

Breaking News – New Tax Incentive Package

The individual tax rebates contained in the Economic Stimulus Act of 2008 have received much attention in the media, but not nearly as much attention has been paid to the Act's business tax incentives. The purpose of this message is to briefly explain the business tax incentives.

The intent of the Act was to encourage immediate spending in the hope that a recession can be prevented or at least shortened. Much as the individual rebates are intended to spur consumer spending, the business incentives are intended to cause businesses to purchase machinery and equipment.

The Act contains two provisions that can reduce the after-tax cost of purchasing equipment:

1. An increase in the amount of property that can be expensed in the year of purchase under Code Section 179, and
2. An additional first-year bonus depreciation deduction equal to 50% of the cost of qualified property. Section 179 applies to tangible personal property used

in a trade or business. In addition, off-the-shelf computer software also qualifies through 2010. Prior to the Act, the maximum amount that a taxpayer could expense under Section 179 in 2008 was \$128,000, and this amount was reduced dollar-for-dollar by the amount of qualified property additions over \$510,000. For example, if \$600,000 of qualified property was placed in service, the maximum section 179 deduction was \$38,000 [$128,000 - (600,000 - 510,000)$].

THE ACT CONTAINS TWO PROVISIONS THAT CAN REDUCE THE AFTER-TAX COST OF PURCHASING EQUIPMENT

Under the Act, the maximum amount that a taxpayer may expense for property additions in tax years beginning in 2008 is \$250,000 and the phase-out applies if qualified property additions exceed \$800,000. For example if \$600,000 of qualified property is placed in service in 2008, the maximum Section 179 deduction

is \$250,000. In our example the effect of the Act is to increase the maximum Section 179 deduction by \$212,000.

The additional first-year depreciation deduction applies to property placed in service in 2008 regardless of the tax year. And it applies only to MACRS property with a recovery period of 20 years or less, computer software, water utility property and qualified leasehold improvement property. Note that the original use of the property must commence with the taxpayer. (In other words, it must be new property as opposed to used property.)

Note that the above is intended to be a general guideline only. As with any tax law change, there is much fine print that can affect the deduction amount in certain cases. If the provisions in the Act may cause you to revise your planned purchases, please consult with us beforehand to ensure that you receive the maximum benefit.

Don't hesitate to call us if you have any questions.

A New Year, A New Look and A New Website!

Ring in 2008 with a bang, KOS is excited to introduce our "new identity" – an updated look for our overall image. It's a fresh, new attitude. You can see the revamped KOS brand on our new stationery, print materials and most definitely at our website www.koscpa.com.



This redesign corresponds with our firm's very deep interest in maintaining focus on the right things: performing above and beyond for you, staying proactive with you, and looking out on behalf of you. We've certainly always cared about these things, but we have set about to internalize this focus as much as externalize it to assure we deliver each with greater consistency. We are passionate and enthusiastic about earning "exceptional firm" status in your eyes.

You can read our formal Service Commitment on our website in the About section:

<http://www.koscpa.com/Service-Commitment.html>. It stays there, front and center, for good reason.

In our December newsletter, we shared with you the results of our 2007 client survey and our intended changes, which were inspired by your responses. This clarified and renewed service commitment is just one

component of the enhancements we pledged to make this year.

Our new look is not just a token branding effort, but truly a reminder to ourselves and to you of the promises we've made. For any organization, living a brand internally is essential to the impressions you make externally.

Most importantly, we're confident these changes and our other forthcoming improvements will have an increasingly positive impact on the results we help you achieve.

Very Truly Yours,

Jeffrey Arnol, Managing Partner

Late AMT Reprieve for 2007 Filers

A tax law change enacted in the waning days of 2007 has saved a multitude of taxpayers from a dire tax fate. The new tax legislation increases the exemption amounts included in the complex alternative minimum tax (AMT) calculation on 2007 returns. It is expected to protect approximately 19 million taxpayers from the AMT and reduce the tax bite for over 4 million others.

BASIC PREMISE

The AMT runs on a separate track beside your regular tax liability. After you have figured out your regular taxable income, AMT liability is calculated using four basic steps:

- First, you must add certain tax preference items to your taxable income and make other technical adjustments required by law.
- Then you subtract the special exemption amount based on your filing status on your income tax return.
- Next, you apply the AMT rate to the net amount. For the 2007 tax year, the applicable rate is 26% on the first \$175,000 of AMT income and 28% for amounts above \$175,000.
- Finally, you compare your AMT liability with your

regular tax liability. If the AMT amount is higher, you are required to pay the excess, in addition to your regular tax liability.

