# Thomas, Judy, and Tucker, P.A.

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*Welcome to the December 2002 Thomas, Judy & Tucker, P.A. newsletter. If you prefer to have this newsletter e-mailed, please call our office at (919) 571-7055 and give us your e-mail address, or e-mail it to us at heather.dickson@tjtpa.com*

**TJT MISSION STATEMENT**

Since our inception, we have always known what our goals and aspirations were for the firm, but they were never formally documented. At a recent partner-manager retreat, we divided up into groups and brainstormed about our mission here at Thomas, Judy & Tucker, P.A. The following mission statement is a product of our combined efforts to make known what we believe.

***Our Mission***

*We strive to build and maintain successful client relationships by providing quality financial, consulting and compliance services at a reasonable cost in a timely manner. We seek continuous improvement in the lives of our clients, our employees and in the community we serve.*

*The source of our strength is our people. We are committed to providing an environment and culture where employees are valued, respected and encouraged to maximize their potential. Our employees will share in the financial success of the company.*

*By operating according to ethical and Christian principles, we will achieve profitable growth and long-term financial success.*

**STAFF NEWS**

- We are very pleased to announce that three of our senior staff accountants have been promoted to managers. Ernie Jackson, Amy Spaulding and Kelly Wise were recently named managers in the firm.

- Kevin Miller has joined our financial statement team as a staff accountant. Kevin is a CPA who brings experience with a "big 5" firm in both audit and tax areas. He is a graduate of East Carolina University. Kevin makes his home in Raleigh with his wife, Miken. We are very pleased to welcome Kevin to our team!

- Janet Whited has joined our firm as a staff accountant. She and her husband, Jim, live in Raleigh. Janet has varied experience in both public accounting and nonprofit financial management. Janet previously worked for Thomas, Judy and Tucker and we are looking forward to having her back.

- We'd also like to welcome Chrissy Bowling who is our new receptionist. She brings with her over 12 year of experience in administrative work. She has

Varina area. Welcome Chrissy!

**New Family Additions!**

- We are happy to announce a new addition to our extended family! Heather Dickson and her husband, Brent, have a new baby girl. Their second child, Katherine, was born August 21, 2002, weighing 8 pounds, 9 ounces. Congratulations, Heather & Brent (and big brother Brady)!

- Maureen Bross and her husband, Guy, have also added to their family! Lea Erin, joined big brothers Brendan and Colin on November 3, 2002, weighing in at 8 pounds, 11 ounces. Congratulations, Maureen and Guy!

- Amy Waddell and her husband, Greg, have tripled their children! Their new twins were born on November 19, 2002. Jessica Faith came into this world at 7 pounds, 9 ounces along with her brother, Chase Gregory, weighing 6 pounds, 2 ounces. Older sister Samantha is in for a treat when they get home! Congratulations to the Waddell family!

S corporation loss on his own 2002 return, but the loss exceeds the basis for his S corporation stock and debt, he can still claim the loss in full by lending the S corporation more money or by making a capital contribution by the end of the S corporation's tax

## YEAR-END TAX PLANNING

Tax planning this year has been overshadowed by a bear market that left many individuals with substantial realized and recognized losses and a weak economy that has hit individuals and businesses alike. On the plus side of the ledger, some tax relief did materialize in 2002. New or improved tax breaks that can reduce an individual's 2002 tax bill include higher phaseout ranges for the student-loan interest deduction, a new above-the-line deduction for higher-education expenses, higher contribution limits to IRAs, 401(k)s, 403(b) annuities, salary reduction SEPs and Sec. 457 plans, higher elective deferrals to SIMPLE plans, and for those age 50 or older, "catch-up" contributions to IRAs as well as to qualified plans, SEPs, and SIMPLE plans. Businesses get enhanced first-year depreciation deductions for most types of new depreciable property (other than buildings) and a temporary increase in the NOL carryback period.

