

# Ideas for Your Success

Third Quarter 2010

## Hire soon to take advantage of the HIRE Act's incentives

Is your company considering hiring new employees? If so, you'll want to take action sooner rather than later to take advantage of incentives included in the Hiring Incentives to Restore Employment (HIRE) Act.

Pared to its basics, the act offers two main incentives to hire new employees: 1) payroll tax breaks, and 2) additional credits for the new workers if they're retained for at least 52 consecutive weeks. Time is running short, though. Payroll tax forgiveness incentives are offered for wages paid only through the end of 2010, and the retained worker credit is limited to employees hired by Dec. 31.

### Payroll tax exemption

If you're a qualified employer (generally employers other than governmental units), you're exempt from having to pay the 6.2% Social Security portion of Federal Insurance Contributions Act (FICA) taxes on certain new hires through the end of the year. To qualify, a worker must be hired after Feb. 3, 2010, and before Jan. 1, 2011, and must have been unemployed (defined as not having worked more than 40 hours) for the 60-day period ending on his or her start date.



A new hire doesn't have to be a full-time employee, but he or she can't take the place of an existing employee unless that employee was terminated for cause or left voluntarily. The new hire *can* be an employee whom you previously laid off.

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Because wages in excess of \$106,800 aren't subject to the Social Security payroll tax, the maximum value of the break per employee is \$6,621.60. Of course, in most cases, the wages will be lower and, thus, the value of the break will be lower. Employers also need to keep in mind that payroll tax paid is a deductible expense, so some of the savings from the tax forgiveness will be offset by the reduction in deductible expenses.

### Qualified employee retention credit

This credit is an incentive to keep the workers who qualify for payroll tax forgiveness on your payroll for at least 52 consecutive weeks. (No partial credit is available if the employee leaves before the end of the 52-week period, even if the departure is voluntary.) The tax savings per qualified retained worker are equal to the lesser of 6.2% of the wages paid to the worker in 2010 or \$1,000.

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## The Patient Protection act, taxes and you

The Patient Protection and Affordable Care Act (PPACA) is a massive law that makes substantial changes to the U.S. health care system. With its many provisions, it can be difficult to decipher how the law will affect you.

In a nutshell, PPACA expands individuals' access to health coverage. But it also includes many tax provisions you need to be aware of — even though most don't go into effect until 2013 or later. Let's take a closer look at a few of the major tax-related provisions for individuals.

### Uninsured individuals face penalties

Beginning in 2014, most individuals who aren't eligible for Medicaid, Medicare or other government-provided coverage will have to purchase minimum essential health coverage. Those who fail to do so will be hit with a penalty (with exceptions for lower income individuals and certain others).

In 2014, the penalty will be the greater of \$95 per person or 1% of household income. Those amounts increase to \$325 or 2% of income in 2015 and \$695 or 2.5% of income in 2016. Flat dollar penalty amounts are cut in half for children who are under 18 or in college. Also, your total liability for all individuals for whom you're liable — generally family members — is limited to three times the applicable dollar amount.

“**To help offset the Patient Protection act's cost, affluent taxpayers will face higher taxes.**”

### Tax credits for lower income families

Beginning in 2014, people with income between 133% and 400% of the federal poverty level (FPL) will be eligible for tax credits or cost-sharing subsidies on a sliding scale to help pay insurance premiums. For example, based on current FPL figures, premium assistance would be available to a single person with income between around \$14,400 and \$43,300 or to a family of four with income between approximately \$29,300 and \$88,200.

The credits are designed to ensure that qualifying individuals don't spend more than a certain percentage of their income (ranging from 3% to 9.5%) on health insurance premiums.



### Affluent taxpayers to help shoulder costs

To help offset the act's cost, affluent taxpayers will face higher taxes. Beginning in 2013, taxpayers with more than \$200,000 in earned income (\$250,000 for families) will pay an additional 0.9% Medicare tax on the excess.

In addition, those with an adjusted gross income (AGI) of more than \$200,000 (\$250,000 for joint filers) will pay a new 3.8% Medicare tax on *unearned* income, such as interest, dividends, rents, royalties and certain capital gains. The tax doesn't apply to retirement-plan distributions.

### Limits on some health-related breaks tightened

Starting in 2013, the act raises the threshold for deducting unreimbursed medical expenses from 7.5% to 10% of AGI. There are some circumstances in which the increase will be delayed until 2017.

PPACA also introduces a new limit on annual contributions to Flexible Spending Accounts for medical expenses. Beginning in 2013, the limit will be \$2,500.

### Time to learn

Understanding how PPACA's provisions may affect your tax situation can be daunting. But because many of the individual tax provisions phase in slowly during the next several years, you have time to discuss with your tax advisor how to best plan for them.

