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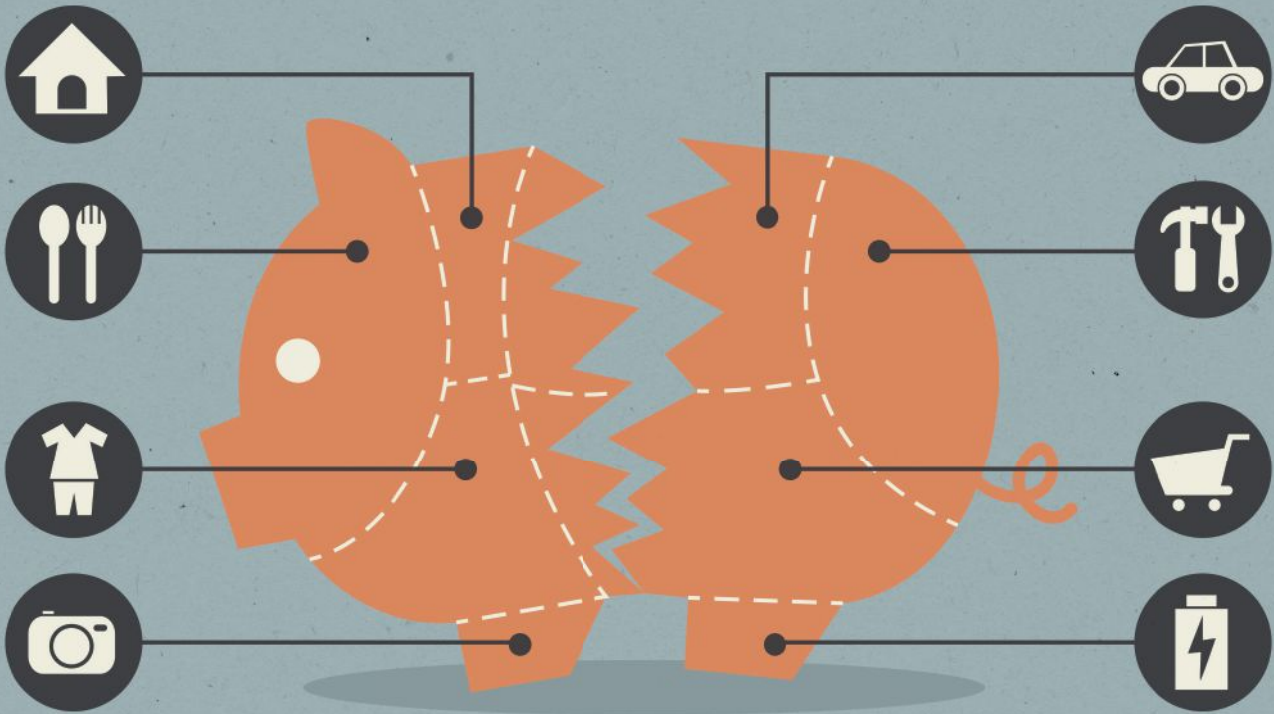
Representing Cash-Intensive Businesses • Tax Law Wrapup • Corporate Formalities

VOL. 32 No. 6

NOVEMBER • DECEMBER 2014

# EA JOURNAL

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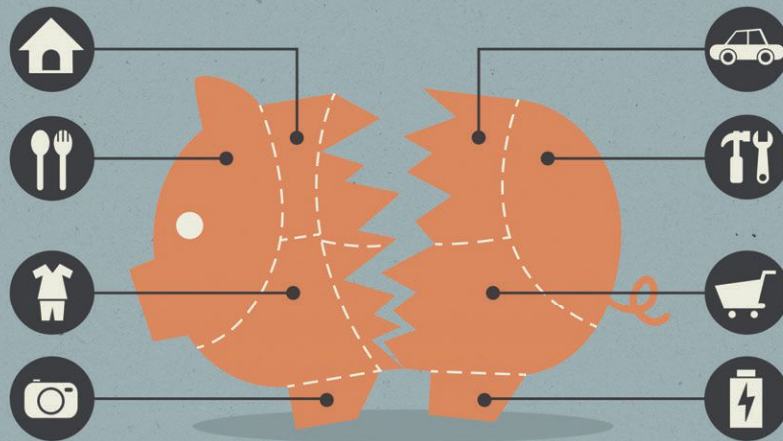
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**EA Journal Staff**

**PUBLISHER**

Michael S. Nelson, CAE  
mnelson@naea.org

**MANAGING EDITOR**

Margaret Mitchell  
mmitchell@naea.org

**TECHNICAL REVIEWER**

Mark Bole, EA  
mark@markboletax.com

**PUBLICATION DESIGN**

Bates Creative  
info@batescreative.com

**GRAPHIC DESIGNERS**

Emily Biondo  
Cecile Jordan  
Bryan Taylor

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# EA JOURNAL

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# Affiliates Are the Key



Lonnie Gary, EA, USTCP

**S**trong affiliates are the key to NAEA's success because strong affiliates promote a strong association. So what does it mean to be a strong affiliate? It starts with practicing good governance.

During my affiliate visits,

I have seen affiliates that were discussing bylaws changes and altering their governance structure in order to achieve the goals that they set out for themselves in their annual meeting. These are just two examples of good governance leading to strong affiliates. On the other hand, there are affiliates that are not aware of what is in their bylaws or when they were last reviewed. These affiliates are missing the opportunity to have their governance documents assist them in developing strategic goals for their society. Up-to-date governance documents are essential tools in building a strong affiliate.

How does an affiliate get help to update its bylaws and other governance documents? The Bylaws Committee will gladly review the bylaws of any affiliate to see if they are up to date and conform to NAEA bylaws. They will also review any proposed bylaw change prior to adoption by the membership of the affiliate.

The Affiliate Council is charged with maintaining frequent contact with affiliate leaders to offer advice and counsel to increase affiliate effectiveness. The Council has been encouraging affiliates to submit their current administrative and governance documents to NAEA. This program has several benefits to affiliates. It allows NAEA to assist affiliates in maintaining their tax-exempt status and to update their governance documents. This will in turn

assist affiliates in providing the kinds of benefits that their members want and need.

Affiliates with strong governance are better able to attract more volunteers, develop better leaders, and host successful education events that provide a valued member benefit and non-dues revenue. Affiliate leaders should contact me, Mike Nelson, or Lee Byrd, EA, for assistance. I urge affiliates to take advantage of these services.

The Schuldiner/Smollan Leadership Academy is yet another tool to help strengthen affiliates. Three academies were held this year to develop new leaders for NAEA, as well as for affiliates. Each attendee must choose a project designed to help benefit their local affiliate. Affiliate leaders should coordinate the projects to be chosen by their attendees to maximize the benefit to the affiliate. This is a great method to train future affiliate leaders and help strengthen an affiliate's governance.

Before I sign off, I would be remiss if I did not remind you of the upcoming election. In December, you will be asked to vote for the next leaders of the Association. Richard Reedman, EA, USTCP, is running unopposed for president-elect, and five director positions are being contested, along with secretary-treasurer. The nominee and candidate profiles directly follow my column. Take advantage of this opportunity to exercise your responsibility to vote. It is a right and privilege of membership. **EA**

# NOMINATING COMMITTEE REPORT



By Betsey Buckingham, EA (Chair); Jim Adelman, EA; Gina Jones, EA; Elizabeth Krug, EA; Winston Macon, EA; Diana Molina, EA; and Sandra Robb, EA

This year, we had more than thirty people nominated for the two officer and five director positions that will be voted upon in December. Of those nominated, nineteen took the time to complete the Leadership Profile Questionnaire, a ten-page document which required the individual's thoughtful consideration of multiple issues.

We were blessed in that every person who was interviewed by the committee brought multiple strengths to the table that would benefit the Association. This made our decisions and deliberation difficult, but very rewarding. The Nominating Committee is empowered to select one person, but not more than two persons, for each open officer or director position. We were required to select two nominees for officers and five nominees for director, but we could select a total of fourteen nominees. We selected ten. Any person who completed a Leadership Profile Questionnaire and was interviewed by the committee but was not selected as a nominee is eligible to "run from the floor" as a candidate in the election.

