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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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New Pension Act Covers More Than Just Pensions

You may have heard about the Pension Protection Act of 2006 (Pension Act). Many of the changes in this legislation actually have nothing to do with pension plans, even though its main purpose was purportedly to shore up traditional defined benefit pension plans, including those of the legacy airlines, and avoid the need for a future taxpayer-funded bailout. Other areas affected by the Pension Act include, but are not limited to, education planning, retirement planning, and charitable giving. This article summarizes some of the key points in the new law, other than those pertaining to large pension plans, most likely to affect individual taxpayers.

Section 529 Education Plans

The Pension Act makes permanent the current ultra-favorable federal income tax treatment of Section 529 plans, which are used to finance college education costs. Of particular importance, qualified Section 529 plan distributions (i.e., money spent for qualified higher education expenses) will continue to be federal-income-tax-free, even after 2010. Prior to passage of the Pension Act, these distributions would have been taxable if made after 2010. This new provision eliminates the uncertainty about the tax status of post-2010 distributions, when many 529 plan beneficiaries would be in college and would need to withdraw plan assets for educational expenses. If you haven't previously invested in one of these plans, it may be time to reconsider them.

Retirement Planning

The Economic Growth and Tax Relief Reconciliation Act of 2001 made many favorable changes to help retirement savers. The most important provisions allow for bigger annual IRA and retirement plan contributions, additional (catch-up) contributions for those who are age 50 and older, and expanded opportunities to arrange for tax-free rollovers from retirement plans. However, all the favorable changes were scheduled to "sunset" (expire) after 2010. In other words, the less-favorable "old-law" rules would be reinstated beginning in 2011. The Pension Act makes the taxpayer-friendly changes in the 2001 legislation permanent by repealing the sunset provisions. So you no longer have to worry about rules from the "bad old days" kicking back in for 2011 and beyond. Therefore, it's basically "business as usual" with no need for adjustments on your part.

In addition, *starting in 2007*, you will be able to arrange to have all or part of your federal income tax refund direct deposited into your IRA (or your spouse's IRA if you file jointly).

Charitable Donations

The Pension Act also includes numerous changes affecting the tax treatment of donations to qualified tax-exempt charitable organizations. Here are the highlights of some of these important changes.

Donations directly out of IRAs

The Pension Act allows those who are age 70½ or older to claim tax-free treatment for otherwise taxable distributions from an IRA when the IRA money is paid out directly to a qualifying tax-exempt charity. This favorable new rule for "qualified charitable distributions" applies for 2006 and 2007. However, there is a \$100,000 annual cap on this privilege. Because this qualified charitable distribution is federal-income-tax-free, you don't get any federal income tax deduction. But, tax-free treatment for the distribution is effectively the same as a 100% write-off. The new rule benefits seniors who don't itemize as well as seniors who would be adversely affected by the "normal" restrictions on itemized charitable contribution deductions.

Qualified conservation contributions

The Pension Act liberalizes the rules for "qualified conservation contributions" made to qualified charitable organizations in 2006 and 2007 by individuals and private corporations. For this year and next, the maximum charitable deduction contribution base limitation (a percentage of adjusted gross income in most cases) and carryover period for unused deductions has been increased.

Cash donations under \$250

The Pension Act generally disallows any deduction for a charitable donation of cash, check, or any other monetary gift unless you have either a bank record (such as the cancelled check) or a written communication from the charity that adequately documents your donation. This unfavorable change is effective for tax years beginning after August 17, 2006, so most individuals won't be affected until 2007. But, starting next year, you'll need to write a check (and be able to produce a copy, if requested) or get some sort of documentation for all of your contributions.

Donations of used clothing and household items

The Pension Act completely disallows deductions for most donations of used clothing and household items that are in less than "good" condition. In other words, no more write-offs for "junk." Household items include furniture, electronics, appliances, linens, and similar items. However, an exception allows deductions for single items that are appraised for more than \$500, even if they are not in "good" condition. This unfavorable change is effective for donations after August 17, 2006, so donations made this year may be affected.

