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Client Update

FALL 2014

in this

tax

SEPTEMBER 15 – Due date for individuals to pay third quarter installment of 2014 estimated tax.

SEPTEMBER 15 – Deadline for filing extended 2013 tax returns for calendar-year corporations.

SEPTEMBER 15 – Deadline for filing extended 2013 partnership and limited liability company returns.

OCTOBER 1 – Deadline for businesses to adopt a SIMPLE retirement plan for 2014.

OCTOBER 15 – Filing deadline for extended 2013 individual tax returns.

OCTOBER 15 – If you converted a regular IRA to a Roth IRA in 2013 and now want to switch back to a regular IRA, you have until this date to do so without penalty.

DURING NOVEMBER – Estimate your 2014 income tax liability and review your options for minimizing your 2014 taxes. Call us to schedule a tax planning review. ■

IRS issues strong warning about bogus e-mails and phone calls

When agents from the Internal Revenue Service call, you shouldn't ignore them. Right? After all, they have the power to assess hundreds or thousands of dollars in unpaid taxes, interest, and penalties. The IRS may even garnish your wages. If you're a recent immigrant, they may send you packing.

It's true, of course, that the IRS has authority to require U.S. taxpayers to comply with the law. But fear of that agency's powers sometimes causes otherwise rational people to commit foolish mistakes, such as providing strangers with confidential information or wiring them money. Fear is a powerful motivator, and crooks posing as IRS agents have used that fear to their advantage.

All bogus schemes have the same objective in mind

Whether initiated by sophisticated overseas operators or homegrown con artists, all bogus IRS schemes have a similar objective in mind: to steal your identity and gain access to your accounts. Phony IRS agents often use common American names and fake badge numbers. To enhance legitimacy, they may provide limited personal information about you, such as the last four digits of your social security number or birth date. Others may manipulate caller ID to show that the call originated from Washington, D.C. If you reply to a call-back number, an answering machine may announce that you've reached the criminal investigation division of the IRS. A fraudster may even become aggressive and threaten jail time if you don't comply with his demands, then hang up and direct a co-conspirator to call back in the guise of a local policeman.

Some employ a different tactic, offering a carrot instead of a stick. You may be told that the IRS owes you some money. But to get your proffered refund you'll need to disclose bank account numbers and other personal information.

Crooks have used e-mail and other forms of electronic communication as well to perpetrate the scam. The text may include links to sham websites designed to mimic official sites, encouraging you to fill in forms with confidential data such as bank account numbers and passwords. E-mail attachments may contain malicious code designed to infect your computer or allow unauthorized access to your financial information.

How can you tell whether the IRS is really contacting you?

The agency's official website (www.irs.gov) makes it quite clear: The IRS "does not initiate contact with taxpayers by e-mail to request

(continued on page 2)

IRS

IRS urges record backup

With the frequent occurrence of natural disasters, the IRS has issued a reminder to taxpayers to safeguard their records with a document backup plan. Backup records should be stored away from the original set. The IRS News Release suggests scanning original records and storing them in the cloud or on storage devices. Individuals should consider taking photos of their home's contents, especially high-value items, to use for insurance or casualty loss claims.

IRS announces vehicle deduction limits

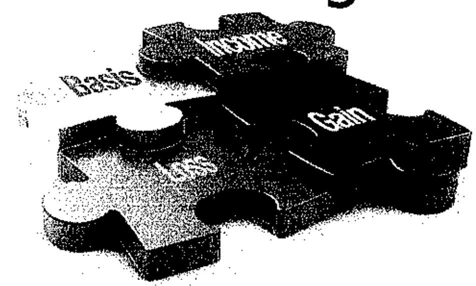
The depreciation limits for business vehicles first placed in service this year have been announced by the IRS. The first-year depreciation for business cars is limited to $3,160. Limits are $5,100 for year two, $3,050 for year three, and $1,875 for each year thereafter. For light trucks and vans, the 2014 first-year depreciation limit is $3,460. Limits are $5,500 for year two, $3,350 for year three, and $1,975 for later years.

Employer survey conducted by IRS

This fall the IRS will be sending a survey to 10,000 employers to collect information on tax compliance issues. The survey will ask employers about the time, money, and other resources they spend in dealing with compliance requirements, such as income tax withholding, processing Forms W-2, and filing taxes. The IRS says it will use the data collected to reduce employer compliance burdens. The survey is voluntary; employers who receive a survey and choose not to respond will not be penalized. ▮

AVOID **YEAR-END** SURPRISES

Know the tax effects of investing in mutual funds



Mutual funds offer an efficient means of combining investment diversification with professional management. Their income tax effects can be complex, however, and poorly timed purchases or sales can create unpleasant year-end surprises.

