



# PERSPECTIVES

Volume 21, Number 2  
2<sup>nd</sup> Quarter 2010

## INSIDE:

Major Health Care Reform (cont.) .....2

Both Employers & Employees Benefit from the HIRE Act ....3

IFRS for SMEs – U.S. GAAP: Making Sense of Alphabet Soup .....4

Substantiating the Research Credit .....5

First-Time Homebuyer Credit Requirements...5

Acquiring Basis in S Corp Shareholder Loans .....6

PA Tax Amnesty .....6

Uncertain Tax Positions – Ready to Disclose?...7

PA Tax Updates .....7

MACRS Depreciation Rules, Section 179 Limits & the Lapse of Bonus Depreciation....8

Using Social Media as a Business Tool.....9

Retirement: An Illusion or a Difficult Possibility? .....9

Major Health Care Reform (cont.) ..... 10

Planning with Life Insurance – Points to Consider ..... 11

IRS Launches High-Wealth Task Force... 11

News About Us..... 12

## Major Health Care Reform Enacted – Impact Uncertain

by: Robert J. Grossman

Legislation designed to fundamentally reform the U.S. health care system was signed into law by President Obama on March 30, 2010. The *Health Care and Education Reconciliation Act of 2010 (2010 Reconciliation Act)* makes some significant changes to the previously passed *Patient Protection and Affordable Care Act (Patient Protection Act)*. Combined, the *Patient Protection Act* as amended by the *2010 Reconciliation Act* (hereinafter referred to as the “health care reform package”) represents the largest social reform in decades.



Once fully phased in (not until 2018), the legislation will provide health care coverage to 32 million uninsured Americans and make it more affordable for millions more. The health care reform package does not include a public health insurance option. Rather, it expands Medicaid; provides for the creation of state-run insurance exchanges, through which certain individuals and families can receive federal subsidies (credits) to substantially reduce the cost of care; forbids insurance companies from excluding coverage for pre-existing conditions (effective in 2010 for children; in 2014 for adults); establishes temporary (through 2014) high-risk insurance pools for adults with pre-existing conditions; and requires health plans to allow parents to keep their children on their family plans until they reach age 26.

The 10-year cost for this reform is estimated to be \$938 billion, which is largely paid for through significant tax increases on higher income taxpayers, Medicare reimbursement savings and various revenue raisers targeting specific health-related industries. Though the legislation does not require employers to provide health care insurance to employees, two key provisions are designed to encourage business owners to do so through incentives and penalties. Small employers are provided tax credits to encourage them to provide employee health coverage, and large employers are assessed excise taxes to discourage them from not providing employee health coverage (or providing unaffordable or inadequate coverage). Individuals will also be assessed excise taxes if they opt out of coverage.

This new legislation is massive and covers numerous areas, both tax and nontax. This article briefly summarizes the tax provisions affecting individuals and small- to mid-sized businesses, based on the timeline for when the provisions are scheduled to take effect. Please call GYF with any questions.

### Provisions Effective in 2010

- **Small Employer Health Insurance Tax Credit** – Effective this year through 2013, the health care reform package provides a new tax credit for small employers that purchase health insurance for their employees. To qualify for this new credit, the employer must:
  - employ no more than 25 full-time equivalent (FTE) employees during the tax year,
  - pay annual FTE wages that average no more than \$50,000 for the year, and
  - have a qualified health insurance plan (or arrangement) under which 50% of the premiums (on a uniform basis) for employees who enroll in the plan are paid by the employer.

(continued on page 2)

## Major Health Care Reform Enacted (continued from front)

Generally, to qualify for the new health care credit, the employer must pay the same percentage (at least 50%) of all employees' premiums. Under a transition rule for 2010 only, employers paying differing percentages of employees' premiums also qualify, as long as all payments are at least 50% of each employee's premium (based on single coverage). Premiums that were paid in 2010 before the new legislation was enacted can also qualify for the credit.

The credit generally equals 35% of the amounts paid by the employer during the year for employee coverage. However, the full amount of the credit is available only for employers that employ 10 or fewer FTE employees and have average annual FTE wages of less than \$25,000 for the year. Also, no credit is allowed for premiums paid on behalf of partners, sole proprietors, 2%-shareholders of an S corporation, 5%-owners of the employer, and dependents of these individuals. Other limitations may apply as well. A tax credit calculator, created by a national non-profit, can be used by businesses to estimate the credit: <http://www.smallbusinessmajority.org/tax-credit-calculator/>

The credit is claimed on the employer's income tax return, and can offset regular income taxes and AMT. Any unused credit can be carried back for one year (not before 2010), and forward for 20 years, to offset future taxes. In 2014 and later, eligible small employers who purchase coverage through a state-run insurance exchange will be eligible for a tax credit for two years of up to 50% of their contribution. Wage limits will be indexed beginning in 2014.

- **Dependent Coverage in Employer Health Plans** – Under the health care reform package, effective March 31, 2010, self-employed individuals can deduct insurance coverage for their children who have not turned age 27 as of the end of the year. Similarly employees can exclude from their taxable income the amounts their employer pays for health care insurance and expense reimbursements for their children who have not attained age 27 as of the end of the year. To qualify, the child must be the individual's son, daughter, stepson, stepdaughter or eligible foster child. The child does not need to be the individual's dependent.

Employers do not have to provide coverage for these adult children if they do not otherwise cover dependents. But, if the employer's plan does cover dependents, it must change its definition of *dependent* to include an employee's unmarried children up to age 26 (different from the income exclusion qualifications), but not until its plan year beginning after September 23, 2010. Thus, employees may need to wait until 2011 before their adult children are covered.



- **Adoption Credit & Adoption Assistance Exclusion** – For 2010, the new legislation increases the adoption credit and the employer-provided adoption assistance exclusion to \$13,170 (from \$12,170). It also makes the credit refundable and extends the exclusion and credit through 2011.
- **Economic Substance Doctrine** – Over the years, this judicial doctrine was used inconsistently to deny tax benefits, when the transaction generating the benefits lacked economic substance. The new legislation clarifies how the economic substance doctrine should be applied by the courts and imposes a 20% penalty on understatements attributable to a transaction lacking economic substance.

