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December 2004

# Client Information Bulletin

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## Section 179 Allowance: It Just Keeps Getting Better

*New temporary regulations give business greater flexibility*

One of the best tax breaks around is the Section 179 "expensing" allowance. And thanks to a recent tax law change, the allowance is bigger and better than ever. For 2004, you can elect to write off up to \$102,000 of qualified assets placed in service during the year.

Now the IRS has issued new temporary regulations that provide greater flexibility for business owners and managers under Section 179 (TD 9146).

**Background:** In the normal course of events, you can recoup the cost of busi-

ness assets through depreciation deductions claimed over a period of time. Currently, the write-off period for most business assets other than real estate is seven years (five years for computers and other technological equipment).

The IRS provides tables with the applicable percentages under its **Modified Accelerated Cost Recovery System** (MACRS). For example, if you acquire a business machine that is a seven-year property at a cost of \$20,000, the applicable percentage under the IRS table is 14.29% for the first year the

property is placed in service. Therefore, your first-year depreciation (discounting any bonus depreciation for qualified business assets) is \$2,858 (14.29% of \$20,000). However, in lieu of claiming depreciation deductions, your business may be able to write off the entire cost this year under Section 179 of the tax code.

Under this tax code provision, you can currently deduct business assets up to a specified limit. The annual limit was quadrupled from \$25,000 to \$100,000 by the **Jobs and Growth Tax Relief Reconciliation Act of 2003** (JGTRRA). After an inflation adjustment, the allowance was increased to \$102,000 for 2004. It is scheduled to revert to the \$25,000 level after 2005.

Therefore, going back to the prior example, you can write off the entire cost of the machine placed in service this year, with plenty of room to spare. **Note:** Special rules apply to vehicles used for business driving. In addition, the Section 179 allowance may be used in conjunction with the **bonus depreciation deduction** for 2004 and regular MACRS deductions. Be aware that the bonus depreciation deduction is scheduled to expire after 2004.

The new regulations focus primarily on revocations and revisions under the Section 179 expensing allowance. Here are some of the highlights:

- ◆ A taxpayer can make or revoke an expensing election without consent from the IRS on an amended return for property placed in service between 2003 and 2005;
- ◆ The election on an amended return must specify the property for which the election applies and the portion of the cost being expensed. If the taxpayer previously elected to expense only part of the cost of property, it can now elect to expense more or all of the remaining cost; and
- ◆ The timely revocation of any expensing election must specify the particular property being expensed and the selected dollar amount allocable to the property.

**Note:** *The annual limit is reduced on a dollar-for-dollar basis if assets costing more than \$410,000 are placed in service during 2004. Furthermore, the amount of your expensing allowance is limited to your taxable income from the business. In other words, you cannot claim an expensing allowance for business assets if your business shows a tax loss for 2004. Any excess can be carried over to future years.*

## Protecting Business Secrets at Trade Shows

### *Three practical steps for companies to follow*

In many industries and professions, it is a common practice to attend certain trade shows or conferences during the year. It gives your representatives a chance to “press the flesh” and put your company’s best foot forward in the mar-

ketplace. Unfortunately, potential clients or customers are not the only **interested observers** -- the competition is likely to be attending as well. And that might provide more risk to certain trade secrets than you are willing to expose.

Despite the obvious risks, a recent study by the **Center for Exhibition Industry Research** reveals that more than half of trade show exhibitors do not set any boundaries on the nature of their presentation. What sort of steps can you take? Here are three basic precautions that may provide some measure of protection.

1. Establish the **criteria** for what constitutes a trade secret and what does not. Once you have put some written guidelines in place, you can train employees to respond appropriately to inquiries. For example, if you have a new product coming out in the spring, you might choose to provide a description of the product without revealing the exact functionality.

2. Not every trade secret is uncovered at the booth, the convention floor or even in the conference rooms. You would be surprised how often competitors are tipped off about new developments through throw-away lines at the elevator or restroom. And, of course, lips have been known to become much “looser” at cocktail parties and other get-togethers after hours. Make sure employees know they are expected to protect secrets **around-the-clock**.

3. Have your employees sign **confidentiality pacts** that prohibit the disclosure of company trade secrets. The agreements should be reviewed by your legal counsel. Remind employees of their responsibilities before and during the trade show or conference.

What happens if one of your employees voluntarily discloses protected information to a third party? Your company essentially forfeits its rights for maintaining and protecting the trade secret. If you subsequently pursue a legal action, you will need to prove that:

- ◆ The information was secret and unknown outside the company;
- ◆ Adequate steps had been taken to protect the information; and
- ◆ The recipient of the information knew, or should have known, that he or she was obtaining a trade secret.

***In summary:** It is important to strike a careful balance between presenting the products or services you provide against the possibility of disclosing valuable information at trade shows. A dose of common sense and good judgment can go a long way.*

## Pleading “Innocent” on a Joint Return

***New case permits intervention by an ex-spouse***

Usually, the protagonists in a romantic comedy end up living happily ever after. But things do not always work out so well in the real world. Besides the emotional and financial aspects, the dissolution of a marriage can result in dire tax consequences.

**Key point:** The basic premise is that tax liability on a joint return is **“joint and several.”** This means that the IRS can go after either spouse -- or both spouses -- to collect any tax, penalties and interest due during the time they were married. Therefore, one ex-spouse may be held liable even if all the income reported on

the return was earned by the other spouse.

