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BEAN KINNEY & KORMAN PC
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# Business Law Newsletter

## TAX LAW

### YEAR-END PLANNING

**By Ronald A. Feuerstein**

2007 year-end tax planning will be more challenging than usual due to uncertainty over whether and how Congress will extend Alternative Minimum Tax ("AMT") relief. Another unknown is whether Congress will extend a number of important tax benefits expiring at the end of 2007. For individuals, these include the option to deduct state and local sales and use taxes; the above-the-line deductions for qualified tuition expenses and educator expenses; the tax credit for making qualifying energy saving improvements to a home, such as insulation and energy-saving windows; and the ability for individuals who have attained age 70 1/2 to exclude up to $100,000 a year for otherwise taxable distributions from an IRA (or a Roth IRA) that are paid directly to a qualifying charitable organization by the IRA trustee.

For businesses, tax breaks that will expire at the end of this year, unless they are extended by Congress, include the research tax credit, faster write-offs for leasehold and restaurant improvements and enhanced deductions for certain contributions to charity.

For your information and reference, we are providing a checklist of actions that may help you save taxes if you act before year-end. Not all actions will apply to everyone, or every business entity, but you will likely benefit from many of them. A review of your specific circumstances will allow us to tailor your particular plan. In the meantime, the following tax-saving options may be available and appropriate to your needs:

- Increase the amount you set aside for next year in your employer's health flexible spending account if you set aside

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**Year-End Planning**

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- too little for this year. Remember that your tax-free set aside may include reimbursement for over-the-counter drugs, such as aspirin.
- If you have any capital gains or losses from sales of stock or other capital assets, or if you have stock or other capital assets that are ripe for sale, you should carefully calibrate your gains and losses to minimize tax on your gains and maximize the tax benefit from your losses.
- If you or a family member are thinking of selling appreciated stock or other capital assets, and your (or their) income is not taxed at a rate higher than 15%, it may be advantageous to defer the sale until 2008. In that way, the gain should be non-taxable; if the sale occurs this year, there would be a 5% tax on the gain.
- It may be advantageous to arrange with your employer to defer a bonus payable this year until 2008 (assuming compliance with Internal Revenue Code section 409A).
- If you own an interest in a partnership, multi-member LLC or S corporation, you may need to increase your basis in the entity so you can deduct a loss from it for this year.
- Consider using a credit card to prepay expenses that can generate deductions for this year.
- If you are thinking of making energy saving improvements to your home, such as putting in extra insulation or installing energy saving windows, consider doing so before year end in order to qualify for a tax credit that may not be available after 2007.
- If you are thinking of buying a hybrid automobile eligible for a tax credit, purchase it before year-end after confirming that the particular model still qualifies for the credit.
- Businesses should consider making expenditures that qualify for the $125,000 business property expensing election.
- You may want to settle an insurance or damage claim in order to maximize your casualty loss deduction this year.
- You may be able to save taxes this year and next year by applying a bunching strategy to "miscellaneous" itemized deductions, medical expenses and other itemized deductions.
- Those facing a penalty for underpayment of estimated tax may be able to eliminate or reduce it by increasing their withholding.
- Self-employed individuals should consider setting up a self-employed retirement plan.
- You can save gift and estate taxes by making gifts sheltered by the annual gift tax exclusion before the end of the year. You can give $12,000 in 2007 to an unlimited number of individuals, but you cannot carry over unused exclusions from one year to the next.
- This year, the so-called "kiddie tax" rules apply to children under age 18; next year they will also apply to most children age 18 and most full time students age 19 through 23. If your child holds appreciated stock, and is not subject to the kiddie tax this year, but will be in 2008, consider having him or her sell the stock this year. In many cases, this will result in a 5% tax on the gain, instead of 15% if the sale is postponed until next year.
- If you are thinking of donating a used automobile to charity, you should inquire whether the charity plans to sell the car or use it in its charitable activities; the latter will most likely yield a larger deduction.
- If you are contemplating marriage or divorce, consider how the "marriage penalty" could affect you.