### Provisions Effective in 2011

- **Reporting Employer-Sponsored Coverage** – Beginning in 2011, employers must report on Form W-2, the value of health insurance coverage provided to employees.
- **Over-the-Counter Medication** – The health care reform package modifies the definitions of *qualified medical expenses* for HSAs, health FSAs, Archer MSAs and HRAs, to conform to the definition used for the medical expense itemized deduction for income tax purposes. Thus, starting in 2011, over-the-counter medications (other than insulin) are excluded from tax-free reimbursement, unless prescribed by a health care professional.
- **HSA & Archer MSA Withdrawals** – The new legislation increases, from 10% to 20%, the additional tax for HSA withdrawals, made before the owner turns age 65, that are not used for qualified medical expenses. The additional tax for post-2010 Archer MSA withdrawals not used for qualified medical expenses increases from 15% to 20%.
- **Simple Cafeteria Plan** – A new plan, the *Simple Cafeteria Plan*, will be available to small employers (average of 100 or fewer employees during either of the two preceding years) starting in 2011. To make it easier for these small employers to provide tax-free benefits to their employees, the Simple Cafeteria Plan and the benefits it provides (including group term life insurance, self-insured medical expense reimbursements and dependent care assistance) will be treated as meeting the applicable nondiscrimination rules if the plan satisfies certain minimum eligibility, participation, and contribution requirements.

### Provisions Effective in 2012

- **Corporate Information Reporting** – Businesses that pay more than \$600 during the year to corporate providers of property and services must file an information report with each provider and the IRS, beginning in 2012.

(continued on page 10)

## *Both Employers and Employees Benefit from the HIRE Act*

by: *Richard E. Dynoske*



In a continued effort to stimulate the U.S. economy, on March 18, 2010, President Obama signed into law the first major tax bill of the year. The main purpose of the *Hiring Incentives to Restore Employment Act of 2010* (HIRE), also known as the Jobs Bill, is to encourage businesses to hire and retain new employees and to invest in new property and equipment. The *HIRE Act* features an \$18 billion job creation package, which includes a tax credit for companies who hire workers who have been unemployed for at least 60 days; and an extension of enhanced expensing for small businesses. The tax benefits of the *HIRE Act* are partially offset by several new provisions, including heightened disclosure and reporting requirements for taxpayers with foreign assets and acceleration of certain corporate estimated tax payments. Some of the major provisions are explained below.

### *Incentives for Hiring and Retaining New Employees*

The *HIRE Act* provides \$13 billion in tax breaks that are intended to serve as an incentive for businesses to hire unemployed workers in 2010. The “Hire Now Tax Cut” forgives a qualified employer’s 6.2% Social Security tax liability for wages paid to qualified new hires for any period between March 19, 2010 through December 31, 2010. This tax forgiveness does not apply to the employer’s Medicare tax; there is no exemption for the 6.2% employee portion of the tax, and there’s no break for individuals who pay self-employment tax. The maximum amount of employer Social Security tax savings for a highly-paid employee is \$6,621.60 (6.2% × \$106,800 Social Security tax ceiling for 2010). Savings will be less for lower-paid employees.

Qualified employers include private-sector companies, tax-exempt not-for-profit organizations and eligible public higher-education institutions. Qualified new employees are full- or part-time workers who start work between February 4, 2010, and December 31, 2010, and who were not employed more than 40 hours during the 60-day period ending on their start dates. However, the new worker cannot replace another worker unless that person quit voluntarily or was discharged for cause.

Employers can also claim an additional temporary new tax credit (up to \$1,000) for wages paid to each qualified new employee, using the same definition as for the Social Security tax exemption. The worker must be kept on the payroll for at least 52 consecutive weeks, and wages during the second 26 weeks of the 52-week period must equal at least 80% of wages paid during the first 26 weeks of that period. To claim the maximum \$1,000 credit, the worker must be paid at least \$16,130 during the 52-week period.

This credit can be claimed only once for each qualified employee through an increase in the Code Sec. 38(b) business tax credit, and can only be claimed for the tax year ending after March 18, 2010, during which the 52-week requirement is first met for the applicable worker. Because the 52-week requirement cannot be met until February of 2011 at the earliest, the credit cannot be claimed on a calendar-year 2010 return, and will have to wait until the calendar-year 2011 return is filed.

### *Extension of Enhanced Code Sec. 179 Expensing*

The new law extends the generous Section 179 small business expensing limits. These favorable provisions, which were introduced in 2008 stimulus legislation, expired December 31, 2009. The *HIRE Act* extends through December 31, 2010, the enhanced Sec. 179 expensing: a \$250,000 maximum deduction with a phase-out threshold of \$800,000. Under the *HIRE Act*, off-the-shelf computer software continues to be Code Sec. 179 property for one more year. However, the bonus depreciation provision was not extended (see related article on page 8).

A package of additional extenders were excluded from the *HIRE Act* to expedite its passage. As of the printing of this newsletter, an extender bill had not been finalized. We will keep you up-to-date through email alerts and postings on our website.

### *Stricter Foreign Tax Compliance Provisions*

For tax years beginning after March 18, 2010, the *HIRE Act* will require new tax return disclosures from individuals with interests in “specified foreign financial assets” if the aggregate value exceeds \$50,000. Failure to make required disclosures can result in a \$10,000 penalty. The new law also suspends the statute of limitations period if the taxpayer fails to make required tax return disclosures for foreign financial assets. An additional 40% penalty will be levied on any understated amount of tax that is attributable to an undisclosed foreign financial asset or to any transaction involving such an asset. The *HIRE Act* establishes a six-year statute of limitations period for tax understatements (in excess of \$5,000) attributable to certain understated income from foreign financial assets.

Effective March 18, 2010, the new law creates a more expansive definition of “beneficiary” used to determine when a foreign trust is treated as a grantor trust owned by a U.S. beneficiary. The *HIRE Act* requires U.S. taxpayers that are treated as grantors (owners) of foreign trusts to report any information about such trusts as the IRS may mandate, in addition to complying with return filing and information reporting requirements. A \$10,000 minimum penalty is imposed for failures to file required returns and notices due after December 31, 2009, for foreign trusts.

