

TAX WARRIOR

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FALL 2007 NEWSLETTER December 1, 2007

AMT RELIEF? THIS YEAR?

As of the date of this newsletter, Congress still has not passed relief related to the Alternative Minimum Tax (AMT). Congress' intent is to have it hammered out by the end of the year. If so, a problem arises for the IRS, tax preparers, and people receiving refunds. Tax forms are fairly extensive and are interactive with each other. Proper forms will not be in place until well into tax season. This backs up work for IRS and delays refunds.

Congress did this in December of 2006, with changes to the Trusts. Forms to file the returns for trusts were available after the first week in February of 2007.

It might be nice if Congress spent more time doing their job than fighting with each other through sound bites.

MULTI-NATIONAL CORPORATIONS/STATE INCOME TAXES

Who gets the money from your Christmas purchases? Your answer could affect tax revenues for the state in which you live.

Purchases you make in California are taxable to the entity that sold it. The seller pays employees and people for other services. They are then taxed on that money. Those people then in turn expend money which is in turn taxable to the next person in the economic chain. Each step in the flow of money through the economy affects the revenue for a state. This can churn through the economy five to seven times. If the profits of the selling company go out of the state, the number can reduce to two (2) times. This reduces the amount of tax revenue your state derives through the income and sales tax. Note, this also applies to charities. Before you make a purchase or a gift, make sure the money is going to be used in your state and not someone else's.

BARRY BONDS' STEROID PROBLEM

What does Barry Bonds and his steroid problem have to do with taxes? Incriminating evidence on Mr. Bonds was found by an IRS agent that went through his garbage. Information in his garbage is now being used against him. The moral of the story: Don't put anything in your garbage you wouldn't want an IRS agent, law enforcement, or a court to be looking at. If you have any questions about it, destroy it.

Did you ever think the day would come when a shredder would be a household appliance.

THE HORRORS OF IRC SECTION 419(e) PLANS

The IRS issued two notices with regard to 419(e) Plans. They are Notice 2007-83 and 2007-84. These notices essentially say that any Section 419(e) Plan is subject to audit. The IRS took a further step and classified 419(e) Plans as "listed transactions". A listed transaction is a transaction classified as a potential tax abuse transaction. If you have a 419(e) Plan, this could be a Halloween horror for 2007. Why? First, since it is a listed transaction, your tax preparer must address your 419(e) and state it as a listed transaction on your return. This means the IRS can automatically select you and your 419(e) Plan for audit.

If you decide to go into a 419(e) Plan, you have to be advised it may cause an IRS audit. If you are going to get an IRS audit, why would you even do it?

Congress has not amended or repealed Section 419(e) of the Internal Revenue Code which means, according to the law, you can do a 419(e) Plan. Essentially, the IRS is administratively attacking and just about eliminating the use of 419(e) Plans.

No, there is not a problem with the Internal Revenue Service. The problem is with Congress and the administration that governs the IRS in the White House. If you have a problem, write to them.

The opinion of tax attorneys is that the IRS would lose any case based on these notices in front of the United States Tax Court. Who wants to pay \$100,000.00 to win a case?

LEASING TO WHOLLY OWNED C CORPORATIONS / ADMINISTRATIVE EXTORTION

The IRS has made administrative adjustments on a number of tax matters resulting in tax increases for taxpayers in specific situations. The leasing of equipment by shareholders to their wholly owned corporations is one of these. Under the lease agreement, the corporation undertakes responsibility for the care, upkeep, and maintenance of the equipment in exchange for lease payments made to the shareholder.

The Shareholder/Lessor takes no active steps in the management of the leased equipment. (See article entitled Leasing to C Corporations on our website at www.taxwarrior.net, under Articles.)

Leasing to a corporation allows the lease payments to the shareholder to not be subject to Medi-Care or self-employment taxes. Issues as to excessive compensation are also avoided.

The IRS has raised the issue simply because of the length of time of the leasing. The leasing activity must rise to the classification of a business for the IRS to win.

