Volume 3, Issue 2

July 2008

Tax Talk

A quarterly publication of Bridges & Dunn-Rankin, LLP

Inside this issue:

The Heroes Earnings Assistance and Relief Tax Act	1
Member in the Spotlight — Laura E. Niklasson	2
The 2008 Presidential Election	2
Multi-State Taxation	2
Client in the Spotlight —Becton Schantz, Inc.	3
Shortening of Extension Period for Partnerships and Trusts	3
Audits, Reviews, and Compilations of Financial Statements	4
IRS Increases Standard Mileage Rate	4

Dear Clients and Friends,

Summer time. Backyard barbecues, swimming, Friday afternoon golf, summer vacation at the beach, and, supposedly, a slower time for CPA firms. While admittedly we don't have the deadline pressure right now of April 15 or October 15, we are quite busy with extended tax returns, financial statements, structuring transactions, handling IRS and DOR matters, and doing ongoing planning for our clients.

New tax legislation, *The Heroes Earnings Assistance and Relief Tax Act of 2008*, has been enacted since the last issue of our newsletter, providing targeted tax relief for members of the military offset with tightened expatriation rules and a new rule which will treat certain foreign subsidiaries of U.S. companies as American employers for employment tax purposes.

The White House will have a new occupant in 2009, and this could mean significant changes to the tax code in the next few years.

Kent Bridges, Managing Partner

In this issue we will review highlights of the recent tax legislation, consider the impact that the upcoming presidential election may have on taxes, address recent changes to the IRS standard mileage rate and extensions for partnerships and trusts, provide an overview of multi-state tax rules, compare audits, reviews and compilations of financial statements, and, as always, highlight a member of our firm and one of our clients.

We hope that you will enjoy this issue and gain from it some useful information.

Sincerely,

Kent Bridges

The Heroes Earnings Assistance and Relief Tax Act of 2008

On June 17, 2008, President Bush signed into law the *The Heroes Earnings Assistance and Relief Tax Act of 2008* (the "Heroes Act"). Highlights of the Heroes Act include:

Targeted tax relief for members of the military – As the name of the Heroes Act implies, its primary purpose is to provide targeted tax relief for members of the military, including: provision that those in the active military filing joint returns are eligible for the 2008 Economic Stimulus rebate check even if their spouse does not have a social security number; making permanent the ability to include combat pay as earned income for purposes of the earned income tax credit; liberalizing certain retirement plan rules for reservists called to active duty; and providing small employers with a 20% tax credit for differential wage payments made to employees who are on active military duty. Provisions designed to offset the revenue lost from these tax breaks are summarized below.

Tightening of expatriation rules – The U.S. taxes its citizens and residents on their worldwide income, from whatever source derived. In the past, if you were willing to renounce your U.S. citizenship (or in the case of a non-citizen surrender your permanent lawful residence status), stay out of the country for 10 years, and wait 10 years to sell substantially appreciated assets, you could potentially avoid the U.S. tax on such gains. Some wealthy individuals were willing to take these steps in order to avoid U.S. tax. Under the new rules, wealthy individuals (generally defined for these purposes as those with net worth over $2 million or annual income tax liability in excess of $139,000) who expatriate will be deemed to have sold all of their assets the day before expatriation for their fair market value and owe tax on the deemed gain in excess of $600,000. These rules apply not only to U.S. citizens who renounce their citizenship, but also to non-citizen long-term (generally 8 years) residents who cease to be permanent lawful residents. In addition to these changes to the income tax rules, new estate and gift tax rules provide that a U.S. citizen or resident who receives a gift or bequest from an expatriate may be subject to gift or estate tax upon the receipt of such.

Treatment of foreign subsidiaries as U.S. employers – In the past, U.S. companies with U.S. citizen employees working abroad have often been able to avoid paying FICA tax by having these individuals employed by their foreign subsidiaries. Under the new rules, foreign subsidiaries of U.S. companies performing services under a U.S. government contract will be treated as U.S. employers for employment tax purposes.

Laura E. Niklasson

Member in the Spotlight — Laura Niklasson

Laura Niklasson joined Bridges & Dunn-Rankin in 1994 as the firm's first administrative employee. She was the perfect person to take on the challenge of a fledgling start-up, bringing order to the chaos of a new firm with few administrative policies and procedures. In her role as Office Manager, Laura handles the firm's internal accounting, human resources, vendor relations, network and information technology, office automation and equipment, and various other duties, while also assisting many of our clients with their accounting and payroll-related needs.

Laura, a native of Florida, holds a B.A. in International Relations from Agnes Scott College. In her spare time, Laura practices Aikido (a Japanese martial art), where she met husband Rob 15 years ago. The Niklasson's and their three children are founding members of Trinity Anglican Church in Douglasville, where Laura serves as Nursery Coordinator and a Building Committee member.

Bridges & Dunn-Rankin is proud to have Laura Niklasson as a member of our firm.

The 2008 Presidential Election

The White House will have a new occupant in 2009; likely John McCain or Barack Obama. So what does this likely mean with respect to taxes?