Keeping these and other tax breaks in mind, here's a checklist of the most important actions that should be taken no later than December 31, 2002 to save taxes:

- Postpone income until 2003 and accelerate deductions into 2002 to lower your 2002 tax bill. This strategy may enable you to claim larger deductions, credits, and other tax breaks for 2002 that are phased out over varying levels of adjusted gross income (AGI). These include Roth IRA contributions, conversions of regular IRAs to Roth IRAs, child credits, higher education tax credits, the new above-the-line deduction for higher-education expenses, and deductions for student loan interest. Postponing income also is desirable for those taxpayers who anticipate being in a lower tax bracket next year due to changed financial circumstances. Note, however, that in some cases, it may pay to actually accelerate income into 2003. For example, this may be the case where a person's marginal tax rate is much lower this year than it will be next year.

- Realize losses on stock while substantially preserving your investment position. There are several ways this can be done. For example, you can sell the original holding, then buy back the same securities at least 31 days later.

- If you are fortunate enough to be expecting a bonus, you may be able to arrange with your employer to defer the bonus (and your tax liability for it) until 2003.

- If you are a partner or an S corporation shareholder, take steps to increase your basis in the partnership or S corporation to make possible a 2002 loss deduction. For example, if a shareholder wants to claim a 2002

- Use your credit card to prepay expenses. For example, charitable contributions and medical expenses are deductible when charged to an individual's credit card account (e.g., in 2002) rather than when she pays the credit card company (e.g., in 2003).

- Put new business equipment in service before year-end to get the special first-year 30% depreciation allowance, plus six months' worth of depreciation deductions on the remaining adjusted basis (or plus 1.5 months' worth of depreciation deductions on the remaining basis if the mid-quarter convention applies).

- If you run a business, make expenditures qualifying for the $24,000 business property expensing option (but note that the amount that can be expensed generally is reduced dollar-for-dollar for eligible property placed in service during the tax year in excess of $200,000). Settle insurance or damage claims if this will maximize your casualty loss deduction for 2002.

- Apply the "bunching strategy" to miscellaneous itemized deductions, medical expenses and other itemized deductions to maximize your itemized deductions.

- Increase your withholding before year-end to eliminate or reduce an estimated tax penalty.

- If you expect to owe state and local income taxes when you file your return next year, ask your employer to increase withholding of state and local taxes (or pay estimated tax payments of state and local taxes) before year-end to pull the deduction of those taxes into 2002.

- Make gifts to family members to take advantage of the $11,000 gift tax exclusion ($22,000 for gifts made by married couples) that applies to each donee for 2002. (You get no carryover of any unused exclusion—it's a "use it or lose it" benefit.)

**Year-End Tax Planning (Cont):**

- Estimate the effect of any year-end planning moves on the alternative minimum tax (AMT) for 2002, keeping in mind that many tax breaks allowed for purposes of calculating regular taxes are disallowed for AMT purposes. This includes the deduction for state property taxes on your residence, state income taxes, miscellaneous itemized deductions, and personal exemption deductions. Other deductions, such as for medical expenses, are calculated in a more restrictive way for AMT purposes than for regular tax purposes. As a result, in some cases deductions should be deferred rather than accelerated to keep them from being lost because of the AMT.

- If you are self-employed and haven't done so yet, set up a self-employed retirement plan.

- Step up the level of your participation in a business activity to meet the material participation standard needed to avoid the passive loss rules. Also, consider disposing of a passive activity to free up suspended losses.

These are just a few of the year-end planning tax moves that could make a substantial difference in your tax bill for 2002. Please call our office so that we can schedule a year-end planning session with you.

## STANDARD MILEAGE RATE DROPS

The IRS has announced that the standard mileage rate for 2003 will drop to 36¢ per mile. This is a reduction from the 2002 rate of 36.5¢ per mile. This is the rate that should be used for mileage reimbursements for business. The rate used for medical and moving expenses will also drop from 13¢ per mile in 2002 to 12¢ per mile in 2003.

## ONLINE PROPERTY TAX LISTING

Beginning in 2001, Wake county allowed taxpayers to list their business personal property online. We can file this listing online for you if we have your account number and county-assigned password. This information is on the tax listing mailed to you by the county. Be sure to send us this tax listing as soon as you receive it if you would like for us to file online for you. To do it yourself, the Wake County website is http://www.co.wake.nc.us/Revenue, then select "Online Resources".