This report completes the 2014–2015 Nominating Committee's work. Each nominee or candidate is required to present to you, the members, a biography, statement of goals, and their vision for NAEA. I urge you to read these statements carefully. Consider the abilities presented by each person. Contact one or more of them if you have questions. Then exercise your right to vote.

NAEA is using the services of a professional election company for this process. Eligible members (those in good standing with NAEA as of November 1, 2014) will be able to cast their vote electronically. There are no longer any paper ballots. All members will receive an awareness message in early November, and on December 1, will receive a message giving a unique identification number and URL for accessing the electronic ballot. The biographies, statements of goals, and vision statements for NAEA found on the following pages will also be accessible via the electronic ballot.

It was my honor to chair this group of outstanding professionals who were willing to donate many hours of their time, not only in Las Vegas, but also prior to that for several phone conferences. Thank you all for your time and effort. If you have any questions about the voting process, please contact NAEA Executive Vice President Michael S. Nelson, CAE, at [mnelson@naea.org](mailto:mnelson@naea.org) or at 202-822-6232 x 101. Please contact Survey and Ballot Systems if you have any problems voting or do not receive a ballot at [support@directvote.net](mailto:support@directvote.net) or at 866-909-3549.

## This year's slate is as follows:

- **PRESIDENT-ELECT**  
Richard Reedman, EA, USTCP
- **SECRETARY/TREASURER**  
(choose one)  
Rich Rhodes, EA  
Laurie Ziegler, EA
- **DIRECTOR** (choose five)  
Steve Banner, EA  
Nancy Lyman, EA  
Joyce Mohr, EA  
Angela Radic, EA  
Don Rosenberg, EA  
Andy Stadler, EA  
Alexander B. Thomson, EA

## Additionally, the following individuals have chosen to run from the floor:

- **DIRECTOR**  
Tim Dilworth, EA, CPA  
Melissa Longmuir, EA  
Conrad Mangapit, EA



NATIONAL ASSOCIATION  
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## National Association of Enrolled Agents 2015-2016 Election

To cast a vote:

- Check the box next to a nominee/candidate name.
- To change your vote, click the box again, and the mark will be removed.
- To review nominee/candidate information, click the "View Bio" button next to each name.
- To review your selections, click the "Proceed to Ballot Confirmation" button.
- You may save your ballot and return later by clicking the "Logout" link.

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### President-Elect

Select **1** from below.

Richard Reedman, EA, USTCP - Nominee [View Bio](#)

### Secretary/Treasurer

Select **1** from below.

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Rich Rhodes, EA - Nominee [View Bio](#)

Laurie Ziegler, EA - Nominee [View Bio](#)

### Director

Select up to **5** from below.

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Tim Dilworth, EA, CPA - Candidate [View Bio](#)

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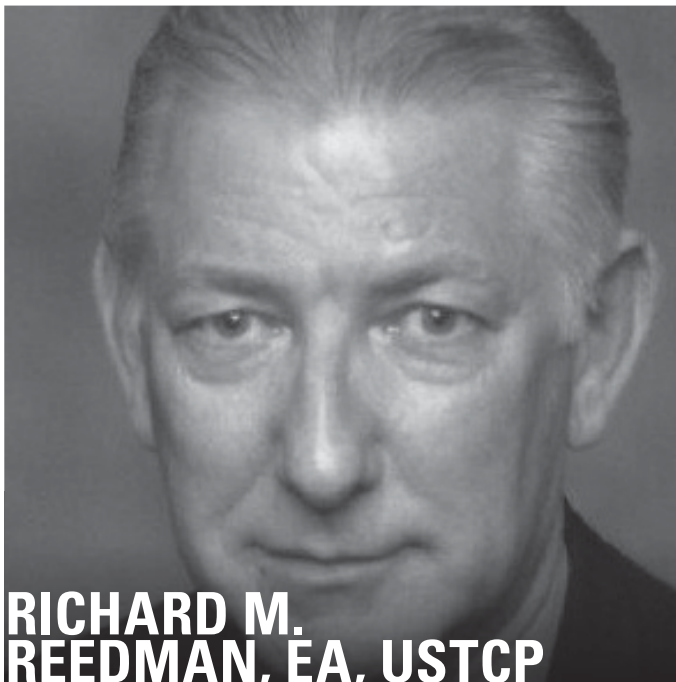
Conrad Mangapit, EA - Candidate [View Bio](#)

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**RICHARD M. REEDMAN, EA, USTCP**  
NOMINEE FOR PRESIDENT-ELECT

**BIOGRAPHY**

**NAEA:** Director (2013–present); Audit Committee (2014); Government Relations Committee (2013); Bylaws Committee (2012); NTPI Fellow (2008); Fly-In Participant (2012–2014); NTPI Part 2 Discussion Leader for three years

**NCSEA:** President (2010–2011), held positions of director, secretary, and treasurer (2005–2009, 2014)

**Education & Credentials:** DeMontford University (UK); Association of Chartered Certified Accountants (ACCA, UK); Enrolled Agent (1999); USTCP (2008); Certified Fraud Examiner (2005); Certified Senior Advisor (2006); Certified Internal Control Auditor (2013)

**Other Qualifications:** Owner of Reedman & Associates, Inc. (2003–present); CFO of an international business for 17 years

**STATEMENT OF GOALS**

It is an honor to be nominated for the position of president-elect. I have enjoyed working collaboratively with other Board members as a director and as a committee member to enhance NAEA at the national level.

There are some exciting programs and initiatives being introduced over the next few months: the Educating America Program, the NAEA president interview on American Airlines flights, and the creation of “Why Join” brochures—all designed to attract new members, to demonstrate the “perceived value” of joining NAEA, and to promote the EA name.

To continue the success of NAEA, we need to increase membership by demonstrating the benefits of joining our Association. Currently, of the 48,887 enrolled agents, approximately 25 percent are members of NAEA. In addition, demonstrating value will help attract a portion of the approximately 350,000 “other tax return preparers” (non CPAs, attorneys, and enrolled actuaries/retirement plan agents). Continued work with state affiliates is important in order to keep expanding membership, as well as promoting excellent education programs, such as the SEE preparation classes, at the national and state levels. The Educating America program (directed toward college students) and the campaign to enhance NAEA’s social media presence will also help to attract younger members to our Association.

I am totally committed to NAEA, and I am totally committed to expanding membership and reaching out to attract new and younger members. I am excited that we will be working on a new strategic plan in November 2014, and we will continue to incorporate as many new plans as we can to achieve these goals.

**MY VISION FOR NAEA’S FUTURE**

My vision for NAEA is very positive, with our aim being to increase membership and make it the leading, most-recognized tax professional association in the industry. We have a great opportunity with the programs we are introducing and the collaborations with state affiliates. It is important to keep moving programs forward, with the goal of showing the benefits of joining NAEA.



**RICHARD R. RHODES, EA**  
NOMINEE FOR SECRETARY/TREASURER

**BIOGRAPHY**

I established my tax practice in 1992 and became an enrolled agent in 1999. Soon after, I became active with NAEA at the local and state (Ohio) levels. In 2009, I became involved at the national level. Most recently, I have chaired the Young Professionals Task Force. In 2012, I became an NTPI Fellow.

Nationally, I am serving as a member of the Board of Directors. I also participate on the PR Committee, the Governance Structure Task Force, and the newly formed IT Focus Group.

**STATEMENT OF GOALS**

My goal as secretary/treasurer is to work diligently to build on the achievements of the past and help guide our Association into the future. As a director on the NAEA Board, I contributed to the development of the strategic plan, and I strongly support the goals reflected within the plan. I will continue to advocate for NAEA to focus and follow the objectives set forth in our strategic plan:

- Increase the public and media recognition of EAs. We must be the primary media source when they are reporting a tax-related story. This in turn will help increase the recognition of EAs.
- Continue to advocate on behalf of our members and taxpayers.
- Continue to be the source for quality CE for members and potential members.
- Increase member services by reinforcing the value of membership.
- Expand our membership by continuing to increase our social media presence and continuing to increase our focus on engaging young people.
- Increase our fiscal reserves and non-dues revenue.

Jim Rohn said, “The challenge of leadership is to be strong, but not rude; be proud, but not arrogant; have humor, but without folly.” I believe that this is an accurate description of my leadership characteristics that are reflected in my business and personal lives, and they will continue to be guiding principles during my leadership tenure. I am proud to have the opportunity to serve my peers in NAEA, and will always do what is in the best interest of our Association. Thank you in advance for your consideration.

