



Client advisor

CURRENT INFORMATION, NEWS AND TRENDS

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Health Care Bill & Taxes: What You Need to Know

The following overview of the tax-related provisions of the new Health Care Legislation will affect virtually every individual and most businesses in one way or another and will significantly impact tax returns in the future. See how these changes will impact you and your finances and be prepared for them as they take effect.

Provisions Effective in 2010:

- **Tax Credits for Small Employers Offering Health Coverage** – For tax years 2010 through 2013, qualified small employers, generally those with no more than 25 full-time employees with an average annual full-time equivalent wage of no more than \$50,000, will be eligible for a tax credit of up to 35% of the cost of non-elective contributions to purchase health insurance for its employees. The maximum credit is available to employers with no more than 10 full-time equivalent employees with an annual full-time equivalent wage from the employer of less than \$25,000.

2014 and Later – In 2014 and later, eligible small employers who purchase coverage through the Insurance Exchange would be eligible for a tax credit for two years of up to 50% of their contribution.

- **Dependent Coverage** – Effective March 23, 2010, the exclusion for reimbursements for medical care expenses under an employer-provided accident or health plan to any child of an employee is extended to children who have not attained age 27 as of the end of the tax year, provided the child also is eligible to be claimed as a dependent for tax purposes.

Provisions Effective in 2011:

- **Over-the-Counter Medication Restriction for Employer-Provided Plans** – Over-the-counter medications, except for doctor-prescribed over-the-counter medication and insulin, will no longer qualify for reimbursement. This restriction applies to health reimbursement accounts (HRAs), health flexible savings accounts (FSAs), health savings accounts (HSAs), and Archer medical savings accounts (MSAs).
- **Increased Tax on Nonqualifying HSA or Archer MSA Distributions** – The additional tax for HSA withdrawals for other than qualified medical expenses before age 65 increases from 10% to 20%, and the additional tax for Archer MSA withdrawals for other than qualified medical expenses increases from 15% to 20%.

- **Employer W-2 Reporting Responsibilities** – Employers will be required to disclose the value of the benefit provided by them for each employee's health insurance coverage on the employee's annual Form W-2.

- **Expansion of Information Return Reporting** – Currently, a business paying more than \$600 per year to a noncorporate service provider who is not an employee is required to file an information return (Form 1099-MISC). The new law expands the return filing requirement to include both corporate and noncorporate providers of property and services, beginning with tax year 2011.

Provisions Effective in 2013:

- **Taxpayers Earning Over \$200,000** – Higher-income taxpayers will be subject to the following additional taxes:

Additional Hospital Insurance Tax – The Hospital Insurance (HI) tax rate (currently at 1.45%) would be increased by 0.9 percentage points on an individual taxpayer earning over \$200,000 (\$250,000 for married couples filing jointly).

Surtax on Unearned Income – A 3.8% surtax, called the Unearned Income Medicare Contribution, would be placed on the net investment income of a taxpayer earning over \$200,000 (\$250,000 for a joint return). Net investment income includes interest, dividends, royalties, rents, gross income from a trade or business involving passive activities, and net gain from disposition of property (other than property held in a trade or business). "Net" investment income is investment income reduced by allowable investment expenses. Distributions from qualified retirement plans and IRAs will not be subject to the surtax.

- **Employer Flexible Health Spending Plan Contributions Limited** – The maximum that can be contributed to an employer's health flexible spending accounts (FSAs) would be limited to \$2,500 per year. The amount will be indexed for inflation in subsequent years.
- **Medical Itemized Deductions Limited** – The itemized deduction for medical expenses will be limited in the following manner:
AGI Threshold – The AGI threshold for claiming medical expenses on a taxpayer's Schedule A is increased from 7.5% to 10%, which is the same as the current alternative minimum tax (AMT) rate. Individuals (and their spouses) age 65 and older will continue to use the 7.5% rate through 2016.

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It's Time to Hire! New Tax Breaks Make It Easy.

