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Current and Past Issues of Tax News are available at  
[www.4-serenity.com/news.htm](http://www.4-serenity.com/news.htm).

**Office meetings are by appointment only.**

### Near-Term Calendar

- January 31<sup>st</sup> – Due date for 4th Quarter Payroll Tax Returns, W-2's and 1099's. [Accounting information must be received by January 10<sup>th</sup>].
- February 15<sup>th</sup> – Due date for business license renewal and business personal property tax returns in some counties.
- March 15<sup>th</sup> – Due Date for Corporation and S-Corporation Tax Returns or Extensions.
- April 1<sup>st</sup> – Due date for Annual Registration with the Georgia Secretary of State. Note: The fee has increased to \$50 per year.
- April 15<sup>th</sup> – Due date for Individual and Partnership Tax Returns or Extensions.
- May 2<sup>nd</sup> – Due date for 2nd Quarter Payroll Tax Returns. [Accounting information must be received by April 15<sup>th</sup>]
- May 15<sup>th</sup> – Due date for Non-Profit Tax Returns or Extensions.

### Administration

Denise Meanor has been my assistant since February of 2010. If I am unavailable, please speak to Denise, and if you leave a message, please be specific regarding the reason for your call.

### Dependents and Divorce

*Who gets to claim the children?*

In general, if you want to claim your child as a dependent, you must be the custodial parent (i.e., the parent with whom the child lived for the greater number of nights during the year). If you are the noncustodial parent, the custodial parent must sign a written declaration that he or she will not claim your child as a dependent, and you must attach this written declaration to your tax return.

Make sure you have the proper written declaration, or the IRS will deny your dependency exemption. To release the dependency exemption, the custodial parent may use either Form 8332, Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent, or a similar statement containing the same information as the form.

If you have a divorce decree or separation agreement that went into effect after 1984 and before 2009, you may be able to attach certain pages from the decree or agreement in place of Form 8332. The decree or agreement must state all three of the following:

- The noncustodial parent can claim the child without regard to any condition, such as payment of support.
- The custodial parent will not claim the child as a dependent for the year.
- The years for which the noncustodial parent can claim the child as a dependent.

The option to attach pages from the decree or agreement is no longer available to noncustodial parents whose divorce or separation went into effect after 2008. These individuals must attach Form 8332 or a similar statement that was executed for the sole purpose of releasing the dependency exemption.

### First-Time Homebuyer Credit

*Benefit still available for certain members of the military*

In general, the first-time homebuyer credit is no longer allowed for homes purchased after April 30, 2010 (September 30, 2010, if you entered into a written binding contract before May 1, 2010). However, if you or your spouse were on qualified official extended duty outside of the United States for at least 90 days after 2008 and before May 1, 2010, you have an extra year to buy a home and claim the credit. In other words, you must buy the home before May 1, 2011 (before October 1, 2011, if you enter into a written binding contract before May 1, 2011).

### Giving Gifts

*What's taxable?*

## Quick Tax Tips

When you give cash or property to an individual, the gift is not taxable to that individual. However, if you give away too much, you may have to report the gift and pay gift tax.

The IRS allows you to give each individual up to \$13,000 during the year without requiring you to report the gift or file a gift tax return. In addition, certain gifts do not count toward the \$13,000 annual exclusion, such as amounts paid directly to qualifying educational institutions for tuition or medical expenses (including health insurance) paid directly to the person or the medical organization.

If you give more than \$13,000 to one individual during the year, you must file a gift tax return to report the taxable gift. Your gift will be taxable to the extent the amount given exceeds \$13,000. However, you can give up to \$1 million in taxable gifts during your lifetime before you are required to pay any gift tax.

### **Coverdell Education Savings Account (ESA)**

*Time to roll it over into a 529 plan?*

Section 529 plans may only be used to pay for qualified higher education (post-secondary) expenses. On the other hand, Coverdell ESAs may be used to pay for qualified higher education expenses or qualified elementary and secondary education expenses (K-12). However, unless a new law extends this provision, Coverdell ESAs can no longer be used for K-12 expenses after 2010.