## ATTENTION: PARTNERSHIPS AND LLC'S WITH OWNERSHIP CHANGES

If your partnership or limited liability company has an ownership change of more than 50% during a 12-month period, it is considered a technical termination under Internal Revenue Code Section 708(b)(1)(B). A short-year return must be filed as of the date of the ownership change, with the return due the 15th day of the 4th month after that date. If your partnership or LLC is in this situation, be sure to call us as soon as possible so that this short-period due date is not missed.

## SALES TAX UPDATE

The General Assembly has enacted new sales tax legislation over the past year. The following are some changes that may affect your business.

Effective January 1, 2002:

- **All** delivery charges made in connection with taxable sales of tangible personal property are subject to sales or use tax.
- A retailer who ships or delivers merchandise sold to a purchaser in a county other than the county in which the retailer's business is located is required to collect and remit tax due for the county to which the property is shipped or delivered. A retailer who has locations in multiple counties or ships or delivers merchandise sold to purchasers in multiple counties is required to complete and submit Form E-536, Schedule of County Sales and Use Taxes.
- A Sales Tax Holiday provides an exemption for certain items of tangible personal property sold between 12:01 A.M. on the first Friday in August and 11:59 P.M. the following Sunday.

Effective December 1, 2002:

- Wake County will increase its local sales tax rate ½%. Wake County is 1 of 81 counties who adopted the increase. For a complete list of counties, please call our office.

Effective November 2002:

- Taxpayers will be able to file their NC sales and use tax returns and pay their taxes online. Taxpayers will be able to access E-File by clicking "Electronic Services" at the top of the Department's home page.

If you have any questions about sales and use tax, you can call our office or access the NC Department of Revenue's website at www.dor.state.nc.us.

## NEW PER-DIEM RATES

Reimbursements of an employee's business travel costs (lodging, meal and incidental expenses) at a per-diem rate are payroll- and income-tax free if properly substantiated and the daily rate does not exceed the federal per-diem rate for the locality of travel for that day. The rates have just been published for the period October 1, 2002 to September 30, 2003. The new rates are $204 per day for a high-cost area and $125 per day for other areas. There have also been some revisions in the definition of "incidental expenses". All of the details are in Rev. Proc. 2002-63, which is available on the IRS website or at our office.

## LLC MEMBERS AND SELF-EMPLOYMENT TAX

Generally, limited liability companies are treated like partnerships for income tax purposes and the members like partners. General partners are usually subject to self-employment tax on their share of partnership profit, while limited partners are not. Which is an LLC member? An LLC member who is active in the business and designated as a "managing member" in the operating agreement will usually be subject to self-employment tax on their share of LLC profit. In drafting the operating agreement, this is a planning opportunity. Are there members that will not be subject to self-employment tax? The tax can be significant, so it is worth considering when you are drafting your agreements. While the IRS seems amenable to this approach, it is to some extent based on "facts and circumstances", and the result may vary from one company to another. Please call us if you have questions regarding how the self-employment tax will apply to your LLC members.

## ELECTRONIC FILING REMINDER

This is a reminder that we do offer electronic filling of your individual tax returns through our tax software provider. If your return shows a refund due, you can receive it substantially faster than if you were to file your return through the mail. In addition, the federal refund can be deposited electronically into your bank account. If you owe additional tax, you can file your return electronically and still put off making the payment until April 15. There are restrictions on some returns, but if you are interested in filing your return electronically please let us know when you bring in your tax information or indicate it on the tax organizer.

## KEEP COPIES OF YOUR RECORDS

While we may often make copies of your records for our files, keep in mind that it is your responsibility to keep the original records. Legal disputes or IRS communication may arise in the future where your original records would be indispensable in supporting a position or deduction taken.

## HOW LONG SHOULD I KEEP THESE RECORDS?

This is a question many business owners and individuals ask. While there are no hard and fast rules, there are guidelines we should follow. They rely on both legal statutes of limitations and the likelihood of the records being needed and/or useful in the future. Below are some general guidelines. While "permanently" sounds like a long time, there are many ways to electronically preserve records to minimize storage costs and space. If you need a more comprehensive list or have specific questions, please call our office.