The "Hiring Incentives to Restore Employment Act of 2010," more commonly referred to as the HIRE Act, was passed by Congress and recently signed into law by the President. The Act provides employers with incentives to hire unemployed individuals. The provisions of this new legislation apply to workers hired after Feb. 3, 2010, but only for wages paid after March 18 (the date the legislation was signed into law).

- **Payroll Tax Holiday** – The law exempts any private-sector employer that hires a worker who had been unemployed or employed for less than 40 hours during the 60-day period ending on the date of his hire from having to pay the employer's 6.2% share of the Social Security payroll tax on that employee's wages for the remainder of 2010. Thus, if the newly-hired and previously-unemployed worker earns \$106,800 after March 18, 2010 and before the end of the year, the company could save a maximum of \$6,621. This provides the employer with an immediate benefit by reducing the amount the employer must pay in employment taxes.

The 60-day qualifying period must be continuous but can span 2009 and 2010.

- **Retention Credit** – As an additional incentive, for any qualifying employee hired under this initiative that the employer keeps on payroll for a continuous 52 weeks, the employer is eligible for an additional non-refundable tax credit equal to the lesser of \$1,000 or 6.2% of the employee's wages. Since the 52-week requirement cannot be met until the subsequent year, the credit will be taken on the employer's 2011 tax return. In order to be eligible, the employee's pay in the second 26-week period must be at least 80% of the pay in the first 26-week period. This credit is not available for domestic workers.

Employee Qualifications – Although there is no minimum number of hours that an employee needs to work in order to qualify for either benefit, an employer cannot claim the tax breaks for hiring family members or household employees. A worker who replaces another employee who performed the same job for the employer isn't eligible for the benefit, unless the prior employee left the job voluntarily or for cause. The payroll tax holiday can be claimed for rehiring former workers as long as that worker was terminated due to facts and circumstances, such as a factory closure due to lack of demand for the product.

Thus, the payroll tax exemption applies to wages paid to an employee who was laid off and later rehired as long as the 60-day qualifying period is satisfied; to new employees who were hired to replace workers that were laid off for lack of work as long as the new employee meets the 60-day qualifying requirement; and to students who had been in school during or some part of the 60 days preceding their date of hire.

Employee Documentation – To validate the new hire for the benefits, an employer must have the employee sign an affidavit, under penalty of perjury, stating that he or she has not been employed for more than 40 hours during the 60-day period ending on the date the employment begins.

Claiming the Exemption – The exemption is claimed on the employer's quarterly federal tax return (Form 941) beginning in the first quarter of 2010, including the exemption for the first quarter's wages paid during the period of March 19 through March 31, 2010.

Interaction with the COBRA Premium Assistance Credit – An employer can claim the premium assistance credit and the payroll tax exemption for new hires on the same employment tax return.

Interaction with the Work Opportunity Credit (WOTC) – An employer must choose, on an employee-by-employee basis, whether to claim the HIRE benefits or the WOTC; double dipping is not allowed. The WOTC is, in many cases, more valuable than the payroll tax holiday, especially for low-wage employees, because it is generally 40% of "qualified first-year wages" of up to \$6,000, for a maximum credit of \$2,400 per worker.

The payroll tax holiday is equal to 6.2% of wages, and applies only to wages paid through Dec. 31, 2010. However, the WOTC is harder to qualify for, because the employee must be certified by an agency as belonging to a targeted group. The main qualification for a payroll tax holiday is that the employee has been unemployed for 60 days, and the employee's affidavit is sufficient for this purpose.

For more information on this topic and other business-related issues, please give this office a call.



(“Health Care Bill & Taxes: What You Need to Know Cont’d...)

Deduction for Employer Part D would be Eliminated – The deduction for the subsidy for employers who maintain prescription drug plans for their Medicare Part D eligible retirees is eliminated.

Provisions Effective in 2014:

• **Penalty For Not Being Insured** – Beginning in 2014, taxpayers will be penalized for failing to maintain the minimum essential coverage. The penalty will be phased in beginning in 2014 and the fully-implemented penalty in 2016 will be the greater of:

- 2.5% of household income over the threshold amount of income required for income tax filing, or
- \$695 (indexed for inflation after 2016) per uninsured adult in the household (\$348 if under age 18).

