

# Client Update



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## Should you treat your home as an investment?

**F**or many people, a home is more than a place to live, eat, and sleep. It may be viewed as a valuable investment, an asset you can borrow against, and a source of tax deductions. But a home can also be a drain on resources and a financial albatross. Let's look at both sides of the ledger.

### ■ On the plus side

Older people often champion the benefits of owning real estate, especially a home, because homes generally appreciate in value through good times and bad. With each mortgage payment, you build up equity, as opposed to simply paying rent. In fact, renting is sometimes equated with "wasting" money while home ownership is considered to be putting money to good use.

The equity can come in handy if you're stuck in a financial pinch or don't have better borrowing options. If you're a qualified homeowner, you may obtain a loan or line of credit that can sustain you through emergencies or fuel other investments. Furthermore, you can generally claim deductions for mortgage interest and property taxes on your federal tax return, and tax benefits may be available on the state level. In comparison, rental payments provide little or no income tax



punch. Although it can't be quantified, home ownership can give you a sense of security and stability, as well as freedom from typical rental concerns. For instance, if you live in a separate structure, you don't have to worry about noisy upstairs neighbors or restrictions against pets. You call the shots.

### ■ On the minus side

Some experts argue that the financial benefits of home ownership aren't as great as they are perceived to be. While most homes have appreciated over the last 20 years, the days of buying a place for \$50,000 and selling it for \$250,000 are probably gone. Also, borrowing against your home can lead to financial trouble and even ruin. Remember the millions of overextended homeowners

who walked away from their investment in the last decade.

Don't discount the costs of home ownership, including maintenance, property taxes, mortgage interest, and unexpected expenses like fixing a ruptured water line. As a renter, these costs are the landlord's responsibility, so you can rest easy. Finally, if you're viewing your home as an investment – probably your biggest one – compare it to others. Could you have prospered more by putting the money into, say, stocks? When you consider the costs of home ownership and the current real estate marketplace, other options may be more appealing.

Regardless of whether you treat your home as an investment or not, it's wise to examine the financial aspects and determine if home ownership is right for you. ♦



## Last-minute tax savers for 2014

That ticking you hear is the tax clock winding down...quickly. There is only a very short time left to cut your taxes for 2014. Here are moves that you can still make.

1. If you believe you will owe state or local taxes, consider prepaying them before the end of the year in order to claim the deduction in 2014.
2. Use your credit card to purchase (and deduct) items in 2014. Remember that using a credit card allows for a deduction when the purchase is made, not when the card is paid. You can use the credit card rule for both business and personal transactions.
3. If you are a business owner and need additional furniture, fixtures, equipment, and computers to operate your business, consider making the purchases before the end of the year in order to qualify for the Section 179 expensing deduction.
4. Don't ignore stock losses, since they can be used to offset stock gains. If you have unrealized losses for 2014, consider selling those positions to offset any gain transactions you might have made. You can also deduct up to \$3,000 in net losses against other income, and net losses greater than \$3,000 can be carried forward and used on your 2015 tax return.
5. Consider making a deductible traditional IRA contribution. If you qualify, you can contribute up to \$5,500 for 2014, plus an additional \$1,000 "catch up" contribution if you are age 50 or older. The beauty of an IRA is that you have until April 15, 2015, to make your contribution and still take a deduction for 2014.
6. Maximize your employer tax deferred retirement accounts, such as 401(k), 403(b), or 457 plans.
7. Donate appreciated stock or mutual funds to charity. You receive a deduction for the appreciated value, but you don't have to report or pay taxes on any of the appreciation. ♦

## To grow or not to grow?

**T**o grow or not to grow is a decision most successful small businesses face at some point. There can be

opportunity and profit in growth, but there can be perils and risks as well. What should you as a business owner consider when you are faced with this important decision?

### Benefits

First, analyze the potential benefits of expanding your business.

- The business can often achieve attractive economies of scale from increased buying power and operational efficiency. This can often reduce your cost structure and improve your margins. Growing your margins at a faster rate than your sales growth can achieve remarkable financial results.
- Growing organizations can often attract more skilled employees who prefer larger organizations with more opportunities for promotion and development.
- Growing organizations generally have a greater opportunity to go public.

### Risks

Next, take a look at the risks your business faces if you expand operations.

- Larger organizations typically require more elaborate systems and tend to be less personal than smaller companies. As it grows, the business will probably have a more rigid management structure.
- Increased complexity can result as operational issues tend to expand faster than anticipated. Operating remote locations can be very challenging.
- Loss of control may be a consequence of expanded operations. Growing com-

panies face significant integration changes, and developing capable managers can be difficult.

### Questions

Answer the following questions as part of your analysis.

- Do you have the necessary temperament, energy level, and commitment for growth? Are you willing to pay the price of working harder and longer to make the transition successful?
- Are your growth markets similar to your existing ones, or will they require significant operational change?
- Can you attract and develop the required management team and implement the necessary control systems?
- Can you improve or maintain margins? Do you really want to have the increased risk of growth if you aren't likely to benefit from economies of scale?
- Can you attract adequate sources of capital and other resources to expand your business?
- Will growth make you more susceptible to economic downturn or increase your dependency on suppliers?
- Can your suppliers handle your expansion and grow with you?
- Can you maintain your competitive advantages as you get larger, or will you dilute your core strengths? Will you face new competitors?

For help in analyzing your company's situation, please talk to us. We can help you weigh the pros and cons of expanding your business. ♦



# Lending money to family members could be taxing

**L**ending to family members probably dates back to the invention of money. The IRS entered the mix

a great deal later, but it now looms large in the equation. Tax problems can arise when you first lend money, as you're being repaid, or if you're not repaid. The issues usually involve imputed income, gift tax, or bad debts.