**MY VISION FOR NAEA’S FUTURE**

I expect to see NAEA become the primary tax resource for all media. We will need to make efficient use of all social media platforms available to us now and in the future. By being a reliable source to all types of media outlets, we will continue to maintain momentum on letting the world know that EAs are America’s tax experts! I also expect to see NAEA become the primary source for member access to a tax research service. This will take time, but I feel strongly that it is a benefit our members should not have to go outside of NAEA to acquire.



**LAURIE ZIEGLER, EA**  
NOMINEE FOR SECRETARY/TREASURER

**BIOGRAPHY**

I am the managing member of Sass Accounting, LLC, in Saukville, Wisconsin. Since 1993, the firm has grown to over 700 clients, including more than 200 small businesses. In addition to being an enrolled agent, I am a QuickBooks certified pro-advisor, providing business consultation, education, and support services.

I have a bachelor's from Lakeland College in Accounting and Business Administration, with an Economics minor. I became an enrolled agent in 2004 and an NTPF Fellow in 2007.

I am the current secretary/treasurer of NAEA, as well as a member of the Executive and Audit Committees, and the Reserves Task Force. I previously served on the NAEA Board as a director, and I have been a member of the NAEA Reserves Task Force, Affiliate Council, the Young Professionals Task Force Review Group, and the Government Relations Committee.

I am a past president of the Wisconsin Society of Enrolled Agents, and previously served as state treasurer and director. I am also actively involved with numerous local charitable organizations.

**STATEMENT OF GOALS**

I fully support NAEA's strategic plan. Of the five key strategic areas, I believe public recognition should be our top priority.

Educating the public about the EA designation is my highest priority. In light of recent court cases involving the regulation of tax return preparers, recognition and public awareness are now more important than ever before. The Association is the collective voice of its members and should be the leader in this process. The taxpaying public needs to be aware of our special status with the U.S. Department of the Treasury.

NAEA needs to encourage those who pursued the RTRP designation to become enrolled agents. I believe there is an enormous opportunity to expand our organization and our profession; however, we need to move forward on these issues. NAEA has developed excellent programs and must continue to focus resources to provide exceptional educational opportunities, outstanding member benefits, and a strong voice with legislators and the IRS.

I feel very strongly about my profession as an enrolled agent, and am equally passionate about NAEA. I have thoroughly enjoyed my involvement with the Association on the state and national levels, and am looking forward to the opportunity to continue to serve my fellow members as secretary/treasurer.

**MY VISION FOR NAEA'S FUTURE**

My vision for NAEA is that it be recognized as the premier organization of choice for America's tax experts and that a greater percentage of enrolled agents come to be members. I believe there is strength in numbers. The more members we have, the louder our voice becomes and greater resources will be available to accomplish our larger common goals.



**STEVE BANNER, EA**  
NOMINEE FOR DIRECTOR

**BIOGRAPHY**

I began my career in the field of income tax in 1977, and have since gathered business experience in a variety of countries and cultures. In addition to the United States, I have lived and worked for extended periods in Australia, Saudi Arabia, Canada, and Sweden. Along the way, I studied Adult Education and earned a bachelor's in Education, master's in Educational Administration, and an MBA. This lifelong combination of interests in taxes and adult education is what ultimately led me three years ago to sell my tax practice and take a position as senior tax editor with the online continuing education provider APlusCPE. I live in Fort Worth, where I am currently first vice president of the Dallas-Fort Worth chapter of TXSEA, having served as secretary the past two years.

**STATEMENT OF GOALS**

My primary goal is to continue to enhance and communicate the benefits of NAEA membership for enrolled agents, with the aim of increasing the number of NAEA members by at least 20 percent each year. The chief means of achieving this goal is through improving the education services currently offered by NAEA. The Association's annual 30 credit hours requirement represents an excellent opportunity to enhance the perceived value of membership, while at the same time providing useful and timely information for members.

**MY VISION FOR NAEA'S FUTURE**

I would like to see NAEA be regarded by all enrolled agents as an organization that they cannot do without. My vision is for NAEA to be an authoritative and indispensable source of guidance and information for all enrolled agents. I have recently heard a number of current members discussing whether they will renew their membership when it becomes due. They feel that they receive much more value from being associate members in their local state chapter than they do from being members of NAEA. I would like to remove such doubts from the minds of EAs and help them to see NAEA as the first place to look to find information on new developments in the industry.

I would also like to see NAEA as the first place EAs look to for continuing education. There are currently numerous providers who offer CE courses, but none of these (apart from the IRS) have the cachet and authority that NAEA would bring to its courses. NTPF exemplifies this principle perfectly.





**NANCY LYMAN, EA**

NOMINEE FOR DIRECTOR

**BIOGRAPHY**

- Employed by a professional corporation of CPAs for twenty-eight years.
- Started as a payroll clerk and continually accepted new challenges.
- Became interested in tax representation and preparation and earned EA license in 1995.
- Current NNESEA president; former vice president, director, and Membership chair. While Membership chair, NNESEA was awarded first place for membership retention for two consecutive years.
- Served NAEA as chair of the Public Relations Committee and as a member of the Public Awareness Committee. During tenure as chair, created *A Guide to Effective Public Relations for NAEA Affiliates* that was included in the Schuldiner/Smollan Leadership Academy handbook.
- Graduate of November 2011 Schuldiner/Smollan Leadership Academy.
- Chair of the Affiliate Council
- Director on the NAEA Board of Directors
- Governance Committee member
- As an NAEA member (1995), an NTPI Fellow (2007), and a constant supporter of the NAEA PAC, I would like to continue to be your voice on the Board.

**STATEMENT OF GOALS**

What an exciting time to be an enrolled agent! I strongly support NAEA's strategic plan, and I will make every effort to implement it while maintaining the high level of professionalism and ethical standards that are at the core of NAEA. We need to expand the public's recognition of the EA license through consistent and aggressive marketing techniques and through public relations and media outreach, such as radio, television, and print. Our members must also be encouraged and empowered to promote themselves. The Affiliate Council is an excellent resource to be responsive to member needs. When connections are made between the national and state levels, achieving our goals as a tEAm will be realized. I will continue to support the NAEA PAC in its efforts to work with the IRS and be our voice on Capitol Hill. I will support the NAEA Board of Directors with the ongoing strategic planning process to advance the enrolled agent profession through advocacy, promotion, and support of its members. I believe in what our Association can do for its members, and I want to continue to be your voice on the Board.

**MY VISION FOR NAEA'S FUTURE**

My vision of NAEA's future would include *all* enrolled agents recognizing the benefits of being a member of a strong association. They would have confidence in an organization that advocates on their behalf, provides quality education, supports their state affiliates as needed, and maintains a financially sound association.



**JOYCE MOHR, EA**

NOMINEE FOR DIRECTOR

**BIOGRAPHY**

**NAEA:** Nominating Committee (2012–2013); Government Relations Committee (2014); Governance Structure Task Force (2014); Government Relations Fly-In Participant (2011, 2012, 2014); NTPI Fellow (2014); Schuldiner/Smollan Leadership Academy graduate (Massachusetts pilot (2011) and Orlando, Florida (2013))  
**MaSEA:** President (2013–present); First Vice President (2009–2013); EA of the Year Award (2013); SEE Preparation Course Instructor (2009–present)  
**Education:** Boston University, BA English (1987)  
**Other Qualifications:** Owner, Taxes Plus, a tax preparation, consulting, and representation business serving clients with a wide range of tax needs (2011–present); co-founder and president of Acacia in Kenya, an educational outreach project

**STATEMENT OF GOALS**

I am honored and excited to be nominated for an NAEA director position. I have been very fortunate to be mentored and engaged at the affiliate and national levels as a member of NAEA and MaSEA. I see pursuing an NAEA leadership position as a way I can give back to the organization that has fostered my personal and professional growth.

I want to be a part of ensuring and expanding the opportunities for other enrolled agents to have the kinds of experiences and benefits I have had. I will work to raise awareness about our designation and ensure that our rights to practice are protected. Participating in NAEA leadership is the best way I can work with others to promote these goals. I fully support the NAEA 2012–2015 Strategic Plan goals of awareness, advocacy, education, member and affiliate services, organization/infrastructure, and financial security.