After 2010, it may be wise to roll your Coverdell ESA into a 529 plan. A distribution from a Coverdell ESA that is used for qualified education expenses is nontaxable. A contribution to a 529 plan is considered a qualified education expense if the contribution is on behalf of the designated beneficiary of the Coverdell ESA. In general, the distribution must be "rolled over" by December 31 of the same year.

Ultimately, you can contribute more to a 529 plan. The annual contribution limit for Coverdell ESAs is currently \$2,000/year. After 2010, this limit is set to drop to \$500/year. On the other hand, 529 plans have no annual contribution limits.\* In addition, you can often deduct contributions to 529 plans on your state income tax return. Also, it is generally easier to change beneficiaries for 529 plans, and funds in Coverdell ESAs must be spent by the time the beneficiary turns 30 or the earnings become taxable and subject to a 10-percent penalty.

\* Contributions over \$13,000 require a gift tax return to report the taxable gift.

1. If you want to get reimbursed from a health flexible spending arrangement (FSA) or a health reimbursement arrangement (HRA) for over-the-counter drugs, you must do so on or before December 31, 2010. After 2010, you can only get reimbursed for prescription drugs and insulin.
2. Don't forget to take your required minimum distribution (RMD) for 2010. RMDs were waived for 2009 only.
3. The 0-percent capital gains rate is set to expire at the end of 2010. If you are in the 10- or 15-percent income tax brackets, consider selling capital assets that have been held more than a year and have substantially increased in value. After 2010, the long-term capital gains rates will be 10 percent and 20 percent (8 percent and 18 percent for assets held over five years).
4. In 2010, the adjusted gross income (AGI) limit on Roth conversions is gone. However, a modified AGI limit continues to apply to regular Roth IRA contributions. To avoid this, you can make contributions to a nondeductible traditional IRA and convert them to a Roth IRA in the following year (only paying tax on any earnings).
5. In the past, if you thought you would be eligible for the earned income credit (EIC) and you had at least one qualifying child, you could choose to get advanced EIC payments with your pay by completing Form W-5, Earned Income Credit Advance Payment Certificate, and giving it to your employer. Starting in 2011, the advanced earned income tax credit will be eliminated.

### **Nonbusiness Energy Credit**

*Qualifying home improvements must be made in 2010*

If you want to make energy-efficient home improvements to your principal residence and qualify for a nonbusiness energy credit, you have until December 31, 2010.

The credit equals 30 percent of the amount paid for:

- Qualified energy efficiency improvements (i.e., insulation, windows, doors, etc.); and
- Residential energy property costs (i.e., central air conditioners, natural gas furnaces, tankless water heaters, biomass fuel stoves, etc.).

For purposes of this credit, costs are treated as paid when the original installation of the item is completed. Thus, you cannot simply purchase the item before year-end; it must be installed on or before December 31, 2010, to qualify for the credit.

The credit is limited to a total of \$1,500 for tax years 2009 and 2010. Thus, if you already claimed a \$1,500 credit in 2009, you are not eligible for a credit in 2010.

## **Deductible IRAs**

*Reduce your taxable income while saving for retirement*

If you are employed and an active participant in an employer sponsored retirement plan [i.e., §401(k), SEP, or SIMPLE IRA], you can still make a contribution to a traditional IRA. You can contribute up to \$5,000 (\$6,000 if 50 or older), but not more than your compensation for the year. If you file a joint return, your spouse can also make an IRA contribution based on your compensation (even if he or she has little or no compensation).

Whether or not the contribution is deductible depends on your filing status and your modified adjusted gross income (MAGI). If you are single and your MAGI is more than \$66,000, you cannot deduct your contribution. If you are married filing jointly and your MAGI is more than \$109,000, you cannot deduct the contribution made for yourself. However, if your spouse is not covered by an employer sponsored retirement plan and your MAGI is less than \$177,000, part or all of your spouse's IRA contribution may be deducted.

Contributions for the year must be made by the unextended due date of your return. Thus, contributions for 2010 must be made by April 15, 2011. You can even file your return and claim an IRA deduction before the actual IRA contribution has been made as long as it is made on or before April 15, 2011.

