

The Cost-of-Living Dollar Limits

for 2005 Tax Year

IRA Contribution Limit \$4,000

50 & Over Catch-up Contribution \$500

401(k) deferral limit \$14,000

50 & Over Catch-up Contribution \$4,000

Annual compensation limit \$210,000

Defined contribution IRC Sec 415 limit \$42,000

Compensation limit for SEP eligibility \$450

Deferral limit for SIMPLE \$10,000

IRC Section 179 \$105,000

Estate Tax Exclusion \$1,500,000

Self-employed health ins. AGI deduction 100%

Business mileage rate \$0.405/mile

Medical mileage rate \$0.15/mile

Charitable mileage rate \$0.14/mile

1st Year depreciation limits:

Passenger Autos \$2,960

Trucks & Vans under 6,000 unloaded GVW \$3,260

Vehicles over 6,000 unloaded GVW \$25,000

JENNIFER A. JONES, CPA, LTD.

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The New Roth 401(k)

Roth IRAs have been available since 1998. Starting in January 2006, the tax-free aspects of the Roth IRAs will be extended to 401(k)s, creating a brand new retirement vehicle-the Roth 401(k).

Up until now, one of the differences between 401(k)s and Roth IRAs has been that with a 401(k), salary contributions and appreciation are tax deferred and the withdrawals are taxable; with a Roth IRA, contributions are made with after-tax dollars, and, generally, withdrawals are tax free if held in the Roth IRA at least five years. Starting in 2006, if a 401(k) plan offers a Roth option, a participant will be able to put some, or all, of his annual 401(k) contribution into a separate account designated as a Roth. The portion of the 401(k) contribution that goes into this account will be taxable to the participant as current compensation, but if the funds are held for the requisite time, withdrawals will be entirely tax free.

The maximum amount that can be contributed to a Roth 401(k) each year will be the same as for a regular 401(k). For 2006, this limit will be \$15,000, or \$20,000 for those age 50 or older by the end of 2006. Participants will be able to split their 401(k) contributions between their traditional 401(k) and the Roth 401(k).

Funds must be held in separate accounts for traditional 401(k) and Roth 401(k) contributions. Where companies provide matching contributions, the matching contribution must be allocated to the traditional 401(k) account.

In contrast to Roth IRAs, that have no lifetime required minimum distribution, funds in a Roth 401(k) are subject to mandatory lifetime distribution rules: which generally say that withdrawals must commence at age 70½.

Taxpayers with an adjusted gross income (AGI) below \$95,000, (\$150,000, married filing jointly) may make the full Roth IRA contribution. If their AGI reaches \$110,000 (\$160,000 on a joint return), they are no longer eligible to make a Roth IRA contribution. **With Roth 401(k)s, there are no AGI limits.**

In addition to high-income taxpayers who are not eligible to make Roth IRA contributions, younger workers, low-income tax bracket taxpayers with bright futures, and those betting on higher tax rates in the future are excellent candidates for the Roth 401(k). Generally, the Roth 401(k)s are not suitable for workers within five years of age 70½, or those within five years of retirement, since the Roth 401(k) account will not have time to qualify for tax-free withdrawals.

Companies are not required to expand their 401(k) plans to include the Roth option. Although the law that permits Roth 401(k)s is set to expire after 2011, this sunset provision will not adversely affect funds in the Roth 401(k) account. It only means that no new contributions would be permitted after 2011 without an extension of the law. Employers should weigh the cost to amend their plan documents and handle the administration of the separate accounts for a short-term arrangement with the benefits for their employees.

Employment Tax Audits

Look for more employment tax audits by the IRS. The IRS has reorganized its employment tax compliance efforts into a new unit and has boosted the audit staff by 15%. More effort will be targeted at non-filers, cash-based businesses, Schedule C filers that appear to have employees but don't file 941s or W-2s, and S Corporation with distributions but no officer wages.

Social Security

Wage Base for 2005 \$90,000

Retirees under 65 may earn up to \$12,000 (\$1,000 a month). For each \$2 earned over the amount for the year, the retiree loses \$1 in benefits. Retirees turning 65 in 2005 can earn up to \$31,800 in the year without losing benefits, counting only earnings before the month they turn 65. For each \$3 earned over this limit, the retiree loses \$1 in benefits. No limit if 65 or over, effective January 1, 2000.

