

• November/December 2003 •

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## New York State Taxes – Update on 2003 Legislation

New York State has been busy this year in the tax legislation arena. In the spring, several laws were enacted to increase taxes and fees (see the July/August and September/October issues of the *HR Adviser* or access them on our website) and recently the State enacted amendments to the spring legislation. Here are some further developments.

1. For “S” corporations, the tax on taxable income has been eliminated for tax years beginning in 2003, 2004 and 2005. Note that the corporate tax on “C” corporations (which are regular tax paying corporations that have not elected the special “flow through of taxable income to owners” status accorded to “S” corporations) has not been changed. An “S” corporation now will pay a fixed dollar minimum, based on its gross payroll, ranging from \$100 to \$1,500.

- *Tip* – Since this change only recently was disclosed by the State, most “S” corporations would have been paying quarterly estimated taxes. You should review any remaining estimated tax

payments and probably not pay them -- but check with us first.

- *Trap* – As part of the “S” corporation change to a fixed dollar minimum, the State is imposing a minimum fee of \$800 (as versus \$100) on “S” corporations which have \$1,000 or less “average value of gross assets”.

Basically this is an expensive tax on inactive corporations which may have been formed for a specific purpose or for future use. The \$800 inactive corporation tax has existed for many years for “C” corporations and it is a reason that many inactive “C” corporations elected “S” status (for the lower annual tax).

Note that there also is an exception to the \$800 minimum for “S” corporations with more than \$1,000 of gross payroll or total receipts but, by its very nature, an inactive corporation would not have payroll or receipts.

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## Notable and Quotable

Partner **Beatrix McKane** was listed as a Resource in the *Long Island Business News* special section devoted to Long Island’s most influential businesswomen.

Tax Partner **Alan E. Weiner** represented the Suffolk County Bar Association at a meeting in Albany with state tax officials and other tax professionals to discuss 2003 tax law changes affecting businesses and individuals.

In a continued commitment to DFK International, several partners take over elected or appointed positions:

Partner **Alan E. Weiner** has been elected Vice President of the Americas for DFK International. Partner **Howard Weiner** has been appointed to both the Task Force on International Accounting Quality and the SEC Interest Group. Partner **Beatrix McKane** has been appointed to the DFK International Healthcare Committee.

Senior Tax Manager **Barry Nagler** attended the Breeders Cup World Thoroughbred Championships in California as the guest of his 12-year old daughter, Jenna. Jenna won a trip to this event in an essay contest sponsored by Kids to the Cup, a non-profit, charitable corporation that attracts, educates and develops young racing fans (ages 8-16) through programs that provide direct access to the sport’s major events and players.

Barry combines his 30 years of experience in the thoroughbred industry as an owner and a fan with his

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## New York State Taxes – Update on 2003 Legislation

- *Tip* – Speak with your Holtz Rubenstein adviser about what action to take so as to mitigate the new “S” corporation minimum \$800 franchise tax.

2. Attention SUV Fans: While Federal tax law provides a special accelerated tax deduction for SUVs used in business and weighing in excess of 6,000 pounds, New York State’s rule is draconian. Not only has New York State decoupled its depreciation rules from various accelerated Federal methods, but New York State says that the taxpayer never gets a tax benefit for New York State purposes if the SUV expensing election is made for Federal purposes.

- *Tip*: New York State taxpayers should seriously consider depreciating the qualifying SUV under regular or bonus methods and not choose the expensing election.

3. Under amended legislation, New York State can waive the requirement that partnerships, LLCs and “S” corporations

pay quarterly estimated taxes for nonresident partners, members, “S” corporation shareholders and “C” corporations (whether resident or nonresident).

- *Tip* – The rules for qualifying for such waivers may be issued by the time you



read this. If you’re interested, either as an entity or as an investor, contact your Holtz Rubenstein adviser.

4. New York State will mail a letter in December to every LLC registered with it. It will describe the 2003 annual fee changes (discussed in the July/August Holtz Rubenstein *Adviser*).