## **2010 Roth Conversions**

*Any distributions before 2012 may need to be included in income*

If you did a Roth conversion in 2010, the conversion income is generally spread over two years (unless you elect out of the two-year period). Half of the income is reported in 2011 and the other half is reported in 2012. However, be careful if you take any distributions from the Roth IRA in 2010 or 2011, because the conversion income may be accelerated or included in income sooner.

Distributions from a Roth IRA are treated as having been distributed in the following order:

- Regular contributions to the Roth IRA and rollover contributions from other Roth IRAs and designated Roth accounts.
- Qualified rollover contributions from accounts other than Roth IRAs or designated Roth accounts.
- The remaining nontaxable portion of the qualified rollover contribution.
- Earnings on contributions.

If your Roth IRA has no regular contributions and only consists of amounts converted in 2010 plus earnings, any distributions before 2012 would be attributable to the conversion income and would have to be included in income in the year distributed.

## **IRA Rollovers**

*Be mindful of the one-year waiting period*

If you don't like how your IRA is being managed, you can transfer it to another IRA with a different trustee. To make this a nontaxable transfer, you can either do a direct trustee-to-trustee transfer, or you can receive a distribution and roll it over within 60 days.

You can do an unlimited amount of trustee-to-trustee transfers during the year. However, there is a one-year waiting period between rollovers from one IRA into another. This means that no further rollovers can be made in the same year from either (1) the IRA from which the rollover was made; or (2) the IRA into which the rollover was made. Watch out! If another rollover has been made during this one-year period, the second IRA distribution is subject to tax, and may also be subject to the 10-percent early distribution penalty and the 6-percent excess contribution tax.

## **Business Taxes**

### **New Credit Available in 2011**

*Hiring in 2010 could pay off*

The HIRE Act of 2010 provides incentives to employers who are contemplating adding staff to their workforce. If a business hires a qualified employee and retains that employee for 52 consecutive weeks, the business will be entitled to a general business credit of up to \$1,000 per qualified employee.

Qualified employees must meet the following requirements:

- The employee must have been hired after February 3, 2010, and before January 1, 2011.

- The employee must certify on Form W-11 that he/she has not been employed for more than 40 hours in the last 60 days.
- The employee is not a replacement for another employee unless that other employee voluntarily separated from employment or was terminated for just cause.
- The individual is not related to the employer, including family and in-laws.

To be considered "retained," the employee must be employed by the employer for 52 consecutive weeks, and wages paid to that employee for the last 26 weeks of the period must be at least 80 percent of the wages paid during the first 26 weeks of the period. The credit is equal to 6.2 percent of the wages paid during the 52-week period, with a maximum of \$1,000.

If the employee is paid more than \$16,129.03, the employer will receive the full \$1,000 credit. The earliest the employee would meet the requirements for this credit would be February 4, 2011, so keeping good records of all wages earned and hours worked is very important.

## **Health Care Credit Available to Small Businesses**

*Complex rules may provide up to a 35 percent credit for premiums paid*

Currently, one of the largest costs for small businesses is health insurance. Whether the insurance is offered in full or the employee pays for a portion, the cost is continually increasing. This deters many small businesses from offering health insurance.

In an effort to assist employers with this ever increasing cost, the IRS is allowing a credit of up to 35 percent of the premiums paid by eligible small businesses (25 percent for tax-exempt employers) beginning in 2010. Several terms must be defined to determine if the credit is available for your business.

**Eligible Small Employer (ESE).** An eligible small employer has no more than 25 full-time equivalent employees (FTE) for the tax year. The average annual wages must be less than \$50,000. Eligible small businesses must pay at least 50 percent of the premium for those employees enrolled in the health insurance plan.

**Full-time Equivalent Employees (FTE).** FTEs are determined by dividing the total hours of service worked by employees by 2,080. This number is rounded down to the nearest whole number (i.e., 14.9 would be 14 FTEs).

If an individual employee works more than 2,080 hours in the year, the hours in excess are not included in the calculation. The hours worked by seasonal workers (employees who work less than 120 days during the tax year) are not included in the calculation. Leased employee hours are included.