As you work and pay Social Security taxes, you earn "Credits", up to a maximum of 4 for each year. The amount of earnings it takes to earn a credit changes each year. In 2005, you earn one credit for each \$920 of your earnings. So if you have earned at least \$3,680 during the year, you get the maximum 4 credits. If you employ family members, you may want to be sure to pay them at least this amount so they earn their credits.

TO CONTACT US:

Jennifer A. Jones, CPA, Ltd.
10615 Judicial Drive, Suite 701
Fairfax, Virginia 22030

Phone: 703-352-1587

Fax: 703-352-1927

VISIT OUR
WEBSITE AT:

<http://www.jajonescpa.com/>

TO EMAIL US:

[Jennifer A. Jones, Certified Public Accountant](mailto:Jennifer.A.Jones@jajonescpa.com)

[Patricia \(PA\) Moss, Enrolled Agent](mailto:Patricia.Moss@jajonescpa.com)

[J. Randolph Shull, Systems Analyst](mailto:J.Randolph.Shull@jajonescpa.com)

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DEADLINES

July

15

Monthly-filers Form 941 federal tax deposit due
DC sales tax return and payment due, quarterly and monthly filers
Maryland income tax withheld return and payment due, monthly filers

20

Virginia and Maryland sales tax return and payment due, quarterly and monthly filers
DC income tax withheld return and payment due, quarterly and monthly filers

31

Form 941 due
Virginia income tax withheld return and payment due, quarterly and monthly filers
Maryland income tax withheld return and payment due, quarterly and monthly filers
State unemployment tax returns and payment due
DC Personal Property Tax Return and payment due
Form 940 federal tax deposit due
Form 5500 Annual Return/Report of Employee Benefit Plan due

August

15

Monthly-filers Form 941 federal tax deposit due
DC sales tax return and payment due, monthly filers
Maryland income tax withheld return and payment due, monthly filers
Federal, DC and Maryland Individual Income Tax Returns due, if Form 4868 or first extension request was filed

20

Virginia income tax withheld return and payment due, monthly filers
DC income tax withheld payment return and payment due, monthly filers
Virginia and Maryland sales tax return and payment due, monthly filers

September

1

Virginia Individual Income Tax return due, if Form 760-E was filed

15

Monthly-filers Form 941 federal tax deposit due
DC sales tax return and payment due, monthly filers
Form 1040-ES voucher #3 with payment due
DC, Virginia, and Maryland individual estimated tax payment #3 due
Maryland income tax withheld return and payment due, monthly filers

20

Virginia income tax withheld return and payment due, monthly filers
DC income tax withheld payment return and payment due, monthly filers
Virginia and Maryland sales tax return and payment due, monthly filers

W-4 Forms Rules Rescinded

Good news: As of April 2005, employers are no longer required to send IRS a copy of the W-4 form if an employee claims more than 10 exemptions or if an employee claims exemption from withholding even though they expect \$200 or more in weekly wages. The W-4 is still subject to review by the IRS, but the employer is only required to submit the W-4 form when directed to do so at IRS' request.

Donating Cars in 2005

Beginning January 1, 2005, charitable contributions of cars (and boats and planes) valued at more than \$500 may be deducted, but the amount depends on the use of the vehicle by the charitable organization. If the charity sells the car without significantly using it before the sale, the deduction is limited to the amount received from the sale. The fair market value of the car is irrelevant. No appraisal is required even if the car is sold for more than \$5,000.

If the charity significantly uses the car before its sale or makes material improvements to it, the donor's deduction is not limited to the gross sales proceeds. Any reasonable method to determine the fair market value may be used. However, if the FMV is more than \$5,000, a qualified appraisal is required.

