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Interested in knowing more about our firm? Then take a minute to browse our website at 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.

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Did You Know?

U.S. real estate properties returned 20.06% in 2005, not counting any leverage. That was the largest gain since 1979, when the return was 20.46%.

Source: National Council of Real Estate Investment Fiduciaries

Tax Increase Prevention and Reconciliation Act (TIPRA)

Preferential Tax Rates on Capital Gains and Dividends Extended through 2010

For individual taxpayers, Tax Increase Prevention and Reconciliation Act (TIPRA) extends through 2010 the preferential federal income tax rate structure for long-term capital gains and qualified dividends. The maximum rate on most long-term gains and dividends will remain at the current 15%. Even better, the current 5% rate will continue through 2007 for long-term gains and qualified dividends earned by individuals in the lowest two regular tax brackets (the 10% and 15% brackets) before dropping to 0% (that's not a typo) for 2008 through 2010. (Prior law called for the rates to rise after 2008).

One-year Alternative Minimum Tax Fix

TIPRA includes two quick fixes, for this year only, to the individual alternative minimum tax (AMT) rules. These changes will prevent millions more (possibly including you) from owing the dreaded AMT this year.

Under the first fix, the 2006 AMT exemption amounts are increased as follows:

- To \$62,500 for married individuals who file jointly (up from the 2005 figure of \$58,000). Without the fix, the 2006 exemption would have been only \$45,000.
- To \$42,500 if you are a single individual or head of household (up from the 2005 figure of \$40,250). Without the fix, the 2006 exemption would have been only \$33,750.
- To \$31,275 if you use married filing separate status (up from 2005 figure of \$29,000). Without the fix, the 2006 exemption would have been only \$22,500.

Under the second fix, you can use your nonrefundable personal tax credits (such as the dependent care credit and the Hope Scholarship and Lifetime Learning higher education credits) to reduce both your 2006 regular tax and AMT bills (same as for 2005). You will also be able to use the new residential and nonbusiness energy property credits to reduce both of these taxes for 2006. So, if you are considering making energy efficient improvements to your home, you might want to do it now rather than waiting until next year.

Favorable “Section 179 Deduction” Rules Extended through 2009

The so-called Section 179 rules allow many small businesses to deduct the full cost of most equipment and software additions (whether new or used) in the first year they are put to use. For tax years beginning in 2006, the maximum Section 179 write-off is a generous \$108,000. However, the maximum Section 179 deduction was scheduled to decrease to only \$25,000 for tax years beginning in 2008 and beyond. Thankfully, TIPRA extends the current taxpayer-friendly Section 179 rules by two years, through tax years beginning in 2009.

Kiddie Tax Rules Now Apply to Older Kids, Starting Right Now!

The so-called Kiddie Tax rules can cause a dependent child’s unearned income (typically from investments) to be taxed at the parent’s higher marginal federal income tax rate. Until now, the Kiddie Tax only applied through the year before a child turned age 14. In other words, the Kiddie Tax issue ceased to exist for the year the child turned 14 and for all subsequent years. Unfortunately, TIPRA extends the Kiddie Tax rules through the year before a child turns 18, starting with 2006. More specifically: for this year and beyond, the Kiddie Tax issue will be lurking until the year that a dependent child turns 18. Children who are still age 17 as of 12/31/06 are potential Kiddie Tax victims this year. The only saving grace is that, for 2006, the Kiddie Tax only affects under-age-18 dependent children with unearned income in excess of \$1,700.

Bottom Line: You may have a dependent child who is exposed to the Kiddie Tax this year, even though it didn’t apply last year.

Mid-Year Tax Planning Tips

Retirement Planning

The middle of the year is a good time to check up on your contributions to a tax-deferred retirement plan. Make sure you’re getting the maximum tax deferral from a 401(k) or other employer-sponsored plan.

If you’re a business owner or if you have self-employment income, there are some other things you might consider at this time of year.

SIMPLE plans

For most types of retirement plans, the key deadlines are year-end, April 15, or the due date of your tax return. There is one exception: You must set up a Savings Incentive Match Plan for Employees (SIMPLE) plan by October 1 of the year for which you wish to make a contribution.

SIMPLE plans may be especially desirable if you have a small amount of self-employment income. With a SIMPLE plan, you can contribute (and deduct) up to 100% of that income, to a maximum of \$10,000 in 2006 (\$12,500 if you're 50 or older by year-end).

Because of the October 1 deadline, you should start making arrangements soon if you want to have a SIMPLE plan in effect for 2006.

SEP plans

In addition, there might still be time for business owners or people with self-employment income to use a retirement plan to shelter income from 2005. That may be the case if you received a filing extension for your 2005 income tax return.

If you have received an extension, you have until October 16 to create and contribute to a simplified employee pension (SEP) plan for last year. Such plans often work best if you have self-employment income or if you run a business with only a few employees.