Some accountants feel that the law is on the IRS' side. It is not. The case the IRS has cited is the case *Cooper Tire & Rubber Co. Employees' Retirement Fund v. Commissioner*, 36 T.C. 96. This case is regarding nonprofit organizations and the issue of unrelated business income. This is a different tax than income tax. It is not applicable. In addition, since it is a different tax under the nonprofit organization, the IRS may not do discovery with regard to those issues from non-profit entities in an income tax audit.

In the leasing structure described in the above article on our Tax Warrior website, there are seven to ten cases decided before the tax court where the taxpayer had activities more extensive than described in the article, and the activity was found not to rise to the level of being a business.

If your accountant or tax advisor is advising you that you need to pay this tax, you should strongly consider getting a second opinion or finding another accountant.

DEDUCTION OF TRUST ADMINISTRATION EXPENSES

In July, 2007, the IRS issued proposed regulations requiring expenses on the administration of trusts to be subject to a two percent (2%) floor rule for miscellaneous itemized deductions. As a general rule, such administrative expenses are deductible to the beneficiaries of the trust as ordinary income, not subject to the two percent floor. This applies to every person who has a revocable trust after the creator has passed on, as well as other trusts.

NOTE: This is not a change in the tax law by Congress. This is an administrative change made by the Internal Revenue Service. As long as an expense is made for the benefit of the assets of the trust, it is deductible. The regulations require a determination of the type of expense. This is time consuming for each trust, and especially so for bank trust departments that manage a large number of trusts.

The entire tax community and the trust administrators are in an uproar over this change. Currently, *Knight vs. Commissioner*, is pending before the U.S. Supreme Court on the same issue. The IRS has totally ignored this case. The proposed regulations are beyond the scope of Section 67 of the Internal Revenue Code. This is another example of the Administration's attempt to increase taxes administratively, as opposed to law changes.

Remember, the head of the IRS and the head of the Treasury Department, Henry Paulsen, were all appointed by President Bush. If you have problems with this, it is not the IRS that is doing it. Do not write to your Congressman and tell them that you want the IRS abolished, write letters to the President and to your Representatives, including Charlie Rangle, the head of the House Ways and Means Committee.

FEDERAL ESTATE TAX REPEAL

On November 14th 2007, the Senate Finance Committee met concerning the Estate Tax. It still appears highly unlikely that the Federal Estate Tax (FET) is going to be repealed. During the hearings estimates were made of an annual income from Estate Tax of twenty-four billion dollars. A few years ago, the annual take was closer to sixty billion per year. Estimates from people doing projections for 2011, based on the current tax law, are looking at those projections as being somewhere between sixty and one hundred billion annually.

Congress' true concern is the loss of tax revenue for 2010 when the FET is repealed for one year.

Since the projected Alternative Minimum Tax (AMT) Legislation will reduce revenue without any corresponding tax increase, there is a greater concern.

SUB-PRIME CREDIT ISSUES / LOCAL GOVERNMENT'S CULPRIT?

The news media and government spokesman have pointed fingers at everybody as culprits in the Sub-Prime lending fiasco. One aspect in this problem was the soaring prices of houses, which caused many people to become Sub-Prime borrowers. Local, state and federal governmental agencies have taken absolutely no action to put any brakes on this issue. Why? Each of them was deriving tax money from the increasing numbers on sales of houses.

For local governments, the higher the value in the house, the greater the property tax. Local government placed numerous fees on developments to finance infrastructure for new construction. Many counties in California local agencies dealing with the developments, bill developers for their time and resources in reviewing the project in addition to these fees. Strange, I thought there were already budgets set up to pay for the sections of local government that provided these services. They can bill whatever they feel is appropriate to the developer, creating additional revenue for local governments. This is like taking a piece of the pie before it is baked. This all contributes to the increase in the cost of houses.

This is also the reason you are seeing more concentration of developments, to allow developers to have an economically viable project. This also reduces the number of trees and aggravates the problems with regard to global warming. Recent screaming and pounding by Mayor Gavin Newsome of San Francisco that the people needed to do something was caused by the fear in local government that when people begin defaulting on houses in large numbers, they will not be able to pay their property taxes, which is going to cause a problem with local budgets.

This Newsletter is not intended as legal or tax advice.

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