New substantiation requirements apply when the value exceeds \$500. No deduction is allowed unless the donor attaches to his return a contemporaneous acknowledgement from the charity that includes the name & TIN of the donor and the VIN of the car. If the charity sold the car without significantly improving it, the acknowledgement must also certify that the car was sold in an arm's length transaction between unrelated parties; certify the gross sales proceeds; and include a warning that the donor's deduction is limited to the amount of the sales proceeds. This acknowledgement must be provided to the donor within 30 days of the sale or 30 days of the contribution if the charity retains the car for its use.

You may now be better off selling the car and donating the money to charity. Rarely will you have any taxable income from the sale of a car. You will probably get a better sales price, increasing the amount available for a contribution. You will also know the amount of the donation immediately, rather than waiting 30 days from the date the charity sells the car.

IRA Creditor Protection

The Supreme Court has ruled that IRAs are exempt from creditor claims in bankruptcy. The Court held that since IRAs "are payable on account of age" they are protected from creditors in the same manner as pensions, overruling lower-court decisions.

Lost Participants

If you are a retirement plan sponsor and have lost contact with one of the participants in your plan, IRS can help you locate the individual. The IRS offers assistance to plan sponsors who have retained the social security numbers of their former employees, but whose address or whereabouts currently are unknown. Under the Letter Forwarding Program, the IRS offers retirement plan sponsors, the opportunity to try and contact former employees. Although precluded by law from giving addresses or other information to you, the IRS will search its database for a recent address and forward your letter to the missing person. For more details, go to <http://www.irs.gov/retirement/sponsor/article/0,,id=134604.00.html> (cut & paste this URL in your browser's address box)

Have a Question?

If you have a subject or question that you would like covered, please email us at jenny@ajonescpa.com

Estate Planning Fundamentals

The purpose of estate planning is to transfer assets to beneficiaries and heirs in a timely, orderly, and tax-efficient manner based on the specific wishes of the individual or family. Estate planning is not limited to the wealthy nor is it limited to the final disposition of assets at death. The following are some points to consider when reviewing your estate plan.

Transfers During Your Lifetime: The annual gift tax exclusion allows you to gift up to \$11,000 per year an unlimited number of beneficiaries without any filing requirements or gift taxes. You are also allowed to make taxable gifts of up to \$1,000,000 during your lifetime without payment of any gift taxes, although these gifts reduce the amount excluded from estate taxes at your death. You may use other gifting strategies to significantly reduce the size of your taxable estate without triggering gift taxes during your lifetime. These strategies may include the use of charitable trusts, irrevocable trusts, family limited partnerships, and limited liability companies.

Transfers at Death: How you have your assets titled plays a major role in the final distribution of your assets.

The assets you own in your own name as the sole owner will fall under the terms of your will. If you don't have a will, state law provides for the disposition of these assets. These assets will be required to go through probate. State laws provide for simpler probate procedures for small estates, usually those of less than \$15,000.

You may simplify or avoid probate in a number of ways. The first is by holding title to your assets in joint ownership with right of survivorship; using transfer of death designations; or using payable on death designations. Another way is with a revocable living trust. This is an agreement that allows you to transfer assets into the trust during your lifetime, provides for asset management should you become physically or mentally incapacitated, and provides for the distribution of assets by your trustee after your death. The revocable living trust has no impact on your income taxes during your lifetime, and does not reduce your taxable estate at your death. Only those assets actually titled in the name of the trust will avoid probate.

Retirement accounts, such as IRAs and employer-sponsored retirement plans, and life insurance policies pass according to your beneficiary designations and cannot be over-riden by your will or revocable trust. Care should be taken in selecting the primary and secondary beneficiaries. The use of disclaimers by the beneficiary should be considered in making your designations. These designations should be reviewed periodically, especially when there are any changes in your family situation.

Jointly owned assets; accounts designated payable of death or transfer on death; or assets with a designated beneficiary will pass to the co-owner or beneficiary regardless of the terms of your will or revocable living trust.

If estate taxes are a concern, you may want to consider having your relatives own the life insurance policies on your life or transfer existing or new life insurance policies into an irrevocable life insurance trust in order to preserve the entire death benefit for your family.

If you are a business owner, a business succession plan can help ensure the orderly transition of your business interests to family members or business partners. Documents such as a shareholder agreements or buy/sell agreements may provide a framework for the purchase of your business upon your death or disability.