Certain employees are specifically excluded from the FTE definition. Sole proprietors, partners, and 2-percent shareholders in an S corporation are excluded. Employees considered 5-percent owners under the key-employee provisions for retirement plans are also excluded. Family members of the self-employed business owner are not considered FTEs, regardless of whether they have a valid employee relationship.

**Average Annual Wages.** Average annual wages are the total wages paid by the ESE to its FTEs for the year divided by the number of FTEs. The wages paid to individuals excluded from the definition of FTEs are not included in the wages number. For example, if a sole proprietor pays his spouse \$50,000 in total wages for the year, those wages are excluded from the total wages paid to FTEs for the year.

The average annual wages determined by the formula are rounded down to the nearest \$1,000. So, if the average annual wages are \$26,789 under the calculation, the average annual wages for purposes of the credit would equal \$26,000.

**Phase-out.** The credit is phased out based on both the number of FTEs and the average annual wages. If there are more than 10 but fewer than 25 FTEs, the credit is phased out. If the employer pays average annual wages in excess of \$25,000, but less than \$50,000, the credit is phased out. In other words, if the employer has fewer than 10 FTEs and pays less than \$25,000 in average annual wages, the full credit is available. If the employer has either 25 or more FTEs or pays more than \$50,000 in average annual wages, no credit is available.

The health care credit will be part of the non-refundable general business credits. However, tax-exempt employers are allowed a refund of the credit up to the amount of payroll taxes withheld from the employees.

## **Tanning Excise Tax Now in Effect**

*Don't get burned for failing to submit Form 720*

The 2010 Health Care Act imposes a new tax on indoor tanning services. The tax is imposed on the person receiving the service, and the service provider is required to submit the tax to the IRS.

The tax is equal to 10 percent of the amount paid for the service. The tax is submitted quarterly by the service

provider using Form 720, Quarterly Federal Excise Tax Return.

The tax does not apply to spray-on tanning, phototherapy performed by licensed medical professionals in their offices, or to separately identifiable goods and services provided with the tanning service. Bundled services that include tanning must be split using any reasonable method to determine the amount subject to the excise tax.

Failure to submit Form 720 and pay the tax due can lead to penalties and interest. The form and tax are due on the last day of the month after the end of the calendar quarter (April 30, July 31, October 31, and January 31).

### Quick Tax Tips

1. The standard mileage rate for business travel in 2010 is 50¢ per mile. The 2011 rate has yet to be announced.
2. The maximum amount of wages subject to social security tax is \$106,800 in 2010. There is no limit on wages subject to Medicare tax. The cap for 2011 has yet to be announced.
3. Beginning in 2011, employers will be required to report the cost of employer-provided health insurance coverage on the employee's W-2 as an information item.
4. For tax years beginning in 2010, the failure-to-file penalty for S corporation returns has increased to \$195 per shareholder, per month. The failure-to-file penalty for partnership returns has increased to \$195 per partner, per month.
5. The depreciation limit for an automobile used in business and placed in service in 2010 is \$3,060.
6. The 50-percent bonus depreciation has been extended to qualified assets placed in service before January 1, 2011.
7. Under the Small Business Jobs Act of 2010, businesses are allowed to deduct up to \$10,000 of start-up costs if business begins in 2010. The deduction is phased out for expenses in excess of \$60,000.
8. For 2010 only, self-employed health insurance premiums can be used to reduce net earnings from self-employment for purposes of calculating the self-employment tax.

9. Under the Small Business Jobs Act of 2010, the 2010 depreciation limit for automobiles (\$3,060) and light trucks (\$3,160) that are "qualified property" under the bonus depreciation rules is increased by \$8,000.
10. Cellular phones have been removed from the "listed property" category of assets beginning in 2010, providing more favorable depreciation rules and reduced substantiation of the expense.

### New Rules for §179 Expensing in 2010 and 2011

*Amounts, eligible property and the revocation have been extended*

The Small Business Jobs Act of 2010 included many changes to the §179 expensing rules. The new rules are effective for tax years beginning in 2010 and 2011. First, the maximum amount of §179 has been increased from \$250,000 to \$500,000. The expense amount begins to phase out when property placed into service exceeds \$2,000,000.

