



## Tax and Business Spring 2010

### The HIRE Act: Tax-Saving Opportunities for Most Employers

In all the attention surrounding the health reform legislation over the past few weeks, many people have missed the benefits provided by another recent piece of Congressional legislation. The Hiring Incentives to Restore Employment (HIRE) Act may have a cutesy name, but it provides employers with two important tax-saving opportunities.

The Act gives incentives to employers - both for-profit entities and not-for-profit organizations - that hire new employees who were previously unemployed or working only part time. There are two potentially beneficial opportunities in the new Act: a "Social Security tax holiday" and a potential credit of \$1,000 per qualified hire.

Businesses, agricultural employers, tax-exempt organizations, and public colleges and universities are all eligible to claim the payroll tax benefit for qualified new employees. Household employers cannot claim this new tax benefit.

Qualified employees are those who:

1. were unemployed for at least 60 days before beginning work, or
2. worked fewer than a total of 40 hours for someone other than the new employer during the 60-day period immediately preceding the date of employment.

Employers who hire qualified workers between February 4, 2010 and December 31, 2010 may qualify for a nice tax incentive: exemption, for the remainder of 2010, from having to pay their portion of the 6.2% Social Security taxes on wages paid to these workers after March 18, 2010.

This reduced tax withholding will not affect the employee's future Social Security benefits. Note that employers still need to withhold the employee's 6.2% share of Social Security taxes as well as income taxes. Further, both the employer and employee's shares of Medicare taxes (1.45% each) would still have to be withheld/paid on these workers' 2010 wages.

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The second strategic tax opportunity in the HIRE Act is a new, per-qualified-hired-worker credit. For each formerly unemployed worker retained for at least a year, businesses may claim an additional general business tax credit of up to \$1,000 per worker when they file their 2011 income tax returns.

“These tax breaks offer a much-needed boost to employers willing to expand their payrolls, and businesses and nonprofits should keep these benefits in mind as they plan for the year ahead,” said IRS Commissioner Doug Shulman.

The two tax benefits are especially useful to employers who are expanding their employee base by adding positions to their payrolls.

There are a couple of catches in the HIRE Act. New hires filling existing positions may also qualify for the “Social Security tax holiday” and the \$1,000 credit - but only if the workers they are replacing left voluntarily or for cause. Note also that family members and other relatives of business owners do not qualify for these incentives.

And, of course, there are administrative requirements in the HIRE Act. The new law requires that the employer get a statement from each eligible new hire certifying that he or she was unemployed during the 60 days before beginning work or, alternatively, worked fewer than a total of 40 hours for someone else during the 60-day period. The IRS is currently developing a form employees can use to make the required statement.

Employers claim the payroll tax benefit on the federal employment tax return they file with the IRS (generally Form 941). Eligible employers will be able to claim the new tax incentive on their revised employment tax form for the second quarter of 2010.

Revised forms and further details on these two new tax provisions will be posted on [www.irs.gov](http://www.irs.gov) during the next few weeks.

Overall, these two new tax incentives can be beneficial to employers who hire workers in 2010. Check with your tax advisor to see if your organization qualifies and to determine which steps you need to take to benefit from these tax-saving opportunities.

## Deduction Tips for Contributors to Haiti Relief Efforts

Congress has passed a bill (HR 4462) to permit taxpayers contributing to Haitian relief charities to elect to treat contributions made after Jan. 11, 2010, and before Mar. 1, 2010, as if the contributions had been made on Dec. 31, 2009. If the election is made, Haiti relief donations would be deductible on the 2009 return, not the 2010 return. This option would be available only if the contribution is made in cash and otherwise meets the requirements for charitable contribution deductions under Code Sec. 170 as summarized below.

- Contributions to domestic, tax-exempt, charitable organizations providing assistance to individuals in foreign lands are tax-deductible, provided that the U.S. organization has full control and discretion over the uses of donations.
- Contributions to foreign organizations generally are not deductible, nor are contributions to benefit specific individuals or families.
- To substantiate charitable contributions of money, regardless of amount, a taxpayer must have a bank record or a written communication from the charity showing the name of the charity and the date and amount of the

Tax Department  
**317.885.2620**

Atlanta  
**678.518.5301**

Chicago  
**630.682.9797**

Colorado Springs  
**719.528.6225**

Dallas  
**214.624.5077**

Denver  
**720.283.7326**

Indianapolis  
**317.885.2620**

Los Angeles  
**714.671.9300**

Orlando  
**407.883.4671**

San Diego  
**858.638.7220**

contribution. One additional substantiation method is allowed individuals for Haitian relief contributions: monetary contributions made via text message on a cellular telephone may be substantiated with a telephone bill that shows the charitable organization's name, contribution date, and the amount of the contribution.

