DYER & ASSOCIATES, P.C.
Certified Public Accountants
10415 Armory Avenue
Kensington, MD 20895
(301) 654-6200 FAX: (301) 692-1990

Client Information Bulletin

February 2010

Giving Gifts of Property to Charity

Avoid tax pitfalls on noncash donations

Despite recent changes requiring stricter substantiation of monetary gifts to charity, the tax rules are pretty straightforward when you write out a check or charge a donation by credit card. In general, you can deduct the full amount of your charitable donation in the year in which you make the gift.

However, the rules are considerably more complex if you give appreciated property to charity. Fortunately, you can realize significant tax savings with some careful planning.

Starting point: The term "appreciated property" applies to property with a fair-market value (FMV) in excess of your basis. Ordinarily, your "basis" is what you paid for the property. Your basis for depreciable property is reduced by any depreciation deductions allowed over the years. In addition, if you acquired the property by gift, you assume the same basis the donor had immediately before the gift.

However, depending on how long the property has been held, a different set of rules may apply. This is where things can get tricky. For this purpose, the deduction for donated property held for one year or less is limited to the property's basis.

Example 1: Suppose you donate shares of stock worth $3,000 to a charity. You acquired the stock six months ago for $2,000. As a result, your deduction is limited to $2,000, your original basis in the property.

On the other hand, there is a different rule if you have held the property longer than one year (i.e., the holding period to qualify for long-term capital gain). In this case, you can generally deduct the full FMV of the property. In other words, the appreciation is untaxed—forever.

Example 2: Assume the same facts as before, except that you bought the stock more than a year before making the charitable contribution. As a result, you can deduct the FMV of $3,000—$1,000 more than before.

But that is not the end of the story. There are several other potential pitfalls to avoid. In some cases, your deduction for property that has been held for more than one year may be limited to your basis.

Say you contribute tangible personal property that is put to an "unrelated use" by the charity. A painting donated to an art museum and prominently displayed would be related to the use. However, artwork given to a hospital and relegated to a closet is not. The deduction is limited to your basis.

Other special rules may apply to gifts of appreciated property. For example, no deduction is allowed for a gift of a "future interest" in tangible personal property (i.e., the

Inside

charity does not receive present possession of the property). Finally, deductions for charitable donations may be reduced for certain high-income taxpayers.

Note that you may need additional records when you file your tax return. A written description is required for noncash gifts exceeding $500. Also, you must obtain an independent appraisal for a gift valued at more than $5,000.

***Final point**: Before you donate property to charity, consult a tax adviser. This is the best approach for maximizing deductions.*

Facing Options on an Inherited IRA

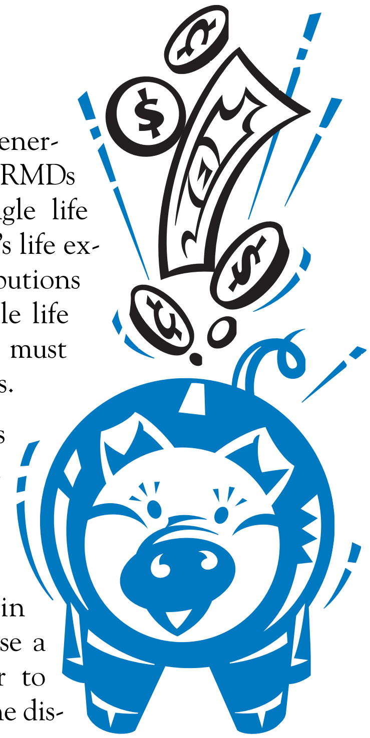
Several choices available to beneficiaries

Did you recently inherit a traditional IRA? The tax rules in this area can be perplexing, especially since you are likely to be emotional over the passing of a loved one. Take a deep breath and consider the options.

For simplicity, this discussion will be divided into two sections: one for spousal beneficiaries and the other for nonspouse beneficiaries. Spousal beneficiaries generally have more flexibility.

Spousal beneficiaries: Assuming you are the sole beneficiary of a traditional IRA, you may choose to treat your spouse's IRA as your own. This means you can contribute to the IRA, if you have compensation. Furthermore, if you are younger than 70½, you do not have to take required minimum distributions (RMDs). **Note**: RMDs are generally required after reaching age 70½, but this requirement for IRAs has been suspended for the 2009 tax year.