Estate tax reform – Under current rules, the exemption from estate tax is $2,000,000 (scheduled to go to $3.5 million in 2009) and the top tax rate is 45%. The estate tax is scheduled to disappear for 2010, and then reappear in 2011 with an exemption of only $1 million and a top rate of 55%. This is obviously not palatable, and Congress will almost certainly have to act to reform the estate tax before then. Neither candidate favors a complete repeal of the estate tax. Obama favors an exemption of $3.5 million with a top rate of 45%. McCain favors an exemption of $5 million with a top rate of 15%. Both favor making the exemption portable for spouses, such that the combined exemption for a couple would be $7 million or $10 million, without requiring the special estate planning that is necessary under current law in order to ensure the full use of each spouse's separate exemption amount.

Corporate income tax – McCain favors reducing the corporate income tax rate from 35% to 25% and permitting businesses to immediately expense their investment in equipment. Obama originally favored keeping the corporate rate at 35%, but has recently suggested perhaps a reduction in the corporate rate to 30.5% while eliminating certain tax breaks for corporations. He favors the elimination of capital gains taxes on start-ups and small businesses.

Individual income tax – McCain favors repealing the alternative minimum tax, doubling the personal exemption for dependents (from the current $3,500 to $7,000), and retaining the existing tax rate structure. Obama favors increasing the capital gains rate from 15% to 20%, taxing dividends as ordinary income (at rates up to 39.6%), and increasing the top individual tax rate to 39.6% (from the current maximum rate of 35%). He favors various benefits for lower and middle income taxpayers, including reforming the alternative minimum tax, a credit of up to $1,000 per family to offset payroll taxes, and exempting senior citizens with income below $50,000 from income tax.

Social security tax – Currently, the social security portion of the FICA tax (6.2% for each of the employer and employee) applies only to earned income up to $102,000. The Medicare portion of FICA (1.45% for each of employer and employee) applies to all earned income with no limit. For self-employed persons, the self-employment tax instead applies (15.3% on the first $102,000 and 2.9% thereafter). Obama has suggested removing the ceiling on the amount of income to which the social security tax applies. For higher income earners, this could mean an additional 12.4% tax on earned income over $102,000.

Multi-State Taxation

Our business clients often conduct business in multiple states, and our individual clients often work in more than one state, own real estate in multiple states, or have ownership in flow-through entities with income from other states. This article provides a brief overview of the general rules of multi-state taxation.

Individuals – Most states tax their residents on their worldwide income, while permitting them a credit for taxes paid to other states, so long as the effective rate paid to the other state does not exceed the effective rate paid to the state of residence on that same income. To the extent that you work in another state or have income from real estate in another state (e.g. rental income or gain from the sale of property) you may be subjected to that other state's income tax. Additionally, if you own an interest in an S-corp, LLC or partnership with income from other states, your income from that entity may be subject to other states' income tax.

Corporations – In addition to being subject to the income tax of their state of domicile, corporations are potentially subject to income tax in any other states with which they have "nexus". What constitutes taxable nexus varies by state, but companies will almost certainly have taxable nexus with any state in which

(Continued on page 3)

Multi-State Taxation — continued

(Continued from page 2)

they own property or maintain an office. Provision of services within a state will typically result in taxable nexus with that state, and licensing of intangibles within a state may also result in taxable nexus. Public Law 86-272 provides a limited safe harbor from state income taxation for companies that sell tangible personal property where the company's only physical contact with a state is in-state solicitation of orders which must be approved outside the state with shipment to occur from a point outside the state. Assuming a company has taxable nexus with a particular state, its income subject to tax in that state is generally determined by multiplying its overall taxable net income by an "apportionment" percentage. Historically, most states computed the apportionment percentage as the numerical average of three factors - property, payroll, and sales – computing the percentage of each of those factors within the state as compared to the amounts everywhere. In more recent years, many states have begun to move away from equally weighting these three factors to more heavily weighting the sales factor (in some cases using only the sales factor). This methodology tends to reward companies based in the state (who likely have a larger percentage of their property and payroll in the state compared to the percentage of their revenue derived within their home state) and punish companies based outside the state (which may have very little property or payroll within the state, but derive revenue from the state). Georgia is amongst the states to have moved in this direction.

Flow-through entities – Most states recognize the flow-through status of entities like partnerships, LLCs and S-corps. However, the individual owners of these entities are subject to the state's income tax on income from the entity, and many states require the entity to remit the income tax on behalf of its nonresident owners. Some states permit the entity to file a composite return on behalf of its nonresident owners, enabling the shareholders or partners to avoid the necessity of filing an individual return with the state. Some states also have entity level taxes that can apply.

Sales and use tax - Sales tax rules vary by state, but in general most states subject to the sales tax the sale or rental of tangible personal property. Many states, such as Georgia, exempt from the sales tax the sale of most services. While the tax is technically a tax on the buyer, the seller is generally obligated to collect and remit the tax. Since the tax is based on gross receipts, even an unprofitable company with minimal exposure to income tax can have substantial exposure for sales tax if it fails to properly collect and remit the tax. In addition to the sales tax, a business may also be liable for "use tax", to the extent that one of its vendors does not collect from it the sales tax on the sale to it of an item subject to the sales tax.