Deductible SEP contributions can be as much as 25% of income, up to \$42,000 for 2005. As their names suggest, both SEP and SIMPLE plans require little paperwork.

Estimated Taxes

Two out of the four annual estimated tax payments are due around mid-year, on June 15 and September 15. If you pay enough to meet a "safe-harbor" test, you won't owe an underpayment penalty.

To reach a safe harbor, you can pay 110% of last year's tax obligation (100%, if your 2005 adjusted gross income was \$150,000 or less). However, if your income will be lower this year, perhaps because you won't have large capital gains, it may be possible to pay less and avoid a penalty. If you would like to review your 2006 estimated tax situation, give us a call.

Business Equipment Purchases

Mid-year is a good time to re-evaluate equipment purchases. Your company may be able to use the "Section 179" election, which permits taxpayers to take an immediate writeoff for equipment outlays rather than taking depreciation deductions over several years.

In 2006, you can deduct up to \$108,000 worth of equipment costs. However, if you buy over \$430,000 worth of equipment, you start to lose the tax benefit. Suppose, for example, your company buys \$450,000 worth of equipment this year. The excess \$20,000 is deducted from your Section 179 allowance so you can deduct only \$88,000 worth of equipment purchases in 2006. The other \$362,000 worth of equipment (\$450,000 minus \$88,000) must be depreciated over a multi-year schedule.

Planning Your Summer Vacation? Mix Business with Pleasure

By knowing the rules and following them carefully, you can get the IRS to help cover the costs of your summer travels. But remember that this tactic taken to excess can be an expensive mistake.

In general, travel and entertainment (T&E) deductions attract a great deal of IRS scrutiny—especially true if these items are large in relation to your income. IRS agents can easily understand these expenses and questions are likely to be raised.

On the Record

When an IRS agent questions you about your T&E deductions, you need to have answers. That's why it's vital to keep records showing where you traveled, whom you entertained, how much you spent, and the business purpose of each expenditure.

Generally, the most important factor is being able to show that a trip was *primarily* for business. If you can do so, your travel expenses (such as air fare) will be fully deductible along with some, if not all, of your hotel bills.

Suppose, for example, you take a business trip that lasts from Monday through Friday. After you've completed all your business meetings, you spend the next weekend (and even the following Monday) at the same hotel, playing golf and tanning by the pool.

Because you devoted more time (five days) to business than to pleasure (two or three days), your air fare will be deductible. Although you can't deduct hotel and meal costs for personal days, such costs may be written off if they relate to business days.

Continuing this hypothetical example, you must demonstrate that the first five days really were focused on business. A log will help, and so will copies of pre-trip correspondence (including email) arranging meetings. You also should follow up on your meetings: not only will this strengthen your tax position, it's likely to help you reap rewards from those discussions.

All in the Family

Summer vacations usually involve traveling with your family. How will that affect your tax deductions?

When it comes to hotel bills, you can deduct the cost you would have paid traveling alone—which generally is more than 50% of the double room rate. Ask your hotel for a room rate schedule showing its single rates for the days you're there.

Foreign Travel

Special rules apply for business trips outside the United States. Generally, all costs, including transportation, must be allocated between the business and personal portions of your trip.

However, if the major reason you took the trip was not for a holiday or a vacation, you can take a 100% travel write-off and deduct a substantial share of other costs. Again, you should keep records to demonstrate that the principal reason for taking a trip was business-related.

Although only amounts directly allocable to business are deductible, you can avoid the allocation issue if you are out of the country seven days or less. The primary purpose of the trip must be for business in order for anything to be deductible.

Tax-Free Fortnight

While you're traveling this summer, for business or pleasure or both, you might rent your house while you're away. If you live in a prime tourist area or near the site of a major golf tournament, you might be able to collect thousands of dollars for a two-week rental.

What's more, those dollars can be tax-free. Under the tax code, you can rent a home for up to 14 days per year without having to declare any taxable income.

TAX CALENDAR

JUNE 2006

June 12

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

June 15

Individuals. If you are a U.S. citizen or resident alien living and working (or on military duty) outside the United States and Puerto Rico, file Form 1040 and pay any tax, interest, and penalties due. If you want additional time to file your return, file Form 4868 to obtain four additional months to file. Then, file Form 1040 by October 16.

If you are not paying your 2006 income tax through withholding (or will not pay in enough during the year tax that way), pay the second installment of your 2006 estimated tax. Use Form 1040-ES.

Corporations. Deposit the second installment of estimated tax for 2006.

Employers. For Social Security, Medicare, withheld income tax, and nonpayroll

withholding, deposit the tax for payments in May if the monthly rule applies.

JULY 2006

July 10

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

July 17

Employers. For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in June if the monthly rule applies.

In accordance with IRS Circular 230, this newsletter is not to be considered a “covered opinion” or other written tax advice and should not be relied upon for IRS audit, tax dispute, or any other purpose.