Retain for 1 year: Bank Reconciliations, Requisitions, Receiving sheets, Routine Correspondence

Retain for 3 years: General Correspondence, Employment Applications

Retain for 7 years: Accounts Payable and Receivable records (e.g. ledgers, schedules, invoices), Cancelled

Checks (routine), Payroll Records

Retain Permanently: Audit Reports, Cash Records, Cancelled Checks for Important Transactions (e.g. property purchase, tax payments), Correspondence (important or legal matters), Deeds & Mortgages, Depreciation Schedules, Financial Statements (year-End), General Ledgers (year-end), Insurance Records, Minute Books, Property Records, Tax Returns

**AFRs FOR DECEMBER 2002**

The Applicable Federal Rates for December 2002 have been announced. Selected rates are as follows:

| | | Compounding | |
|---|---|---|---|
| Term | Annual | Monthly | Quarterly |
| Short-term (0-3 years) | 1.82% | 1.83% | 1.84% |
| Mid-term (4-9 years) | 3.26% | 3.27% | 3.31% |
| Long-term (over 9 years) | 4.81% | 4.83% | 4.92% |

**WEIGHT LOSS PROGRAMS MAY BE DEDUCTIBLE**

The IRS has ruled that the unreimbursed cost of participating in a weight-loss program as treatment for a specific disease or diseases (including obesity) diagnosed by a physician qualifies as a medical care expense. The cost of diet foods, however, is not deductible. Individuals who might otherwise join a weight-loss program to improve their general health or appearance should first be examined by a physician to see if there is a medical reason for participating, such as to aid in alleviating hypertension, reducing high cholesterol, or combating diabetes. If a medical reason exists, and is documented in a written report from the physician, the cost of the program may be deductible. Note that medical expenses, including qualifying weight-loss expenses, are deductible only to the extent they cumulatively exceed 7.5% of adjusted gross income (AGI). Individuals who participate in a company medical flexible spending account may obtain a reimbursement from the account for qualifying weight-loss expenses.

**NC ADJUSTMENT FOR 30% BONUS DEPRECIATION**

The North Carolina Budget Bill, signed into law by Governor Mike Easley on September 30, 2002, conforms the North Carolina income, pension and estate tax provisions to those of the Internal Revenue Code as amended as of May 1, 2002. However, it also includes mandated adjustments to the additional 30% bonus depreciation. Effective January 1, 2002, the law requires corporate and individual income tax payers to make an addition to taxable income for the amount of the additional 30% bonus depreciation claimed for federal tax purposes as follows: 2002 tax year, 100%; 2003 tax year, 70%; and 2004 tax year and thereafter, 0%. The law allows taxpayers to deduct in each of their first five taxable years beginning on or after January 1, 2005, an amount equal to 20% of the amount added to taxable income in a previous year as accelerated depreciation. Also, if a taxpayer took the additional 30% bonus depreciation on their 2001 NC return, that amount must be an addition on their 2002 tax return.

**THE SARBANES-OXLEY ACT OF 2002**

The recent accounting scandals and implosion of several large corporations has shaken the public's confidence in the capital markets and in the audit function. On July 30, 2002, President Bush signed The Sarbanes-Oxley Act of 2002 into law. The main premise behind the Act was to strengthen corporate accountability and restore public confidence.

The Act created a five-member board referred to as the Public Company Accounting Oversight Board (PCAOB) that will be certified no later than April 2003. The board has the authority to set and enforce auditing, attestation, quality control, and ethics standards for public companies. It will oversee and investigate the audits and auditors of public companies and impose disciplinary action for violations of the board's rules, securities laws and professional auditing standards.

A couple of the newly created provisions include: 1) Registered public accounting firms are prohibited from providing any non-audit services to an audit client, 2) The CEO and CFO of public companies must prepare a statement to accompany the audit report that declares the financial statements present fairly, the operations and financial condition of the company.