- *Tip* – As noted in the aforementioned *Adviser*, we are especially interested in, and concerned about, the new filings required by single member limited liability companies (“SMLLC”). **Be**

**sure that we know** about the existence of each and every SMLLC. Whether you receive a letter for a SMLLC or a multi-member LLC, when you receive the letter (or letters), forward a copy of the page with the LLC name on it, along with your name if not readily apparent, to your Holtz Rubenstein

partner or manager so that we can make sure that it’s on our due date monitor control, which for all calendar year LLCs will be January 30 (not 31), 2004.

5. And now for our “favorite” new requirement – the compensating use tax line, which will appear on your 2003 New York State personal income tax return as an addition to your income tax.

In summary:

- For the one line on the tax return, there are 5 pages of instructions.

- There are 3 potential work sheets to be completed.

- The instructions state that if there is no use tax (another name for the sales tax) to be paid on out-of-state/country, internet or catalog purchases, **-0-** must be entered on the applicable line.

- For purchases under \$1,000, you will be allowed to pay a use tax, in accordance with a table, based upon your Federal adjusted gross income (“AGI”) (the maximum amount being \$200 for a taxpayer with AGI in excess of \$200,000), without having to scour your paid bill file; however, for each and every purchase over \$999, you are expected to pay the precise use tax based upon your county’s rate.

- Note: The table cannot be used for business (e.g., Schedule C) or real estate rental activity purchases, no matter the amount.

- If you paid a sales tax, at a lower rate, in another state, or another county within New York, you are entitled to reduce the use tax due.

For more information, please contact Tax Partner Alan E. Weiner at 631-752-7400 ext. 330 or [aeweiner@hrcpa.com](mailto:aeweiner@hrcpa.com).

### CyberNotes

#### Gocollege.com


Are you looking for a good college in the US for your kids? Do you want to know what scholarships are available? If so, take a look at **Gocollege.com**. The site can be used to search for colleges by region, cost and academic field.

**Gocollege.com** even has a Crime Statistics search engine, to see how safe the prospective school is.

Don’t have enough money to pay for college? **Gocollege.com** also hosts one of the largest scholarship databases in the country, as well as a testing practice section for the SAT and ACT exams.

#### Enature.com

Provided by the National Wildlife Federation, **Enature.com** is a great site for anyone interested in birds, wildlife, or native plants and wildflowers. It has an impressive collection of information and top-quality photographs. **Enature.com** allows you to browse alphabetical lists or search for a species by name.

Do you want to know if all birds migrate south for the winter? Find out the answer in the Ask an Expert section. At **Enature.com** you also can browse questions to the three resident experts (birding, wildlife, and backyard) by topic, or perform a search based on a keyword. (By the way – some birds migrate east or west, in search of food in winter.) 

## New York State IMB Credit


New York State provides industrial and manufacturing businesses a credit (known as the "IMB Credit") against corporate franchise (or income) tax for energy taxes paid by or passed through to a company. The energy taxes that qualify for this credit are for gas; electricity; steam; water; or refrigeration, or for taxes paid on these services, used by a qualifying business in New York.

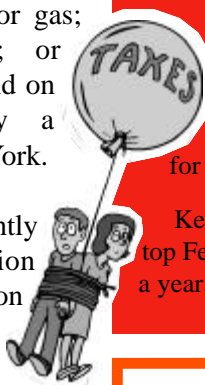
New York State has recently issued an Advisory Opinion determining that a corporation whose headquarters is located in New York and whose manufacturing operations are conducted outside of New York (in Connecticut) was allowed to take a credit for energy taxes paid for during the year to operate the New York headquarters.

Although there were no manufacturing operations in New York State, the corporation was entitled to an IMB credit for New York State energy taxes paid. Therefore, any operation located in New York State for a qualifying industrial or manufacturing business (regardless of whether the manufacturing operations are located in New York) qualifies for the IMB credit.

