

“THE NEWSLEDGER”

MARYLAND DIEING OVER LIVING WAGE

Maryland has become the first state in the nation to require certain “contractors” to pay a “living wage” to employees who perform work on Maryland state contracts. During 2008, the living wage is set at \$11.30 per hour for Montgomery, Prince George’s, Howard, Anne Arundel, and Baltimore counties, and Baltimore city. All other counties are set at \$8.50 per hour. The Commissioner of Labor will adjust these rates annually for inflation. The higher rate applies to eligible contracts in which contract services valued at 50 percent or more of the total value of the contract will be performed in the higher rate jurisdictions. There are numerous exceptions, exemptions and deductions built into the law. Each contract must be reviewed carefully, on an individual basis.

SMALL BUSINESS AND WORK OPPORTUNITY TAX ACT OF 2007 NOW A REALITY

Congress recently enacted a \$4.8 billion tax incentives tax bill with various incentives to help businesses absorb the costs related to the new federal higher minimum wage. Also included is a package of S corporation reforms – and, of course, substantial revenue raises. The following is a summary of the key components of the Small Business and Work Opportunity Tax Act of 2007:

- the new law gradually raises the federal minimum wage over the next two years to \$7.25 per hour;
- the new law increases the dollar limit for Section 179 equipment expending to \$125,000 for tax years beginning in 2007 through 2010. This amount will be indexed for inflation. The investment limitation is increased for the same period to \$500,000. The deduction is disallowed if the taxpayer income in the year the property is placed in service. However, now the amount of the deduction disallowed for this reason may be carried forward to a non-loss year;
- the new law allows employers to base tip credits on a \$5.15 per hour minimum wage;
- the new law permits a married couple who own a joint venture and who file a joint return to elect not to be treated as a partnership for federal tax purposes.
- For S corporations the new law addresses passive investment income, the reserve method of accounting by banks, sales of interest in a Q Sub, and the computing of taxable income of the S portion of an electing small business trust;
- the law extends the age limits relative to the imposition of the “Kiddie Tax”. The Kiddie Tax will now apply to children who are under age 19 or who are full-time students under age 24. The treatment applies only to students over 18 whose earned income does not exceed one-half of the amount of their support. The new limits kick in on January 1, 2008;
- the law allows for various tax incentives relative to damages caused by Hurricane Katrina;

- on the other hand the new law extends higher IRS user fees;
- increases IRS bad check penalties;
- extends and increases return preparer penalties;
- imposes penalties in taxpayers who claim erroneous refund or credit claims;
- and extends the period of time before which accrual of interest and IRS penalties are suspended.

TOO MANY BEERS – GET A ROOM – BE READY FOR THE MORNING AFTER

The IRS has announced that it will no longer contest an employers’ deduction of the cost of employee lodging that is located in the same town as the employer, provided the lodging is necessary for the employee to take part in a meeting or function of the employer the next morning. So if you drink a few too many one night; make sure to set up a business meeting for the next morning – late morning that is!

IRS CRIMINAL DIVISION BLOWS FRAUD CASE AGAINST KPMG EXECUTIVES

The U.S. Court of Appeals for the Second Circuit recently ruled that the district court had not authority to assert jurisdiction over a million dollar legal fee dispute between KPMG, a national accounting firm, and 16 former executives facing criminal tax fraud charges in connection with tax-shelter activities. This court ruled that the government violated the constitutional rights of the executives and recommended that the district court dismiss the indictments against the KPMG former executives. It was stated that government prosecutors pressured the accounting firm to stop paying the defendants legal fees. (If they didn’t stop KPMG would face an indictment as well.) The eventual forced non-payment of the defendants legal fees by KPMG resulted in a violation of their Fifth and Sixth amendment rights. All 16 indictments were dropped by the government!

SOLE OWNER LIMITED LIABILITY COMPANY – A MAJOR PAYROLL TAX PITFALL

When the owner of a single-member limited liability company (LLC) fails to elect to be treated as a corporation for federal income tax purposes, the LLC will be held liable for owner personal payroll taxes on the LLC net income by the IRS. The federal tax rules state that “eligible entities” with only one owner are not required by Code to be treated as a corporation; they may elect to be treated as a corporation, they may elect to be classified as a corporation or as a sole proprietorship. In order to elect corporate status the LLC must file form 8832, Entity Classification Election. In absence of this election; the entity is disregarded as a separate entity and treated as a sole proprietorship for federal tax purposes. The Court ruled that the IRS collection of a sole owned LLC’s unpaid payroll taxes from the LLC were appropriate; even when the LLC legal status

was different from that recognized by state law. The Court ruled that “the liability for taxes under state law may differ from liability for federal taxes as the result of the overriding force of the check-the-box regulations for federal tax purposes only.”