However, the tax law provides some relief for an “**innocent spouse.**” Under a special provision of the Internal Revenue Code, a spouse may not have to pay the tax, interest and penalties on a joint return, even though he or she signed the return in question.

To qualify for this special tax relief, the following requirements must be met:

- ◆ A joint tax return was filed for the year in question;
- ◆ There is an understatement of tax attributable to grossly erroneous items of one spouse;
- ◆ The innocent spouse did not know -- or have reason to know -- about the understatement of tax; and
- ◆ Considering all the facts and circumstances, it would be **inequitable** to hold the innocent spouse liable for the tax deficiency.

A critical element for the IRS is whether the spouse making the innocent spouse election received any substantial benefits or later divorced, separated or was abandoned by the other spouse.

**Note:** Be aware that certain other special rules may come into play in community property states.

Of course, some breakups are more amicable than others. In a new Tax Court case, one spouse tried to come to the tax rescue of the other.

**The facts:** Ms. Van Arsdalen filed joint tax returns with her then-husband, Mr. Murray, for the tax years 1992 through 1996. The IRS subsequently denied her claim for relief from joint and several tax liability. However, Murray sought to intervene on his ex-spouse’s behalf, stating that his sole purpose in doing so was to offer support in evidence of Van Arsdalen’s right and entitlement to equitable relief.

**Result:** The Tax Court permitted the intervention on behalf of an ex-spouse. It noted that the information provided by Murray was relevant to the determination of whether Van Arsdalen was entitled to equitable relief (Van Arsdalen, 123 T.C. No. 7).

*In the usual situation, you cannot count on an ex-spouse to help you qualify for innocent spouse relief. The best course of action is to seek assistance from a professional tax adviser.*

### **A Like-kind Exchange Goes Off-track**

In a new Technical Advice Memorandum, the IRS denied tax-free treatment for an exchange of properties with a similar nature (TAM 200424001).

When you swap “like-kind property,” there is no tax on the exchange, except to the extent the parties receive any “boot” in the deal. Boot is defined as cash or other benefit received (e.g., assumption of a mortgage). Traditionally, the IRS has taken a broad view of what constitutes like-kind property. For instance, you can swap an improved building for a vacant lot tax-free. However, the IRS takes a tougher stance in the new ruling.

**The facts:** A taxpayer exchanged assembled railroad track components that are attached to the land and treated as real property under state law for unassembled and unattached railroad track components treated as personal property under state law. The taxpayer argued that the components have the same nature, even though they have a slightly different character. He also pointed out that the properties would be treated as like-kind properties in other states.

**Result:** The IRS says that the exchange of properties is taxable. It noted that no case has ever held that the character of like-kind properties may be dissimilar in nature. Furthermore, it’s not unusual for federal tax treatment to vary under state law.

## **How to Cut Down E-mail Spam**

### *Ways to reduce congestion in your mailbox*

In just a few short years, communicating via e-mail has become a way of life. You might wonder how you ever lived without this advanced technology. But electronic communications can also have some undesirable side effects. **Case in point:** What can you do about e-mail spam?

**Spam** is the term used to define unsolicited junk mail that clogs your inbox. Many are advertisements for products or services. Not only are the messages annoying to most people, they may also offend your sensibilities. Even worse, the spam may contain harmful viruses that can cause computer problems.

Is spamming illegal? Although the law in this area is still evolving, the short answer is “no.” In any event, enforcement against spamming is a difficult proposition. The best way to handle spam is to try to avoid it in the first place, if possible. Here are a few helpful hints:

- ◆ Do not post your real e-mail address on a **forum** or **bulletin board**. **Reason:** Spammers rely on special programs to collect these addresses. Once you are on the list, it is virtually impossible to get off.
- ◆ Establish **multiple e-mail addresses**. If you regularly subscribe to services or products through web sites, keep

just one e-mail exclusively for this purpose. You can restrict your other e-mail addresses to friends, family and business contacts.

- ◆ When you register an e-mail address with a web site, do not give them the right to sell the address to spammers. Frequently, you will be able to avoid this by checking, or not checking, a box. Read the **fine print** carefully to make sure you are making the right choice.

Of course, it is extremely difficult to completely shut down spam at this point, especially if your e-mail address has been active for several years. When you receive unsolicited junk e-mail, use common sense and discretion. Try to traffic mostly on secure web sites. Do

not click unnecessarily on unknown links and be careful about accessing links that invite you to “unsubscribe.” This action may simply notify a spammer that your account remains active. **Result:** Eventually you end up receiving even more spam.

*There are a myriad of services and programs you can purchase that are designed to reduce the spam that’s filling up your mailbox. However, remember that the spammers also have the new technology at their disposal and often seem to be one step ahead of the pack. At the very least, if you follow the steps outlined, you may be able to cut down on the proliferation of e-mail spam.*

## Facts and Figures

### *Timely points of particular interest*

- ➔ Health Savings Accounts (HSAs) -- The IRS has detected considerable interest in HSAs. These new products, used in conjunction with high-deductible health insurance plans, operate much like IRAs for qualified medical expenses. Now the IRS has issued a new notice providing guidelines on HSAs, including contributions and distributions, eligibility, rollovers and a host of related issues.
- ➔ Corporation Differences -- Although distinctions exist between S corporations and limited liability companies (LLCs), shareholders of both entities are not personally liable for corporate obligations. Also, profits and losses are passed through to both types of shareholders. However, there are additional restrictions for S corporations, such as being limited to 75 shareholders and being allowed only one class of stock (but different voting rights are permitted).