



E. Cohen and Company, CPAs

One Research Court, Suite 101
Rockville, MD 20850

**CPAs serving Maryland,
Virginia and DC**



Visit us on the Internet at
www.ecohencpas.com



LESSONS FROM TAX COURT

Can a Home Office Take Up 70 Percent of a Residence?

Decades ago, it wasn't uncommon for shopkeepers and blacksmiths to live above or behind their stores. Today's home offices often involve business owners operating out of a portion of their residences. Generally, to claim a business deduction for your home, you must use part of it "exclusively and regularly:"

- As your principal place of business;
- As a place to meet or deal with patients, clients or customers in the normal course of your business; or
- In connection with your trade or business where the business portion is a separate structure not attached to your home, such as a garage.

In a recent Tax Court case, a taxpayer claimed

that about 70 percent of his home was used for marketing and computer software businesses, even though he lived in the residence with his family. The Court found he did use a large part of the home for business but not 70 percent. It ruled that 43 percent of the house was exclusively used for business. The rest didn't qualify and the expenses attributed to it weren't eligible for deductions. (*Jeffrey L. and Simone I. Rayden*, T.C. Memo. 2011-1)

Lessons: If you have a home office, keep in mind that the "exclusivity" requirement is strictly interpreted. Keep good records of expenses. Take pictures of your office setup in case you sell the house or discontinue using the office while the tax return is still open to audit.

Consult with us about how your business use of a home office affects your tax situation. Home office deductions may affect the tax results when you eventually sell your home.

Current Rules May Dictate Changes

The *Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act* made beneficial changes for high-net-worth individuals.

- The federal estate tax exemption is now \$5 million for estates of individuals who die in 2011 or 2012 (the 2012 amount will be indexed for inflation). A 35 percent tax rate applies to the value of an estate in excess of the \$5 million exemption.
- For married couples, if one spouse dies in 2011 or 2012, any unused federal estate tax exemption is now “portable,” which means it can be left to the surviving spouse.

- The federal gift tax exemption is also set at \$5 million for 2011 and 2012 (indexed for inflation in 2012). For 2010, the exemption was only \$1 million. Gifts in excess of \$5 million will be taxed at 35 percent.

Your estate plan may need an update to take advantage of the new rules. For example, married couples may have to make changes to a bypass trust. Here are some ideas for reducing your federal taxable estate:

1. Make annual gifts to relatives and loved ones.

Thanks to the annual federal gift tax exclusion (\$13,000 for 2011), gifts reduce the value of your taxable estate, but they will not reduce your \$5 million federal estate tax exemption or your \$5 million lifetime federal gift tax exemption. For example, say you have two adult children and four grandkids. You could give

them each \$13,000 in 2011 for a total of \$52,000. So can your spouse for another \$52,000. Then, you can both do the same thing again next year. Your joint taxable estate would be reduced by \$208,000 with no adverse federal estate or gift tax effects.



2. Pay college tuition (not room and board) or medical bills for relatives and loved ones.

You (and your spouse) can give away unlimited amounts for these purposes without reducing your \$5 million federal estate tax exemption or your \$5 million lifetime federal

gift tax exemption—as long as you make the payments directly to the college or medical service provider.

3. Give away appreciating assets to relatives and loved ones while you're still alive.

Thanks to the new federal gift tax exemption, you and your spouse can each give up to \$5 million worth of appreciating assets right now without triggering any federal gift tax hit. This can be on top of cash gifts that take advantage of the \$13,000 annual exclusion and gifts to directly pay college tuition or medical expenses.

Important: If you make gifts that chip away at, or use up, your \$5 million federal gift tax exemption, the \$5 million federal estate tax exemption will be reduced dollar-for-dollar. But that is okay if you're giving away appreciating assets because future appreciation will be kept out of your taxable estate.

Pay Attention to State “Death Taxes” Too

With the relatively generous \$5 million federal estate tax exemption for 2011 and 2012, most people are free of any federal estate tax worries—until 2013 when the rules are scheduled to change again.

The bad news: Twenty states and the District of Columbia impose their own estate or inheritance taxes and have exemptions of less than \$5 million. If you live in one of them, your estate can be exempt from federal estate tax but still exposed to significant state death taxes.

And if you own property or a business in more than one state, consult with your estate planning adviser to ensure you establish domicile where you want. State tax residency rules are complex and like estate tax rules, they vary from one jurisdiction to another.



INTERNAL CONTROLS



Smart Ways to Detect Fraud

Internal fraud is difficult to detect, but it's not impossible. Here are three methods, along with some cases to illustrate how fraud can devastate companies.

1. Scrutinize Expenses.

When employees feel that expense claims aren't stringently reviewed, they may pad them with inflated or nonexistent expenses. These padded expenses can mount up quickly.

Case in Point: The Chief Operating Officer of a paper company routinely submitted monthly expense claims of more than \$10,000. On the face of it, the charges seemed legitimate.

But in reality, the executive claimed full-fare airline tickets to destinations unrelated to the company's business. He then refunded the tickets to his credit card without reimbursing the company. In addition, he claimed \$3,000 a month in non-existent lodging and car rental costs. The deceptions weren't discovered until a routine audit.

Expense account fraud represents a greater threat because employees become comfortable with

it and might then move on to submitting higher claims or switch to more lucrative fraud schemes. When reviewing expense reports, be rigorous and make sure everyone from the top down knows claims will be scrutinized.