For additional information about the provisions of the *HIRE Act* and their impact on your business, please call GYF at 412-338-9300

## IFRS for SMEs vs. U.S. GAAP – Making Sense of the Alphabet Soup

by: Erika F. Heinzl

**Y**ou have heard about the globalization of the economy, but did you know that financial reporting standards are also going global? International Financial Reporting Standards (IFRS), a set of accounting standards developed by the International Accounting Standards Board (IASB), are becoming the global guide for preparation of public-company financial statements. The Securities and Exchange Commission (SEC) intends to decide on its commitment to IFRS by 2011, and adoption by public companies may then be required between 2014 and 2016. To this end, the IASB and the U.S. Financial Accounting Standards Board (FASB) are working on the convergence of IFRS and U.S. generally accepted accounting principles (GAAP).

IFRS is not just for public companies. The IASB has also developed IFRS for Small- and Medium-sized Entities (SMEs). SMEs are entities that publish general-purpose financial statements for external users and do not have public accountability. Many private companies in the United States would be considered SMEs. These companies do not have the size and resources to implement full IFRS. Therefore, IFRS for SMEs acts as a modification and simplification of full IFRS aimed at meeting the needs of private company financial reporting users and easing the financial reporting burden on private companies. At this time, nonprofits are not addressed by IFRS or IFRS for SMEs.

IFRS for SMEs was issued in July 2009, and the American Institute of Certified Public Accountants (AICPA) accepts IFRS for SMEs as an alternative to U.S. GAAP. Consequently, there is no waiting period – U.S. SMEs may use IFRS for SMEs now, and Certified Public Accountants can report on financial statements prepared in accordance with IFRS for SMEs. However, there is currently no requirement for IFRS for SMEs to be adopted, and no requirement is expected in the future.



If using IFRS for SMEs is not required at this time, and may never be required, then why should companies change? A company may choose to prepare its financial statements in accordance with IFRS for SMEs for a number of reasons. First, because IFRS for SMEs takes a principles-based approach rather than a rules-based approach, adherence to the standards may ultimately be less costly than adhering to U.S. GAAP. Second, due to the focus of IFRS of SMEs on shorter-term cash flows, liquidity and solvency, it may be more relevant to the users of SME financial statements. Finally, companies owned by a foreign parent, or having a significant foreign investor, lender or venture partner may be well-served to conform with international standards.

Though some of the features of IFRS may be appealing to U.S. private companies, taking the leap from U.S. GAAP to IFRS for SMEs will present challenges as well as opportunities. Although companies may have more freedom to present relevant information under IFRS for SMEs, the principles-based focus of IFRS for SMEs requires interpretive judgments that could ultimately impair the comparability of two companies' financial statements, even if both companies are using IFRS for SMEs. The addition of another reporting option further damages comparability – how can a user properly assess two similar companies if one prepares its financial statements in conformity with IFRS for SMEs, and the other adheres to U.S. GAAP? Further, adopting IFRS for SMEs at this point in time may be difficult, given its evolving state and continued debate between the SEC, FASB and IASB on “hot topics” such as fair value accounting.

Decision makers at private companies should familiarize themselves with IFRS for SMEs and carefully consider the pros and cons of potential adoption. Going global may be the right course of action for their companies' financial reporting. ■

### KEY DIFFERENCES BETWEEN IFRS FOR SMES AND U.S. GAAP

#### IFRS for SMEs

#### U.S. GAAP

- |   |   |
|---|---|
| <ul style="list-style-type: none"> <li>• Simplified disclosures for pensions, leases and financial instruments</li> <li>• Use of the LIFO inventory method is prohibited</li> <li>• Amortization of goodwill and indefinite-lived intangible assets is required over a period no greater than 10 years</li> <li>• Simplified temporary difference approach to income tax accounting</li> <li>• Reversal of prior impairment charges permitted under certain criteria</li> <li>• Focus on cost in accounting for financial assets and liabilities</li> <li>• Curing of debt covenant violations after year-end is prohibited</li> <li>• Less extensive guidance for revenue recognition</li> </ul> | <ul style="list-style-type: none"> <li>• Voluminous disclosures for pensions, leases and financial instruments</li> <li>• Use of the LIFO inventory method is permitted</li> <li>• Amortization of goodwill and indefinite-lived intangibles is prohibited; annual impairment tests are required</li> <li>• Complex temporary difference approach to income tax accounting</li> <li>• Reversal of impairment charges is prohibited</li> <li>• Focus on fair value in accounting for financial assets and liabilities</li> <li>• Curing of debt covenant violations after year-end is permitted</li> <li>• Extensive guidance for revenue recognition</li> </ul> |
|---|---|

## FIRST-TIME HOMEBUYER CREDIT REQUIREMENTS INCREASED

Interim IRS statistics indicate that more than 1.7 million returns claiming the 2008 and 2009 First-Time Homebuyer Credits were filed through November 21, 2009, with a total amount claimed of about \$12 billion. If you did not enter into a binding contract to purchase a home by April 30, 2010, time is up for claiming this credit.

One of the most popular tax credits for individuals, the First-Time Homebuyer Credit has also been one of the most widely abused. In response, the *Worker, Homeownership and Business Assistance Act of 2009* authorized the IRS to require the taxpayer to submit a properly executed copy of the settlement statement with the return. The IRS also instituted pre-refund computer filters to prevent fraud. As of Feb. 1, 2010, it had frozen about 140,000 refunds pending civil or criminal investigation, according to the GAO.

Because of the necessary attachments, tax returns that claim the First-Time Homebuyer Credit cannot be electronically filed. Processing these returns could take four to eight weeks. Many taxpayers who claimed the credit on their returns have received notices requesting additional information. The additional information is specified on Form 886-H-FTHBC, *First-Time Homebuyer Credit Supporting Documents*, which requests, in addition to the settlement statement: a copy of the most recent monthly mortgage statement, and a copy of the occupancy permit, if the home is newly constructed.

In addition, a copy of two of the following may be required to verify that the property is the taxpayer's personal residence:

- Driver's license or state-issued identification showing home address.
- Recent pay statement (within the last two months) showing the home address.
- Recent bank statement (within the last two months) showing name and home address.
- Current auto registration showing name and home address.