## Year-End Planning

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- If you are age 70 1/2 or older and own IRAs (or Roth IRAs) and are thinking of making a charitable gift before year-end, arrange for the gift to be made directly by the IRA trustee. Such a transfer can achieve important tax savings, but will not be available after 2007 under current law.
- If you are receiving Social Security benefits, there are a number of steps you can take to reduce or eliminate tax on your benefits. Consider asking your employer to increase withholding of state and local taxes to pull the deduction of those taxes into this year (but only if doing so will not cause an AMT problem).
- Consider extending your subscriptions to professional journals, paying professional dues, enrolling in (and paying tuition for) job-related courses, or paying other expenses in order to bunch into 2007 miscellaneous itemized deductions subject to the 2%-of-AGI (adjusted gross income) floor.
- Depending on your particular situation, you may also want to consider deferring a debt-cancellation event until 2008, electing to deduct investment interest against capital gains, and disposing of a passive activity to allow you to deduct suspended losses.

If we can help you with your personal or business year-end tax planning, please contact us.

## Change in Virginia Grantor Tax

As a result of the recently enacted Virginia Congestion Relief Bill, certain real estate filing fees will be increased, effective July 1st 2008. The increase will not affect all of Virginia, but only certain communities in Northern Virginia and the Tidewater area. In the counties of Arlington, Fairfax, Loudoun and Prince William and in the cities of Alexandria, Fairfax, Falls Church, Manassas, and Manassas Park an additional 40 cents per $100 will be charged in addition to the current grantor's tax of $1.00 per $1,000, for a total grantor's tax of $5.00 per $1,000. The congestion relief fee for the tidewater area will be increased to $4.00 per $1,000. The tidewater increase applies to the counties of Isle of Wight, James City, and York, and the cities of Chesapeake, Hampton, Newport News, Norfolk, Portsmouth, Suffolk, Virginia Beach, and Williamsburg. For all other Virginia counties, grantor's tax will continue to be $1.00 per 1,000 dollars by statute, the grantor's tax continues to be payable by the seller.

## New I-9 Requirements for Employers

On November 8th, 2007 the U.S. Immigration Service published a new I-9 form. All employers must use this form for all new hires, and for certain employees whose continuing employment authorization must be verified anew. While a law requiring employers to complete I-9's verifying the identity and employment of all new hires has been on the books since 1986 but it has only recently been enforced with regularity. The law applies to all employers regardless of the number of employees.

## Virginia Non-Resident Owner Withholding Rule

Effective for tax years beginning on or after January 1st, 2008, the Virginia Non-Resident Owner Withholding Rule applies to all pass through entities such as partnerships, LLC's, or Sub S corporations doing business in Virginia and having owners that are not Virginia residents. The new law requires such entities to pay withholding tax equal to 5% of the non-resident owner's share of taxable income from Virginia sources. The Department of Taxation has not yet issued requirements for quarterly estimated payments, or other advanced payments and has yet to publish forms for filing

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and paying the tax, or for claiming exemptions. These forms should be available after the 1st of the year. Tax liability will be determined annually without regard to whether or not the pass through entity has withheld required amounts. The withholding tax must be paid and return filed on the 15th day of the 4th month following the closing of the tax payee's taxable year. In 2008, if the pass through entity seeks an extension at least 90% of the tax due for 2008 must be paid by the original due date, in order to avoid a penalty. In subsequent years, the pass through entities will be required to pay either 90% of the tax due for the taxable year, or 100% of the tax due for the prior year, if that was a taxable year of 12 months and withholding tax was paid for the taxable year. Paid withholding tax is to be accounted as a distribution to the owner and not as a deduction from the firm's income.

*U.S. Treasury Circular 230 Notice: Any tax advice contained in this communication (including any attachments) was not intended or written to be used, and cannot be used, for the purpose of (a) avoiding penalties that may be imposed under the Internal Revenue Code or by any other applicable tax authority; or (b) promoting, marketing or recommending to another party any tax-related matter addressed herein. We provide this disclosure to assure compliance with new standards of professional practice, pursuant to which certain tax advice must satisfy requirements as to form and substance.*



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