



**COHEN, SMITH & COMPANY, P.A.  
CERTIFIED PUBLIC ACCOUNTANTS  
133 EAST INDIANA AVENUE  
DELAND, FLORIDA 32724-4329  
(386) 738-3300  
[www.cohensmithcpas.com](http://www.cohensmithcpas.com)**

**Interested in knowing more about our firm? Then take a minute to browse our website at [www.cohensmithcpas.com](http://www.cohensmithcpas.com) – read [about us](#) - [our services](#) - and the [people behind the name](#).**

**We are pleased to provide you our online informational newsletter which we believe you will find of interest. Each month brief articles on relevant topics will be included, along with a tax calendar for the current and following months.**

### **August 2006**

#### **In This Issue**

Intangible Tax repealed  
Consider selling, rather than trading-in used business vehicles  
Diesel fuel and electricity use for agricultural purposes  
S-Corporation compensation to owners  
SIMPLE IRA Plans – keeping the Plan Document current  
Tax Calendar

#### **Intangible Tax repealed**

Governor Jeb Bush has signed HB209 which eliminated the often maligned Florida Intangible Tax for 2007 and thereafter. Prior to eliminating the tax, Governor Bush had championed the cause to reduce the tax to on-half mil. Thousands of Florida residents, corporations, partnerships and limited liability companies will benefit from this tax relief measure.

### **Consider selling, rather than trading-in used business vehicles**

Although a vehicle's value typically drops fairly rapidly, tax rules limit the amount of annual depreciation that can be claimed on most cars and light trucks. Thus, when it's time to replace the vehicle, it's not unusual for its tax basis to be higher than its value. If you trade the vehicle in on a new one, the undepreciated basis of the old vehicle simply tacks onto the basis of the new one (even though this extra basis generally doesn't generate any additional current depreciation because of the annual depreciation limits). However, if you sell the old vehicle rather than trading it in, any excess of basis over the vehicle's value can be claimed as a deductible loss to the extent of your business use of the vehicle.

### **Diesel fuel and electricity use for agricultural purposes**

New Florida tax legislation provides that electricity used directly and exclusively for production or processing of agricultural products on the farm is exempt from sales and use tax. This exemption applies only if the electricity used for the exempt purposes is separately metered. If the electricity is not separately metered, it is conclusively presumed that some portion of the electricity is used for a nonexempt purpose, and therefore, all of the electricity is taxable. Therefore, agricultural users should review their consumption to determine if the sales tax benefit of separate metering is cost effective.

### **S Corporations compensation to owners**

One of the potential tax benefits of using an S-corporation for business purposes is lower Social Security and Medicare taxes that might otherwise be paid on profit earned by the business. For example, operating a business as a partnership or sole proprietorship exposes all earnings (profit) to the combined 15.3% tax rate on the first \$94,200 of earnings. On the other hand, profit earned by an S corporation is not subject to Social Security or Medicare tax. Often business owners attempt to maximize this tax benefit by paying themselves minimal, or even zero, wages which are subject to Social Security and Medicare tax.

The IRS has recently stepped up its enforcement and audit efforts in this area. Furthermore, recent court decisions make it clear that S corporation profits can be recharacterized as wages subject to payroll taxes, when actual wages paid are unreasonably low. Businesses can then become subject to a host of penalties, in addition to the payroll taxes.

To avoid running afoul of this issue, it is extremely important for S corporation owners to receive a reasonable compensation for the services provided to their business. Should you have questions in this area, we can assist in evaluating your exposure to this potential payroll tax liability issue.

### **SIMPLE IRA Plans – keeping the Plan Document current**

#### **Background**

SIMPLE IRA plans are an easy way for employers with no more than 100 employees (counting only those who make at least \$5,000) to offer a retirement plan. Under such a plan, employees may choose to defer a portion of their salaries into the plan and employers either contribute matching or nonelective contributions on behalf of each eligible employee

One of the advantages of a SIMPLE IRA plan is that it's easy to set up. Eligible employers simply complete a three-page form (Form 5304-SIMPLE) if they want the employees to select their own financial institution to be the trustee of their account or Form 5305-SIMPLE in the event the employer wants to make the selection to ensure that all employees' SIMPLE IRA accounts are at the same place. The plan is deemed to be adopted once the employer completes its portion of the form and the employees receive a copy of the form and complete their portion.

The paperwork doesn't even go to the IRS. Instead, the employer maintains the originals in its files. Then, once a year (and more than 60 days prior to the start of the calendar year), employers must provide employees with a notice about the plan. The simplest way to meet this requirement is to give the employees a copy of the Form 5304-SIMPLE (including instructions) or Form 5305-SIMPLE and the plan's withdrawal and transfer procedures.

### **Keeping the Plan Document Current**

The procedures outlined above work fine, as long as the rules for SIMPLE IRAs don't change. However, the 2001 Tax Act made several improvements to these plans (e.g., to allow catch up contributions for individuals age 50 and up and to increase the allowable elective deferrals for all participants). As a result, employers were supposed to adopt an updated version of their SIMPLE IRA plans by the end of 2002.

Based on their examinations of employer's plans, the IRS recently announced that many of the plans haven't been updated for the 2001 Tax Act changes. That's not surprising because employers who adopted plans using a version of Form 5304-SIMPLE or Form 5305-SIMPLE released prior to March 2002 or a financial institution's plan dated prior to April 2002 likely have out-of-date plans.

Given the confusion over the need to update the plans and in keeping with the spirit of simplicity, which is the premise of the plans, the IRS is offering a period of relief for employers to bring their SIMPLE IRA plan documents into compliance. To take advantage of this relief, employers with out-of-date plans need to readopt the plan using a current (August 2005) Form 5304 or 5305 or adopt a financial institution's plan that includes the 2001 Tax Act's changes. The deadline for taking this action is the end of 2006.

### **Tax Calendar**

#### **AUGUST 2006**

##### **August 10**

Social Security, Medicare, and withheld income tax. File Form 941 for the second quarter of 2006. This due date applies only if you deposited the tax for the quarter in full and on time.

##### **August 15**

Social Security, Medicare, withheld income tax. If the monthly deposit rule applies, deposit the tax for payments in July.

Nonpayroll withholding. If the monthly deposit rule applies, deposit the tax for payments in July.

## **SEPTEMBER 2006**

### **September 11**

Employees who work for tips. If you received \$20 or more in tips during August, report them to your employer. You can use Form 4070.

### **September 15**

Individuals. Make a payment of your 2006 estimated tax if you are not paying your income tax for the year through withholding (or will not pay in enough that way). Use Form 1040-ES. This is the third installment date for estimated tax in 2006.

Corporations. File a 2005 calendar year income tax return (Form 1120 or 1120-A) and pay any tax due. This due date applies only if you timely requested an automatic six-month extension.

Deposit the third installment of estimated income tax for 2006. Use the worksheet Form 1120-W to help estimate tax for the year.

S corporations. File a 2005 calendar year income tax return (Form 1120S) and pay any tax due. This due date applies only if you timely requested an automatic six-month extension. Provide each shareholder with a copy of Schedule K-1 (Form 1120S).