Attaching these documents to your tax return may prevent processing delays and time-consuming correspondence with the IRS. If you have questions about the new requirements, please call Tressa Holden at 412-338-9300.

## Substantiating the Research Tax Credit

by: Sarah A. Eshleman

The *Economic Recovery Act of 1981* introduced a progressive, general tax credit to U.S. companies. This Research and Experimentation Tax Credit (hereafter, the "Credit"), which is generally equal to 20% of the company's incremental qualified research expenditures, has provided substantial tax savings to many companies in the past years. In contrast to its taxpayer-friendly motive, the guidance, or rather, lack thereof, may discourage some taxpayers from claiming the Credit because they do not fully understand the types of activities that qualify the applicable substantiation requirements.



Because the activities that qualify for the Credit have caused some confusion for taxpayers, it has been the endowed responsibility of tax professionals to translate the tax Credit qualifications to industry professionals. It would be easy to assume a direct association between research and development activities within an organization to the qualifying activities allowed under the Credit. However, as is typical in tax law, there are explicit tests that must be fulfilled in order for an activity to be deemed a qualified "research" expense, and strict, implicit rules that must be followed in order to substantiate an activity's qualification.

The strict documentation rules are a result of the Internal Revenue Service (IRS) having deemed the Credit a "Tier I" examination issue. A Tier I designation indicates the IRS's recognition of the Credit as a "listed" transaction, a designation given to transactions that are often abused and pose a high-dollar risk across a large number of taxpayers. Generally, IRS examinations in this area are extremely difficult, and the IRS routinely denies and/or reduces such claims. The difficulty for taxpayers is that the IRS seems to be holding them to strict documentation standards for which the Service has yet to provide guidance in the Treasury regulations.

As of late, two Tax Court cases have shown some leniency in favor of the taxpayer regarding the use of estimates in the substantiation of the Credit. In one case, the Tax Court ruled in favor of the taxpayer, who maintained that "reasonable substantiation" was sufficient to support claims of qualified research expenses. Specifically, in lieu of detailed time records, the Court accepted oral testimony from company personnel estimating the time they had spent on various projects. In another case, the taxpayer contested an IRS decision to deny their claim based on insufficient documentation. On appeal, the Fifth Circuit reversed the ruling and reinstated a tax refund to the taxpayer.

It is clear that there is a discrepancy between the expectations of the IRS and the Tax Court. A recent report issued by the General Accounting Office has addressed the issues taxpayers face and the potential discouragement these issues pose to a taxpayer when considering whether to claim the Credit. The report asks the Treasury to compose a forum of both IRS and taxpayer representatives to develop a group of standards for substantiation. Since the Credit has lapsed (expired on December 31, 2009) and Congress is currently considering its modification and extension, this may be the opportune time for the provision of such guidance. GYF will keep you updated of any changes to the application and requirements of the credit through tax alerts and posts to our website ([www.gyf.com](http://www.gyf.com)) ■

## Acquiring Basis in S Corporation Shareholder Loans

by: Shawn M. Firster

Unlike a partner in a partnership, who can increase his basis for debts of the partnership, a shareholder of an S Corporation is only permitted to increase his basis in the S Corporation when the debt is directly to that shareholder. Because of this distinction, when shareholders make loans to an S Corporation, it is extremely important that the loans be structured properly and that proper planning takes place to ensure that the shareholders will have sufficient basis to deduct any loss that will be passing through to them from the S Corporation.

To obtain debt basis in a loan to an S Corporation, the Tax Courts have ruled that a shareholder must incur a true economic outlay. That is, to increase the shareholder's basis, there must have occurred a transaction that left the shareholder poorer in a material sense. Generally, the loan should come directly from the shareholder personally and not as an intercompany loan. Even if loans are from other entities entirely or predominately owned by the shareholder, if the loan is not executed directly from the shareholder, it is very likely that the shareholder increase in basis would be disallowed.



Back-to-back loans are sometimes utilized to loan money from another entity in which a shareholder has ownership to the shareholder first; then, the shareholder makes a loan to the S Corporation. While back-to-back loans have been confirmed to increase shareholder basis in an S Corporation in a few court decisions, this scenario will generally be closely scrutinized by the IRS. To support the position of a bona fide back-to-back loan, parties should verify in advance that all initial loan payments and subsequent repayments are directly between the S Corporation and the shareholder. Direct payments between the S Corporation

and the shareholder's related entity should be avoided whenever possible. Journal entries to accurately reflect all items associated with the loans should be recorded on the books of each respective party from the inception of the loans.

Because a shareholder is required to make an "economic outlay" to acquire basis, a scenario in which funds for the shareholder loan to the S Corporation begin and end with the same entity (also called a circular loan) will generally not be found to have left the shareholder poorer in a material sense, and, thus, will not increase his basis.

As an alternative to a loan, if the circumstances exist, the shareholder should consider taking the funds as a distribution from the entity rather than as a loan. The shareholder can then loan the distributed funds to the S Corporation and increase his basis in the S Corporation. This distribution would serve to reduce the shareholder's basis in the other entity, so it is important to ensure adequate basis exists in that entity.

Proper planning is critical to ensure that loans between shareholders and S Corporations are substantiated properly and that the economic outlay requirements will be met. In every situation, it is important to accurately document loans from shareholders to an S Corporation from their origination and maintain the character of a true loan between the parties involved. Promissory notes that are interest-bearing should be drafted, and shareholders should report the applicable interest income on their tax returns. Also, all loans should be contemporaneously documented in the Corporation's minutes. If these measures are not taken, S Corporation shareholders may have pass-through losses disallowed due to basis limitations. ■

**FIND US.  
BEFORE  
WE FIND  
YOU.**



**PAY UP BEFORE JUNE 18**

Time is running out for Pennsylvania tax delinquents to avoid additional penalties by participating in the PA Tax Amnesty program, which ends June 18, 2010.

From now until June 18<sup>th</sup>, the State of Pennsylvania is waiving 100% of penalties and half the interest for anyone who applies for Tax Amnesty and pays eligible delinquent taxes. The program is generally available to all individuals, businesses and other entities with PA tax delinquencies as of June 30, 2009.

