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CERTIFIED PUBLIC ACCOUNTANTS

The Accountant's Corner

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Estate and Gift Tax Planning for 2011 and Beyond

The new 2010 Tax Relief Act provides estate-tax relief to certain families, but the "fix" is only temporary. Unless Congress acts again, the new law provisions will expire after 2012. Therefore, estate planning for the future remains somewhat uncertain.

First, here are the old rules: Under the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), the estate-tax exemption equivalent gradually increased from $1 million in 2001 to $3.5 million in 2009. At the same time, the top estate-tax rate decreased from 55% to 45%. Among other changes, EGTRRA also separated the estate- and gift-tax regimes and maintained a $1 million lifetime gift-tax exemption.

Then the estate tax was completely repealed for decedents dying in 2010. Beginning in 2011, the estate tax was scheduled to be reinstated under pre-EGTRRA levels.

Now, here are the new rules: Under the new tax law, the estate-tax exemption is increased to $5 million, with a top estate-tax rate of 35%. These figures will remain in effect for 2011 and 2012 (with indexing for 2012). The new law also reinstates the rules allowing a step-up in basis for heirs.

The new law also allows estate-tax exemption to be "portable" for decedents dying in 2011 or 2012. As a result, a family may be able to utilize the full $10 million in exemptions for a married couple, regardless of how they have divided up assets. Reminder: The portability provision expires after 2012.

For gifts made in 2010, the new law provides a lifetime gift exemption of $1 million with a top gift-tax rate of 35%. The estate- and gift-tax systems are "reunified" for transfers after 2010 with an exemption of $5 million and a top gift-tax rate of 35%. Finally, the new law coordinates changes in the generation-skipping transfer tax with other estate- and gift-tax law changes.

Although the estate-tax future remains cloudy, it generally makes sense to continue giving gifts that qualify for the annual gift-tax exclusion. This can reduce the size of a taxable estate. For 2011, a family member can give each recipient up to $13,000 without triggering any gift tax ($26,000 for joint gifts by a married couple). Any excess may be covered by the $5 million gift-tax exemption (but that reduces the estate-tax shelter).

Do not make any assumptions or be lulled into inaction by the temporary tax relief. Please contact our office if you have any questions or concerns.

Lead Tax Partner David A. Johnson, CPA is one of our firm's most experienced estate and gift tax specialists. David's involvement with complex estate planning includes working with attorneys and other advisors to create plans that provide value to our clients and their heirs. Please feel free to contact him if you have any estate planning questions.

Now May Be the Right Time for Refinancing

Mortgage interest rates reached historic lows in 2010 but are still very attractive at around 4.7% on a 30-year fixed rate mortgage. The average rate for a 15-year fixed rate mortgage is even lower at around 3.9% while introductory rates for certain adjustable-rate mortgages may be even lower.

Double-digit percentage interest rates are a distant memory. In the current interest-rate environment, many homeowners are tempted to refinance an existing mortgage, even for the second or third time. But refinancing is not as straightforward as it first seems.

Basic issues: Besides interest rates, a homeowner must factor in all the required fees before determining if he or she will actually save money. Refinancing usually involves many of the same closing costs incurred when the mortgage was initially obtained. The exact expenses can differ among lenders, but typically a borrower will have to pay for title insurance, a survey, appraisals, other administrative fees and attorney costs.

Also, consider the number of points attached to the loan. Each "point" represents one percentage point of the amount being borrowed (e.g., two points on a $200,000 loan is $4,000). Frequently, a low-interest mortgage carries one or more points. On the other hand, a loan offered at a slightly higher rate may be available without paying any points.

Unfortunately, a borrower currently cannot deduct the points paid on a refinanced mortgage. Instead, this cost must be amortized over the course of the loan (as opposed to an initial mortgage where points are currently deductible).

Once all the figures are available, analyze whether it pays to refinance. For instance, a key factor is the length of time a person expects to stay in the home. Estimate how long it will take to recoup the costs of refinancing.

Simplified example: John Q. Public is currently paying $2,000 a month in mortgage interest and principal (excluding property taxes). If John refinances the mortgage, his mortgage interest and principal will be reduced to $1,800, a monthly savings of $200. He expects to incur $3,000 in fees relating to the closing.

On these facts, John will recoup his costs in 15 months ($3,000 divided by $200 in monthly savings). From that point on, the mortgage savings are his to keep. Assuming John expects to live in the home for a few more years, refinancing generally makes sense. Conversely, if John anticipates moving in one year or less, refinancing clearly is not the best approach.

Of course, this is only a brief overview of the analysis. Other factors, such as the impact of mortgage interest deductions, can play a significant role.