2. Shake Up Routines.

Fraudsters may develop habits based on a

company's regular schedules. For example, they know when monthly audits are due and take steps to suspend fraud until the audits are complete.

Case in Point: A company's warehouse manager was taking kickbacks from vendors in return for preferential treatment

during contract bids. One day, auditors turned up for an unannounced inventory count. When they arrived, the manager was with one of the vendors and the kickback payment was on his desk.

If an out-of-sequence audit uncovers fraud at your company, publicize it. Be certain employees know that unexpected reviews could happen at any time.

3. Periodically Review Controls.

Even if audits are routinely conducted, you should still occasionally review the mechanisms aimed at deterring fraud. Criminally inclined employees learn how to circumvent controls.

Case in Point: A senior bank teller and her manager regularly stole large sums of cash from the vault of a community bank branch.

Each month, just before the scheduled branch audit, the teller replaced the missing cash with bundles of blank paper. Her manager "counted" the cash and certified the fictional amount was correct.

The bank required another employee to make the actual count. But to save time and meet audit quotas, the employee counted the stacks rather than the individual notes. The fraud remained undetected and wasn't discovered until the manager was fired. If the process was reviewed, the company would likely have discovered the fraud sooner.

The "perception of detection" is crucial in fighting fraud. Consult with us about systems and controls for your organization.



BizBrief: 1099 Rules Repealed But Increased Penalties Remain

A new law repealed two sets of rules that had business owners, company managers and landlords up in arms because of the paperwork nightmare they created. The rules that involved businesses issuing a blizzard of 1099 forms were created by two laws enacted in 2010. Rental property owners had to begin complying with one of the sets of rules this year. The second set for other types of businesses was not scheduled to go into effect until next year.

While the repeal was welcome news, there is another rule businesses should keep in mind. Penalties for failing to file proper 1099s with the IRS and issue payee statements to recipients were increased by a 2010 law. Despite the expanded 1099 reporting repeal, the increased penalties remain in effect. For 2011, each time your business fails to file a 1099 and issue the related payee statement, the IRS can assess a penalty of \$200 or more (up from the previous \$100).

We Now Have Expanded Global Resources for Clients

E. Cohen & Company, CPAs is pleased to announce that we now have significant new global resources to offer our clients through membership in IGAF Polaris, the powerful new global accounting association forming out of the merger of Polaris International, Fidunion, and IGAF Worldwide.

The independent member firms of the merged IGAF Polaris will have a combined annual revenue of over US\$1.82 billion, with 2,400 partners, 16,300 employees, and 843 offices in 89 countries around the globe, making the combined group one of the largest associations of independent accounting

firms in the world. The substantial increase in size for the merged association will enhance our ability to provide expertise and resources to meet growing client needs, both internationally and domestically.

“We are pleased and proud to have E. Cohen & Company, CPAs as our member firm in Rockville, MD,” said IGAF Polaris CEO Kevin Mead. “Many

of Polaris International’s member firms and their clients have relied on E. Cohen & Company, CPAs expertise and quality service over the years, and we eagerly anticipate the contributions they will make on a global scale to the new, much larger association. In turn, I know that E. Cohen & Company, CPAs will benefit from the significant additional expertise and resources being extended to their clients from their

peer member firms around the globe.”

IGAF Polaris will maintain a regional governance structure, with Boards of Directors providing oversight for each of four regions: Asia Pacific; Latin America & Caribbean; Europe, Middle East, & Africa; and North America.

A World Board of Directors comprised of members of the Regional Boards, plus a World Chairman, will provide global guidance and governance. The World headquarters office for IGAF Polaris will be in Miami, Florida, with regional offices to be located in Europe, the Americas, and Asia Pacific.



E. Cohen & Company, CPAs Launches New IT Division

We are excited to announce the expansion of our services and the launch of our new company, ECC IT Solutions, LLC to help better serve our customers and solve their technology needs.

As the accounting landscape has shifted and is merging with technology, we are at a critical point where accounting and IT services are converging. We believe that we must be a driving force of this change and become leaders in the technology field instead of waiting for change to happen.

We have become the accounting firm you’ve come to trust, through our ability to anticipate and provide reliable, cost-effective and result-driven solutions that meet your needs. We believe that we can provide the same results for your technology needs.

We have a team of three senior IT professionals, Frank Noone, Jeff Savitsky and Ethan Smith as well as the support of all of the members of our accounting team. ECC IT Solutions stands ready to provide you

with solutions to all of your technology needs including the following:

- New Server Installations, Upgrades & Monitoring
- Help Desk Services
- IT Assessments and Recommendations
- Acquisition of New Hardware and Software
- Network Security and Backup Solutions
- Complete IT Outsourcing
- Support of Custom Applications
- Cloud Computing
- Or any other IT project you may have!

For over 20 years, E. Cohen and Company, CPAs has been committed to growing your bottom line. We are looking forward to the opportunity to provide you with the same value-added service and commitment as we begin to develop and implement solutions to overcome your IT challenges and needs.

To learn more about ECC IT Solutions, please visit www.eccitsolutions.com or contact Frank Noone at (301) 337-3101 or fnoone@eccitsolutions.com or myself, Eric Cohen at (301) 917-6201 or ecohen@eccitsolutions.com.