"This is an opportunity to avoid paying costly penalties," said PA Department of Revenue Secretary C. Daniel Hassell. "Taxpayers who settle up during Tax Amnesty will avoid additional action taken by the Department of Revenue."

After the PA Tax Amnesty period ends, eligible individuals who did not take advantage of the program to settle back taxes will have a 5% non-participation penalty added to delinquencies and may face other enforcement actions.

Taxpayers must apply for PA Tax Amnesty online at [www.PATaxPayUp.com](http://www.PATaxPayUp.com) – no paper applications are available.

A toll-free hotline and call center is dedicated to the PA Tax Amnesty program. Taxpayers may call 1-877-34-PAYUP from 7:30 am to 7:00 pm, Monday - Friday, and 8:00 am to 4:00 pm on some Saturdays.

[www.PATaxPayUp.com](http://www.PATaxPayUp.com)

If you have questions about basis in S Corporation shareholder loans, please call 412-338-9300

## Uncertain Tax Positions – Are You Ready to Disclose Them?

by: Donald S. Johnston

**E**arlier this year, the Internal Revenue Service issued Announcement 2010-9, wherein it was noted that the IRS is “considering changes to reporting requirements regarding certain business taxpayers’ uncertain tax positions in order to improve tax compliance and administration.” The announcement further noted that the Service is developing a new schedule, which will require certain business taxpayers to report uncertain tax positions on their tax returns. Existing business tax returns do not currently require that taxpayers identify and explain uncertain tax positions included on their returns.

The concept of disclosing an uncertain tax position was developed as part of FASB Interpretation No. 48 (“FIN 48”), which was issued in 2007. After FIN 48, certain business enterprises were required to disclose in their financial statements, the potential tax liabilities related to uncertain tax positions that were previously taken on any (open) tax return. Initially, FIN 48 only applied to publicly-traded entities, but has now grown to include all business entities that issue (GAAP) financial statements.

FIN 48 has created an obligation for companies to identify their uncertain tax positions and determine the level of assurance or likelihood that the position will or will not withstand audit, appeals and litigation scrutiny. Once that is determined, FIN 48 requires companies to disclose and create a reserve for those uncertain tax positions that reach the “more-likely than not” (51%) threshold. With that said, up until now, this has only been a financial statement reporting standard. However, it looks as if the IRS may be moving toward requiring companies to report uncertain tax positions in their tax returns as well.

Announcement 2010-9 is a proposal to create a new schedule that will be filed as part of a business tax return. The new schedule will be required to be filed by a business taxpayer with total assets in excess of \$10 million. The draft copy of the schedule was released by the IRS on April 19, 2010, and it is anticipated that reporting will be required for the 2010 tax year.

It is important to note that this new schedule points to a significantly increased level of required tax return disclosure. Without question, and as pointed out in the announcement, “the information developed in the course of complying with... accounting standards is highly relevant to understanding the taxpayers’ tax positions and assessing how those positions affect the taxpayer’s total tax liability.”

The new schedule will require a concise description of each uncertain tax position in sufficient detail so that the Service can determine the nature of the issue. The sufficiency of a description will depend on the taxpayer’s particular facts and the nature of the underlying transaction. As currently contemplated, this concise description will include the rationale for the position and a concise general statement of the reasons for determining that the position is an uncertain tax position. To be sufficient, the description must contain the following information:

- IRC sections involved;
- The tax year or years to which it pertains;
- Whether the position involves an item of income, gain, loss, deduction or credit;
- Whether the position involves a permanent inclusion or exclusion of an item, or its timing; and
- Whether the position involves a valuation determination or computation of basis.

In addition, the schedule will require a taxpayer to specify, for each uncertain tax position, the entire amount of U.S. federal income tax that would be due, if the position were disallowed in its entirety on IRS audit. This amount is the maximum tax adjustment for the position reflecting all changes to items of income, gain, loss, deduction or credit if the position is not sustained. As such, one may expect that the new form will, effectively, provide a map for Internal Revenue Service examiners pointing directly to any and all material uncertain tax positions.

Note that, while the Service intends to require the reporting of uncertain tax positions, they are proposing to otherwise retain the existing policy of restraint towards summoning tax accrual and other financial audit workpapers.

In the years since FIN 48 was adopted, this ultimate outcome has been expected by practitioners, and the announcement and subsequent release of the tax schedule confirms our anticipated concerns, bringing a new level of disclosure for our clients. ■

**Please call your GYF Tax Executive at 412-338-9300 for assistance in complying with these anticipated new IRS disclosure requirements.**



### PLEASE NOTE THE FOLLOWING CHANGES FOR CORPORATIONS FILING TAX RETURNS IN PENNSYLVANIA

The **corporate net operating loss (NOL) deduction** was limited to the greater of: 12.5% of taxable income or \$3 million. For 2009 and 2010 the percentage was increased to 14% and 20%, respectively. The **capital stock tax phaseout** was extended from 2011 to 2014. The 2008 rate of 2.89 mills will apply to tax years 2009-2011. The rate will decrease to 1.89 mills in 2012 and .89 mills in 2013. In addition, the **capital stock tax exemption** is increased from \$150,000 to \$160,000.

## MACRS Depreciation Rules, Section 179 Limits and the Lapse of Bonus Depreciation

by: Nicholas A. Mannerino

Most business assets placed in service after 1986 are depreciated over defined useful lives under the Modified Accelerated Cost Recovery System (MACRS.) The MACRS depreciation method only applies to new and used tangible depreciable property, which includes buildings, land improvements and equipment used in a trade or business or held for the production of income that has a determinable life. Land, intangible assets, and personal use assets cannot be depreciated under MACRS, although most purchased intangible assets can be amortized on a straight-line basis over 15 years.

Other special rules included in the Internal Revenue Code (IRC) allow for additional depreciation in certain situations. Over the last several tax years, two significant incentives were made available to business taxpayers making capital expenditures: bonus depreciation, also known as [IRC] Section 168(k) bonus depreciation, and an increased “expensing” allowance under [IRC] Section 179. Both of these incentives were added to the tax law to motivate investment in capital expenditures, which, in turn, would lead to job creation. The *HIRE Act* (see article on page 3) extends the Section 179 provision through 2010. Unfortunately, the law providing for bonus depreciation was allowed to expire as of December 31, 2009.