In summary: The decision to refinance or not must be based on a homeowner's particular circumstances. Please contact our office if we can help with the calculations related to this decision.

Are Donor-Advised Funds An Option For Your Charitable Giving?

Setting up a private foundation can be costly and time-consuming. One alternative is catching on with some wealthy entrepreneurs: the donor-advised fund. It is even possible to convert an existing foundation into a donor-advised fund.

With a donor-advised fund, an individual donates a lump sum to the fund, which is often managed by an experienced charitable organization. The donor is able to divide the subsequent contributions among certain charities. Although the fund legally controls the money, the donor effectively decides who gets what and when.

Typically, a donor-advised fund will require an initial donation of $25,000 or more. It will also generally charge a fee (e.g., 1% of managed assets) for administrative services. But the benefits are often worthwhile.

- A donor qualifies for current charitable deduction. In fact, due to certain tax law limits, the current deduction may be higher than the deduction allowed for gifts to a private foundation.
- The arrangement is relatively simple. The fund does all the "grunt work."
- A donor's privacy is protected. Gifts can be made anonymously. In contrast, private foundations must publicly disclose certain information.
- There are no mandatory distributions. In contrast, a private foundation must distribute at least 5% of net assets each year.

However, be aware of certain complexities with this arrangement, especially if an existing foundation is being converted into a donor-advised fund. Please feel free to contact our office if you have any questions.

Time to Update Your Internal Controls?

Does your company perform an annual risk assessment and then follow up by updating and adjusting its internal controls? If not, you could be gambling with the security of your company. Risk assessment is an organization's process of identifying and analyzing business risks to the achievement of its objectives, as well as determining how those risks should be managed. These risks may be internal or external. Some common risks include: shifting economic conditions, new legislation, changes in technology, corporate restructuring, increase or changes in competition, personnel changes and rapid expansion of operations. As organizations evolve so do their internal control systems. The risk that those internal controls may be inadequate changes as well. What may have been an ideal internal control a year ago will not necessarily be an ideal internal control today.

Four of the most common mistakes when it comes to internal control systems are:

1. Assumption that it is only the auditor's job – because management is ultimately responsible for the internal control system in place and management will bear the brunt of the consequences if those controls fail.
2. Failure to link the risks and the controls – the first procedure in setting up a proper internal control system is to perform a risk assessment. A company cannot properly establish controls within the organization if the risks have not been identified.
3. Inadequate monitoring of controls – If there were a posted speed limit on I-40 but no police to monitor, how many drivers would actually drive the speed limit?
4. Even the best set of internal controls cannot overcome management override. Trust your management team, but always maintain objectivity when it comes to possible risks.

The audit team at TJT is experienced with assessing the internal controls and procedures of a business. Please feel free to contact us if we can assist with a review of your internal controls.

FASB Proposal to Amend Goodwill Impairment Testing

On April 22, 2011, the FASB issued a proposed Accounting Standards Update ("ASU") to address concerns from privately held companies related to the cost and complexity of performing the first step of the two-step goodwill impairment test required under ASC Topic 350. The objective of the proposal is to simplify how an entity is required to test goodwill for impairment. The proposed ASU would allow companies to use a qualitative approach to determine whether it is more likely than not (defined as more than 50%) that the fair value of the reporting unit is less than its carrying amount. Current guidance requires companies to test goodwill impairment by performing a fair value assessment of the reporting unit on an annual basis. The option of reviewing qualitative factors would reduce the level of complexity and provide a more cost efficient option.

Please feel free to contact a member of our audit team with any questions or concerns.

1099 Reporting Requirements Changed

President Obama recently signed into law a bill repealing the onerous 1099 reporting provisions of the health-care reform law. This act basically restores the 1099 filing requirements as they existed before healthcare reform and should relieve small businesses and rental property owners from certain aspects of 1099 filings. However, businesses and rental property owners still have to issue 1099's to any non-corporate entities to whom they paid more than $600 in a calendar year. This would include individuals and partnerships that provide goods or services as a vendor or if rents were paid to individuals or partnerships. If you have any questions about your 1099 filing requirements, please contact our office.

Firm Awards and Recent Hires

Thomas, Judy & Tucker was recently named as the **2011 Business Leader of the Year for Triangle Accounting Firms by Business Leader** magazine. Thank you to our clients, both new and longstanding, who have helped us to earn this recognition. Our firm growth continues, as TJT recently hired Adam Heinlein, CPA as a member of our tax team. Adam is a Michigan grad and appreciates the warmer weather and golf courses of the Triangle area.