If you have a revocable living trust created before 2001, and some that were created after that date, your trust may call for the creation of sub-trusts based on the lower estate tax exemption of \$675,000. Under the current law, these trust provisions may no longer be necessary and may create unanticipated problems. You should have your will and trust documents reviewed by your estate attorney.

Also see "[Don't Flunk Estate Planning 101](#)"

Informing Your Heirs

Even if you have a formal estate plan, having your personal paperwork organized and informing your heirs of the basics will make it easier for your heirs to locate all the assets and follow your preferences.

One way to approach this task is to prepare a personal letter of instruction, covering the following topics:

- 1) Your assets and important documents. List all assets and where important documents concerning assets are located. Prepare a list of all checking and savings accounts, including bank names, account numbers, and individuals on the accounts. Detail all insurance policies, policy numbers, coverage and location of policy. List all outstanding debts.
- 2) Individuals to contact. List names, addresses and phone number for employers, attorneys, accountants, insurance agents, investment managers and financial planners.

- 3) Personal papers. Indicate where your personal documents are kept, including birth certificate, marriage certificate, divorce or separation agreements, diplomas, military records, and naturalization records.
- 4) Safe deposit box. Indicate where the box is located, what is contained in it, where the key is kept, and who has access to the box.
- 5) Disposition of personal items. Detail how you would like personal items distributed, including jewelry, photographs, pets, furniture, and personal collections.
- 6) Funeral arrangements. Indicate your preferences for funeral arrangements, including whether you want a religious or secular service, whether you want flowers or donations to charity, whether you want to donate your organs, and where you would like to be buried or how your remains should be disposed of. You may also want to list any friends and family you would like contacted after your death.

Your thoughts and preferences can change over time, so you should review and update your letter periodically. Keep it in a place where heirs can find it immediately after your death and be sure they know where it is.

Websites of Interest

Small Business Sites

National Federation of Independent Business's tools and tips for small business owners at www.nfibonline.com

Current and archived versions of *Entrepreneur*, *BizStartups* and *HomeOfficemag* magazines www.entrepreneurmag.com

Free articles on buying, selling, or determining the value of your business at www.businessbookpress.com

Help for small businesses with sample business plans, employment and other legal forms, articles and guidance on various topics www.businessknowhow.com

To keep informed on tax related issues quickly and easily, visit Small Business and Self-Employed Community at <http://www.irs.gov/businesses/small/index.html>

The Center for Business Planning offers sample business plans, analyses of business strategies, info on evaluating business and marketing plans www.businessplans.org

Want to know what IRS examiners will look for, and how, when auditing certain industries?
<http://www.irs.gov/businesses/small/article/0,,id=108149,00.html> (cut & paste this URL in your browser's address box)

Tools for evaluating the lease vs. purchase of a new vehicle: www.leaseguide.com/index2.htm

How do your employee benefits compare with the federal government's? <http://www.opm.gov/oca/leave/HTML/factindx.asp>

College Savings

College Savings and 529 Plans: www.collegesavings.org www.savingforcollege.com
www.dccollegesavings.com www.collegesavingsmd.org www.vpep.state.va.us
College savings and 529 Plan rebates www.upromise.com

Retirement Savings and Retirement Plan Information

To determine your required minimum distribution: <http://www.newrmd.com/>

Roth IRA information: www.rothira.com

Retirement Plan options <http://www.dol.gov/ebsa/pdf/choosing.pdf>

Retirement Plan Dollar Limitations (COLA): http://www.irs.gov/pub/irs-tege/cola_table.pdf

Small Business 401(k) Plans: <http://www.dol.gov/ebsa/publications/401kplans.html>

General Interest

Product reviews www.consumerreview.com

Missing Records and Unclaimed Property

To track down missing records, locate lost assets, or discover property you didn't know you had:

Birth, marriage, and death certificates www.cdc.gov/nchs/howto/w2w/w2welcom.htm

Military records www.nara.gov/regional/mprsf180.html

Missing a pension from a previous employer www.pbgc.gov

Holders of abandoned or unclaimed property reporting requirements (new rules effective 7/1/04):