## ■ Imputed income

Imputed income is revenue presumed earned but neither recognized nor received by the alleged recipient. The IRS may impute interest on a loan at the "applicable federal rate" (AFR) when a lower rate (or no interest) is charged. The agency then assesses tax on the excess of the imputed interest

over the amount required by the terms of the loan.

## ■ Gift tax issue

When the IRS imputes phantom interest, it also creates phantom taxable gifts. The imputed interest is treated as though the borrower actually paid it to the lender, whereupon the lender returned it to the borrower as a gift. Since the lender "constructively received" the additional interest, he or she owes income tax on it. Since the lender then presumably gave the interest back to the borrower, he or she also owes gift tax on it, unless an exclusion or credit applies.



## ■ Bad debt deduction

Normally, a loan that goes bad is deductible, either against ordinary income (if made for a business purpose) or as a short-term capital loss. However, when the defaulting party is related, the IRS may demand clear and convincing evidence that the original loan was not actually a gift. Once a loan is recharacterized as a gift, no bad debt deduction will be allowed if the loan isn't repaid, and the lender also may owe gift tax on the principal unless an exclusion or credit applies.

Interest need not be charged and will not be imputed on a family loan of \$10,000 or less unless the loan directly relates to purchasing or carrying income-producing assets. Without a written document imposing interest at the applicable federal rate (AFR) or higher, the loan probably will be considered a gift and thus will not be deductible if not repaid.

Interest will be imputed on a family loan over \$10,000 if the stated rate is below the AFR. However, unless the principal exceeds \$100,000, imputed interest will be limited to the borrower's annual net investment income, and no interest will be imputed if that income is \$1,000 or less.

Obviously, lending to relatives can create unintended tax consequences. You should always have a written loan agreement on family loans to document the transaction for the IRS.

Please contact us for guidance before you make any family loans. ♦

## Mark Your Calendar

**JANUARY 2015**  
**15** – Due date for the fourth installment of 2014 individual estimated tax.

**FEBRUARY 2015**  
**2** – Employers must furnish 2014 W-2 statements to employees. 1099 information statements must be provided to payees. (1099-B and consolidated statements must be provided by February 16.)  
**2** – Employers must file 2014 federal unemployment tax returns and pay any tax due.

**MARCH 2015**  
**2** – Payers must file information returns (such as 1099s) with the IRS.\*  
**2** – Employers must send 2014 W-2 copies to the Social Security Administration.\*  
**2** – Farmers and fishermen who did not make 2014 estimated tax payments must file 2014 tax returns and pay taxes in full.  
**16** – Deadline for calendar-year corporations to elect S status for 2015.  
**16** – 2014 calendar-year corporation income tax returns are due. ♦

\*March 31 if filing electronically.



# Inform your employees about their total pay package

## IRS posts taxpayer "Bill of Rights"

The IRS has issued a new "Taxpayer Bill of Rights" to highlight the agency's commitment to providing quality service to taxpayers.

The IRS has lost more than \$850 million in funding – about 7% – since 2010 and is finding it challenging to "properly serve taxpayers." The IRS Commissioner John Koskinen said the 10-item Bill of Rights is intended as a "cornerstone document" to give taxpayers a better understanding of their rights.

Included in the ten rights are the right to be informed, to quality service, to pay no more than the correct amount of tax, to challenge the IRS's position and be heard, to appeal an IRS decision, to finality, privacy, confidentiality, to retain representation, and to a fair and just tax system.

## 2015 HSA limits announced

The IRS has announced the inflation-adjusted contribution limits for health savings accounts (HSAs) for 2015. HSAs allow taxpayers with high-deductible health insurance plans to set aside pretax dollars that can be withdrawn tax-free to pay unreimbursed medical expenses. The 2015 contribution limit for individuals is \$3,350; the limit for family coverage is \$6,650. A catch-up contribution of an additional \$1,000 is permitted for individuals who are 55 or older. ♦

At this time of year, you're probably putting together your business budget for 2015. As you work on the

payroll numbers, it's always surprising how much the cost of fringe benefits adds to base wages. And if you offer health insurance to your employees, that number has probably been increasing even faster.

What's disappointing is that most employees have no idea how much the company pays on their behalf. That's why you should consider preparing a personalized statement for each employee, showing the value of their company-provided fringe benefits.

Although it may sound complicated, your accounting system should allow you to produce the numbers quickly and easily.

- ▶ Begin with premiums you pay for health, life, and disability insurance. Include costs you pay for any other benefits, such as parking or transit passes.
- ▶ Add in any dollars you contribute for the employer match in your 401(k) plan. Or if you offer a profit-sharing plan, include those contributions.
- ▶ Include the company's share of Medicare and social security taxes paid for each employee. Employees would have

to pay that themselves if they were self-employed. You can also include costs for unemployment and workers' compensation insurance if you want to be really precise.

- ▶ Conclude the statement by listing the hours of paid vacation or sick leave that you grant.

The end result is likely to be an impressive total for each employee. The statement should give your employees a new appreciation for their overall salary package. It's also a useful tool when you discuss salaries.

Don't overlook low-cost ways to boost your existing benefits. If you're in an urban area, consider offering free transit passes. You may get a special deal from your local transit authority, and the benefit will appeal especially to your lower-wage employees. Even better, consider offering no-cost benefits such as flex-time. If it works with your business, consider half-day Fridays in the summer months, with slightly longer hours on other weekdays. Employees will love arrangements that simplify their lives or give them longer weekends. ♦



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*W*ishing you a happy holiday season and a prosperous 2015!

Thank you for giving us the opportunity to serve you this past year. Your business is appreciated, and your referrals are welcome.