IRC Section 179 is a non-mandatory election that allows taxpayers to immediately deduct the cost of qualifying property placed in service during the current year as an expense on their income tax returns, rather than capitalizing the property as an asset that is gradually depreciated over a certain period of time. Generally, qualifying property consists of tangible personal property used fully or partially for business. The types of property ineligible for the election include real property, rental/investment property, inherited property, and intangible property (including certain computer software), among others. Property does not need to be brand new (original use) to qualify as a Section 179 expense – it must only be new to the taxpayer’s business. Also, the full Section 179 deduction can be taken even if the eligible property was placed in service on the last day of the year.

The Internal Revenue Code imposes a cap on allowable Section 179 expenses. In 2008 and 2009, taxpayers were permitted to deduct up to \$250,000 of most types of qualifying property placed in service. Furthermore, the maximum permitted Section 179 deduction is reduced dollar-for-dollar for the cost of most types of qualifying property placed in service exceeding a certain threshold amount. For 2008 and 2009, this threshold was \$800,000. Under the 2010 *HIRE Act*, these \$250,000 and \$800,000 limits remain unchanged.



Application of the Section 179 deduction is illustrated below:

ABC, Inc., a C Corporation, places the following assets in service during 2010:

Factory Equipment .....	\$ 850,000
Computer Equipment .....	\$ 10,000
Leasehold Improvements.....	\$ 25,000

The Section 179 deduction allowable for 2010 is \$190,000 [\$250,000 maximum deduction – (\$860,000 total cost of qualifying property – \$800,000 threshold)]. Note that leasehold improvements are not qualifying Section 179 property. Also note that the allowable deduction does not take into consideration what is known as the income limitation discussed below.

A final restriction to the amount of Section 179 expense a business can deduct is the taxable income limitation. Businesses operating as C Corporations cannot claim a Section 179 deduction that would either create or increase a tax loss for the year. In other words, the deduction is limited to the amount of corporate taxable income before the deduction. For a sole proprietorship, partnership, LLC or S Corporation, these deductions are passed through to the owner and written off on the owner’s personal Form 1040. Keep in mind that the \$800,000 property-placed-in-service limit and the taxable-income limit apply at both the pass-through entity level and the individual owner level. This means that pass-through members/partners must separately apply the \$250,000 and \$800,000 limits on their own Form 1040 tax returns, and that individuals cannot claim Section 179 deductions that would create or increase an overall business tax loss on their Form 1040.

Pennsylvania tax law currently conforms to Federal Section 179 rules for regular C Corporations, so the calculation used for federal taxable income is also used in the calculation of PA Corporate Net Income. However, the Section 179 expense is limited to \$25,000 under the Personal Income Tax law. Conformity of other states to federal rules varies, and should be checked.

Even bigger changes have occurred in regards to Section 168(k) bonus depreciation. The *Economic Stimulus Act of 2008* and the *American Recovery and Reinvestment Tax Act of 2009* permitted taxpayers to immediately deduct 50% extra (i.e. “bonus”) depreciation of the adjusted cost (following any Section 179 elections) of brand new qualifying property placed in service under IRC Section 168(k). Generally, bonus depreciation was allowed for qualified new “original use” leasehold improvement property. Intangible property, with the exception of certain computer software, was ineligible. Unfortunately, as noted earlier, this provision expired as of the end of 2009. Therefore, as of the print date of this article, the 50% bonus depreciation is not permitted for 2010. ■

## RETIREMENT – AN ILLUSION OR A DIFFICULT POSSIBILITY?

During the course of the past couple of years, both companies and individuals have been re-evaluating retirement. Many companies have reduced contributions to employee benefit plans in light of the economic downturn. Similarly, employees may have adjusted their contributions to plans and many have had to seriously consider deferring retirement because of decreased savings, higher costs of retirement and longer life expectancies.

In its 2009 *Benefits and Talent Survey*, Aon Consulting reported the following interesting statistics, which were compiled from 1,313 responding companies:

- 87% of employers said that their employees are delaying retirement
- More than a third of the employers reported that 70% of their employees are enrolled in their plans. The majority of responding companies felt that those not participating had decided it was not affordable to participate.
- Only 8% of employers felt that employees had a strong understanding of the resources needed for retirement.

The ability to retire is dependent on important choices that each individual must make, many of which involve sacrificing current lifestyle items for deferred rewards, something that is not easily achieved. Like most things, achieving retirement is dependent on purposeful decisions, a commitment to a plan and starting the saving process early.

While employees must evaluate the benefits provided by employers, as well as social security income, recognition also needs to be given to savings outside of retirement accounts to achieve the results that are hoped for in the golden years. Calculators and other information available through various financial web resources can be a good start in ascertaining what will be needed in retirement and will usually need to be supplemented by professional advice to make good decisions.

Source: **Aon Consulting** ([www.aon.com](http://www.aon.com))

## Using Social Media as a Business Tool

by: *Karen T. Mangis*

Over the past few years, social media has rapidly evolved and is as commonplace as the cell phone. For many organizations the use of social media is an integrated part of their overall business strategy. This article is the first in a series on the topic of social media and business. Following this high-level overview of the benefits of using social media, future articles on the topic will focus specifically on marketing usage and measurement as well as strategies and concerns.

On the surface, “social” media does not sound very corporate, and in its early days, it was not. Social media was primarily an avenue for people seeking friendship on the internet. Some people consider dating sites to be the first social networks since they allowed users to post a profile and contact other users. However, the first modern social network was Six Degrees, which was in existence between 1997 through 2001, and during its run was quite popular.



Today there are social and user-generated sites for almost anything you can think of; for example, shopping sites, financial planning sites, and sites that provide information and feedback of a wide range of topics. Hence, savvy businesses have begun to realize the value of linking up with others via the vast array of available networks. The most well-known sites – My Space,

Facebook and Twitter – contain some business pages, but are typically used for social content. The top business and professional social networks are LinkedIn, Plaxo and Ryze. These social media outlets provide a new and innovative way to keep in touch with customers, vendors, contacts and many others. The social networking benefits available to business are many, but a few are detailed below.