Maryland: <http://compnet.comp.state.md.us/compliance/>

Virginia: <http://www.trsvirginia.gov/ucp/ucp.asp>

DC: <http://cfo.dc.gov/cfo/cwp/view,a,1326,q,590614,cfoNav,|33208|.asp>

Estate Planning

To assist in various aspects of estate planning: <http://www.learnestateplanning.com/index.html>

DON'T FLUNK ESTATE PLANNING 101

(RETURN TO NEWSLETTER)

[The following is taken from The Washington Post's article by Michelle Singletary, Sunday, May 26, 2002; Page H01 outlining advice given by Thomas D. Murphy Jr., a probate lawyer and senior partner at Murphy, McCoubrey & Auth in Massachusetts. It's always good to stop and review these basic rules and their application to your situation.]

So much focus in estate planning is on avoiding taxes and probate court that many people overlook some simple steps that will make sure money from a life insurance policy or retirement plan ends up with their beneficiary of choice.

Insurance policies and retirement plans are specifically designed to allow an easy transfer of assets to dependents and survivors, yet simple mistakes often thwart the best of intentions. Many of those mistakes are made by people whose disbursement of assets should be relatively simple.

Assigning beneficiaries is something people often do their first day on the job when they are going over benefits with a new employer and they don't realize the importance of their choices.

Several common pitfalls in designating beneficiaries are:

- Naming your estate as the beneficiary. This can undo certain policy or retirement-plan advantages. For example, insurance benefits are generally not subject to claims from creditors, but an estate is. If your estate is the beneficiary, your insurance benefits may no longer be exempt. Also, naming an estate as beneficiary will result in the liquidation of an individual retirement account upon your death, with taxes becoming due immediately. This can deprive a surviving spouse of continued tax-free growth of that money. Check with a tax expert or lawyer before naming your estate as a beneficiary.
- Failure to name a secondary beneficiary. If your primary beneficiary dies before you, or at the same time, and you have not named a secondary beneficiary, your insurance policy or retirement plan will bounce back to your estate. In that event the money will be distributed according to your will or, if you have no will, according to your state's laws.
- Naming minor children as beneficiaries. Generally, insurance companies, pension plans and retirement accounts will not pay death benefits to minors. Benefits are held until a court-approved guardian or trustee is appointed. If you want to provide for minors, name a trustee or establish a trust. Failure to do so will mean the court will name one for you.
- Overlooking tax ramifications. Many people have misconceptions about what is and isn't taxed. Life insurance benefits are generally free from federal income tax. As for tax-deferred accounts, in general, spouses are the only party that can continue to defer taxes in tax-deferred accounts and this is usually done by rolling it into another tax-deferred account of similar type. Consult a tax professional to find out the tax ramifications when naming beneficiaries.
- Failing to update records. People often neglect to make changes to their insurance policies or retirement accounts when their family situation changes. Even in instances when a will indicates otherwise, designated beneficiaries in policies and insurance plans usually supersede any other indications. And generally, there is no satisfactory recourse. So make it a habit to review your insurance policies and retirement-plan records. A checklist of life events requiring a document update can be found at www.familyfiles.com.
- Failure to be specific. Ambiguities can complicate payment and leave a door open for dispute. For example, don't just write on the line for beneficiary "my wife" or "my child." That wording may not be sufficient, particularly in instances of multiple marriages. In naming beneficiaries, use full names.
- Assuming your will "has you covered." Generally, beneficiaries named in insurance policies and retirement plans trump any instructions you leave in your will. Make sure you have specified beneficiaries in your policies and plans. Many bank and investing accounts have mechanisms for naming beneficiaries so those assets can avoid probate. Check your bank and credit union accounts, CDs, equities and mutual funds to see if "payable on death" or "transferable on death" options are available.
- Not leaving instructions as to where your will, insurance papers and other important records are kept. All the financial and tax advice in the world is useless if people can't find your documents or don't know of their existence. Make sure your family is familiar with your most important records and where they are kept. Store important records in a secure file, vault or online file and inform your family of their location.

Do your loved ones a favor. Check your records so you can avoid these estate mistakes.