Furthermore, manufacturers whose business operates solely in New York State can receive the IMB credit for energy taxes paid on utilities that operate all industrial and management facilities located in New York.



If you have questions regarding the tax credit program, contact Senior Tax Manager Sid Leibowitz at 631-752-7400 x-265 or [SLeibowitz@hrcpa.com](mailto:SLeibowitz@hrcpa.com). 



## Tax Trap! Year-End Purchase of Mutual Funds

Be careful before purchasing mutual funds for taxable accounts between now and the end of the year.

Fund companies usually distribute all of their capital gains and dividends at year-end, and you could be taxed on the payout without enjoying any increase in the value of your investment.

Generally, the gains are taxable unless you are investing for an individual retirement account or some other tax-deferred account.

Before investing, call the fund and ask about its payout dates. If a large distribution is coming soon, consider waiting until after the record date to invest for taxable accounts.

Keep in mind that if you receive a year-end distribution, under the new tax law, the top Federal income tax rate on long-term capital gains, investments held for more than a year, decreases to 15% from 20%. 

## Social Security Update – 2004

### Taxable earnings:

The Social Security Administration recently announced a \$900 increase in 2004 taxable earnings of FICA wages and self-employment. Although the total tax rates will remain unchanged, the maximum amount of taxable earnings that are subject to the Social Security tax (at 6.2% for an employee and 12.4% for a self-employed person) will increase from \$87,000 to \$87,900.

As in 2003, there is no limit on earnings subject to the Medicare tax (at 1.45% for an employee and 2.9% for a self-employed person).

In summary, the combined tax rate on the first \$87,900 of earnings will be 7.65% for employees (plus a matching 7.65% by the employer) and a 15.3% self-employment tax rate; however, self-employed individuals may deduct one-half of their self-employment tax, resulting in an effective rate of approximately 12%.

### Nanny tax:


During 2003, if you paid a household employee \$1,400 or more in cash wages in the calendar year, you are required to withhold and pay Social Security and Medicare taxes.

Household employees include housekeepers, maids, babysitters,

gardeners and others who work in and around your private residence. Repairmen, plumbers and contractors are not included, as they are not considered your employees. For 2004, the wage threshold for household employers to withhold these taxes will remain at \$1,400. Additionally, household employers are required to pay Federal unemployment tax if they pay total cash wages of \$1,000 or more in any calendar quarter of the current or preceding year to household employees.

These taxes are paid and submitted to the IRS along with your 2003 Federal income tax return. You also must provide the employee with Form W-2 by February 2, 2004 and to the IRS by March 1, 2004.

It also is important to note that the law still requires employers, who live in New York and pay wages of \$500 or more in any calendar quarter, to file quarterly unemployment insurance returns.

Keep in mind that worker's compensation and disability insurance are required for a household employee who is employed for at least 40 hours per week by any one employer. 

**Mortgage Rates are Rising. Is it Still a Good Time to Borrow?**

By Paul E. Becht, CPA

According to recent economic data reported by the Commerce Department, orders have been rising for machinery, household appliances, and cars. With consumer spending up and confidence in the economy steadily improving, Americans are noticing that mortgage interest rates are beginning to rise.



**Paul Becht**

While mortgage interest rates are still relatively low when compared with rates of the past five or ten years, they still are up about one percentage point from where they were this spring. Many financial analysts feel that as the

economy rebounds, long-term interest rates will continue to rise. As home prices also are increasing, it may be a good time to lock into a low mortgage rate now, before mortgage rates rise any further.

The interest rate increase will affect people who are ready to move or buy a new home (or planning on making substantial home improvements). An increase in the interest rates could result in a homebuyer no longer being able to afford a mortgage on a new home.

For instance, a few months ago a \$250,000, 5.25%, 30 year fixed-rate mortgage would cost approximately \$1,381 per month. At current rates, typically 6.25%, the cost of borrowing \$250,000 is \$1,539 per month.