Property tax – In most states, real estate, business tangible personal property and certain personal use assets like automobiles, motorcycles and boats are subject to a tax on the value of the asset.

Payroll tax – If a company has employees providing services within a state (even though the employees may be resident of another state and providing services there only temporarily), then the company likely has an obligation to withhold that state's income tax and pay its payroll taxes.

Client in the Spotlight — Becton Schantz, Inc.

Becton Schantz, Inc. was founded in 1984 when Marc Schantz partnered with Bob Becton to develop the premier order processing and sales force automation software for the food brokerage industry.

Today, under the leadership of CEO Marc Schantz, the Duluth, Georgia based software company has become a leading provider of order management systems and other software solutions for the consumer packaged goods industry. The company has processed orders and provided other services for over 10,000 manufacturers and over 15,000 retailers and distributors. Last year, over 5 million orders representing over $100 billion of product were processed through Becton Schantz's system.

Bridges & Dunn-Rankin is proud to be associated with Becton Schantz, Inc.

Shortening of Extension Period for Partnerships and Trusts

In 2005, the IRS did us a great favor by changing the extension rules such that individuals, partnerships and trusts could get an automatic six-month extension of time to file income tax returns (in contrast to the prior rules whereby individuals had to file for a 4-month extension at April 15 and then request another 2 months at August 15, and partnerships and trusts filed for a 3-month extension at April 15 and then requested another 3 months at July 15). This means that the extended due date for such returns is generally October 15.

Now the IRS has decided that a 6-month extension is too long for partnerships and trusts, because it can result in individuals not getting their Schedule K-1s in sufficient time to complete their returns by the October 15 deadline. New regulations provide that for returns due after January 1, 2009 the extension period for partnerships and trusts will be shortened to 5 months, making the extended deadline for these returns, in most cases, September 15.

Audits, Reviews, and Compilations of Financial Statements

There are essentially three levels of service that a CPA firm may provide with respect to financial statements: audit, review or compilation. Audits, reviews and compilations are all performed in accordance with generally accepted accounting principles (GAAP) or another comprehensive basis of accounting (such as the income tax basis of accounting). Each is a term of art, and we often get questions about the differences between the three, so here is a brief overview in reverse order from lowest level of assurance to highest level.

Compilation – A compilation involves the preparation of financial statements using information provided by the client, without audit or other verification of the information provided. Although no level of assurance is provided in a compilation, we never want our name associated with financial statements that are inaccurate. Accordingly, we will typically perform some limited procedures to verify the accuracy of the financial information that is provided to us. However, because of the limited scope of such, our report on the financial statements will indicate that a compilation is limited to presenting in the form of financial statements information that is the representation of management and that we have not audited or reviewed the financial statements and, accordingly, do not express an opinion or any other form of assurance about them. Compilations come in two flavors: (1) those with the normal disclosures you would see in audited or reviewed financials (e.g. the footnotes) and (2) those with substantially all disclosures omitted (e.g. just a balance sheet and an income statement).

Review – The procedures performed as part of a review fall somewhere in between those performed in a compilation and those performed in an audit. Performing a review requires the CPA firm to perform certain analytical procedures and inquiries of management in order to provide limited assurance on the accuracy of the financial statements. However, unlike in an audit, a review does not require obtaining an understanding of internal control and performing tests of accounting records. As with a compilation, our firm will typically perform additional procedures beyond the minimum required in order to gain a higher level of comfort that the financial statements are accurate. With a review, our report indicates that we are not aware of any material modifications that need to be made to the financial statements in order for them to be in conformity with GAAP (or another comprehensive basis of accounting, as the case may be).

Audit – With an audit, the auditor has a responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. Audits are performed in accordance with Generally Accepted Auditing Standards (GAAS) that include general, fieldwork and reporting standards which dictate how an audit is conducted. Audit procedures include evaluating the Company's system of internal control, assessing the risks of material misstatement of the financial statements, and designing and performing tests of the underlying transactions supporting the financial statement balances to address the risks identified. Our report indicates that in our opinion the financial statements are materially accurate and in accordance with GAAP (or another comprehensive basis of accounting, as the case may be). This is the highest level of assurance that a CPA firm can give with respect to financial statements.

Bridges & Dunn-Rankin, LLP
CERTIFIED PUBLIC ACCOUNTANTS

200 Galleria Parkway
Suite 1950
Atlanta, GA 30339

Phone: 770-563-8888
Fax: 770-563-8885
www.bridgesdunnrankin.com

IRS Increases Standard Mileage Rate

In light of the dramatic increase in the price of gasoline, the IRS has increased the allowable business mileage rate from 50.5 cents to 58.5 cents per mile, effective July 1, 2008.

Bridges & Dunn-Rankin, LLP is an Atlanta-based full-service accounting firm serving clients in the technology, real estate, services, manufacturing, distribution, construction and healthcare industries, as well as high net worth individuals.

The information provided in this newsletter is presented for educational and informational purposes only, and is not intended to constitute legal, tax or accounting advice. The articles provide only a very general summary of complex rules. For advice on how these rules may apply to your specific situation, contact a professional tax advisor.