- Contributions are deductible in the year made unless donated for Haitian relief after Jan. 11, 2010, and before Mar. 1, 2010, in which case the contribution can be taken in on either the 2009 or 2010 return. To claim the donations, the taxpayer must itemize deductions.
- Generally, the deduction for charitable contributions is limited to 50% of the taxpayer's adjusted gross income, with a 5-year carryover period for excess deductions. The Haitian relief donations are subject to the normal limitations and carryover.
- For high-income taxpayers, there is also a limitation on overall itemized deductions for 2009, but there is no overall limitation for 2010. Therefore, the tax benefit for these individuals may be greater by waiting until 2011 to claim their Haitian relief donations on their 2010 returns.

On its website, the IRS has posted deduction tips for taxpayers planning to make contributions to aid Haitian earthquake victims.

**California** - At this time, California does not conform to the accelerated deduction for Haiti contributions but did enact conformity when similar federal legislation was passed in regards to Indian Ocean tsunami contributions. It is anticipated that California will likely conform.

## What's Best...Tax-Free or Taxable Interest Income?

A frequent tax strategy question is whether it is better to invest for tax-free or taxable interest. Generally, taxable interest will provide the greater return, but this may not hold true after taking into account taxes on the income. The question, then, is really which option provides the greater "after-tax" return. Interest derived from "municipal bonds" is generally tax-free for federal purposes and also tax-free for a particular state if the bonds are issued by that state or its local governments. In addition, interest from U.S. Government Bonds cannot be taxed by any state.

Here are some issues to consider when deciding between taxable or tax-free income:

- Municipal bond interest. Interest earned from general-purpose obligations of states and local governments, which are issued to finance their operations, are generally tax-exempt for federal purposes. However, the various states usually only exempt interest from bonds issued from the state itself and local governments within the state. This results in two categories of municipal bonds, the tax-free federal and state and the tax-free federal only. Individuals can invest in municipal bonds by directly purchasing a bond or through funds that invest in municipal bonds. Some funds invest in bonds issued in a particular state only, providing residents of that state with income that is excludible on their state's return.

In general, tax-free bonds are likely to be more attractive for taxpayers in higher brackets, since they receive a greater benefit from excluding interest from income. For lower-bracket taxpayers, on the other hand, the tax benefit from excluding interest from income may not be enough to make up for the lower interest rate generally paid on this type of bond.

## We Can Help!

The staff at CapinCrouse LLP works with hundreds of churches and not-for-profit organizations. This experience base allows us to quickly identify areas for improvement in many organizations. If your organization desires to improve its efficiency, please contact your Capin Crouse representative or one of our offices to discuss how we may help you.

## About CapinCrouse LLP

With more than 500 not-for-profit organizations and 1,500 tax clients, CapinCrouse is the country's leading accounting and advisory firm primarily serving the Christian not-for-profit community.

Since 1972, CapinCrouse has been serving not-for-profit entities including mega churches, institutions of higher education and secondary schools, and international missions agencies by providing a full range of audit, review, tax, and advisory services.

CapinCrouse is dedicated to helping our clients operate with financial integrity so that they can dedicate themselves to fulfilling their mission.

Even though municipal bond interest isn't taxable, it must be shown on the return. This is because tax-exempt interest is taken into account when determining the amount of Social Security benefits that are taxable, and may affect the alternative minimum tax computation, as well as the earned income credit, investment interest deduction, and sales tax deduction.

- Tax-deferred retirement accounts. It generally doesn't make sense to buy and hold municipal bonds in your regular IRA, Keogh, or 401(k) plan account. The income in these accounts is not taxed currently, but once you start making withdrawals, the entire amount withdrawn is likely to be taxed even though it includes income from tax-free sources. If you want to invest your retirement funds in fixed-income obligations, it is generally advisable to invest in higher-yielding taxable securities.
- Alternative minimum tax consequences. Even though interest on municipal bonds is generally excluded from income for purposes of the regular federal income tax, interest on certain "private activity bonds" is included in income for purposes of the alternative minimum tax. Your broker can tell you whether the particular bond you are considering is a private activity bond subject to this rule.

The alternative minimum tax is a separate tax system that applies if the tax determined under that system exceeds your regular income tax. Whether or not the alternative minimum tax applies will depend on your overall tax picture. In general, however, the effect of the alternative minimum tax would be to prevent you from achieving too low an effective tax rate by means of tax-favored techniques, such as investing in municipal bonds. This office can help you determine how the alternative minimum tax would apply to your situation, and how it would affect the after-tax yield if you were to invest in municipal bonds.