Thank you for your consideration. I would love the opportunity to represent NAEA members and to participate in the important work NAEA does to ensure that enrolled agents are increasingly known as America's tax experts.

**MY VISION FOR NAEA'S FUTURE**

Through the Schuldiner/Smollan Leadership Academy, APEX (Affiliate Presidents Exchange), Affiliate Council, and other programs at NAEA, we will continue doing great work to strengthen and support affiliates.

I strongly support the Educating America initiative. I believe that it will enable NAEA to promote the designation and to increase membership in ways we have not had the opportunity to do in the past.

By increasing membership, we increase our ability to support affiliates and members and to have our voice heard in matters that are important: the protection of our rights to practice, oversight regulations, the tax code, and issues currently unforeseen.





**ANGELA RADIC, EA**  
NOMINEE FOR DIRECTOR

**BIOGRAPHY**

**NAEA:** Young Professionals Task Force; Fly-In Day Participant; Professional Partner Representative for Beta Alpha Psi; APEX Participant; PAC Supporter  
**OSSEA:** Treasurer  
**GCCOSSEA:** Treasurer; Social Media Chair

In 2007, I became the CEO of Parker’s Tax Accounting, a firm established more than twenty years ago. Prior to my joining, the firm enjoyed a positive reputation within the community and solid financial performance. However, by implementing procedural and technology-based solutions, I increased revenues by 70 percent.

Continuing our firm’s tradition of involvement with NAEA, I am an active member at the local, state, and national levels. For my local chapter, I designed and launched a website that has increased our visibility as a provider of quality, affordable continuing education. During my tenure on the Young Professionals Task Force, I designed documents compiling the group’s best practices for affiliate websites and mentorship programs.

I have a BS in Organizational Behavior Management from Miami University.

**STATEMENT OF GOALS**

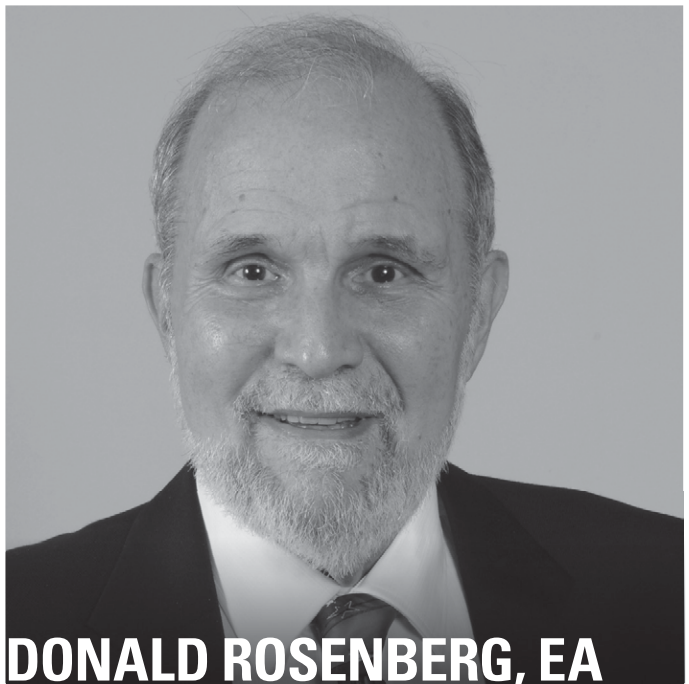
By creating a welcoming environment at all levels of our organization and mentoring those who are new to our profession and NAEA, we can increase membership and encourage active participation. I would like to explore the ways that NAEA, at the national level, can provide resources and support to local chapters to assist in their efforts to mentor our newer members. Educating America is an important first step to bringing new members in the door, but establishing personal connections will ensure that members are engaged and understand the value of NAEA membership.

We also have the opportunity to strengthen the education offerings available to local chapters, so that those who are unable to attend NTPI can experience the same top-tier education at their state and local chapters. Advances in technology have created the pathways, such as webinars, online courses, and tutorials, by which NAEA can offer distance learning options.

**MY VISION FOR NAEA’S FUTURE**

My vision is that the EA credential will become widely recognized and that NAEA membership will be considered essential for dedicated tax professionals. We can accomplish this by fostering a culture of mentorship, which will provide new members with the support they need as they launch their careers, as well as encouragement to become actively involved in our organization.

Focusing on recruiting and developing active membership not only supports our advocacy and promotion efforts through increased financial resources, but it will also ensure the longevity of our organization.



**DONALD ROSENBERG, EA**  
NOMINEE FOR DIRECTOR

**BIOGRAPHY**

I have been an enrolled agent for twenty years. My practice includes business and individual tax returns, business write-up, and taxpayer representation. For more than thirty-five years, I have served as an adjunct lecturer at CUNY’s Hostos Community College in the Bronx, guiding hundreds of students toward the tax and accounting profession. I am proud of the impact I have made on many students’ careers, and am pleased that I play a strong role in the courses offered by Hostos for the SEE and preparation for the EA profession.

I have served NAEA as an NTPI Level 2 instructor for eight years, and I have trained many NTPI Fellows. I chair the Schuldiner/Smollan Leadership Academy Advisory Board and have just completed my second term as president of NYSSEA. I am a Leadership Academy graduate, an NTPI Fellow, former chair of the NTPI Planning Committee, and have served as a consultant to the Educating America Implementation Task Force.

**STATEMENT OF GOALS**

I am honored to be nominated for an NAEA director position. As a director, I will continue to push for the strategic goals outlined in the NAEA 2012–2015 Strategic Plan: recognition of EAs, advocacy, and education.

The best way to increase recognition is to train more people to become EAs. My experience at the community college level enables me to bring insight to the Board to help further our Educating America initiative.

Without the right to practice, all our goals would be meaningless. We would not have a credential to be recognized. I support and will work with the Government Relations team to codify the EA credential and make sure the IRS develops meaningful regulation of the tax preparation industry.

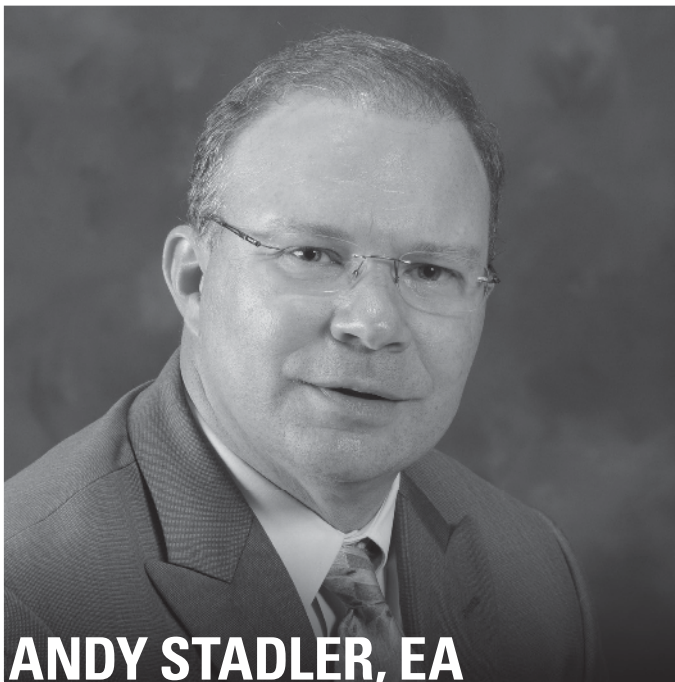
My goals for education are simple: continue to offer premier programs like NTPI. We should develop a basic representation course for our affiliates, providing members with local representation training.

**MY VISION FOR NAEA’S FUTURE**

NAEA needs strong visionary leadership to promote the EA credential, advocate on our behalf, and provide outstanding education for our members and young professionals.

Solid support of our state and local affiliates is crucial to a strong national organization. We should cultivate strategies that fortify our solid affiliates, while providing assistance to struggling affiliates.

The Educating America program will increase membership by training students to become EAs, elevating the enrolled agent to the most widely recognized credential synonymous with America’s tax experts.



