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SUMMER 2008 NEWSLETTER

This summer the Housing and Economic Recovery Act of 2008 (H.R. 3221) provided 15.1 billion dollars in tax incentives and offsets. Selected items from this Bill will be addressed in this and future newsletters. California has not done well in court on tax issues, including both California courts and Nevada courts. (See below).

1. Corporate Start-Up Expense Deduction. The American Jobs Creation Act of 2004 allowed businesses to deduct start-up expenses for the year of start up. Prior to that, start up expenses had to be amortized over a 60 month period. Temporary regulations now assume start-up costs will be deducted as incurred. To choose not to deduct the expenditures currently, the business must clearly elect to capitalize on them on a timely filed return for the year the business begins. A formal election to deduct the expenses is not required.

2. What the Franchise Tax Board Does in Las Vegas, Stays in Las Vegas. This involves Gilbert P. Hyatt and the California Franchise Tax Board (FTB). Mr. Hyatt worked in the development of microprocessors. He filed for patents in late 1970. This started a 20 year battle over his patents with a number of computer companies. The patents were awarded in 1990 and Mr. Hyatt moved to Las Vegas in 1991. Thereafter, Mr. Hyatt began to reap the rewards of his patents and efforts. FTB alleged he owed 7.4 million dollars in California income tax in 1993, which has since grown to in excess of 40 million dollars. Mr. Hyatt brought a tort action in Nevada over FTB auditors' conduct in the matter.

An extensive battle occurred with the FTB, including an unsuccessful challenge to the U.S. Supreme Court by the FTB, contending a tort action could not be brought against the FTB in Nevada. The FTB lost. Jurors in Clark County, Nevada, awarded Hyatt the sum of 388 million dollars, including approximately 250 million dollars in punitive damages. This action in Nevada was for tort actions based on the outrageous conduct of FTB auditors.

If you are a California resident, you will be helping to pay this award, assuming the FTB does not appeal the matter. This sends a warning to all taxing agencies. No one is above the law.

3. Probate Fees an Estate Tax? Proposition 6 was adopted June 8, 1982, adding Section 13301 of the Revenue and Taxation Code for California stating there cannot be any gift, inheritance, succession, legacy, income, or estate tax on the estate or inheritance of any person. In 2003, additional new probate filing fees were imposed in California based on the gross fair market value of the estate being probated.

Mr. Pierre P. Claeysens passed away with an estate of approximately 35 million dollars. The total filing fee with surcharges was in excess of \$74,000.00. The Executor of the Estate objected to the fees and appealed the Probate Court determination. The California Appeals Court determined the graduated fee imposed by the

Probate Court was in fact an inheritance tax and in violation of the Constitution of the State of California. It is yet to be seen whether this matter will be appealed to the California Supreme Court.

If you are an Executor or probate attorney, action should be taken to preserve the right to claim refunds on California Probate Court filing fees where possible.

4. Under New Preparer Penalties Regulations Anybody Could be a Tax Preparer. Our Winter 2007 Newsletter addressed the effect of tax preparer penalties and liabilities driving people out of the accounting profession. There are not enough qualified accountants to go around, while Congress has been expanding tax preparer penalties.

Recent proposed regulations are expanding preparer penalties to people that did not sign the return or even see it. On June 16, 2008, the IRS issued Proposed Regulations for IRC 6694 concerning preparer penalties. Any person providing advice substantially affecting a single item on any IRS return may be subject to preparer penalties.

If a return is audited and the examiner feels the position on an item would “more likely than not” not be sustained, any person that had any role in affecting that item could be subject to an audit for determination of preparer penalties. This could include your attorney, appraiser, financial advisor, bookkeeper, life insurance agent, next door neighbor, etc.

Note, for an audit to occur concerning preparer penalties, the taxpayer would have to tell the IRS about it as part of the audit. Conflict of interest issues may cause the loss of your legal advisor. If one of the advisors provided information detrimental to the taxpayer, would it reopen the initial audit? This could turn into a circus.

Attorneys have a problem. If they are aggressive, they risk penalties, and if not aggressive enough, malpractice lawsuits. Legal and accounting fees will be rising.

Are these Regulations supposed to help us out of a Recession? WRITE TO YOUR CONGRESSMAN OR SENATOR!

5. Election 2008. Considering the budgetary issues occurring across this country, you should not look at tax reform being high on the issue of either major political party.

6. Housing Bill: First Timers. The Act provides a 10% tax credit on the price of a home up to a maximum of \$7,500.00 per married individuals. Note, this credit unlike other credits is to be paid back in equal installments over 15 years. This makes it an interest free loan. (Feel the love?)

7. Exempt Organizations/Redesigned IRS Form 990. The IRS has redesigned IRS Form 990 for exempt organizations, for years beginning 2008. Tax exempt organizations should begin reviewing Form 990 and its instructions ASAP! The new form requires substantially more detailed information for the return. Check the IRS website for a draft of the new form and instructions.

8. Bail-Outs and Sovereign Wealth (SW). Hedge Funds and private equity have been joined by Sovereign Wealth in the economic and investment battlefield. SW's are hedge funds created by foreign countries and municipalities. Little regulatory or tax control by USA laws is available for SW's, hedge funds or private equity. This is one reason many oppose a repeal of the estate tax.

During bail-outs in the past with savings and loans and other banking institutions, help was provided to bail-out the shareholders, primarily for political reasons. If it turns out many of the shareholders of a governmental bail-out target are owned by SW of countries with whom we do not get along, we may wish to allow the risk of investing to take its course. After all, other countries do it to us.

A thought: If a country of origin of an SW fund causes turmoil in strategic areas of the world causing their stock to either go up or down which benefits their SW fund, can the Securities and Exchange Commission allege insider trading? This is taking “war” to a totally different battlefield.

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