Maximum Penalty – The total household penalty cannot exceed 300% of the per-adult penalty (\$2,085) or national annual premium for the “bronze level” health plan offered through the Insurance Exchange that year for the household size. Penalties are based upon the months that the required insurance is not in force.

Penalty Phase-In – The maximum penalty will not be imposed until 2016. The phase-in rates are:

	2014	2015
Per-adult annual penalty	\$95	\$325
% of income penalty	1%	2%
Family maximum	\$285	\$975

Taxpayers Exempt from the Penalty – Individuals are exempt from the penalty if either their employer’s sponsored coverage or the lowest-cost “bronze” coverage exceeds 8% of household income. Also exempt are individuals residing outside of the U.S., those exempted for religious purposes, and those with income below the threshold for having to file a return.

• **Low-Income Health Exchange Participation Credits** – Tax credits will be available for low-income individuals and families with incomes up to 400% of the federal poverty level that are not eligible for Medicaid, employer-sponsored insurance, or other acceptable coverage. To qualify for the credits, these individuals and families would have to obtain coverage in the newly-established Insurance Exchange. Based upon the current poverty levels, the credit would phase out at \$42,420 for individuals and \$88,200 for a family of four. Additionally, a cost-sharing subsidy will be provided for low-income individuals to help pay for their coverage.

• **Large Employer Responsibilities** – Large employers, generally those with 50 or more full-time employees in the prior calendar year, that:

- Do not offer coverage for all full-time employees,
- Offer minimum essential coverage that is unaffordable, or
- Offer minimum essential coverage where the plan’s share of the total allowed cost of benefits is less than 60%,

Would be required to pay a penalty if any of its full-time employees were certified to the employer as having purchased health insurance through a state exchange and qualified for either tax credits or a cost-sharing subsidy as discussed previously.

Penalty – The excise tax penalty for any month would be \$167 times the number of full-time employees in excess of 30.

• **Free Choice Vouchers** – Employers who offer minimum essential coverage through an eligible employer-sponsored plan and pay a portion of that coverage will be required to offer an equivalent value voucher, allowing a qualified employee the option of purchasing coverage through the Insurance Exchange. An employee qualified to make this choice is an individual with a required contribution to the employer plan that exceeds 8%, but does not exceed 9.5%, of his or her household income and has income that does not exceed 400% of the poverty line for the family.

Provisions Effective in 2018:

• **Excise Tax on High-Cost Employer-Sponsored Health Coverage** – There will be a 40% non-deductible excise tax on insurance companies and plan administrators for any health coverage plan where the premiums exceed the following amounts:

Single Coverage:	\$10,200
Single Coverage, high-risk employment, or retired age 55 and older:	\$11,850
Family Coverage:	\$27,500
Family Coverage, high-risk employment, or retired age 55 and older:	\$30,950

The tax would apply to self-insured plans and plans sold in the group market, but not to plans sold in the individual market (except for coverage eligible for the deduction for self-employed individuals). Stand-alone dental and vision plans would be disregarded in applying the tax. The dollar amount thresholds may be later adjusted for inflation.

The finite details and regulations regarding these changes will become available as the implementation phases in through 2018. However, if you have questions related to how any of these provisions might impact your situation, please give this office a call.

Preparing Yourself for Business Ownership

Purchasing an ongoing business or starting one from scratch can be a complicated process. Therefore, if you are looking for a business to acquire, here are some things you should know in advance.

Document What You Are Purchasing – The acquisition of a business frequently involves the purchase of multiple assets, and the tax treatment of those assets will depend upon the type of property being purchased. Often, the seller and buyer will have adversarial interests in the allocation of the business purchase price among the various assets of the business. For example, a seller might want to allocate the greater portion of the sale price to goodwill since he benefits from capital gains tax rates on the sale of goodwill. However, the buyer can only amortize goodwill over 15 years and would prefer to allocate the purchase price to assets with faster write-offs. The IRS does not care how the price is allocated so long as both the buyer and the seller use the same allocation. Therefore, it is important that the contract specify the allocation for every asset purchased.