## ANDY STADLER, EA

NOMINEE FOR DIRECTOR

### BIOGRAPHY

**NAEA:** Excellence in Public Awareness Award (2014); Educating America Committee (2013–present); PAC Steering Committee (2011–present); Education Committee (2013–present); IT Focus Group (2014); Membership Committee (2014); Fly-In Participant (2009–2014); NTPI Fellow (2013); Schuldiner/Smollan Leadership Academy (2012)

**ISEA:** President (2012–present); Director (2004–2011)

**Education:** BS, Business Management, Oakland City University; AS, Accounting, Ivy Tech; AS, Paralegal Studies, Community College of the Air Force

**Military:** Rank, Chief Master Sergeant (E-9); Duty title: ANG Paralegal Career Field Manager/Senior Enlisted Advisor to the Judge Advocate General

**Duties:** Management of enlisted legal personnel at eighty-eight bases; instituting policies to enhance training, morale, and welfare; member of Information Technology Committee; instructor, speaker, and trainer

**Honors:** Military awards include Air Combat Command Paralegal of the Year (2006); Outstanding Airman of Quarter (2004); Meritorious Service Medal; Air Force Commendation Medal; National Defense Service Medal; Global War on Terrorism Expeditionary Medal

**Deployment:** Operation Iraq Freedom (twice), and numerous other times for many other operations

**Other Qualifications:** Founder and executive CFO for Stadler & Co., Inc., a small firm that grew to five locations, servicing more than 7,000 clients. My duties include instituting policy for all tax preparers to achieve the EA credential; planning and implementation of office policies and procedures; CE training for over thirty employees on tax law; guest speaker at IRS national tax forums and several organizations on tax law; and office management

### STATEMENT OF GOALS

As a concerned enrolled agent, I have three areas of focus. My primary goal is increasing recognition of the EA designation. I support NAEA's strategic goals, and I believe that with a focused and effective plan, we can change the general public's perception of what is an EA. For the 35,000 EAs who are not members, we need to address the questions, "What has NAEA done for me?" and "Why should I join?" We can accomplish these objectives through three tools: the Educating America program; motivating/encouraging EAs to be proud and promote their credentials; and selecting a model for states to use in the state tax preparer licensing movement.

### MY VISION FOR NAEA'S FUTURE

- Grow public awareness.
- Substantially increase NAEA/affiliates membership.
- Strongly encourage tax preparers to become enrolled agents.
- Grow Educating America so that accounting students, tax preparers, and those who seek a second career have an outstanding opportunity to become and succeed at being an EA, America's tax expert.



## ALEXANDER B. THOMSON, EA

NOMINEE FOR DIRECTOR

### BIOGRAPHY

I am president of the Thomson Management Group, a firm of tax and financial management specialists serving people involved in the political and public interest community.

**NAEA:** Recipient of the Bill Payne Advocacy Award (2011); Secretary/Treasurer (2010–2011); Member, Board of Directors (2008–2011); PAC Steering Committee (2005–present); Chair, 2006–2010, 2014–2015; Executive Committee (2009–2011); Chair, Governance Structure Task Force (2014); Government Relations Committee (2004–2010); Nominating Committee (2004); Audit Committee (2010–2011); Chair, Schuldiner/Smollan Memorial Fund Task Force; Subject matter expert for the SEE; NTPI Fellow; NTPI Graduate Fellows Association Vice President (two terms); three-time panelist on *Tax Talk Today*

**VaSEA:** President (2008–2010); Vice President (2 terms; member since 1999); Chair, Budget Committee; Co-Chair, 25th Anniversary Celebration; Editor for rewrite of Bylaws and Policies & Procedures Manual

**Northern Virginia Chapter of VASEA:** President (2008–2009); Vice President (2 terms); Tri-State Annual Tax Conference Coordinator (2007–2011)

**Other Qualifications:** CFP, CDFP, CLU, ChFC, RHU, Series 7 registered rep with H.D. Vest; Undergraduate studies, Kalamazoo College; Master's degree, Antioch School of Law; Adjunct faculty in tax at GWU, American University, and College for Financial Planning

### STATEMENT OF GOALS

I support the strategic plan. I am committed to increasing recognition of the EA credential, educational opportunities for our members, creating more opportunities for member participation, and promoting a spirit of unity in NAEA. I pledge to represent our members and state leaders to the best of my ability and to keep NAEA moving forward with professionalism. By working together, we can make NAEA even better. I will never forget that NAEA exists to serve the needs and interests of our members. *I ask for your support and vote.*

### MY VISION FOR NAEA'S FUTURE

I see an NAEA that will continue to be the premier membership organization for those most qualified to prepare tax returns and represent taxpayers—the enrolled agent, America's tax expert. Recognition of the EA credential will increase; NAEA membership will grow with the implementation of new return preparer requirements and regulation; staff will expand to meet membership needs; publications and resources will improve; and NAEA's reputation will soar as it continues to play a meaningful role in the legislative and regulatory processes.





**TIM DILWORTH, EA, CPA**  
CANDIDATE FOR DIRECTOR

**BIOGRAPHY**

I currently serve on the NAEA Board of Directors. I spent two years on the NTPI Planning Committee. I served the Michigan Society of Enrolled Agents for the past six years, including a year as conference director, a year as VP, two years as president, and two years as immediate past president. During my time as president of MISEA, we earned a membership award from the Affiliate Council for increasing membership. In November 2013, I attended the Schuldiner/Smollan Leadership Academy. My SSLA project to raise money for NAEA PAC earned our affiliate an award for government relations.

**STATEMENT OF GOALS**

My goal for the next two years is to continue toward making the term "enrolled agent" known to every household in America. We have some great tools for achieving this goal. The number one tool is our own members' dedication and enthusiasm. The Educating America initiative to bring enrolled agent education to America's colleges is a fantastic opportunity for us. It will enable us to get the word out among the general public that being an EA is a viable and attractive career option. A by-product of being in the schools is more name recognition for our profession. Contact your local affiliate or the NAEA national office if you have contacts at a community college or just a passion to bring our program to a local school. It will take all of us to create a successful grassroots movement to make enrolled agents the preferred tax professionals for America.

**MY VISION FOR NAEA'S FUTURE**

We have all been asked to give our vision for NAEA's future. I have many ideas on that, but it is imperative that we move quickly. The future is now! We should be the number one organization for enrolled agents in America. We should be the first to contact those who have passed the SEE to invite them to join us in the only organization dedicated solely to representing the interests of enrolled agents. We should be the primary source of information relevant to our members on tax and representation issues. We should be using social media to the greatest advantage possible because that is where we will find the future—the young people of America.

Join me in being an "agent" for change. Let's bring the future into the present so that we aren't left behind.



**MELISSA LONGMUIR, EA**  
CANDIDATE FOR DIRECTOR

**BIOGRAPHY**

I have an MBA in Information Systems, a BS in Biology and Psychology, and I completed an internship for my MBA with the American Red Cross. As an adjunct professor at several colleges in Seattle, Washington, I taught business and computer courses. After my father died in 2000, I was hired by a prominent company where I took a tax course. I was quickly promoted to a supervisory position of several tax offices, and subsequently became a director of a premium office. In 2005, I left that company and started my own practice.

I have been a volunteer with ARC Disaster Services for over twenty-five years, serving whenever needed locally and nationally in leadership roles, such as being a supervisor in financial and statistical information (related to accounting).

As president-elect of WSSEA in 2009, I was involved with the presentation of a bill to the legislature. After a lengthy procedure using a lobbyist, the final vote was in favor of EA rights.

**NAEA:** Affiliate Council Member (2010–present); APEX and Board Meetings (2009–present); Fly-In Day (2009–present); PAC supporter (2009–present); Alaska Task Force (2012–2013); Online SEE Course (2009–2013); Schuldiner/Smollan Leadership Academy (2012); *EA Journal* articles (2006, 2009); NTPI Fellow (2005); Enrolled Agent (2003)

**WSSEA:** President and other Board positions (2005–2011)

**STATEMENT OF GOALS**

I want to increase the recognition of what an EA is to the public. I propose that through various methods of publicity, the public will become more aware of what an EA stands for. I would like the term "EA" to be as recognizable as a "CPA" is to the public.

**MY VISION FOR NAEA'S FUTURE**

- Increase the number of members, both young and not so young.
- Work on increasing the number of associate status and academic associates. This can be done not only at the college level, but also at high schools, unemployment offices, and even within our own membership.
- If we increase the leadership training at the state level, then NAEA and the state affiliates will have a larger base of applicants they can pull from, thus strengthening the organization.
- Offer more education that non-credentialed preparers can take and receive credit for.
- Update members regarding IRS changes in a more timely fashion.

