

REITZ & COMPANY

CERTIFIED PUBLIC ACCOUNTANTS

CONTACT US:

PHONE: (714) 437-1288

FAX: (714) 437-1294

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Tax Year 2014 started off with one set of rules, but changes are coming. Law-makers decided to allow dozens of tax breaks to expire after 2013 such as the R&D tax credit, bonus depreciation, the sales tax deduction, the exclusion of up to \$2 million of forgiven debt on a debtor's primary home, and the ability of taxpayers who are 70 ½ and older to make direct distributions of up to \$100,000 annually from their IRA's to charity. However, when it comes to passing legislation, it appears Congress needs a crisis to act; the highway funding bill is a perfect example. The Federal highway trust fund is close to running dry because the revenues from the 18.4 cent-a-gallon gas tax have been insufficient in covering road building outlays. Congress has known about the depleting highway trust fund for some time, but like tax reform, a sense of urgency is missing until it is (almost) too late.

Tax Updates

Reviving expired tax breaks for individuals and businesses will likely wait until after the November midterm elections. While there is much debate regarding the subject, the House and Senate are on different tracks; the House is passing bills to extend the breaks one by one while the Senate has crafted a measure to revive nearly all of them at once.

Corporate Inversions: Recently, a handful of multinational U.S. companies have merged with foreign companies and then moved their headquarters overseas to countries with far lower corporate tax rates than the U.S. In this way the foreign headquartered companies pay less income taxes on their foreign profits and can use the cash held offshore for foreign operations or to pay dividends without having to repatriate the money and pay U.S. tax.

Democrats want to put a stop to tax-motivated inversions right away but Republicans believe that the issue is best addressed in a broad tax overhaul.

Children's summer camp yields a write off in the form of the dependent care credit. If you sent your child (under age 13) to any special day camps this summer such as those for sports, computers, math, or theatre, don't forget about this break. The costs for summer school and tutoring are considered educational costs and thus do not qualify for the credit. The credit is limited to 20% of the dependent care cost capped at a credit of \$600 for one child, or \$1,200 for two or more.

IRS Scams: Reitz & Company has seen an uptick in calls from clients reporting that they are receiving scam calls and emails from individuals claiming to be Internal Revenue Service (IRS) agents or Criminal Investigation Division (CID) agents. These scam calls and emails are designed to get the taxpayers to respond and to divulge personal identity information.

If you receive a telephone call or email from an individual claiming to be the IRS, do not reveal any personal information. Remember that the IRS will never contact you initially via telephone or email; the first correspondence will come via snail mail.



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Our Team

Neal M Reitz, CPA, MBA

neal@reitzcompany.com

Spencer M Reitz, CPA, MBT

spencer@reitzcompany.com

Brittany Reitz Morton, CPA, EA, CGMA

brittany@reitzcompany.com

Brian R Morton, CPA/ABV, ASA, CDFA™

brian@reitzmorton.com

Joe Macaluso, EA

joe@reitzcompany.com

Phillip Reitz, CPA

phil@reitzcompany.com

Titi Ung, MBA

titi@reitzcompany.com

Laura Morton

laura@reitzcompany.com

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Tax Updates Continued...

IRS Struggling on Enforcement: IRS examinations are plummeting. Last year's audit rate of 0.96% for individuals was the lowest since 2005. Stated another way, the IRS audited just one out of every 104 filed tax returns. That rate is expected to drop to 0.80% for 2014.

Due to IRS budget cuts the number of correspondence audits done by the IRS is expected to nose-dive this year. The IRS plans to conduct almost 140,000 fewer correspondence exams than in 2013, a 13% drop. Correspondence audits, which are done by mail, account for approximately 75% of all audits in a typical year.