The list of preferences and technical adjustments is too long for the space allotted here. In brief, you are required to add back certain itemized deductions and personal exemptions. This is one reason why large numbers of taxpayers have become unsuspecting victims of the AMT. For instance, taxpayers who report high state income tax deductions are particularly vulnerable.

A SHORT HISTORY

Ever since the monumental Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001 was passed, Congress has tweaked the exemption amounts to account for inflation in a series of short extensions. The latest increase is effective only for the 2007 tax year. Unless subsequent legislation is enacted, the exemption amounts will return to the pre-EGTRRA levels. Thus, you could be facing similar challenges in 2008.

Under the new law, the exemption amount for joint filers in 2007 is \$66,250 (up from \$62,550). If you are a single filer, the exemption amount is \$44,350 (up

from \$42,500). Finally, the amount for married couples filing separately is \$33,125 (up from \$31,275).

However, the benefit of these exemption amounts is reduced for certain high-income taxpayers. Each exemption is reduced by 25 cents for each dollar of AMT income over \$150,000 for joint filers; \$112,500 for single filers and heads of household; and \$75,000 for married couples filing separately. These figures have not been adjusted in recent years.

Also, be aware that the change occurred too late for the IRS to include in its 2007 tax return packages. It will also take time for the IRS to reprogram its systems and make changes in all AMT-related forms. Consequently, the new law is expected to result in delays in processing refunds for certain taxpayers.

This is an extremely complex area of the tax law. It is recommended that you seek our assistance at your earliest convenience.



IRS Serves Up New Cafeteria Plan Regulations

A so-called “cafeteria plan” generally allows the employees of a company to choose from a wide variety of tax-free fringe benefits. The result is a two-way winner.

(1) The employees opt for those benefits that best fit their situation.

(2) The employer may reduce its overall costs by providing only those fringe benefits that the employees choose. Both sides can come out ahead on the deal.

Now the IRS has issued new proposed regulations that provide some much-needed guidance in this area.

BASIC CONCEPT

Typically an employer sets up a written cafeteria plan and notifies its employees. Those who participate must be given a choice between at least two options.

The available benefits are those that employees are permitted to receive tax-free under law. Employees can also be given the option to receive cash in lieu of some or all of the available benefits.

The employer generally will pay for certain benefits, such as basic medical and disability coverage. The employee then customizes the rest of the benefits package by choosing the “extras” such as dental coverage and up to \$50,000 of group-term life insurance coverage.

The new proposed regulations cover the following points:

NONDISCRIMINATION RULES

Any tax-free fringe benefits that are provided to highly compensated employees and key employees are treated as taxable income if the cafeteria plan is discriminatory in nature. The new regulations impose tests concerning eligibility, contributions and benefits. Previously, there was no substantive direction in this area.

PLAN BASICS

A cafeteria plan must be formally established in writing. Only employees may participate, but former employees may be allowed to participate if they do not predominate. Sole proprietors, partners, corporate directors and 2%-or-more shareholders of S corporations are not treated as employees for this purpose.

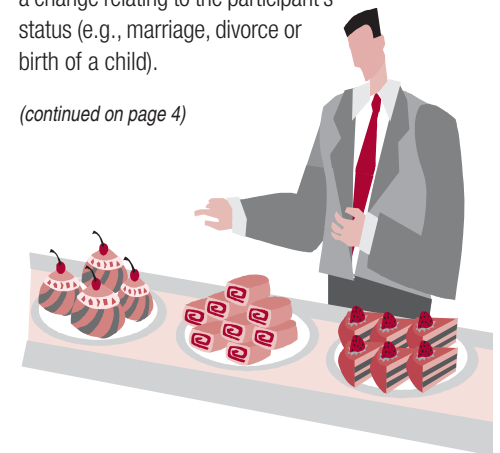
BENEFIT OPTIONS

A cafeteria plan enables an employee to choose from a statutory tax-free benefit or a taxable benefit. The new regulations state that such a plan is the only mechanism that may be used for this purpose. This was not entirely clear under prior regulations. Furthermore, a cafeteria plan will be treated as having violated the rules if it offers a taxable fringe benefit.