Finally, I hope to implement these goals with your help, and would appreciate your vote in the upcoming election. Thank you.





**CONRAD MANGAPIT, EA**  
CANDIDATE FOR DIRECTOR

**BIOGRAPHY**

I am a proven leader who gets the job done, and an accomplished EA with over forty years of business acumen who has made a difference. My forte is “retiring” business problems. My motto is, “I’m a solution looking for a problem!” I am a candidate because I choose to serve. I believe that our low membership numbers can be resolved now. Join me and together we can:

- Reenergize and reinvigorate NAEA.
- Elect a leadership that shepherds a tEAm effort in partnership with our affiliates to focus on membership resolution.
- Develop a “best value” membership package to include: *The Enrolled Agent’s Book of Knowledge*, an interactive online tax almanac for EAs, and an adjunct website (AskAmericasTaxExperts.com) that answers taxpayers’ questions. The elements of the package are designed to create significant streams of non-membership dues revenue.
- Develop programs that engage and support us from the time we are EA candidates to the time we retire.

Remember, you are important to NAEA because you are its financial foundation and the reason for its existence. Do you feel that your importance to NAEA is being matched by the value you are receiving as a member? With your help, I will lead efforts to ensure that the value of your membership is the best in the industry.

Do you realize that NAEA had a 25 percent chance of recruiting you? This means 75 percent (30,000+ EAs) are not members of NAEA. How long are we going to settle, to just get by with 25 percent? What’s disheartening is NAEA, our home, has for years tolerated this. It is by actions—and not by words—that transformations occur. Imagine how much more you can be served when a reenergized NAEA doubles or even triples its membership!

**STATEMENT OF GOALS**

With your help and as your advocate, I will:

- Ensure that NAEA’s leadership remains continually focused on its membership challenges.
- Lead, encourage, and champion the implementation of new ideas that optimize the capabilities of NAEA, state affiliates, and local chapters in satisfying all the needs of members.
- Generate significant non-membership dues revenue.

**MY VISION FOR NAEA’S FUTURE**

I envision a very proactive NAEA, serving and satisfying the needs of over 30,000 happy members. In the future, NAEA is a world-class organization and a respected leader in the tax industry.

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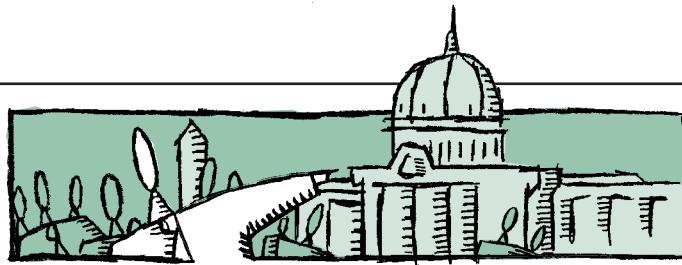
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# Plans Are Useless, but Planning Is Indispensable

By Robert Kerr

**O**ctober 15 brought sighs of relief to enrolled agents throughout the country. Or perhaps those were gasps of panic rather than sighs of relief? In any event, those crises are (mostly) behind you, and you are now able to focus in earnest on the upcoming filing season and the Thanksgiving and December holidays. With the holidays in mind, you may be asking what your box of 2015 filing season joy looks like.

Well ... not great.

The two most salient characteristics of the upcoming filing season are not presents from Washington, D.C., either to you or to your clients. That said, it is not too late to plan.

I see two issues—one recurring and the other new—each of which has potential to complicate the filing season. The recurring issue is driven by expired temporary tax provisions. The new issue is driven by the Affordable Care Act (ACA), the 2010 law mandating and subsidizing health insurance (and sometimes called Obamacare). As tax experts, however, you'll need to be aware of these issues in order to provide the level of service your clients expect and require.

We'll take the issues one at a time, starting with the expired temporary tax provisions, about which most of you will have read in *E@lert*, and then moving on to take a look at ACA.

The vast majority of temporary tax provisions (or “extenders” in D.C. shorthand) exist for two main reasons:

- The provision was too costly to offset through other spending reductions (the AMT “patch” used to be Exhibit A) back when Congress actually paid for the ten-year cost of tax law changes.
- The provision was intended to meet a need Congress believed was temporary (bonus depreciation, for instance).

Now back in the day, extenders were troublesome only because they complicated tax planning. How, you might ask? Because Congress repeatedly stated a tax goodie (the significant increase in Sec. 179 expensing limits, for instance) was temporary and then without fail extended the temporary provision. As a result, tax planners were never certain whether a provision would continue from year to year.

The planning problems were rather benign until the past six years or so, which is when Congress stopped extending the temporary provisions well before they expired. Things went from bad to worse when our legislators discovered they could, without repercussion, renew the provisions retroactively.

So here we are in 2014, which looks a lot like 2012, which was the first time that Congress extended the provisions retroactively, twelve months after they expired. At the stroke of midnight on December 31, 2013, roughly 55 temporary tax provisions expired. Among the biggies on the individual side:

- tax-free discharge of indebtedness on principal residence
- state and local general sales tax deduction
- tax-free distributions from individual retirement plans for charitable purposes

And on the business side:

- research and experimentation credit
- fifteen-year straight-line deduction for leasehold improvements
- increase in Sec. 179 expensing limits

Aside from the planning nightmare this uncertainty becomes for some taxpayers, the other very real consequence is that late tax law changes are a challenge for IRS to program into its returns processing system.

Conventional wisdom in D.C. is that Congress will return in a week or two and address extenders during the post-election “lame duck” session. If we're lucky, we'll have a resolution by early to mid-December. If we're unlucky, we'll see lots

## About the Author

**Robert Kerr** has served as NAEA's senior director, Government Relations since 2004. Prior to joining NAEA, Kerr worked on the Senate Finance Committee Oversight and Investigation staff, where he assisted the committee chairman in providing oversight to, among others, IRS, U.S. Postal Service Office of Inspector General, and General Services Administration. He also spent a dozen years in a variety of positions at IRS and is well-versed in a variety of tax administration issues. Kerr holds an MBA from Case Western Reserve University and a BA from Mount Union College.



of squabbling and no resolution until very early in 2015. The former outcome (more likely than not) is terrible and would probably delay the filing season similarly to the 2013 filing season (a slight delay in the start of the filing season and a significant delay for taxpayers with particular filing circumstances). The latter outcome (unlikely but non-zero probability) would be catastrophic and would ensure a significantly delayed filing season for all or nearly all.

\*\*\*\*\*

While you can't do much about extenders except keep your clients informed and possibly schedule the first couple weeks of the filing season more carefully than usual, you can do something about ACA-related filing season challenges.

But first, let's outline the tax-related issues, which fall mostly into the following three buckets for individual taxpayers:

- advanced premium tax credit
- minimum essential coverage
- individual shared responsibility payment

In a nutshell, taxpayers (and this includes each family member) must either have qualified health insurance (also called minimum essential coverage) or pay a fee (the individual shared responsibility payment) unless they

receive an exemption from the requirement. Further, subsidies (premium tax credits) were available for individuals who did not have health insurance coverage through their employers if they met certain income requirements. Advanced premium tax credits estimates were based on 2012 income and will be "trued up" based on actual 2014 income.

Enrolled agents will find themselves facing two new tasks. The first is to determine whether an individual taxpayer (and his or her family members) had qualified health insurance for the full year (or the months of the year they were required to do so). If they did not, then you'll need to determine whether they were exempt. If they were not exempt, you'll need to calculate their individual shared responsibility payment, which in 2014 is the higher of either one percent of annual income or \$95 per person.

Individuals may qualify for one of nine exemptions, one of which is hardship. Fourteen hardships are in play, including the death of a close family member, domestic violence, or receipt of a shut-off notice from a utility company. The exemptions are provided by IRS, the Marketplace, or both. Some are requested on the tax return, others are not.

Further, you'll need to determine whether your clients who purchased health insurance through the Marketplace qualified for a health premium tax credit based on their 2014

incomes, and if they requested an advanced credit, you'll need to determine whether the credit was too small (in which case they'll receive the balance of the credit after filing the return) or too large (in which case they'll be required to pay back the overage).