- Effect of exempt interest on taxation of Social Security benefits. In general, a portion of Social Security benefits is taxable if your adjusted gross income, subject to certain modifications, exceeds specified amounts. For this purpose, the modifications to adjusted gross income include adding in tax-exempt interest. The effect of this rule is that if you receive Social Security benefits, investing in municipal bonds could increase the amount of tax you have to pay with respect to your Social Security benefits. While the municipal bond interest technically remains exempt from tax, the effect is the same as though a portion of that interest were taxable. One technique to solve this problem is to invest in tax-deferred, rather than tax-free, investments. For instance, income earned by an annuity is not taxable until the annuity is cashed in, and thus would not impact the Social Security taxation except in the year cashed in. This office can assist you in determining the impact of tax-free income on the taxability of your Social Security benefits.
- Effect of exempt interest on earned income credit. If you are otherwise eligible to take an earned income credit, you will lose the credit completely for 2009 and 2010 if you have more than \$3,100 of "disqualified income," generally, interest, dividend, non-business rental, passive, and capital gain net income. Disqualified income includes tax-exempt income, so municipal bond income could cause loss of the credit. However, in most cases an individual who's eligible for the earned income credit will be in a low tax bracket, thus making municipal bonds an unattractive investment in view of their lower yield. Disqualifying income can be avoided by using tax-deferred investments as discussed under Social Security benefits above.
- No deduction for interest on obligations incurred in connection with tax-exempt investments. If you borrow money for the purpose of investing in municipal bonds, you can't deduct the interest expense with respect

to that borrowing. Moreover, even if the proceeds of borrowing aren't directly traceable to tax-exempt investments, interest deductions could be disallowed if the IRS could establish that you continued the borrowing in effect (that is, you didn't pay it off) for the purpose of acquiring or carrying the municipal bonds.

- No deduction for investment expenses related to tax-exempt investments. If you itemize your deductions, you may deduct the costs of investment advisory, custodial, or agency fees, if your total miscellaneous deductions exceed 2% of your income. However, if the investment management services you paid for are connected to the account from which you receive tax-exempt income from municipal bonds or bond funds, the related expenses are not deductible.
- Sale, call, or redemption of bond. Normally, the sale, call before maturity, or redemption of a municipal bond is treated the same as a taxable bond. If you held the bond long enough, any gain is taxed at favorable rates. Capital losses can be used to offset other capital gains. Up to \$3,000 of any remaining losses can generally be applied against other income, with a carryover of any excess to later years.
- U.S. government bond interest. By federal law, the interest income of direct obligations of the U.S. government cannot be taxed by the states (but it is federally taxed). This includes interest from U.S. Savings Bonds, U.S. Treasury bills, notes, bonds, or other obligations of the United States. Interest earned from the Federal National Mortgage Association (Fannie Mae), Government National Mortgage Association (Ginnie Mae) and the Federal Home Loan Mortgage (FHLMC) Corporations are not direct obligations of the U.S. government, and therefore are not excludable from state taxation unless specifically allowed by state law (generally not the case). If you reside in a state with no state income tax, U.S. government bond interest provides no tax benefit.
- Itemized deductions. If you do have a state tax and the investment is tax-free in your state, then it also makes a difference whether or not you itemize your deductions on your federal return. When you do itemize deductions, the state income tax you pay is included as a deduction on your federal return. Since having state tax-free income reduces your state tax, the reduced state tax lowers your itemized deductions and increases your federal tax.
- Municipal bond funds. If you are looking for diversity and professional management for your municipal bond holdings, you may want to consider buying shares of a fund that invests in tax-exempt municipal bonds. These funds may be broadly based or targeted to the bonds of a particular state. Dividends on municipal bond funds are treated essentially the same as municipal bond interest. To preclude a potential tax loophole, if an investor buys fund shares, receives an exempt-interest dividend, and then sells the shares at a loss within six months after the purchase, the loss is disallowed to the extent of the exempt-interest dividend.

Use the worksheet below to determine the tax-exempt interest equivalents for your particular tax bracket, state tax (if applicable), and type of tax-exempt investment. Enter all rates in decimal format. For example, 5.75% would be entered as .0575. Carry all calculated values to at least 4 places after the decimal.

