

Monthly Tax and Accounting Newsletter

Gregg Harvey, CPA

About This Newsletter

This monthly Newsletter is a free service provided by Gregg Harvey, CPA. It is emailed every month to clients and to select members of the Rochester Regional Chamber of Commerce.

This Month's Contents:

This month's newsletter covers 401(k) rollovers, education credits and educator expenses, commuting between two job sites, husband-wife partnerships, mortgage debt forgiveness, and other topics.

Rollover of 401(k)

Schedule C taxpayer has two separate solo 401(k)'s with two different brokerage firms. He wants to close one of them and transfer the funds to the other.

It is possible with a regular 401(k) and it sounds reasonable that since the taxpayer is the plan administrator (employer) that he can choose another vendor and transfer all the monies to the new vendor. Since he an employee as well as the employer and he still is employed, can this be done?

Yes he can rollover 1 solo 401(k) into another. Here is a good rollover chart from the IRS.

http://www.irs.gov/pub/irs-tege/rollover_chart.pdf

Child Tax Credit

With the Child Tax Credit, you may be able to reduce the federal income tax you owe by up to \$1,000 for each qualifying child under the age of 17.

A qualifying child for this credit is someone who meets the following criteria:

- Age - Was under age 17 at the end of 2007
- Relationship - Is your son, daughter, adopted child, stepchild or eligible foster child, brother, sister, stepbrother, stepsister, or a descendant of any of these individuals
- Citizenship - Is a U.S. citizen, U.S. national or resident of the U.S.
- Support - Did not provide over half of his or her own support, and
- Lived with you - Must have lived with you for more than half of 2007 (note that some exceptions to this criteria exist)

The credit is limited if your modified adjusted gross income is above a certain amount. The amount at which this phase-out begins varies depending on your filing status:

- Married Filing Jointly \$110,000
- Married Filing Separately \$55,000
- All others \$75,000

In addition, the Child Tax Credit is generally limited by the amount of the income tax you owe as well as any alternative minimum tax you owe.

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If the amount of your Child Tax Credit is greater than the amount of income tax you owe, you may be able to claim some or all of the difference as an “Additional” Child Tax Credit. The Additional Child Tax Credit may give you a refund even if you do not owe any tax. For 2007, the total amount of the Child Tax Credit and any Additional Child Tax Credit cannot exceed the maximum of \$1,000 for each qualifying child.

You may claim the Child Tax Credit on Form 1040 or 1040A. Details on how to compute the credit can be found in the forms’ instructions and in Publication 972, Child Tax Credit.

Education Credits

Education tax credits can help offset the costs of higher education for yourself or a dependent. The Hope Credit and the Lifetime Learning Credit are two education credits available which may benefit you. Because they are credits, rather than deductions, you may be able to subtract them in full dollar for dollar from your federal income tax.

The Hope Credit

Applies for the first two years of post-secondary education, such as college or vocational school. It does not apply to the third, fourth, or higher years of undergraduate programs, to graduate programs, or to professional-level programs.

It can be worth up to \$1,650 per eligible student, per year.

You're allowed a credit of 100% of the first \$1,100 of qualified tuition and

related fees paid during the tax year, plus 50% of the next \$1,100.

Each student must be enrolled at least half-time for at least one academic period which began during the year.

The student must be free of any federal or state felony conviction for possessing or distributing a controlled substance as of the end of the tax year.

The Lifetime Learning Credit

Applies to undergraduate, graduate and professional degree courses, including instruction to acquire or improve job skills, regardless of the number of years in the program.

If you qualify, your credit equals 20% of the first \$10,000 of post-secondary tuition and fees you pay during the year, for a maximum credit of \$2,000 per tax return.

You cannot claim both the Hope and Lifetime Learning Credits for the same student in the same year. To qualify for either credit, you must pay post-secondary tuition and certain related expenses for yourself, your spouse or your dependent. The credit may be claimed by the parent or the student, but not by both. Students who are claimed as a dependent cannot claim the credit.

These credits are phased out for Modified Adjusted Gross Income over \$47,000 (\$94,000 for married filing jointly) and eliminated completely for Modified Adjusted Gross Income of \$57,000 or more (\$114,000 for married filing jointly). If the taxpayer is married, the credit may be claimed only on a joint return

Educator Expenses

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If you are an eligible educator, you may be able to deduct up to \$250 of expenses you paid for purchases of books and classroom supplies. These out-of-pocket expenses may lower your 2007 tax bill even if you don't itemize your deductions.