Mutual fund investors (excluding qualifying retirement plans) are taxed based on activities within each fund. If a fund investment generates taxable income or the fund sells one of its investments, the income or gain must be passed through to the shareholders. The taxable event occurs on the date the proceeds are distributed to the shareholders, who then owe tax on their individual allocations.

If you buy mutual fund shares toward the end of the year, your cost may include the value of undistributed earnings that have previously accrued within the fund. If the fund then distributes those earnings at year-end, you'll pay tax on your share even though you paid for the built-up earnings when you bought the shares and thus realized no profit. Additionally, if the fund sold investments during the year at a profit, you'll be taxed on your share of its year-end distribution of the gain, even if you didn't own the fund at the time the investments were sold.

Therefore, if you're considering buying a mutual fund late in the year, ask if it's going to make a large year-end distribution, and if so, buy after the distribution is completed. Conversely, if you're selling appreciated shares that you've held for over a year, do so before a scheduled distribution, to ensure that your entire profit will be treated as long-term capital gain.

Most mutual fund earnings are taxable (unless earned within a retirement account) even if you automatically reinvest them. Funds must report their annual distributions on Forms 1099, which also indicate the nature of the distributions (interest, capital gains, etc.) so you can determine the proper tax treatment.

Outside the funds, shareholders generate capital gains or losses whenever they sell their shares. The gains or losses are computed by subtracting selling expenses and the "basis" of the shares (generally purchase costs) from the selling price. Determining the basis requires keeping records of each purchase of fund shares, including purchases made by reinvestments of fund earnings. Although mutual funds are now required to track and report shareholders' cost basis, that requirement only applies to funds acquired after 2011.

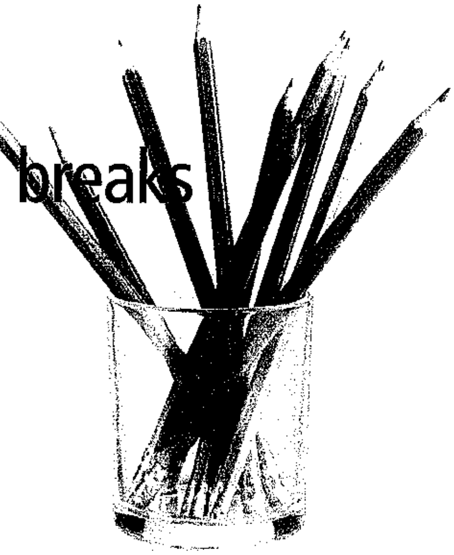
If you're considering buying or selling mutual funds and would like to learn more about the tax issues, give us a call. ▮

IRS ISSUES STRONG WARNING *(continued from page 1)*

personal or financial information. This includes any type of electronic communication, such as text messages and social media channels." The IRS website further states that the agency "will always send taxpayers a written notification of any tax due via the U.S. mail." IRS agents will never ask for credit card, debit card, or prepaid card information over the telephone. Nor will they ask for PINs, passwords, or other confidential access information.

If you think you might actually owe taxes, call the IRS directly. If you receive a call that appears bogus, ask for a call back number and employee badge number. Then report the details to the Treasury Inspector General for Tax Administration and the Federal Trade Commission (FTC) using their "FTC Complaint Assistant" at FTC.gov. ▮

Self-employment gives you some tax breaks



When it comes to taxes, being self-employed has some advantages. Whether you work for yourself on a full-time basis or just do a little moonlighting on the side, the government has provided you with a variety of attractive tax breaks.

■ **Save for retirement.** When you're self-employed, you're allowed to set up a retirement plan for your business. Remember, contributing to a retirement plan is one of the best tax shelters available to you during your working years.

Take a look at the SIMPLE IRA, SEP IRA, or Solo 401(k), and determine which plan works best for you.

■ **Hire your kids.** If your business is unincorporated, employing your child under the age of 18 might make sense. That's because your child's earnings are exempt from social security, Medicare, and federal unemployment taxes. This year, your son or daughter can earn as much as $6,200 and owe no income taxes. You get to deduct the wages paid as a business expense.

■ **Deduct health insurance.** Are you paying your own medical or dental insurance? How about long-term care insurance? As a self-employed individual, you may be able to deduct 100% of the cost of these premiums as an "above the line" deduction, subject to certain restrictions.