## Tax-Exempt Interest Equivalents

### Taxpayer Information:

1. Enter the taxable interest rate you wish to compare..... \_\_\_\_\_
2. Enter your Federal tax bracket..... \_\_\_\_\_
3. Enter your State tax bracket (Enter zero if your state has no state income tax)..... \_\_\_\_\_
4. If you itemize your Federal deductions, multiply line 2 times line 3 and enter the result here (if you don't itemize Federal deductions, enter zero)..... \_\_\_\_\_

### Tax-Free Equivalent - State AND Federal Tax-Free:

5. Line 2 plus line 3 minus line 4..... \_\_\_\_\_
6. Multiply line 5 times line 1 ..... \_\_\_\_\_
7. Tax-Free Equivalent (line 1 less line 6)..... \_\_\_\_\_

### Tax-Free Equivalent - Federal ONLY Tax-Free:

8. Multiply line 2 times line 1..... \_\_\_\_\_
9. Tax-Free Equivalent (line 1 less line 8)..... \_\_\_\_\_

### Tax-Free Equivalent - State ONLY Tax-Free:

10. Line 3 minus line 4..... \_\_\_\_\_
11. Multiply line 10 times line 1..... \_\_\_\_\_
12. Tax-Free Equivalent (line 1 less line 11)..... \_\_\_\_\_

Please contact us if you would like assistance deciding whether to make a taxable or tax-free investment. Making the right decision for your particular circumstances can have a significant effect over long periods of time.

## Tax Breaks for Charity Volunteers

If you volunteer your time for a charity, you may qualify for some tax breaks. Although no tax deduction is allowed for the value of services performed for a charity, there are deductions permitted for out-of-pocket costs incurred while performing the services. The normal deduction limits and substantiation rules also apply. Here are some examples:

- Away-from-home travel expenses while performing services for a charity. This includes 100% out-of-pocket roundtrip travel cost, taxi fares, and other costs of transportation between the airport or station and hotel, plus lodging and meals. Unlike other areas of taxes, meals are not subject to the 50% limitation. These expenses are only deductible if there is no significant element of personal pleasure associated with the travel, or if your services for a charity do not involve lobbying activities. Any "significant element of personal pleasure" negates a deduction (i.e., not even partial deduction is allowed). Significant personal pleasure is assumed if the taxpayer has only minor duties and is not required to perform any duties for the charity for major portions of the away-from-home stay.
- The cost of entertaining others on behalf of a charity, such as wining and dining a potential large contributor, is deductible, but the cost of your own entertainment or meal is not.
- If you use your car while performing services for a charitable organization,

you may deduct your actual unreimbursed expenses directly attributable to the services, such as gas and oil costs, or you may deduct a flat 14 cents per mile for the charitable use of your car. You may also deduct parking fees and tolls.

- You can deduct the cost of the uniform you wear when doing volunteer work for the charity, as long as the uniform has no general utility. The cost of cleaning the uniform can also be deducted.

No charitable deduction is allowed for a contribution of \$250 or more unless the contribution is substantiated with a written acknowledgment from the charitable organization. To verify your contribution:

- Get written documentation from the charity on the nature of your volunteering activity and the need for related expenses to be paid. For example, if you travel out-of-town as a volunteer, request a letter from the charity explaining why you're needed at the out of town location.
- If you are out of pocket for substantial amounts, submit a statement of expenses, and, preferably, a copy of the receipts, to the charity. Also arrange for the charity to acknowledge the amount of the contribution in writing.
- Maintain detailed records of your out-of-pocket expenses. This should include receipts plus a written record of the time, place, amount, and charitable purpose of the expense.

Please call us if you have questions related to your volunteer expenses or any other charitable contributions.

## Little-Known - But Important - Credit Card Rules for Merchants

Businesses that accept credit and debit cards must comply with privacy laws that aim to protect customer identity. There are regulations that even the most seasoned of merchants aren't always aware of. It's important for merchants, as well as consumers, to be aware of these little-known credit card rules to protect themselves and their information.

### Stay Compliant with Federal Laws

The Fair Credit Reporting Act is the federal law that establishes the foundation of consumer credit rights. This law regulates the collection and use of consumer credit information by merchants.

Passed as an amendment to the Fair Credit Report Act, the Fair and Accurate Credit Transaction Act prohibits merchants from showing credit card numbers on receipts. To comply with this law, businesses must truncate credit card information on electronically printed receipts. Merchants can include no more than the last five digits of the card number and must delete the card's expiration date.

Example: ACCT: \*\*\*\*\*00714  
Exp: \*\*-\*\*

The law does not apply to imprinted or handwritten receipts; however, merchants using these are also required to protect customer identity. For more information, check out the Federal Trade Commission's guide, "Slip Showing"?

### Comply with State Laws

After complying with the Fair Credit Reporting and Accurate Credit Transaction Act, be sure to familiarize yourself with your state's laws on the use of consumer credit information.

Many states have laws that establish what kind of information merchants can and cannot ask for or write down when a customer uses a credit card. For example, California prohibits merchants from requesting or requiring that a consumer write any personal information (like their address or telephone number) on any form associated with their credit card transaction.

Not all states have additional laws that specifically regulate credit card practices. For more information, read more about state merchant laws or check with a small business expert in your state.