- ***Marketing and Public Relations*** – Social media provides several advantages over traditional public relations methods. News and announcements are communicated much more quickly via social media than is possible with standard written press releases. Online blogs and forums help customers, prospects and contacts develop a sense of community. This comfortable atmosphere leads to a more open dialogue, providing businesses with better insight about how best to meet customer needs.
- ***Customer Service*** – Many customers are very receptive to using social media sites that provide a convenient, alternative way of communicating with a company. Customers save time and money they may have spent making a phone call and waiting on hold for a response or writing an email and waiting for a reply. With social media vehicles, they can send a short tweet, direct message or post.
- ***Talent Search*** – Believe it or not, social media is the new platform for recruiting and career development. Human resources professionals can leverage social media to reach potential candidates. Recruiters are using social media sites to connect with like-minded individuals to fill voids in their organizations. Additionally, the open and informal chatter exchanged online helps recruiters learn more about a candidate’s character as well as talents.
- ***Competitive Research*** – Social media is a means to follow what competitors are doing and saying, and better yet, what their customers are saying about them. This information can help a company to identify ways to differentiate its products and services.

For more information about social media, please contact Karen Mangis at 412-338-9300.

## Major Health Care Reform Enacted (continued from page 2)

### Provisions Effective in 2013

- **Additional Taxes for Higher-Income Taxpayers** – Beginning in 2013, two new taxes will be levied on higher-income taxpayers. The employee portion of the hospital insurance (HI) tax rate will be increased by 0.9% for employees who earn wages over \$200,000 (\$250,000 married filing jointly; \$125,000 married filing separately\*). Similarly, an additional HI tax of 0.9% will be imposed on self-employment income in excess of \$200,000 (\$250,000 married filing jointly; \$125,000 married filing separately\*) reduced (but not below zero) by wages taken into account to determine the FICA tax with respect to the taxpayer. \*Note: these thresholds are not indexed for inflation.

In a double-whammy for high wage-earners, an additional surtax will be charged on net investment income. Starting in 2013, taxpayers with modified adjusted gross income (MAGI) over \$200,000 (\$250,000 for a joint return or \$125,000 for married filing separate) will be subject to this *Unearned Income Medicare Contribution*. Specifically, the tax equals 3.8% of the lesser of the following amounts:

- Net investment income (interest, dividends, royalties, rents and gains on the sale of investment property).
- The excess of MAGI over \$200,000 (\$250,000 for joint filers; \$125,000 for married filing separately). MAGI is AGI increased by the amount excluded from income as foreign earned income, net of deductions and exclusions disallowed with respect to the foreign earned income.

This tax also applies to estates and trusts, equalling 3.8% of the lesser of: undistributed net investment income; or the excess of AGI over the dollar amount at which the highest estate and trust income tax bracket begins.

- **Medical Expense Deductions & Contributions** – The threshold for the itemized deduction for medical expenses for regular income tax purposes will be increased from 7.5% to 10% of AGI beginning in 2013. However, for 2013-2016, if the taxpayer or his/her spouse turns 65 before the end of the tax year, the increase will not apply.

Also starting in 2013, the maximum amount an individual can contribute to an employer-provided health FSA will be \$2,500 per year. Note, however, that health FSA plans can (and typically do) limit contributions to an amount that is already less than \$2,500 per year.

- **Retiree Drug Coverage** – Prescription drug coverage, provided by employers for Medicare Part D eligible retirees, is subsidized by the government. This subsidy, which is excluded from the company's income, previously, did not reduce the deduction allowed for the payment. Starting in 2013, the subsidy will reduce the allowed deduction.

### Provisions Effective in 2014

- **Penalty for Not Having Health Insurance Coverage** – Beginning in 2014, most U.S. citizens and legal residents will be required to maintain health care coverage or pay a penalty based on their household income and the number of uninsured individuals in the household. Individuals who, based on household income, cannot afford coverage under their employer-sponsored health plan are exempted from the penalty, as are individuals who reside outside the U.S. and those with certain religious beliefs. This penalty is intended to entice individuals to obtain health insurance. Payment of the penalty does not entitle them to any health insurance coverage.
- **Health Care Cost-Sharing Subsidies (or Tax Credits)** – A cost-sharing subsidy (or tax credit) will be provided to low-income individuals to help cover health insurance costs. Individuals and families with incomes up to 400% of the federal poverty level (\$43,320 for an individual or \$88,200 for a family of four for 2009) that are not eligible for Medicaid, employer-sponsored insurance, or other acceptable coverage can obtain cost-sharing subsidies or tax credits that can be used to reduce premiums for health insurance obtained through the newly established state-run insurance exchanges.
- **Penalty for Employers Not Offering Coverage** – Beginning in 2014, large employers (generally, with an average of 50 full-time employees during the preceding calendar year) that do not offer health insurance coverage for all full-time employees, or offer unaffordable or inadequate coverage, will be assessed a penalty if any full-time employee uses a tax credit or cost-sharing subsidy to purchase health insurance through a state-run insurance exchange. Any penalty paid under this provision is not deductible as a business expense.
- **Free Choice Vouchers** – Starting in 2014, employers that pay a portion of their employees' health insurance coverage must provide certain low-income employees who do not participate in the plan with a voucher (for the amount the employer would contribute to the employer-offered plan) that can be applied to purchase health insurance through a state-run insurance exchange.

### Provisions Effective in 2018

- **Excise Tax on High-Cost Plans** – In 2018 a nondeductible excise tax will be assessed on employer-sponsored health plans with annual premiums exceeding \$10,200 for single coverage and \$27,500 for family coverage (higher thresholds apply for retired individuals 55+ and those in high-risk professions). This tax will be levied at the insurer level. ■



## *Planning with Life Insurance – Important Points to Consider*

*by: Robert J. Grossman*

**L**ife insurance is often viewed as merely a necessary evil in planning for one's financial protection. However, properly used, life insurance policies can grow to constitute a substantial portion of personal wealth and can be used to accomplish any number of financial and economic objectives. The key to successful utilization of life insurance policies to meet these objectives is to monitor evolving needs, goals and products. The steps outlined below are intended to serve as a roadmap to understanding how best to monitor this evolution. Planning with life insurance is a complex process, and final decisions should not be undertaken without consulting an insurance professional or financial advisor for advice and confirmation.