CPAs in non-public companies and the CPAs that provide services to them need to be cognizant of the new regulations the Act imposes. Many of the reforms may be viewed as best practices and used as a model for future regulations that would then include a broader range of financial entities.

## IRS GUIDE TO SMALL BUSINESS RETIREMENT PLAN OPTIONS

The IRS has released "Publication 3998, choosing a Retirement Solution for Your Small Business", which describes the retirement plan options available to small businesses. Recent tax law changes have provided additional incentives to start a retirement plan. The publication discusses these as well as plan choices and a chart outlining the advantages of the most popular plan types. It presents the information in a very clear and concise format. The publication is available on the IRS website at http://www.irs.gov/formspubs/index.html. For more information or help determining which plan is the best fit for your business, please give us a call.

## ELECTRONIC TAX ORGANIZER!

It's that time of year again! We will be mailing out individual tax organizers in January 2003. If you prefer to receive your tax organizer electronically, we would be glad to e-mail the organizer to you rather than mailing a paper version. To select this option, email Heather Dickson at heather.dickson@tjtpa.com. prior to December 20, 2002. The organizer should be helpful in accumulating your 2002 tax information and will help us prepare your return more efficiently and accurately. Please fill out the organizer and return it to us as soon as you have received all of your 2002 tax information.

## GIFTS ?

As we enter the holiday season, it seems appropriate to talk about gifts. In 2002, you can make gifts of up to $11,000 in cash to as many persons as you desire without filing a gift tax return. If you and your spouse want to combine your exclusion amounts, the checks must be out of a joint account or you must file a gift tax return to elect to split your gifts. Also, if you are gifting property, it is important to file a gift tax return. The IRS is taking an aggressive position when they audit estate tax returns by disallowing gifts of property whose value has not been properly documented. If you have made or are thinking about making any gifts of property, please contact our office to discuss it.

## 2001 IRS & SSA TAX FORM CHANGES

| | 2001 | 2002 | 2003 |
|---|---|---|---|
| Personal Exemption | $2,900 | $3,000 | $3,050 |
| Child Tax Credit | $600 | $600 | $600 |
| Earnings ceiling for Social Security | | | |
| Below Age 65 | $10,680 | $11,280 | |
| Age 65 and above | Unlimited | Unlimited | Unlimited |
| Gift and Estate Tax Applicable Exclusion Amount | $675,000 | $1,000,000 | $1,000,000 |
| Section 179 Deduction | $24,000 | $24,000 | $25,000 |
| Self-Employed Health Insurance Deduction | 60% | 70% | 100% |
| Retirement | | | |
| Max Deductible 401(k) and 403(b) | | | |
| Employee Contribution | $10,500 | $11,000* | $12,000* |
| Traditional and ROTH IRA Contributions | $2,000 | $3,000* | $3,000* |

| | | | |
|---|---|---|---|
| Mileage | | | |
| Business | $.345/mile | $.365/mile | $.36/mile |
| Charitable | $.14/mile | $.14/mile | $.14/mile |
| Medical / Moving | $.12/mile | $.13/mile | $.12/mile |
| Payroll | | | |
| Social Security | 6.2% | 6.2% | 6.2% |
| Maximum taxed | $80,400 | $84,900 | $87,000 |
| Medicare | 1.45% | 1.45% | 1.45% |
| NC Taxable Wage base | $14,700 | $15,500 | $15,900 |

*Over age 50, may contribute an additional $1,000

## HABITAT FOR HUMANITY

Wake County Habitat for Humanity started their 200th house this year. Thomas, Judy & Tucker was one of the few that sponsored this 200th house. Along with the sponsorship, the owners and employees volunteered in the participation of building these simple houses for those in need. We closed the office on Friday, October 25 and spent the day working on Habitat homes going up in Cary. It didn't matter if you were skilled or unskilled; there were plenty of projects for everyone. We really enjoyed the opportunity to get involved in helping the community and work on such a great project as a firm.

*Please do not hesitate to get in touch with us if you have any questions about the above.*
*Very truly yours,*

**THOMAS, JUDY & TUCKER, P.A.**