Though the odds of most people hearing from the IRS are pretty low, there are some red flags that can draw extra IRS attention. We will review some here:

- **Claiming 100% business use of vehicle:** this is red meat for IRS agents. They know that it is virtually impossible to use a vehicle 100% of the time for business, especially when no other vehicle is available for personal use.
- **Big deductions for meals, travel, and entertainment:** A large deduction here will set off alarm bells, especially if the amount seems too high for the business. Agents are on the look-out for personal meals or claims that don't satisfy the strict substantiation requirements.
- **Hobby Losses:** your chance of being audited increases if you have wage income and also file a Schedule C with a large loss. If the activity sounds like a hobby such as horse racing, dog breeding, car racing, etc., the IRS's antennas go up.
- **Deducting rental losses:** The IRS is scrutinizing rental real estate losses, especially those written off by a taxpayer claiming to be a real estate professional and whose W-2 or other non-real-estate business shows a lot of income. Agents are coming down hard on the real estate professional substantiation requirements.
- **Running a small business:** Owners of cash-intensive small businesses such as taxis, hair salons, car washes, and such are in the IRS's crosshairs. The IRS knows that these types of small businesses receive mainly cash and are less likely to report the income.

Health Care Premium Tax Credit

With healthcare reform in full swing, let's take a look at the premium tax credit. The credit is available to those individuals who purchase a health plan through a state-run exchange and have a household income between 100% to 400% of the Federal poverty level; \$11,490 to \$45,960 for singles and \$23,550 to \$94,200 for a family of four. Taxpayers eligible for Medicare or another Federal insurance program do not qualify. The credit will affect 2014 tax returns and is estimated when one applies through an exchange. Those who qualify for the credit can choose to have it paid in advance and applied against health insurance premiums. The ultimate amount of the credit will be determined on the 2014 tax return and will be compared to the 'estimated' credit if paid in advance. This can lead to greater or lesser refunds/taxes owed depending on how one's estimated credit compares to the actual numbers.

The IRS recommends keeping your exchange up to date with changes in family size, income, and other circumstances, such as starting with an employer that provides health-coverage to employees. If you notify the exchange of changes in income, etc., it can adjust the subsidy for the subsequent months and your tax return reconciliation will be closer to the estimated credit.

Tax Deferred Savings Accounts for the Disabled

A *proposal* moving through Congress, which is receiving bipartisan support, is the expansion of 529 plans to include nondeductible contributions to accounts for the benefit of individuals with long-term physical or intellectual disabilities or those who are blind. Traditionally, 529 plans allow for after tax contributions to educational savings plans operated by a state or educational institution. The earnings and principal can then be withdrawn tax free by the beneficiary and used for higher educational expenses.

These proposed 529 plan tax savings accounts for the disabled will likely cap contributions at the gift tax exclusion amount (\$14,000 for 2014) and payouts would be tax free if used for housing, education, transportation, job training, dental care, financial management assistance and other qualified disability expenses. Balances in the accounts as well as payouts wouldn't be counted for Medicaid eligibility. We will keep you updated on this recent proposal.



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Worker Classification

The stakes continue to be high on worker classification; lost taxes for federal and state governments continue to motivate the taxing agencies to examine and audit this area. The health reform magnifies the importance of worker classification because reclassified workers can put a small firm over the limit of allowable full time employees and trigger the employer mandate to offer health insurance. Historically the IRS has used a 20-factor test in classifying workers as employees or independent contractors, although not all factors apply in every case. For audit purposes the IRS has boiled down the 20 factors into three categories: the behavioral test, the financial test, and the type-of-relationship test.

- The behavioral test relates to whether the company has control over the worker and when and where the work is performed. Important factors include the type and degree of instruction given, plus detailed evaluation criteria and training.
- The financial test looks at who controls the economics of the worker's job such as who provides the tools and supplies or whether travel expenses are reimbursed. Hourly pay is indicative of employee status while a single one-time payment lends itself to independent contractor status. The ability of the worker to work for more than one company is also indicative of independent contractor status.
- The type-of-relationship test examines how the parties perceive each other from a business perspective. Evidence of an employer-employee relationship include paid vacation, sick leave, retirement benefits, and hiring a worker that provides services over the long run instead of a specific period of time. A written contract stating the worker's classification as an independent contractor is not determinative in itself and the workers classification must be considered as a whole based on the 20 factor test and categories above.

