedule. There are exceptions if you owe $100,000 or more on any day during a deposit period, if you owe $2,500 or less for the calendar quarter, or if your estimated annual liability is $1,000 or less.

* Monthly depositors are required to deposit payroll taxes accumulated within a calendar month by the fifteenth of the following month.

* Semiweekly depositors generally must deposit payroll taxes on Wednesdays or Fridays, depending on when wages are paid.

For more information on tax deadlines that apply to you or your business, contact our office.

What's New in Taxes

IRS increases correspondence audits

As part of its plans to increase audit coverage, the IRS will be doing more correspondence audits - notices mailed to taxpayers that typically focus on a single item on the tax return. Correspondence exams can be as simple as asking about a tax return data discrepancy or requesting a missing form. But the IRS is also using these audits to focus on other issues, such as employee business expenses, the earned income credit, charitable deductions, and the tax credit for buying a home.

If you receive an IRS notice, don't ignore it. Let your tax advisor know about it right away. The problem can be resolved in less time and with less fuss if an experienced professional is involved right from the beginning.

Gambling winnings and losses can affect your tax bill

From time to time, some of you are lucky enough to win a shilling or two at your local casino, the track, or your state lottery. How will that gambling income impact your taxes?

All gambling winnings are taxable. This is true for cash winnings and for the fair market value of any non-cash prizes you might win (e.g., a car, vacation, etc.). Depending on your other income and the amount of your winnings, your federal tax on such winnings can go as high as 35%. You don't receive any capital gains rate break for gambling winnings, nor is there any income averaging to help lower your tax bill.

However, you are entitled to a tax deduction for gambling losses. These are taken as an itemized deduction and your losses can't exceed your winnings. In other words, if you report no gambling income, you can't report gambling losses. When you gamble and lose, you must keep documentary evidence of your losses (canceled checks, credit card charges, losing tickets, ATM receipts, etc.). Many casinos keep track of your wins and losses for electronic games if you belong to their player clubs.

But gambling deductions might not be all that beneficial. You can't simply "net out" your winnings and losses. Instead you must report your entire winnings as income, and use your losses as itemized deductions. In many cases (especially for older taxpayers with little income other than social security benefits, and with very few itemized deductions), the losses might not be tax beneficial. If you take the standard deduction rather than itemizing deductions, you will receive no tax benefit whatsoever. However, the winnings could have a significant impact on your income and may cause you to pay additional taxes (such as making some of your social security benefits taxable when they otherwise wouldn't be).

New Business

Congress passes Small Business Act

Small businesses get some tax breaks in a new law just passed by Congress. The Small Business Jobs Act of 2010 extends 50% bonus depreciation for new equipment purchased during 2010. It increases for 2010 and 2011 the first-year expensing limit for new and used business equipment purchases to $500,000, and raises the phase-out limit on expensing to $2 million.

The law increases the deduction for business start-up expenses in 2010 from $5,000 to $10,000. The deduction phases out after expenditures exceed $60,000; that's up from the prior phase-out threshold of $50,000.

For 2010, self-employed taxpayers will be able to deduct the cost of their health insurance in computing self-employment taxes.

The new law also provides a $30 billion fund to encourage community banks to lend to small businesses.

If you drive for business, choose your deduction method wisely

You're entitled to deduct your automobile expenses attributable to business driving. However, the tax law has several twists and turns that affect what you can deduct.
For starters, you can't deduct the cost of commuting back and forth from work. This is a purely personal expense. But trips between your regular workplace and a client's business location count as business travel. In addition, you may deduct expenses for traveling between different branches of your business.

There are two basic ways to deduct business auto expenses: the actual expense method or the standard mileage method.

*** Actual expense method**

With this method, you deduct the actual costs of using your automobile for business travel. This includes expenses such as oil and gas, insurance, repairs, license and registration fees, etc.

Significantly, you're also entitled to an annual depreciation deduction, although this amount may be limited by the "luxury car" rules.

For instance, if you place a car in service in 2010, the maximum first-year depreciation you can claim is $11,060 no matter what the car costs. (This amount includes $8,000 of bonus depreciation provided in the recent Small Business Jobs Act.) If you lease the car, you can deduct the lease payments instead, subject to limits under IRS tables.