Alternatively, you may leave the IRA in your spouse's name, with you as the beneficiary. If your deceased spouse died after age 70½, you generally must base subsequent RMDs on the longer of your single life expectancy or the deceased's life expectancy. Otherwise, distributions may be based on your single life expectancy, or the account must be emptied out in five years.



Another possible option is to roll over the inherited IRA assets into your own IRA. The rollover is exempt from current tax liability if completed within 60 days. **Best approach**: Use a "trustee-to-trustee" transfer to avoid tax withholding on the distribution from the IRA.

Nonspouse beneficiaries: If you have inherited an IRA from someone other than a spouse, you cannot treat the IRA as your own. Thus, you are neither permitted to make subsequent contributions to the inherited IRA, nor can you roll over the funds to your own IRA. However, you can still arrange a trustee-to-trustee transfer to another IRA maintained in the name of the deceased IRA owner, with you as beneficiary. You must begin taking RMDs subject to the rules for IRA beneficiaries. (Remember, RMDs are suspended for the 2009 tax year.)

Distributions from an inherited IRA are taxed at ordinary income rates. (The maximum tax rate for 2010 is 35%.) If you fail to take an RMD, you must pay a penalty tax equal to 50% of the required amount of the distribution.

Be aware that this article only summarizes the main rules when you are the sole beneficiary. You must also be careful that the IRA is properly titled. In addition, other rules may apply when a Roth IRA is inherited. Contact a tax professional for assistance.

Do You Need Extra Time to File?

Due to your personal circumstances, you may not be able to complete your 2009 federal tax return on time. **But fear not**: You can still request a filing extension.

The IRS will grant an automatic extension of six months when a valid request is made before the tax return due date. The new deadline for your 2009 return will be October 15, 2010.

Be aware that you still must provide an estimate of your tax liability based on the information available to you. Also, you are generally required to pay at least 90% of your tax liability, through income tax withholding or estimated tax payments, by the original tax return due date. Otherwise, a late payment penalty will be assessed.

Seize More Control Over Your Business

Six areas for business owners to focus on

Without the proper "controls" in place, a small business can struggle or go under, especially in this tough economy. Although there are no guarantees, the following are basic guidelines to follow in six areas:

1. Sales: It is important that accurate sales figures are used to establish company revenue and direct inventory purchases. Implement detailed procedures for cash, checks, credit cards and online sales.

♦ Use an invoicing system for shipping goods.

♦ Ensure that sales figures are correct and commissions are not paid until funds are received.

♦ Reconcile sales with payments. Double-check sales against original invoices.

♦ Obtain proof of delivery when goods are shipped.

2. Accounts receivable: Failure to collect past due accounts can create cash-flow problems and erode profit. Establish credit and collection policies in writing, and follow through on their implementation (e.g., review credit balances on a regular basis).

♦ Separate accounts receivable from cash reporting.

♦ Have accounts "aged" regularly and authorize an independent review of the report.

♦ Cross-check noncash credits and bad debt write-offs.

♦ Establish numerical or batch-processing for billing.

♦ Initiate security measures for outside communications.

3. Accounts payable and purchases: Many companies are prone to mistakes in this area. Below are procedures for your staff to follow:

♦ Record purchase and accounts payable procedures.

♦ Initiate controls to cross-check duplications.

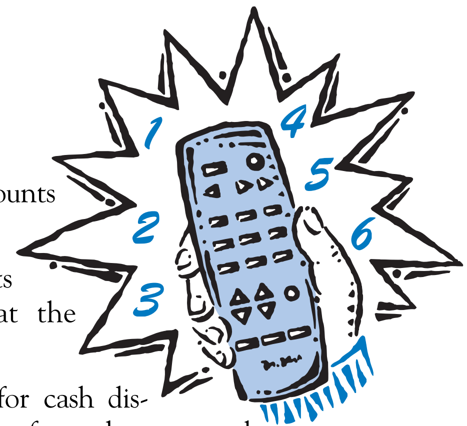
♦ Check pricing information and prices of competing vendors.

♦ Focus on large billings and items that may be disguised under smaller entries.

4. Cash accounts: If your business processes a significant number of cash transactions, it can easily fall prey to theft, especially if internal controls are substandard.