While the extra \$158 per month may not seem like much, the aggregate cost over the 30-year life of the mortgage is close to \$57,000. The difference in cost increases further as the size of the mortgage increases. If we apply these same variables to a \$500,000 mortgage, the difference in aggregate cost of the two mortgages would be approximately \$114,000.

Recently, a friend of mine called to ask for advice regarding a house she was considering buying. She was concerned that she would be unable to afford a new home now that interest rates have increased. Further, she worried that the price of the home was so high that the mortgage would be too much for her to handle.

What she didn't know is, she could probably afford more than she thought. With mortgage interest rates still as low as they've been in decades, homebuyers have been rushing out to purchase larger and more expensive homes. Even with the escalating cost of real estate over the years, the drop in interest rates has allowed buyers to be able to handle more debt. After putting together a budget of monthly income and expenses, my friend realized that the monthly mortgage payment on a substantial fixed-rate mortgage was well within her means.

There are other options available for the homebuyer other than the traditional fixed rate mortgage. The most popular option available, now that rates are rising, is an adjustable-rate mortgage, or ARM, which starts out as a fixed-rate mortgage and then converts to a variable interest rate after a set period.

The typical ARM costs about 5.25%, roughly a percentage point cheaper than the fixed-rate 30-year mortgage. A \$250,000 adjustable-rate mortgage during its five-year fixed period would cost about \$1,381 a month, compared to a cost of \$1,539 on a 6.25% fixed-rate 30-year mortgage, generating a savings over five years of \$9,500.

When considering an ARM, homebuyers first need to ask themselves how long they plan to stay in the home. If they do not plan to stay past the fixed term of the mortgage, which usually lasts

anywhere from three to ten years, an ARM may be the right type of mortgage.


However, ARMs may not make sense for the homebuyer who is not looking to move in the foreseeable future. Homeowners who plan to remain in their current home will most likely want a fixed-rate mortgage, especially if they are concerned that rates will rise over time. Because ARMs adjust to current market conditions after a set period, they could end up paying a higher interest rate in the future if they have an adjustable rate mortgage.

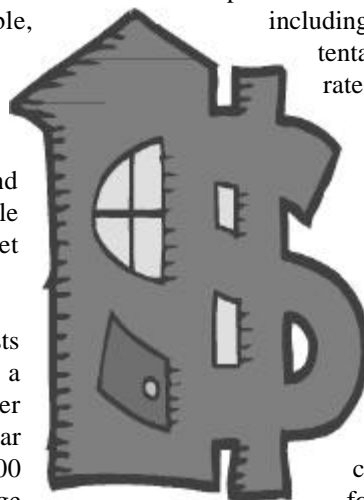
Homebuyers should shop around, as mortgage rates vary between banks. Also, interest rates can change on a daily basis. By conducting a search on the internet, homebuyers can obtain current mortgage rates offered by various lending institutions. Some people may be cautious about borrowing now that rates are increasing. They may want to wait and save some money if rates fall again. Therefore, most lenders offer various options to lock in a mortgage rate,

including a more flexible option that tentatively locks in a range of rates. The important thing to remember with locking in rates is to get the agreement in writing if you want to lock in today's rates.

Once you find a lender who is willing to offer a relatively low mortgage interest rate, you should be careful not to take any actions that might cause you to be turned down for the mortgage. Borrowers should keep a close watch on

their spending habits, saving as much as possible for their down payment and any closing costs. Preparing a budget and sticking to that budget will save the homebuyer a lot of time, money, and aggravation.

For more information on mortgage rates and budgeting, contact Audit Manager Paul E. Becht at 631-752-7400 x-224 or [PBecht@hrca.com](mailto:PBecht@hrca.com). 



## Extended Deadlines for Certain Retirement Plans


The IRS has extended the deadline for certain determination letters for selected pre-approved qualified retirement plans until January 31, 2004.