The new law has expanded the definition of §179 property to include qualified real property. Qualified real property is qualified leasehold improvements, qualified restaurant property and qualified retail improvement property. Businesses can take up to \$250,000 of §179 expense on these assets. The amount of §179 taken on the qualified real property reduces the \$500,000 maximum that can be used on other eligible property.

Finally, the new law has extended the time period under which a business can revoke the §179 election. Using an amended return, businesses can now revoke the §179 expense on assets placed in service before 2012.

### Simple Cafeteria Plans Escape Non-discrimination

*New safe harbor may make it easier to provide medical assistance to employees*

Employers are allowed to offer many nontaxable benefits to their employees under a cafeteria plan. The benefits provided under the plan are not included in the employee's gross wages, and the employer is not required to pay FICA, Medicare, or unemployment tax on the benefits. However, the strict non-discrimination rules cause problems when highly compensated employees and key employees are participants.

The 2010 Health Care Act has provided a solution called a "simple cafeteria plan" to help employers solve the non-discrimination issues. The law provides a safe harbor under the cafeteria plan rules as well as for specified benefits provided under a cafeteria plan

including group term life insurance, self-insured medical expense reimbursement plans, and dependent care assistance for tax years beginning after December 31, 2010.

Eligible employers, those with an average of fewer than 100 employees on business days during either of the two preceding years, will meet the discrimination test if they meet three requirements. These requirements are establishing the plan, making prescribed contributions, and meeting the eligibility and participation requirements of the particular plan.

The employer is required to contribute a specific amount on behalf of each qualified employee. This amount can be calculated under two methods. The first method is calculated using a uniform percentage of the employee's annual compensation (not less than 2 percent). The second method is calculated by comparing 6 percent of the employee's compensation for the year to twice the amount of the employee's salary reduction contributions. The lesser of the two is the amount the employer is required to contribute.

Each employee who worked at least 1,000 hours is eligible to participate. The employer can exclude employees under age 21, employees with less than one year of service, those under a collective bargaining agreement, and non-resident aliens working outside the U.S.

## 1099 Reporting

### *Expanded reporting starts in 2012*

Businesses that pay another non-employee taxpayer more than \$600 total in any tax year are required to furnish that taxpayer with a Form 1099. These amounts include compensation for services rendered, interest, rents, royalties, and other fixed or determinable income.

For tax years beginning in 2012, the business is going to be required to add gross proceeds and amounts in consideration for property to the list of reportable items.

For example, if the business purchased an asset from another business for more than \$600, the business would need to issue the seller a Form 1099 listing the gross amount paid for the asset.

Businesses will also be required to issue a Form 1099 to an expanded list of taxpayers. Corporations are exempt from receiving Form 1099 until 2012, but for that year and for future years, corporations are going to receive them if they are paid more than \$600 for any of the previously mentioned items.

So, for 2010, if a business paid \$1,000 rent to a corporation, it would not be required to issue the

corporation a Form 1099. However, if it pays that same rent in 2012, it will be required to provide a Form 1099 to the corporation.

## Using EFTPS for Making Tax Deposits

### *Treasury Department to stop accepting deposit coupons*

Many businesses currently use Form 8109, Federal Tax Deposit Coupon, to deposit their payroll tax withholdings and estimated tax payments. The IRS has proposed regulations that will require those businesses making deposits to use the Electronic Federal Tax Payment System (EFTPS) in lieu of the coupons.

After December 31, 2010, the Treasury Department will no longer accept deposit coupons. However, some small businesses may be able to simply pay the tax due with the return itself. For example, businesses with less than \$2,500 in quarterly payroll tax withholding can make their payment with Form 941, Employer's Quarterly Federal Tax Return. Businesses allowed to file Form 944, Employer's Annual Federal Tax Return, are allowed to pay the tax with the form if the liability is less than \$1,000.

Enrolling in the EFTPS program is easy, and can be more convenient. The system allows employers and other depositors to have the funds directly taken from their checking account, and payments can be set up 120 days prior to the due date.

Please stay tuned to our website for updates throughout the year at <http://www.4-serenity.com>.

*Happy Holidays,*

*Larry Walker, Jr., EA, CFS*