IRS FINDS NO CHARITY IN MARIJUANA

The IRS and its compatriot, the Tax Court, have declared that expenses related to providing medical marijuana to seriously ill individuals by non-profit organizations were actually costs incurred in connection with the trafficking of a controlled substance. Therefore a charity providing medical marijuana could not deduct the related expenses. Even though some states have “compassionate use” laws that allow individuals with chronic health conditions to use medical marijuana when approved by a doctor; these state laws do not protect you from federal criminal prosecution. The Tax Court ruled that marijuana is a controlled substance within the meaning of the “Controlled Substance Act.” Therefore a charity’s supplying of marijuana to its members was within the definition of trafficking in that the charity consistently bought and sold illegal drugs.

WHAT A CHANGE – TAX RELIEF ON TAX REFUNDS

In quite a surprising statement the IRS Chief Counsel recently determined that local property tax rebates are not includable in a taxpayer’s income. Instead a rebate should reduce the taxpayer’s itemized deduction for real estate taxes paid. It was also decided that the State issuing the rebates will not be required to report the individual refunds to the IRS.

OLD VACATION HOME SALE AND NEW VACATION HOME PURCHASE NOT A LIKE-KIND EXCHANGE

In this situation a couple who sold their vacation property and purchased another, using an escrow agent, were not entitled to exclude the gain from the sale of the first vacation home because the properties were not held primarily for use in a trade of business or for investment purposes. The fact that the couple held the property partially because they anticipated its value to increase was insufficient to qualify the transactions for gain exclusion.

NATIONAL TAXPAYER ADVOCATE WARNS – “BEWARE OF ALTERNATIVE MINIMUM TAX”

According to the National Taxpayer Advocate, Nina Olson, in excess of one-third of all taxpayers will be paying Alternative Minimum Taxes by the year 2010. In her annual report to Congress, Nina Olson listed the AMT as the most serious problem facing taxpayers. Her list of top ten taxpayer problems were:

1. The Alternative Minimum Tax;
2. The tax gap;

3. Private tax debt collection;
4. Early intervention in IRS collection cases;
5. Collection payment alternatives;
6. Levies;
7. Centralized lien procedures;
8. IRS transparency;
9. Collection issues of lower income taxpayers; and
10. Excess contributions.

Olson has repeatedly urged Congress to reform the AMT so it returns to its original purpose; preventing the very wealthy from escaping federal taxation. She has informed Congress that, if left unchecked, 32.4 million individual taxpayers, or approximately 34 percent of all individual filers who pay income tax, will be subject to AMT by 2010.

Approximately 90 percent of all married couples with combined adjusted gross income between \$75,000 and \$100,000, with two or more children, will owe additional AMT taxes. In her report Olson also highlighted the following top ten most litigated issues:

1. Collection due process appeals;
2. Gross income;
3. Enforcement of IRS summonses;
4. Accuracy-related penalty;
5. Failure to file penalty;
6. Frivolous issues penalty;
7. Trade or business expenses;
8. Innocent spouse relief;
9. Family status; and
10. Charitable contribution deductions.

CONGRESS PRESSURES IRS TO DECLARE “WAR” ON TAXPAYERS TO SUPPORT “WAR” EFFORTS

In the past when the Democrats controlled Congress the posture of the IRS was that of a kinder, gentler, more understanding “Uncle Sam”. When the Republicans control Congress the IRS becomes a “Big Brother” who carries a big stick and cares little for the average lying, cheating, dishonest taxpayers under constant congressional enforcement, pressure IRS has announced, and statistics prove, that enforcement, collection and punishment of taxpayers over the last seven years has risen dramatically. The IRS’s “Data Book” touts that the number of individual audits along now exceed double those examined just seven years ago. Even with this dramatic enforcement increase Congress isn’t happy. Recently the IRS Commissioner was grilled by members of a House Ways & Means subcommittee about reports that IRS agents feel pressured to close audits prematurely. The question, now that the Congress is again controlled by the democrats, is whether the IRS will maintain its “Big Brother” attitude or revert to its old friendlier “Uncle Sam” posture!

OFFER-IN-COMPROMISE – YES IRS CAN GET BLOOD FROM A TURNIP!

The IRS has devised a new offer-in-compromise application. The new form comes with an IRS warning – use it but don't abuse it! This new form was designed not only as an application; but also as a guide to be used by taxpayers to determine if they may be eligible for an offer-in-compromise. The IRS concept here is to impose greater responsibilities on taxpayers who must now make payments with their offers. IRS feels that with the submission of more realistic offers, with payments, they can get Congress off their backs for not using this avenue of settlement more frequently. On the other hand don't expect any miracles, the IRS continues to insist that all offers be "reasonable and within existing guidelines." In the future any lump sum cash offers must include 20 percent of the offer as a non-refundable deposit when filing your application. The remaining balance of the offer can be made in up to 5 payments. Failure to make regular payments while the offer is being considered will cause the offer to be treated as a withdrawal. The application must also be accompanied by a \$150 filing fee. No fee included; no processing by IRS!