Companies whose classifications are challenged may qualify for relief. Please contact us if you have any questions in this area or if you recently received a notice from the taxing agencies regarding worker classification.



Neal's (health) Niche

- Number of cents out of every dollar earned by the average American that were paid in state and local taxes in 2010: 9.9 cents;
- Rank of New York (based on state-local tax burden), with residents paying 12.8% of their income on state and local taxes: First;
- Rank of Alaska (based on state-local tax burden), with residents paying 7% of their income on state and local taxes: Last.

Good tax advice is important, but your overall **health is more important**. As I tell all of my clients, to obtain great health you must eat, sleep, and exercise properly. In addition, what goes in must come out properly.

- "Eat to Live" by Dr. Joel Fuhrman is a great book to lose weight and learn about the proper foods to eat. Also, only drink water. Get rid of the sodas and alcohol and no fast foods;
- Ear plugs, I like "Hearos" brand. They can block out the "white noise" and allow you to get the proper 8 hours of sleep per night;
- 30 minutes of walking on a treadmill, 1 to 5 % incline at a 3 miles per hour pace will do the trick supplemented with some light weight lifting and stretching;
- Other health items which I have found to be important are:
 - Probiotic—Improves your gut bacteria. "Align" brand is the best.
 - Dry Skin—As we get older our skin dries out. I hate the greasy feeling of regular lotion, but also don't want dry skin. I have found Neutrogena Norwegian hand cream to be the best.

Hopefully, the above health suggestions will allow you to live a more long and healthy life so that you can remain our tax clients long into the future.

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A Note to Our Clients

Reitz & Company...

- Is a family owned business which has sustainable continuity for many decades to come;
- Employs a full range of Tax and Accounting Experts with professional designations and licenses including: Certified Public Accountant (CPA), Enrolled Agent (EA), Chartered Global Management Accountant (CGMA), American Society of Appraisers- Business Valuation (ASA and ABV), Series 6 and 7 licenses, Certified Divorce Financial Analyst, Masters in Taxation, and Masters in Business Administration;
- Makes client communication and service a top priority;
- Delivers a quality product in a timely manner at a competitive and affordable price;
- Has over 50 years of combined tax and accounting experience including in-depth interface with the IRS;
- Always has a CPA available to answer your questions: we are far from a "one man firm";
- Offers newsletters and opinions to keep you up to date on financial and tax issues happening now;
- Has a track record of success with the IRS, Franchise Tax Board, and EDD;
- Makes it a priority to keep you healthy financially.

Upcoming Tax Deadlines

September 15, 2014

- Final deadline to file 2013 corporate, partnership, and LLC income tax returns
- Final deadline to fund profit sharing plans in corporations and partnerships for tax year 2013
- Third quarter 2014 individual estimated tax payments are due
- Third quarter 2014 corporate, partnership, and LLC estimated tax payment are due

October 15, 2014

- Final deadline to file personal income tax returns

October 31, 2014

- Final deadline to file third quarter payroll tax returns: Forms 941, DE9, DE9C

Our Team

Neal M Reitz, CPA, MBA

neal@reitzcompany.com

Spencer M Reitz, CPA, MBT

spencer@reitzcompany.com

Brittany Reitz Morton, CPA, EA, CGMA

brittany@reitzcompany.com

Brian R Morton, CPA/ABV, ASA, CDFA™

brian@reitzmorton.com

Joe Macaluso, EA

joe@reitzcompany.com

Phillip Reitz, CPA

phil@reitzcompany.com

Titi Ung, MBA

titi@reitzcompany.com

Laura Morton

laura@reitzcompany.com

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Questions or comments? Please email or call the editors: Spencer M. Reitz, CPA, MBT or Brittany Reitz Morton, CPA, EA, CGMA