Eligible Educator: The deduction is available if you are an eligible educator in a public or private elementary or secondary school. To be eligible, you must work at least 900 hours during a school year as a kindergarten through grade 12 teacher, instructor, counselor, principal or aide.

Qualifying Expenses: You may subtract up to \$250 of qualified expenses when figuring your adjusted gross income. Qualified expenses are unreimbursed expenses you paid or incurred for books, supplies, equipment (including computer equipment, software and services) and other materials that you use in the classroom. Supply expenses for courses in health and physical education are qualified only if they are related to athletics.

To be deductible, the qualified expenses must be more than the savings bond interest excluded on Form 8815, any nontaxable distribution from a qualified tuition program, and any tax-free withdrawals from your Coverdell Education savings account.

Commuting Expenses Between Two Job Sites

A taxpayer, who is a physical therapist, drives to five different places of employment. He drives at least 75 miles

per day. Sometimes he also drives from one place of employment to another to another and then home. Is there any way to take an employee expense on a 2106 here or are these miles just considered commuting?

Use the home to the first place of employment as commuting, between each job site as business use on 2106, then last site to home as commuting.

The problem is that you will have meticulous records including going from a job site to the post office or grocery store would be personal mileage or last site to a personal stop would be commuting then to home would be personal. Unless you have a mileage log that is very detailed it might be risky to take the deduction.

Final 1065 For Husband-Wife Partnership

The scenario is the partners were boyfriend/girlfriend in 2006 and girlfriend helped fund majority of startup and operating costs even though she wasn't really involved. The 2006 preparer filed 1065 in order to "benefit" girlfriend since the business incurred a loss, result for girlfriend was lower taxable income.

General partnership filed 1065 for 2006. Partnership was dropped in 2007 and sole proprietorship was assumed, no partnership business transacted in 2007.

Question: Do they need to file a 1065 for 2007 and mark final return? Obviously,

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they will file Schedule C for the remaining partner.

Yes. Also need final K-1s for the partners. At a seminar last fall, there was a discussion about the new rule that a husband/wife partnership doesn't have to file a 1065 anymore. The IRS spokesman suggested that we file a 1065 for 2007, put zeros on it, and mark it "final" to avoid getting a letter about a missing 1065. The IRS was expecting a lot of 1065s to "disappear" in 2007, and they weren't going to pursue them. It is still better to do the final return, just to be sure they know.

Mortgage Debt Forgiveness

Homeowners whose mortgage debt was partly or entirely forgiven during 2007 may be able to claim special tax relief by filling out newly-revised Form 982 and attaching it to their 2007 federal income tax return, according to the Internal Revenue Service.

Normally, debt forgiveness results in taxable income. But under the Mortgage Forgiveness Debt Relief Act of 2007, enacted Dec. 20, taxpayers may exclude debt forgiven on their principal residence if the balance of their loan was less than \$2 million. The limit is \$1 million for a married person filing a separate return. Details are on Form 982 and its instructions, available now on IRS.gov.

"The new law contains important provisions for struggling homeowners," said Acting IRS Commissioner Linda Stiff. "We urge people with mortgage problems to take full advantage of the valuable tax relief available."

The late-December enactment means that reporting procedures for this law change were not incorporated into tax-preparation software or IRS forms. For that reason, people using tax software should check with their provider for updates that include the revised Form 982. Similarly, the IRS is now updating its systems and expects to begin accepting electronically-filed returns that include Form 982 by March 3. The paper Form 982 is now being accepted, but the IRS reminds affected taxpayers to consider filing electronically, which greatly reduces errors and speeds refunds.

The new law applies to debt forgiven in 2007, 2008 or 2009. Debt reduced through mortgage restructuring, as well as mortgage debt forgiven in connection with a foreclosure, may qualify for this relief. In most cases, eligible homeowners only need to fill out a few lines on Form 982 (specifically, lines 1e, 2 and 10b).

The debt must have been used to buy, build or substantially improve the taxpayer's principal residence and must have been secured by that residence. Debt used to refinance qualifying debt is also eligible for the exclusion, but only up to the amount of the old mortgage principal, just before the refinancing.

Debt forgiven on second homes, rental property, business property, credit cards or car loans does not qualify for the new tax-relief provision. In some cases, however, other kinds of tax relief, based on insolvency, for example, may be available. See Form 982 for details.