## Change can be good

### Switching from FIFO to LIFO can save your company taxes

In the wake of the economic downturn, many businesses are fighting to improve their cash flows and profits. One way to do this is by reducing your tax liability. If your company produces, purchases or sells merchandise, it's worth your while to take a closer look at how changing your inventory accounting method from first-in, first-out (FIFO) to last-in, first-out (LIFO) can help save you tax dollars.

#### FIFO and LIFO defined

A common inventory accounting method for financial statement purposes is the FIFO method. FIFO assumes that merchandise is sold in the order it was acquired or produced. Thus, the cost of goods sold is based on older — and often lower — prices. The LIFO method operates under the opposite assumption: It allocates the most recent costs to the cost of sales.

If your inventory costs generally rise over time, LIFO offers a definite tax advantage. By allocating the most recent — and, therefore, higher — costs first, it maximizes your cost of goods sold, which minimizes your taxable income. Keep in mind that LIFO involves more sophisticated record keeping and more complex calculations, so it's more time-consuming and expensive to use than FIFO.

#### Ins and outs of LIFO

If you're contemplating a switch to LIFO, beware of the IRS's "LIFO conformity rule." It requires you to use the

same inventory accounting method for both tax and financial statement purposes. Switching to LIFO may reduce your tax bill, but it will also depress your earnings and reduce the value of inventories on your balance sheet, which may place you at a disadvantage in comparison to competitors that don't use LIFO.

In addition, LIFO can create a tax problem if your inventory levels are declining. As higher inventory costs are used up, you'll need to start dipping into lower-cost "layers" of inventory, triggering taxes on "phantom income" that the LIFO method previously allowed you to defer. If you use LIFO and this phantom income becomes significant, consider switching to FIFO. It will allow you to spread out the associated taxes over a four-year period while giving your balance sheet a boost.

One of the biggest challenges in using LIFO is the need to measure changes in inventory costs. If you currently use LIFO, you may be able to enjoy additional savings by electing to use the inventory price index computation (IPIC) method.

#### Do your homework and make a decision

Weathering today's uncertain economy is the top priority for many businesses. Whether it makes sense to switch your inventory accounting method depends on several variables. Your tax advisor can work with you to assess your company's financial situation and determine the best course of action.

## Worried about divorce?

### What to do before, during and after

Statistics show that divorce will become a reality for more than half of all married couples. Whether you're worried it could happen to you someday or you're already in the midst of a breakup, there are steps you can take to protect your financial interests.

Unfortunately, you can't wait until divorce becomes a *probability* to start thinking about it as a *possibility*. You need to think about it long before. First, when making any investments or asset purchases with your spouse, make sure both names are on the titles, when appropriate, and keep copies for yourself.

Also, continue to maintain some credit in your name alone after you marry — not jointly with your spouse. Monitor your credit reports annually to ensure you're in good standing.

Finally, keep abreast of all financial-related activities and obligations throughout your marriage. It's common for one spouse to assume primary responsibility for managing the finances, while the other is less involved.

If you and your spouse decide to divorce, copy and organize all financial-related documents. Your attorney will need them to prove ownership of items or assets.

It's often a good idea to close any jointly held bank and credit card accounts once a divorce is expected. This may prevent your spouse from draining bank accounts and racking up excessive bills that you could be left responsible to pay.

In addition, carefully consider whether to cease contributing to any retirement accounts until a legal agreement is reached as to how they'll be divided. It's often difficult to tell in advance how assets will be divided.

After the divorce is final, update information in your estate plan. It's especially critical to revise your beneficiary designations in wills, trusts, retirement plans and life insurance policies. If you don't, on your death, proceeds from the settlement of your estate or insurance policies may still go to your ex-spouse.

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Because of the 52-week requirement, you generally won't enjoy the benefit from this credit until you file your 2011 tax return. Also, during the last 26 weeks of the 52-week period, the retained worker must be paid wages equal to at least 80% of what he or she was paid during the first 26 weeks.

### Time is of the essence

If your company is in a position to hire employees, the HIRE Act provides two added incentives. But additional rules apply to both tax breaks, so be sure to consult your tax advisor before making any hires. Also, remember that, to take advantage of these breaks, you must act by year end.

### Section 179 increase extended

If your company is in the market to make major asset purchases, now may be an ideal time. Why? The Hiring Incentives to Restore Employment (HIRE) Act extends the increase in the Section 179 limit for initial year expensing to \$250,000 (from \$134,000). The Sec. 179 expensing election allows a current deduction for newly acquired assets that otherwise would have to be depreciated over a number of years. The expensing election begins to phase out dollar for dollar when total asset acquisitions for the tax year exceed \$800,000 (up from \$530,000).

The higher expensing and phaseout limits apply for calendar year 2010 or a fiscal year that begins in 2010. As of this writing, legislation has been proposed that would increase the amounts further and extend higher amounts beyond 2010. Check with your tax advisor for the latest information.