Prepaid Expenses – A question that often arises is whether prepaid business expenses can be deducted in the year they are paid. Unfortunately, that is not possible. Generally, where an expense relates to a period covering more than 12 months, the IRS and most courts agree that the deduction must be spread over the period to which the expense applies.

Start-Up Expenses – These include all of the expenses incurred to investigate the formation or acquisition of a business or to engage in a for-profit activity in anticipation of that activity becoming an active business. Generally, start-up expenses must be amortized over 15 years except that up to \$5,000 can be written off in the first year of the business’ operation. If the expenses are more than \$50,000, then the \$5,000 first-year write-off is reduced, dollar-for-dollar, for every dollar that start-up expenses exceed \$50,000. For example, if start-up costs were \$54,000, the first-year write-off would be limited to \$1,000 (\$5,000 - (\$54,000 - \$50,000)).

If you have questions related to any of the above, please give this office a call. Starting a business also entails obtaining licenses and permits, setting up payroll and accounting systems, as well as tax reporting or other federal and state compliance issues. Please call this office for assistance in any of these areas.



Tax calendar

June – September

June 15, 2010:

- U.S. citizens living abroad on April 15, 2010 must file a 2009 income tax return (if not already filed) or file for an extension.
- The second installment of your 2010 individual estimated taxes is due. If your income or deductions have significantly changed, you should call this office to determine if any adjustment in estimates is appropriate.

June 30, 2010:

- This is the last day to purchase a home and qualify for the homebuyer credit if you had entered into a binding contract to purchase prior to May 1, 2010.
- For taxpayers who had a financial interest or signature authority over a foreign financial account where the account was greater than \$10,000 at any time during 2009, this is the final due date for filing form TD F 90-22.1 - Report of Foreign Bank and Financial Accounts and avoid civil penalties of up to \$10,000 for non-willful violations.

The purpose of this newsletter is to provide current information on tax, financial and business developments. It suggests general tax planning ideas that may only be appropriate when claiming tax benefits in a manner consistent with the statutes and Congressional purpose. The information and opinions are generalizations and may not apply to all taxpayers and cannot be used by a taxpayer for the purpose of avoiding penalties that may be imposed on the taxpayer. Therefore, it is important that you seek appropriate advice before implementing any of the ideas suggested.

July 2010:

- It's time to review your 2010 year-to-date income and expenses to ensure that your estimated tax payments and withholding are adequate to avoid underpayment penalties. There have been a significant number of tax changes for 2010 that can impact your estimated taxes for 2010.

August 2, 2010:

- This is the due date for self-employed individuals and employers to file 5500 series returns for 2009 calendar-year benefit plans (including Keogh/HR-10 plans).

September 15, 2010:

- The third installment of your 2010 individual estimated taxes is due.
- This is the due date for filing calendar-year 2009 Fiduciary Income Tax (Form 1041), Corporation (Form 1120 and 1120S), and Partnership (Form 1065) returns for which extensions were previously filed.

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Since You
Asked...



You Asked: I am considering buying some new machinery for my business this year but I am not sure what the expensing limitation is for 2010?

Answer: Congress, as part of the "Hire Act," extended the expensing amount to \$250,000 for 2010 (same as it was in 2008 and 2009). The maximum deductible expense is reduced (i.e., phased out, but not below zero) by the amount by which the cost of property placed in service during the tax year exceeds \$800,000. Barring any additional legislation, the maximum amount will drop approximately to \$134,000 in 2011.

You Asked: I heard the other day that the government is thinking about raising the capital gains rates in 2011. Is that true?

Answer: Actually, Congress lowered the capital gains rates for 2003 through 2010 and they have not shown any inclination to extend the lower rates past 2010. Therefore, unless Congress acts, the rates automatically return to the pre-2003 levels of 10% (up from the current 0%) for those in the 15% or less bracket and 20% (up from 15%) for everyone else. If you have capital gains, you may wish to consider whether or not to take them in 2010 while the rates are still low.