Many employers have established profit sharing or pension plans for its employees. These employees and employers can enjoy specific tax advantages if the plan is a qualified plan. In order to ensure the plan is, in fact, a qualified plan, the plans sponsor must follow IRS procedures to obtain a determination letter. It is through the use of these determination letters that the IRS will establish the plan's qualified status.

The IRS provides for a remedial amendment period, during which a plan may be retroactively amended, to comply with the qualification requirements. These qualification requirements are referred to as GUST, which are a series of public laws that have changed various pension rules.

As we alerted you in the January/February 2003 issue of the *HR Adviser*, if the requirements for extension are satisfied, the GUST remedial amendment period for the employer's plan won't end before the later of September 30, 2003, or the end of the 12<sup>th</sup> month beginning after the date on which the IRS issues a GUST opinion or advisory letter for the pre-approved plan.

Just recently, the IRS extended until January 31, 2004, the deadline for applying for determination letters establishing compliance with GUST legislation. A plan is eligible for the extension only if the plan's GUST remedial amendment period ends on or after September 30, 2003 and before January 1, 2004, and either the plan is amended to comply with GUST or a compliance fee of \$250 is paid with the application for a determination letter.

If you have not heard from your retirement plan adviser, contact him/her immediately to make sure your plans are properly amended to reflect the GUST provisions and all future amendments. 

## Publication Required by LLCs and LLPs – Barklee Decision Reversed

When the limited liability company ("LLC") law was enacted in New York in 1994, it contained a requirement (the only one of its kind in the United States) that the entity publish a notice of its existence in two newspapers (chosen by the county clerk) for six consecutive weeks in the county in which the principal office of the LLC is located.

Holtz Rubenstein, a limited liability partnership ("LLP") complied with this requirement in 1994 at a total cost of under \$200; however, the cost in Manhattan is notoriously expensive and for that reason a lawsuit was brought against the State based upon the perceived unconstitutionality of the statute.

The plaintiff, Barklee, won the case (in 2001) but the State appealed and in October 2003, the Appellate Division reversed the lower court and held that the publication requirement was constitutionally within the purview of the New York State legislature.


*Note:* While we agree with the plaintiff that, in this day and age, publication in a newspaper serves no real purpose, we continued to advise clients, after the 2001 decision, to check with their attorneys as to whether to publish (which we felt was the prudent course of action given that the State had filed a notice of intention to appeal shortly after the 2001 decision).

It remains to be seen whether the plaintiff will (or can) appeal the Appellate Division decision to the New York State Court of Appeals.




### To Deduct or Not to Deduct

If you own real estate, you may be entitled to deduct the cost of repairing parts of your property, which normally would be capitalized as building improvements.

A United States Tax Court opinion stated that owners of a commercial property are entitled to deduct the cost of repairing the building's roof. The purpose of the repair was to prevent leakage and maintain the property in an operating condition. It was not performed to prolong its life, increase its value, or make it adaptable to another use – thus, the expense could be deducted and did not have to be capitalized. 


## Increase in Standard Mileage Rate

The standard mileage rate for business use of autos during 2004 will be 37.5¢ per business mile, up from 36¢ a mile for 2003. If an employee is reimbursed at 37.5¢ per business mile, the employee will not have to report the reimbursement as taxable income. However, the employee must substantiate to the employer the time and business purpose of the auto's use.

For autos operated in connection with charitable activities, the rate used for calculating your deduction remains at 14¢ per mile. For medical and moving expense deductions, the rate increases to 14¢ per mile, up from 12¢ per mile in 2003. 



Companies that have not published are well advised to consult with their attorneys about doing so at this time and filing affidavits of publication with the Department of State. It is unknown as to whether there will be any adverse consequence should a case arise involving a period during which the publication should have been made but was not.

For more information, please contact Tax Partner Alan E. Weiner at 631-752-7400 x-330 or [aeweiner@hrca.com](mailto:aeweiner@hrca.com). 