IRS SAYS THERE IS NO SUCH TAX THING AS A "PROFESSIONAL GAMBLER"

Traditionally, courts have held that poker is a wagering activity. Under this theory losses from poker "wagering" transactions are only deductible to the extent of gains from such transactions during the same calendar year. In a recent Tax Court case a taxpayer who played in nine poker tournaments during the same calendar year, claimed a net loss on her income tax return because she was a "professional gambler." The IRS denied any losses beyond her gross poker earnings of \$11,000. At trial, the taxpayer argued that tournament poker should be classified as an entertainment and sporting activity, not as a wagering activity. The taxpayer pointed out the similarities between poker and other professional sporting tournaments. IRS's friend, the Tax Court, ruled that simply because a sport or activity is played in a tournament does not change the underlying activity into something else. "Betting is intrinsic to poker, it being played in a tournament does not change the basic nature of the game as a wagering activity." According to the Tax Court this taxpayer is a LOSER!

FEDERAL GOVERNMENT MISCONDUCT LEAVES BANKS RELYING ON TAX BENEFIT LIES – AND SUBSTANTIAL LEGAL BILLS

During the Thrift loan crisis the Federal Government agreed to provide banks with financial and tax benefits if the banks would "bail out" the dying Thrifts. The banks did their part; however the U.S. Government breached its promise to provide financial and tax benefit assistance. The Court ruled that the government's misconduct violated the agreement with the banks and justified a future suit for damage awards, however when the banks asked for legal fee reimbursements, they were denied. The Court said that although the Government lied and violated the agreement, it

did not demonstrate "bad faith" as to the judicial process that would justify an award of attorneys' fees.

DETERMINING THE VALUE OF DONATED PROPERTY – MAY CONTRIBUTE TO YOUR AUDIT

The Pension Protection Act of 2006, did a major overhaul on the rules pertaining to the donating of used clothing and household items to charity. The IRS has now followed the Act up with its own publication, Determining the Value of Donated Property. Now, by regulation, the IRS can deny a deduction for the contribution of a clothing or household item that has minimal monetary value. The new IRS position states that the valuation of items of clothing does not lend itself to fixed formulas or methods; the value should be determined as the price that buyers of used items actually pay in used clothing stores. Taxpayers need to be especially careful for all future donations as Congress has demanded a rigid enforcement of the new valuation and appraisal donation rules. Weak documentation "WILL CAUSE AN IRS AUDIT!"

AIRLINE MECHANICS FLY BUT NEVER LEAVE HOME

In a series of "stupid" decisions the Tax Court has decided that airline mechanics who lost their long-term positions, resulting from the recent airline industry downsizing, and who exercised their seniority to give them relatively short-term positions in different state; were not "away from home" for tax purposes. The travel expenses incurred to work at those assignments were not deductible according to the IRS a taxpayer must have a principal place of employment and accept temporary work in another location to be considered away from home. Once the mechanics were bumped their original jobs they had no jobs to return to there; thus their employment there had ended. Therefore each new location in which they worked became their new tax homes, regardless if they maintained homes near their original job. Is this stupid or what!

ZIMMERMAN & ASSOCIATES EVENTS

Z&A Realty, LLC is excited to have Mustang Construction become a member of our Z&A Professional Building Group. Our building is now filled to capacity!

Z&A is in its tenth year as a proud sponsor of The Firebirds Annual Celebrity Golf Tournament. This year's tournament was again held at the Montgomery Country Club – and all proceeds go to support the Maryland Firebirds Track Club. This year our Z&A team was represented by:

RICH BRUNNER – Z&A
NELSON OSTER – HMS INSURANCE
JONATHAN OLMSTEAD – TRANE
TODD WARREN – SUSQUEHANNA BANK

Bob & Carol Zimmerman recently enjoyed a wonderful four day getaway to their ocean resort home with their great friends and our clients Mike and Nancy Stevenson. The food was great and the companionship outstanding!

Z&A would like to take this opportunity to introduce you to our new found friendly clients:

CONNS PEST & TERMITE CONTROL, INC.
MONTENEGRO PRODUCTIONS, LLC
BRAWNER BUILDERS, INC.
BRAWNER/CORE JOINT VENTURE
MJL CONSTRUCTION, INC.
MIRABILE MANAGEMENT, INC.
SAFE LOCK SECURITY & SURVEILLANCE,
INC.
HGA SECURITY, INC.
OUTSOURCE BUSINESS SERVICES, INC.
CUSTOM SECURITY & WIRING, INC.
MUSTANG I MANAGEMENT, INC.
MUSTANG II MANAGEMENT, INC.
J.C. DEVINE ICE, LLC
HAUL OR NOTHIN', INC.
WOLVERINE CONTRACTORS, INC.

FOOD FOR THOUGHT

Life begins at the age of awareness – be that two or eighty-two!