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Borrowers whose debt is reduced or eliminated receive a year-end statement (Form 1099-C) from their lender. For debt cancelled in 2007, the lender was required to provide this form to the borrower by Jan. 31, 2008. By law, this form must show the amount of debt forgiven and the fair market value of any property given up through foreclosure.

The IRS urges borrowers to check the Form 1099-C carefully. Notify the lender immediately if any of the information shown is incorrect. Borrowers should pay particular attention to the amount of debt forgiven (Box 2) and the value listed for their home (Box 7).

New Form for Employees Misclassified as Independent Contractors

In 2007 were you an employee whose employer paid you as an independent contractor? Employees usually receive a Form W-2 while independent contractors usually receive a Form 1099-MISC.

Generally, a worker who received a Form 1099 for services provided as an independent contractor must report the income on Schedule C and pay self-employment tax on the net profit using Schedule SE. However, if the worker was actually an employee, rather than an independent contractor, the worker is not required to pay the full self-employment tax, and expenses can only be deducted as an itemized deduction.

Beginning in 2007, Form 8919, Uncollected Social Security and Medicare Tax on Wages, may be used if

you were an employee and your employer did not withhold your share these taxes and you meet certain criteria. These taxes will then be credited to you social security records.

To be eligible to use Form 8919 you must meet one of several criteria indicating that you were an employee while performing these services. The criteria include:

- You filed Form SS-8, Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding, and received a determination letter from the IRS stating that you are an employee of the firm.
- You have been designated as a “section 530 employee” by your employer or by the IRS prior to January 1, 1997.
- You have received other correspondence from the IRS that states you are an employee.
- You were previously treated as an employee by the firm and you are performing services in a similar capacity and under similar direction and control.
- Your co-workers are performing similar services under similar direction and control and are treated as employees.
- Your co-workers are performing similar services under similar direction and control and filed Form SS-8 for the firm and received a determination that they were employees.

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- You have filed Form SS-8 with the IRS and have not yet received a reply.

Income From Foreign Sources

Many United States citizens and resident aliens receive money from foreign sources. These taxpayers must remember that they must report all such income on their tax return, unless it is exempt under federal law.

U.S. citizens and residents are taxed on their worldwide income. This applies whether a person lives inside or outside the United States. Foreign income must be reported on a U.S. tax return whether or not the person receives a Form W-2, Wage and Tax Statement, a Form 1099 (information return) or the foreign equivalent of those forms.

Foreign source income includes but is not limited to earned and unearned income, such as:

- Wages and tips
- Interest
- Dividends
- Capital Gains
- Pensions
- Rents
- Royalties

An important point to remember is that individuals living outside the U.S. may be able to exclude up to \$85,700 of their 2007 foreign earned income if they meet certain requirements. However, the foreign earned income exclusion does not apply to payments made by the U.S. government to its civilian or military employees living outside the U.S.

For more information, check out IRS Publication 54, Tax Guide for U.S. Citizens and Resident Aliens Abroad.

IRS Food Allowance For Child Care Providers

Breakfast \$ 1.06

Dinner \$ 1.97

Lunch \$ 1.97

Snack \$0.58

Stimulus Payment Note

Are you wondering what to do to ensure that you receive your economic stimulus payment which the IRS will begin to send out this May? In most cases you will not have to do anything extra. If you are eligible for a payment, all you have to do is file a 2007 tax return and the IRS will do the rest.

However, recipients of Social Security, certain Veterans' and Railroad Retirement benefits and low-income workers who don't normally need to file may have to take steps to insure receipt of the stimulus payment.

If you are in this group and normally would not be required to file a tax return, you need to file a 2007 tax return this year to receive an economic stimulus payment. The return must show at least \$3000 in qualifying income.

Qualifying income includes Social Security benefits, certain Railroad Retirement benefits, certain veterans' benefits and earned income, such as

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income from wages, salaries, tips and self-employment. While these people may not be normally required to file a tax return because they do not meet the filing requirement, the IRS emphasizes they must file a 2007 return in order to receive a payment.

The IRS has released a sample version of a Form 1040A that highlights the simple, specific sections of the return that can be filled out by people in these categories to qualify for a stimulus payment.

For more information see IRS Fact Sheet FS 2008-16 Stimulus Payments: Instructions for Low-Income Workers and Recipients of Social Security and Certain Veterans' Benefits available on www.irs.gov.

For More Information

For more information on anything covered in this Newsletter, please contact me. I provide tax, accounting, consulting, and other business services such as payroll and medical billing.

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