## Guidance on the Definition of “Material Participation”

The Tax Reform Act of 1986 disallowed the deduction of net passive losses (i.e., losses from activities in which the taxpayer did not “materially participate”). But what constitutes material participation? It is something with which taxpayers and their advisers have wrestled since passage of the Act. Although temporary and final regulations provided guidelines on how to determine material participation in many circumstances, the regulations explicitly withheld any guidance on what constitutes material participation when the activity is conducted through a trust or an estate.


However, a United States District Court decision provided guidance that had been omitted from the Treasury Regulations and issued an opinion that is favorable to taxpayers.

The court was faced with a testamentary trust (i.e., a trust created under a will) that managed its assets, including a 15,000-acre ranch used for cattle ranching and for oil and gas interests. The IRS argued that the material participation of a trust should be made by reference only to the trustee’s activities. The trust argued that, as a legal entity, it could participate in the business through the action not only of the trustee, but also through the action of its employees and agents.

The court’s succinct analysis and holding first looked at the language of the

### DFK Firm Spotlight: Holtz Rubenstein & Co., LLP

DFK International is the worldwide association of independent accounting and business advisory firms in which Holtz Rubenstein is actively involved. Through our affiliation, we are able to provide enhanced services to you and to other clients throughout the United States and the world.


Since we just have significantly enhanced our website, this issue we spotlight our own website. We invite you to visit us at [www.hrcpa.com](http://www.hrcpa.com). 

## The Gift That Counts

This holiday season, give your friends and business associates the gift that counts. Holtz Rubenstein is gratified by the results of a client satisfaction survey that shows 95% of clients are pleased with the quality of our services and would recommend the firm to others if asked. So we’re asking!

Holtz Rubenstein offers a wide variety of accounting, tax, and business advisory services to clients throughout the New York metropolitan area. Our clients have access to a continually-expanding range of resources, including employee benefits and computer consulting. We make it our business to meet with our client’s management team frequently to forge long-term relationships.


We provide experience and expertise to a wide variety of clients, from public companies and real estate contractors to family-owned businesses, not-for-profit, and health care organizations. Through our affiliation with DFK International, we also provide services to clients throughout the United States, Canada, Europe, Asia, Mexico and other parts of the world.

We would appreciate it if you would spread the word! 



relevant statute, which defined “taxpayer” as “any individual, estate, or trust.” The court noted that when a statute is unambiguous, it must be applied as it was written, not as it could have been written. In such circumstances, there is no room for the court to consider Congressional intent. It then held that, “It is undisputed that [the trust], not [the trustee], is the taxpayer.”

As the evidence was clear that the collective activities of the trust’s employees with respect to the ranch was regular, continuous and substantial so as to constitute material participation, the ranching activity was held to be nonpassive, and the trust was allowed to deduct the losses from this activity to offset other taxable income.

It is interesting to note that in this case, even if the court had upheld the IRS position, the taxpayer would not have incurred any additional tax liability. The court concluded that based on the undisputed evidence, “[the trustee’s] activities with regard to the ranch operations, standing alone, were regular, continuous, and substantial so as to constitute material participation by him.” 

*(continued from page 1)*

### Notable and Quotable


professional background to provide a special perspective when providing services to clients in the equine industry.

Holtz Rubenstein is proud to welcome three new staff auditors to the firm, all graduates of Hofstra University.

**Fred Catalano** graduated Hofstra with a BBA degree in accounting and is a candidate member of the New York State Society of CPAs (NYSSCPA).

**Christine DiPasquale** also has a BBA degree in accounting and is a candidate member of the NYSSCPA. In addition, last year Christine was the recipient of the William J. Holtz Endowed Memorial Scholarship.

**Lara Speranza** graduated with a BBA degree in accounting and is a candidate member of the NYSSCPA.

In addition, we welcome two people to our administrative staff, Administrative Assistant **Janice Amato** and File Room Clerk **Keishan Rowe**. 

To change  
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