How are you going to get the job done? Suffice it to say, IRS has new forms for you: Form 8962 (Premium Tax Credit), Form 1095-C (Employer-Provided Health Insurance Offer and Coverage), and has changed Form 1040 as well ...

\*\*\*\*\*

General Dwight D. Eisenhower once said, "In preparing for battle I have always found that plans are useless, but planning is indispensable." Our question then becomes what's the plan? I suggest for the coming filing season, ACA training will be critical. I recommend a special emphasis on the individual shared responsibility provision exemptions and hardship exemptions. Further, think about the 2013 filing season and make contingency plans for a bumpy ride based on those experiences.

We know the season won't go according to plan, but we also know that those with an initial plan will provide their clients with the best service and maintain their sanity throughout. **EA**

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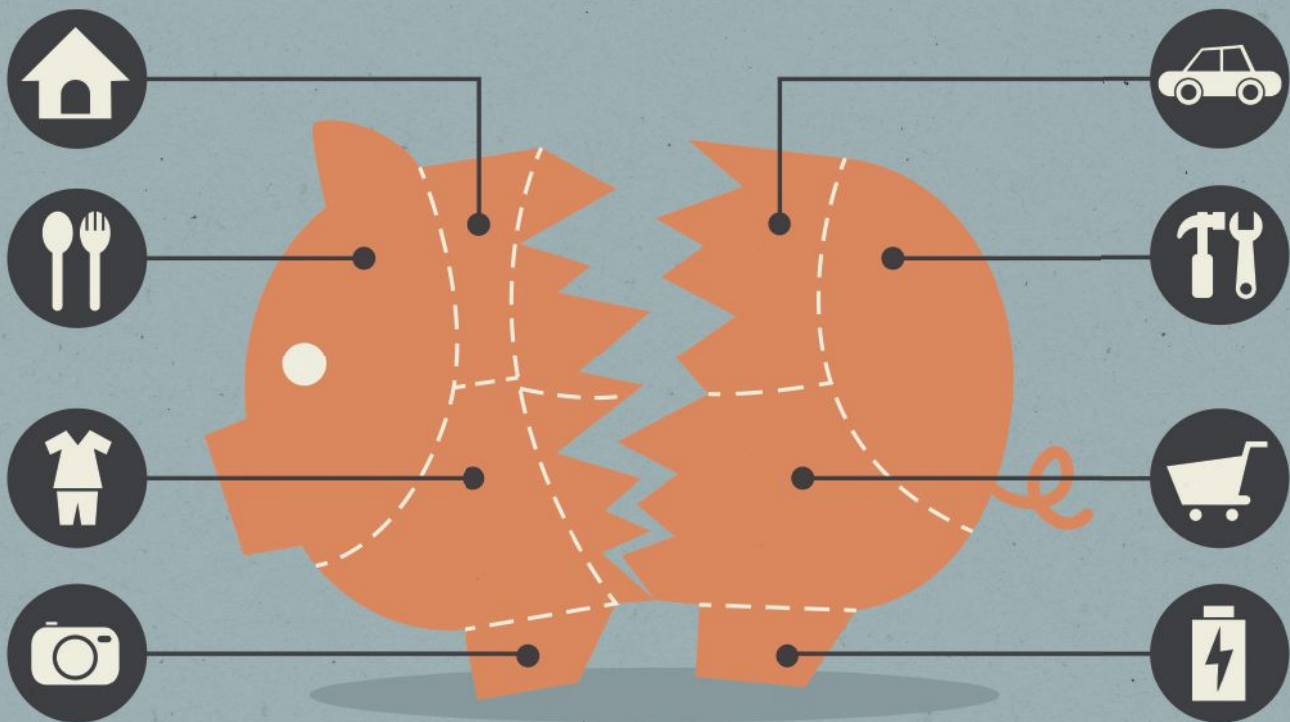


GOING BEYOND

# FORM 433-A

PROTECTING ASSETS IN AN OFFER IN COMPROMISE

BY HOWARD S. LEVY, JD



**T**he formula the IRS uses to value an offer in compromise is widely published by the IRS, both on its website and in the OIC instruction booklet. It is no secret that to settle a tax debt, the IRS wants money from two pots: the value of a taxpayer's assets and the present value of the taxpayer's ability to make monthly payments on the debt.

What is less publicized, however, are the exclusions the IRS allows in the value of assets in a compromise. The nooks and crannies of the Internal Revenue Manual and Internal Revenue Code reveal significant savings in how the IRS values automobiles, cash in bank accounts, business equipment, and household goods in an OIC.

The IRM allows a value reduction for cash in bank accounts equal to one month's living expenses. That's not all: The IRM also provides a \$3,450 blanket reduction off the value of an automobile, and it permits a business to retain equipment that is critical to its operations without including the value in the settlement of the compromise.

The IRC restricts IRS' ability to seize most taxpayers' household goods and personal belongings, as well as the tools of a trade or business. These restrictions on IRS' collection power are also value reductions in an offer compromise. In other words, if the IRS cannot seize and collect from property, then the equity in that property (i.e., household goods or tools of the trade) is not included in the valuation of a compromise.

We want to save money for our clients and secure the lowest settlement possible. So let's take a more detailed look at how to claim value exclusions for automobiles,

cash in bank accounts, business equipment, and household goods in an OIC, and how to incorporate those exclusions into an IRS financial statement, Form 433-A (Collection Information Statement for Wage Earners and Self-Employed Individuals).<sup>1</sup>

### Automobiles

Don't claim the full value of your client's automobile on Form 433-A for an offer in compromise without first reading IRM 5.8.5.12. This provision allows for a blanket exclusion of \$3,450 from the quick sale value (QSV) of an automobile that is used by a taxpayer for work, the production of income, or the welfare of a taxpayer's family. For taxpayer's with joint tax liabilities, this value reduction is for two cars—\$3,450 for each primary automobile driven by a taxpayer (one vehicle limitation for each taxpayer).

Let's run through an example of how to value an automobile in an OIC and incorporate the IRM exclusions into Form 433-A.

**Example:** Your client owns a 2006 Toyota Camry with 106,000 miles, purchased new in 2006 in very good condition. The Kelly Blue Book private party value is \$6,500, and there is \$1,300 owed on the original loan from the purchase of the car. The monthly payment on the car is \$235/month.

**Result:** In an offer in compromise, the IRS wants the net realizable equity in an asset, and for a car, that's usually less than the actual value. Here's how we value the Camry to arrive at net realizable equity on Form 433-A, Line 18a, Personal Vehicles:

- **First step: Fair market value.** Go to KBB.com for the Kelly Blue Book private sale value of the vehicle. In our example, that is \$6,500, which we consider to be the fair market value. Now let's start taking our value exclusions to get to net realizable equity.
- **Second step: Reduce to quick sale value.** The IRS allows us to reduce the FMV of most assets, including cars, to the QSV. See IRM 5.8.5.4.1. To the IRS, QSV represents the price a seller could get for an asset if it had to be sold quickly under financial pressure. The standard IRS reduction for QSV is 20 percent, although a greater percent can be used if a reason is demonstrated as to limited marketability of the asset. In our example, the Camry is readily marketable, so using the \$6,500 as the FMV, a 20 percent reduction gives us a value of \$5,200.
- **Third step: Claim \$3,450 exclusion.** Claim the IRM 5.8.5.12 blanket allowance for the \$3,450 exclusion against the



# FORM 433-A

PROTECTING ASSETS IN AN OFFER IN COMPROMISE

value of the car. This further reduces the value to the Camry in an OIC to \$1,750 (\$5,200 QSV less \$3,450).

- Fourth step: Subtract loan balances.** Subtract the balance that remains due from the purchase of the Camry. The remaining balance on the loan is \$1,300, resulting in a net realizable equity for purposes of an OIC of \$450 (\$1,750 less \$1,300). (Yes, we have just used the Internal Revenue Manual to reduce the compromise value of the Camry from \$6,500 to \$450, net realizable equity.)
- Fifth step: Completing Form 433-A, Line 18a, Personal Vehicles.** Complete Form 433-A for the Camry, showing the net realizable equity at \$450. It is good practice to show the IRS your calculations and citations, either by attaching a form to the 433-A or on the form itself, space permitting, as shown in Table 1.

After reductions to quick sale value, taking the \$3,450 exclusion permitted in the IRM, and subtracting the loan balance, the net realizable equity of the \$6,500 Toyota Camry is \$450. The offer will consider the Camry to be an asset worth \$450, the net realizable equity.