1. ***Review all current policies*** – This initial step should be undertaken with a focus on the reasons for obtaining the policies in the first place. Items to consider in this review include an assessment of your needs, goals and objectives at the time the policy was acquired. If these needs, goals and objectives have changed, it is likely that some modification of the policies might be in order.
2. ***Address estate tax exposure*** – Next, the focus should turn to understanding the estate tax exposure on property transfers at death. At the present time, this is somewhat difficult, given the elimination of the federal estate tax in 2010. However, taxpayers can and should expect the tax to return, in some form, no later than 2011. Currently, it appears reasonably possible that the 2009 federal lifetime estate tax exclusion of \$3.5 million will be reinstated. As such, if the objective of the policy is to provide funds to cover estate taxes, some modification may be appropriate, dependent upon current estate values and the reinstated level of exemption.
3. ***Evaluate policy structure*** – It is also important to review the policy design, as the structure has changed dramatically over time. For those looking for life insurance to provide only a death benefit, it might not be necessary to pay higher premiums for a more complex policy providing cash value accumulations for enhanced retirement income.
4. ***Analyze performance*** – Another key step is to conduct analysis of the insurance policy's actual performance versus projections prepared at the policy's outset. Volatility in investment returns could lead to variance in premium outlays. It is also prudent to check the financial well-being and credit quality of the insurance company underwriting the policy. Credit-worthiness is easy to obtain through insurance company rating services. Moreover, it may be wise to review the insurance company's current financial statements.
5. ***Identify policy ownership*** – For estate tax purposes, a policy owned by the insured party is includable in his/her estate. Other entity structures that prevent this inclusion should be considered for policy ownership. Most common among these alternatives is an irrevocable life insurance trust.
6. ***Verify advisor independence*** – Finally, when choosing an insurance professional or other financial advisor, it is important to make certain that he/she is completely independent of certain products and companies. This measure will help ensure that the planning is undertaken in the most comprehensive and objective manner.

**These few steps, periodically followed, will serve to optimize use of life insurance in financial planning. If you have any questions regarding these issues, please contact Bob Grossman at 412-338-9300.**

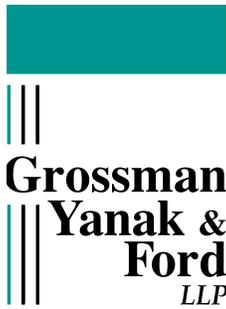
### **IRS LAUNCHES HIGH-WEALTH TASK FORCE AND PREPARES TO BEGIN AUDITS**

Last October, the Internal Revenue Service (IRS) announced an initiative targeting high-wealth individuals. No formal definition of "high-wealth individuals" has been determined, but the IRS will initially focus on those with tens of millions of dollars in assets or income.

Although the IRS has always targeted high-income taxpayers, prior efforts typically involved identifying single returns for audit based on the usual scoring systems for audit selection. The newly-formed Global High Wealth Industry Group will look at everything connected to a single taxpayer, including trusts, private foundations, partnerships, equity-sharing arrangements, royalty and licensing agreements and privately-held and related entities where the taxpayer may have ownership interests. The IRS has already hired flow-through specialists and international examiners for the team and is considering adding economists, appraisal experts and industry specialists.

This new program will concentrate on compliance efforts for high-wealth individuals because of the sophisticated financial, business, and investment arrangements with complicated legal structures and tax consequences the IRS has to examine. The task force will take an integrated approach to its audits by focusing on all business entities controlled by a wealthy individual, especially arrangements involving offshore structures, foreign income sources and tax residency implications. Many other countries utilize similar specialized high-wealth tactics.

*If you have any questions or need assistance preparing for an IRS audit, please contact your GYF Tax Professional at 412-338-9300.*



Three Gateway Center

Suite 1800

Pittsburgh, PA 15222

Ph: 412-338-9300

Fax: 412-338-9305

[www.gyf.com](http://www.gyf.com)

[CPAs@gyf.com](mailto:CPAs@gyf.com)

Certified Public Accountants

*Quality you deserve!*

---

If you would like additional copies of this newsletter or to add your name to our firm's mailing list, call Mary Lou at 412-338-9300.

---

## News About Us

---

Congratulations to *Adam Smith*, who recently passed all sections of the CPA exam. He is working to meet his experience requirements before officially becoming a Certified Public Accountant.

*Susan Harry* was nominated to serve on the PICPA's CPA Image Enhancement Committee for 2010-2011. This statewide committee is charged with helping the PICPA team with advertising and public relations endeavors.

*Chris Anderson* and her husband, Don, are proud to celebrate their son's graduation from Franklin Regional Senior High School on June 11, 2011. John will attend Duquesne University this fall, majoring in Biology.

*John Yanak* and his wife, Becky, proudly celebrated their son's wedding. Jay Yanak married Lissa Swanson on February 27, 2010 – during a big snowstorm in Jamestown, New York!

### *GYF is pleased to welcome our new professionals:*

*Amy Mattie*, a graduate of Robert Morris University, joins the Business Valuation Services Group as a Manager, bringing over 11 years of experience to the firm. Amy and her husband, Tom, live in Sewickley with their sons, Hunter and Noah. She stays busy as a hockey mom and also enjoys reading.

*Steve Dasta* recently joined the Technology Services Group as a Business Systems Consultant. Steve, a graduate of Robert Morris University, has over five years of IT experience as well as a year of accounting experience. He enjoys golf, exercising and walking his dog in his South Hills neighborhood.

## NEWSLETTERS VIA EMAIL

By choosing to receive your *GYF Perspectives* newsletter electronically, not only will you help us to conserve paper, but you will also enable us to send you time-sensitive tax information and other updates in an efficient manner.

We will utilize email to send you future GYF newsletters, tax alerts, invitations and other pertinent information. To choose the paperless option, simply email your request to Mary Lou Harrison at [harrison@gyf.com](mailto:harrison@gyf.com).

Thank you to our clients and friends who have selected this option!

Questions? - Call GYF:  
412-338-9300