♦ Have employees balance cash at the end of their shifts.

♦ Safeguard checkbooks and other methods of disbursing funds.



♦ Reconcile all bank accounts on a regular basis.

♦ Separate cash deposits from other functions at the bank.

♦ Divide responsibility for cash disbursements and purchases from the approval process.

5. Payrolls: Thanks to recent technological advances, it is easier than ever for employees to commit fraud if tight internal controls are not established.

♦ Ensure that electronic passwords are protected and changed frequently.

♦ Review bank account deposits to ensure that wages are being disbursed properly.

♦ Separate responsibilities for payroll preparation, disbursement and distribution.

♦ Investigate variations in payroll expenses and monthly budgets.

♦ Train backups for critical payroll responsibilities.

6. Physical assets: It is also relatively easy for physical assets to be misplaced or misappropriated. Protect valuable property from external, as well as internal, access.

♦ Lock up laptops and other electronic devices.

♦ Record all asset purchases and maintain detailed records.

♦ Assign responsibility for supervising physical assets to a particular employee and a backup.

♦ Divide responsibilities involving expensive equipment among employees, if possible.

Finally, coordinate these activities with your business advisers. They can help you install some meaningful controls.

Give Us A Call!

Do you have any questions or comments about this newsletter or your individual situation? Please do not hesitate to contact our office. We would be glad to serve you in any way we can.

Computer Protection: Call a Traffic Cop

Install network firewall to filter Internet data

Security is increasingly becoming a major component of running a small business. This need has been complicated by technological advances in recent years. In particular, you cannot run the risk that unscrupulous computer hackers might "steal" your company's proprietary information.

If you have not yet installed an adequate firewall on your network, do not put this off any longer. And, if you already have a firewall in place, it may be time for an upgrade.

What exactly is a firewall? In basic terms, it is a software program or hardware device that filters data coming through Internet connections into your company's computer network. If the data sets off alarms due to perceived threats, the firewall will not allow it through.

In many cases, a small-to-midsized business will now have its computers interconnected on the network. The company might be connected to the Internet through a T1 or T3 line. If you do not have a firewall in place, all of the company's computers are at risk from someone else on the Internet.

What could happen? A knowledgeable hacker could probe those computers by trying to make FTP connections or telnet connections to them. If one of your employees unintentionally creates a security opening, an outsider could conceivably exploit the hole in the system.

What does a firewall do to deter hackers? It acts like a traffic cop because it uses a protocol to distinguish between legitimate and suspicious network traffic. Thus, it allows your employees to function in a normal manner, but it denies access to outsiders who may be malicious.

If you establish a firewall at every Internet connection through a T1 or T3 line coming into the network, the firewall can implement specific security rules. One idea is to limit the number of computers able to receive FTP traffic. Similarly, your company can implement comparable security measures for FTP servers, Web servers and so on.

Furthermore, a firewall enables a company to establish a methodology for connecting to Web sites and transmitting files over the network. To summarize, the firewall provides you with control over how and when employees use the computer network.

Be aware that a firewall may be customized to fit your company's needs. This means that you can add or remove filters based on several conditions. Some of these conditions are IP addresses, domain names, protocols, ports or specific words or phrases. As an example, your company might set up only one or two machines to handle a specific protocol and ban that protocol on all other computers.

What should you do now? If you're not computer-savvy, seek guidance from technology experts within your company, or enlist the services of outside consultants. The worst thing to do is to ignore the problem if you do not think you can handle it yourself. The future of your small business could be at risk.

Facts and Figures

Timely points of particular interest

➡**Tax Formula**—The tax law does not allow medical deductions for expenses that benefit an individual's general health. **New ruling**: A woman who could not breast-feed her child purchased infant formula instead. The IRS said the formula satisfies the baby's basic nutritional requirements, so it cannot be deducted as a medical expense. Accordingly, the cost does not qualify for reimbursement under a flexible spending account.

➡**Serious Business**—You may have seen first-hand how humor can lighten the mood in a somber workplace or defuse a potentially explosive situation. It can also increase productivity. But know that humor should have its boundaries. Although everyone's sensibilities will differ, it is usually better to poke fun at situations rather than people. Use your moral compass to avoid crossing the line.