ELECTION OF BENEFITS

The election to choose a specific benefit must be made by the earlier of the first day of coverage or when benefits are first available. This irrevocable election cannot be revised during the year unless there is a change relating to the participant's status (e.g., marriage, divorce or birth of a child).

(continued on page 4)



TIPS, TRAPS & TRENDS

IRS AUTHORIZES LATE "S" CORPORATION ELECTIONS

As a general rule, you must elect S corporation status for a business entity by the 15th day of the third month of the tax year. Therefore an election for 2008 must be made by March 17 (March 15 falls on a Saturday). Otherwise, you have to wait until next year.

However, under certain conditions, you may be able to obtain tax relief for a late election. Previously, the IRS required taxpayers to request a private letter ruling. Now it has authorized a simplified method for certain taxpayers.

To qualify for this special tax relief you must have "reasonable cause" for failing to file in a timely manner, among other requirements. In addition, shareholders must treat their returns in a consistent fashion. We can provide the necessary guidance in this area.

FIVE WAYS TO SPEED UP YOUR COMPUTER

"My computer is running way too slowly." This is a common complaint among PC users. But you don't necessarily have to trash your machine in frustration or run out and buy a new one. Here are five basic tips for improving performance.

If you run Windows and you use the Internet, you should keep up-to-date with system patches concerning privacy and security issues. To obtain fixes and configure your system for automatic updates, open Internet Explorer, click on Tools and then Windows Update.

A good antivirus program featuring automatic updates can help out. Viruses and bad software programs can slow down your system because they take resources to generate popup ads and often interfere with the operation of good programs.

You may have software packages on your hard drive that are no longer needed or never were. This might include toolbars, file-sharing programs, free e-mail enhancers, online shopping "companions" and download managers. They can put an unnecessary drag on your computer. Go to the Control Panel and view the Add/Remove Software to see what packages

are installed. Search online to find out what you need and what you don't.

Both Windows and application programs leave temporary files that will take up space on your hard drive. A hard drive that is close to being full can cause Windows to act erratically. Wipe out unneeded files and scan for disk errors to speed up the system. Go to "My Computer," right click on your "C" drive and under "Properties," click on "Disk Cleanup."

Begin by clicking on "Tools" after you have clicked on "Properties." Then click the "Check Now" button to scan your disk for errors. After the scan is complete, click the "Defragment Now" button. This reorganizes your hard disk so Windows can access files more efficiently. It is recommended that you close all programs and disable your screen saver before running a defragmentation.

These are just the preliminary steps you can take to optimize performance. Other measures are best left to the computer experts.



BRIEFS

SOCIAL SECURITY WAGE BASE

For the first time ever, the Social Security wage base has cleared the "century" mark. The wage base for 2008 is \$102,000 (up from \$97,500 for 2007). But the OASDI tax rate on wages up to the amount of this threshold remains at 6.2%. Also, the 1.45% HI portion of the tax continues to apply to all wages. These tax rates are doubled for self-employment tax purposes, but a self-employed individual can deduct half of his or her self-employment tax.

ONLINE IRA ROLLOVERS

What happens if you make a mistake with an online rollover to an IRA? The IRS will not be very lenient. A new private ruling states that a taxpayer inadvertently designated funds for a

non-IRA account by checking the wrong box on an online form. Technically, the taxpayer failed to meet the 60-day requirement for a timely rollover. The IRS said the transfer was taxable. Note that additional time might be granted for failures that are the fault of a financial institution.

HOMEOWNER TAX BREAKS

Congress passed legislation late in 2007 granting relief to homeowners in debt. For a three-year period, joint-filers may exclude from tax up to \$2 million of debt forgiveness on a mortgage for a principal residence. The new law also enables widowed spouses to claim the full \$500,000 exclusion on the sale of a principal residence if the home is sold within two years of the deceased spouse's death. Finally, deductions for mortgage insurance premiums have been extended through 2010.

GEAR UP FOR 2008

The IRS recently announced an increase in the standard mileage rate for 2008. The new rate is 50.5 cents per business mile plus business-related tolls and parking fees (up from 48.5 cents per business mile in 2007). On the other hand, the standard mileage rate applicable for medical or moving expense deductions has been reduced from 20 cents per mile to 19 cents per mile. The rate for charitable driving remains at 14 cents per mile for the 2008 tax year.