If you also use your vehicle for personal driving, you must divide your expenses between business and personal use, based on the mileage.

Example: You drive your car 15,000 business miles and 5,000 personal miles in 2010. Thus, 75% of your mileage (15,000 business miles divided by 20,000 total miles) is business-related. So you can deduct 75% of your actual expenses.

A drawback to the actual expense method is that you must account for all of your expenses in addition to keeping records of each business trip.

*** Standard mileage method**

With this method, you multiply the annual flat rate prescribed by the IRS by the number of business miles you drive, and add on any business-related parking fees, taxes, tolls, and interest expense on your car loan. (Interest expense is not deductible by employees.) All other costs, including depreciation, are built into the flat rate. The rate for 2010 is 50¢ per mile.

Example: Suppose again you travel 15,000 business miles this year. Under the standard mileage rate, you may deduct $7,500 (50¢ x 15,000), regardless of your personal use of the car.

Although the standard mileage rate is generally more convenient than the actual expense method, you still must record the date, mileage, business location, names and relationships of clients, and the business purpose for each trip. It is recommended that you keep a contemporaneous diary for both methods.

The rules governing business car deductions are full of exceptions and limitations. For guidance in choosing the method that's right for you, give us a call.

What's New in Finances

New law raises insurance coverage on bank accounts

For years, bank accounts were FDIC-insured up to $100,000. Then during the recent financial crisis, the insurance limit was increased to $250,000. But this increase was only temporary; it was scheduled to drop back to $100,000 in 2014.

The good news is that the financial reform law just signed permanently sets the FDIC insurance limit at $250,000 per depositor, per bank. The $250,000 coverage applies for each of four categories of ownership: individual, joint, retirement, and trust accounts.

Keep score of your finances with a personal balance sheet

The recent economic downturn hit Americans' net worth hard. "Net worth" is the value of assets (such as homes, bank accounts, and investments) minus debts (such as mortgages, loans, and credit cards). According to the Federal Reserve, Americans' net worth hit a low of $48.3 trillion during the recent recession, but has since risen 13% to about $55 trillion.
Do you know your current net worth? Do you know how much your net worth is changing from year to year?

We all want to enter retirement with a comfortable nest egg, owning more than we owe. A good way to chart your progress toward that goal is to prepare a personal balance sheet at least every year. That will give you a score card to measure how you're doing. A balance sheet shows your assets and your liabilities. Think of them as what you own and what you owe. The difference between them is your net worth.

Here's a quick guide.

* Pick a date such as the end of the year or the end of a quarter when you'll have statements available for your financial accounts.

* Start by listing all your financial assets. Include bank accounts, balances in IRAs and retirement plans, stock and bond investments, etc.

* The next step is the least precise. You must assign a value to your nonfinancial assets, such as house, car, and personal belongings. Don't get hung up at this stage.

For most purposes, it's not essential that you find an exact value. Using the same approach from year to year is more important.

* To value your house, look at classified ads for comparable properties, or talk to a friendly real estate agent. Another approach is to use the assessed value shown on your property tax statement. This is generally less than market value, but yearly changes should reflect changes in the local property market.

* For personal property, just make a reasonable estimate. Hold that constant each year unless you make any major purchases.

* Liabilities are next. List your mortgage balance and all loans. Include credit card debt, car and boat loans, student loans, and any other debt.

* Total up your assets and liabilities. The difference between the two totals is an estimate of your net worth. Hopefully it shows an increase from the previous year.

If your net worth is not increasing, use your balance sheet to see where you're falling short. Look for ways to boost the growth of your assets, or set a budget to reduce your liabilities. Your personal balance sheet is more than just a good financial score card. It can be a valuable planning tool, too.

Take a Break

The Entitlement Dilemma: Some interesting numbers
* According to the Census Bureau, nearly half of Americans live in a household in which someone receives government benefits.

* 45% of U.S. households pay no income tax, up from 39% five years ago. Half of those don't earn enough to pay income tax, and the rest use credits and deductions that eliminate their tax liability. Most of these households still pay social security and Medicare payroll taxes.

* 13% of all U.S. households pay neither income tax nor payroll taxes.

* An estimated 47.4 million people are covered by Medicare today. Projections indicate that by 2030, that number will grow to 80.4 million.

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