■ **Take business-use deductions.** Self-employed individuals can also deduct "mixed-use" items directly against their business income. Use your car for business and you can deduct 56¢ per business mile driven. The business-use portion of your computer purchases, Internet access, and wireless phone bills is also allowable. And if you meet the strict requirements, claiming the home office deduction makes a portion of your home expenses tax-deductible.

Please give us a call to find out more about the tax breaks available to self-employed individuals. ▮

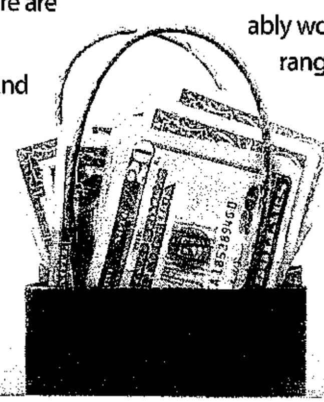
Setting Your Salary: *What's the right amount for a small business owner?*

One of the greatest perks of owning a small business is flexibility. You can set your own hours and salary. You can plot the firm's trajectory without consulting your boss, upper management, or even corporate policy. But that same flexibility may become a curse if handled unwisely. A small business owner without discipline and a well-thought-out strategy may fall into serious financial trouble. Employees in larger firms often rely on the human resources department to establish pay scales, retirement plans, and health insurance policies. In a small company, all those choices – and many more – fall to the owner, including decisions about personal compensation.

While there's not a one-size-fits-all formula for determining how much to pay yourself as a business owner, here are three factors to consider:

▸ **Personal expenses.** Tracking your business and personal expenses separately makes it easier to track the firm's cash flow, and lets you know how much salary you can realistically draw without hurting profitability.

Start with your household budget, then determine how much you're willing to draw from personal savings to keep your household afloat as the company grows. For a start-up company, owner compensation may be minimal. Beware, however, of going too long without paying yourself a reasonable salary. Be sure to document that you're in business to make a profit; otherwise the IRS may view your perpetually unprofitable business as a hobby – a sham enterprise aimed at avoiding taxes.



▸ **The market.** If you were working for someone else, what would they pay for your skills and knowledge? Start by answering that question; then discuss salary levels with small business groups and colleagues in your geographic area and industry. Check out the Department of Labor and Small Business Administration websites. In the early stages of your business, you probably won't draw a salary that's commensurate with the higher range of salaries, but at least you'll learn what's reasonable.

▸ **Affordability.** Review and continually update your firm's cash flow projections to determine the salary level you can reasonably sustain while keeping the business profitable. As the company grows, that level can be adjusted upward.

For assistance with this issue or other business concerns, contact our office. ▮

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Analyze your breakeven point to make better business choices

Breakeven analysis is an important and useful tool in business. Whether starting a new business, expanding current operations, contemplating an acquisition, downsizing, or approaching banks and other potential lenders, one should know what the breakeven is.

Breakeven is simply the point at which costs equal income – no profit, no loss. It's an excellent starting point for finding out where the business is and where it can go. It's the first step in planning future growth. It shows how much sales volume is needed to cover fixed and variable expenses. Once a company has reached breakeven, all gross profit beyond that point goes directly to improving the bottom line.

There are certain limitations for the use of breakeven analysis. It ignores the importance of cash flow and makes the assumption that fixed and variable expenses will stay within the parameters used to calculate the breakeven. Sound business assessment will overcome these shortcomings.

■ Calculating breakeven

Breakeven is relatively easy to understand and use. First, review the annual financial statement in order to figure out fixed and variable expenses. Fixed expenses are those that don't generally vary in relation to sales volume. Rent, for example, usually stays constant, whether sales are $400,000 or $500,000. The same is generally true for depreciation, utilities, insurance, and so on.

Variable expenses are the cost of goods sold and other costs of sales, such as direct labor and sales commissions.

There are, of course, some costs that are, or seem to be, part fixed and part variable. One must use good business judgment to split these items into reasonable proportions.

Knowing selling price and variable costs allows you to compute gross profit percentage. The rest is pure arithmetic. Divide your fixed costs by your gross profit percentage to arrive at breakeven. For example, if you have fixed costs of $10,000 and your gross profit percentage is 25%, your breakeven point is sales of $40,000 ($10,000 ÷ 25% = $40,000).

Call us; we would be happy to assist you with calculating your business's breakeven point and evaluating your profit structure. ■

NOTE: 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.