Conclusion

The Pension Protection Act of 2006 is truly a massive piece of legislation. While this article covers only a few of the changes, we hope you find it helpful. Please contact us if you have questions or require more information about this new legislation.

Money Market Funds Deserve Another Look

The yields of most fixed-income investments—including money market funds—are climbing as the Federal Reserve tightens short-term credit in its effort to stave off inflation fears, both real and imagined. While this may eventually put the brakes on economic growth, there is an upside: safe and easily accessible fixed-income investment alternatives are now yielding as much as 5% per year. At current rates, these investments will not only preserve your precious capital for short-term needs, but they also provide a small return in excess of the inflation rate, meaning the real value (i.e., the purchasing power) of your assets will grow. Just a few years ago, money market fund yields were laughably low and most investors took their short-term investment funds elsewhere (e.g., to short-term and intermediate bond funds). That's no longer the case as money market funds can offer competitive rates to complement the attributes that made them popular in the first place: liquidity and low risk.

Obtain Peace of Mind with Umbrella Liability Insurance

Umbrella liability insurance policies can provide protection against large personal liability claims. This coverage supplements your underlying liability coverage (such as your homeowners' policy). In fact, an underlying basic liability policy is a prerequisite for obtaining and maintaining umbrella coverage. Umbrella policies cover losses up to the stated maximum amount *less* the amount covered by the underlying basic policy.

For example, assume the Smith family carries \$300,000 of liability insurance under their homeowners' policy and supplements that coverage with a \$1 million umbrella policy. If a child is injured on their front lawn and the child's parents win a \$1 million judgment against the Smiths, the Smiths' homeowners' policy will pay \$300,000 of the claim and their umbrella policy will pay \$700,000 (\$1 million less the coverage limit of the underlying homeowners' policy).

Umbrella policies are a relatively inexpensive source of protection against catastrophic legal liability. A typical policy with a \$1 million coverage limit can be obtained for a few hundred dollars per year in most cases. Basic coverage under an umbrella policy is broad. Generally, they cover liability for bodily injury, mental anguish, shock, sickness, disease, disability, false arrest, false imprisonment, wrongful entry, wrongful eviction, malicious prosecution, discrimination, libel, slander, defamation of character, and invasion of privacy. Umbrella policies can be tailored to cover other types of claims, depending on your needs.

Umbrella policies often exclude coverage for the following: (a) the insured's obligation for workmen's compensation, unemployment compensation, or disability benefits; (b) property owned by the insured; (c) business pursuits; (d) owned or leased aircraft and certain watercraft; and (e) professional services (unless covered by the underlying policy).

Before purchasing an umbrella liability policy, you should make sure that the policy limitations and exclusions mesh with your activities and circumstances. You should also have your insurance agent confirm that the underlying auto and homeowner policy coverages are consistent with those required by the umbrella policy.

Due to policy exclusions and the possibility of insurer default, umbrella liability coverage, like any other form of insurance, does not provide complete protection. However, its relatively low cost and broad coverage make it a valuable part of most insurance plans.

Tax Calendar

October 16—Personal returns that received an automatic six-month extension must be filed today and any tax, interest, and penalties due must be paid.

Partnerships that received an additional six-month extension must file their Forms 1065 today.

Calendar year-end Estates and Trusts that received an additional six-month extension must file their Forms 1041 today.

October 31—The third quarter Form 941 (Employer's Quarterly Federal Tax Return) is due today and any undeposited tax must be deposited. (If your tax liability is less than \$2,500, you may pay it in full with a timely filed return.) If you deposited the tax for the quarter in full and on time, you have until November 13 to file the return.—If you have employees, a federal unemployment tax (FUTA) deposit is due if the FUTA liability through September exceeds \$500.

December 15—Calendar-year corporations must deposit the fourth installment of estimated income tax for 2006.