### Bank Account Balances

The cash balances in our clients' personal bank accounts are an asset for purposes of

valuing the compromise—it is money on hand, a valuable asset, no different from equity in a house or vehicle.

But don't offer the IRS the full value of the balances in a taxpayer's bank account in a compromise. Be sure to claim the value exclusion for bank account balances found in IRM 5.8.5.7. The bank account exclusions apply to savings accounts and checking accounts.

For savings accounts, IRM 5.8.5.7 provides an exclusion of \$1,000 from the cash balance in the account. The IRS will usually require the last three months' bank statements for review. If the account has minimal withdrawal activity, use the balance on the most recent statement on Form 433-A, less the \$1,000 exclusion.

For checking accounts, a taxpayer is entitled to exclude one month's allowable living expenses from the value of a compromise. If there are no savings accounts, the IRM allows the \$1,000 savings exclusion to be added to the amount excludable from a checking account. In other words, the IRS will allow your client \$1,000 plus enough money to pay one month's allowable living expenses, and will not include those funds as a cash asset in the value of the offer. These exclusions apply only to individual bank accounts, not business accounts.

The IRS will usually require a minimum of three months' checking account statements, and will usually use the average daily balance in the account over that time as the value of a checking account.

For purposes of the checking account value exclusion, the IRS defines "one month's allowable living expenses" as those expenses that are within the IRS allowable expense standards. The intent of the allowable expense standards is to limit a taxpayer's expenses—and increase his cash flow—to amounts the IRS publishes as reasonable. Common expenses that are limited by the IRS include housing and utilities, auto payments, as well as food, clothing, and entertainment.

Here's an example of how to use the IRS bank account exclusions on Form 433-A for an offer in compromise:

**Example:** Your client does not have a savings account, but does have a checking account that is used for everyday bill paying. The average balance in the account over the last three months is \$7,000. Living expenses total \$4,500, all of which fall within the IRS schedules of standard allowable expenses.

**Result:** Even though the account has \$7,000 in it, on Form 433-A, Line 13a, Bank Accounts, the net realizable equity for purposes of the compromise would be shown as \$1,500. The calculation is as follows: \$7,000 (average balance), less \$4,500 (allowable living expenses for one month), less \$1,000 (IRS exclusion) = \$1,500. Show your work and how you arrived at the net realizable equity for purposes of the account balances on Form 433-A or on an attachment, as shown in Table 2.

**Table 1. Calculating Net Realizable Equity for Automobiles**

Year	Make/Model	Purchase Date	Fair Market Value	Loan Balance	Payment	Equity
2006	Toyota Camry 106,000 miles	June, 2010	\$6,500	\$1,300	\$235	\$450

**Equity calculation:** FMV is \$6,500. QSV is \$5,200 (20% reduction), less \$3,450 exclusion per IRM 5.8.5.12, less \$1,300 financing encumbrance = \$450 net realizable equity.



**Table 2. Calculating Net Realizable Equity for Bank Accounts**

Type of Account	Name of Bank	Account Number	Account Balance
Checking	Wells Fargo	xxxx0134	\$1,500

**Equity calculation:** \$7,000 (average balance), less \$4,500 (allowable living expenses for one month per IRM 5.8.5.7), less \$1,000 (IRS exclusion) = \$1,500 FMV.

Don't overvalue a compromise by offering actual bank account balances; it can be challenging to go down from an offer that is too high. Apply the exclusions in IRM 5.8.5.7 to get the best settlement value for your clients.

### Business Equipment

If your client is self-employed and has large business equipment, carefully review IRM 5.8.5.15, "Income-Producing Assets," before completing Form 433-A and submitting an offer in compromise. Here's why: The IRS has a general policy against simultaneously including both the net realizable equity in business equipment and the revenue that the equipment generates into the value of an OIC. Subject to the discretion of the offer investigator, IRS policy is to include *either* the equity in the equipment or the revenue the equipment generates into the offer valuation, but not both.

The determination of whether equipment can be excluded from the value of a compromise is based on whether the asset is critical to business operations.

If the equipment is critical to operations, IRM 5.8.5.15 *excludes* the equity in the asset from the compromise valuation but *includes* the revenue the equipment generates in the business' cash flow to calculate ability to pay. (See IRS Internal Guidance Memorandum for Offer in Compromise from Scott Reisher,

director, IRS Collection Policy, Dated May 21, 2012, Control SBSE-05-0512-041.)

The IRS has expressed a desire to work with taxpayers to maintain business operations, particularly in a lumbering economy, and not force liquidation of assets that would affect business operations to fund a compromise.

What makes an asset critical to business operations? Although this is a facts-and-circumstances test, IRM 5.8.5.15 provides the following situational example to guide us:

*A business depends on a machine to manufacture parts and cannot operate without this machine. The equity is \$100,000. The machine produces net income of \$5,000 monthly (\$60,000/year). The reasonable collection potential (RCP) should include the income produced by the machine, but not the equity. Equity in this machine will generally not be included in the RCP because the machine is needed to produce the income, and is essential to the ability of the business to continue to operate.*

In this example, the IRS would consider excluding the equity in the machine from the valuation of the compromise, as it was demonstrated that the machine is critical to business operations. The IRS does not want to upset the business' ongoing operations, so it will factor the positive cash flow the equipment generates into the monthly ability to pay

valuation, but will not add the value of the asset itself to the compromise.

Conversely, if the business did not need the machine, or the product it produced resulted in very minimal revenue (i.e., \$500/month), the IRS would include the value of the equipment in the compromise, but would not include the small income it generated into a cash flow analysis of ability to pay. The IRS is essentially agreeing to take the value of the asset or the cash flow it generates, but not both.

The IRC provides additional methods to exclude smaller equipment and tools of a business from the value of an offer in compromise. IRC Sec. 6334(a)(3) exempts from levy the books and tools of trade, profession, or business up to \$4,470 in value. If the IRS cannot seize and collect from property, then the equity in that property (i.e., business tools) is not included in the valuation of an offer in compromise. (See also IRM 5.8.5.16, "Inventory, Machinery, Equipment, and Tools of the Trade," which recognizes the use and application of the statutory exemption of IRC 6334(a)(3) to exclude the value of small business equipment and tools in an offer in compromise.)

Here's an example of how to use IRC 6334(a)(3) in an offer in compromise:

**Example:** Your client is a self-employed contractor who has tools of the profession—ladders, hand tools, small equipment, a computer, etc.—that is valued at \$5,700.

**Result:** Even though the small tools and equipment are worth \$5,700, on Form 433-A, Line 66a, Business Assets, the net realizable equity for purposes of the compromise would be shown as \$90. The calculation is as follows: FMV is \$5,700. QSV is \$4,560 (20 percent reduction), less \$4,470 exclusion per IRC 6334(a)(3) and IRM 5.8.5.16 = \$90 net realizable equity. Show your work and how

# FORM 433-A

PROTECTING ASSETS IN AN OFFER IN COMPROMISE

you arrived at the net realizable equity on the Form 433-A or on an attachment, as follows:

- **First step: Fair market value.** Based on the age and condition of the equipment and what the cost would be if purchased new, you accept your client's appraisal of \$5,700 as the depreciated value. The IRS wants net realizable equity in the compromise, which we are about to see will be less than the actual value.
- **Second step: Reduce to quick sale value.** To arrive at net realizable equity, the IRS will allow a 20 percent reduction from the FMV to account for a theoretical quick sale of the property. The 20 percent reduction yields a QSV of \$4,560.
- **Third step: Claim \$4,470 exclusion.** Claim the \$4,470 exclusion permitted in IRC Sec. 6334(a)(3) and IRM 5.8.5.16 against the quick sale value of the tools and equipment. This further reduces the value of the property in the OIC to \$90 (\$4,560 less \$4,470).
- **Fourth step: Completing Form 433-A, Line 66a, Business Assets.** Complete Form 433-A for your values, showing the net realizable equity at \$90. As always, it is good practice to show the IRS your calculations, either by attaching a form to the 433-A or on the form itself, space permitting, as shown in Table 3.

## Household Goods and Personal Belongings

Contrary to popular belief, the IRS cannot levy every single item of our clients' personal property and leave them without basic essentials. Sec. 6334(a)(2) of the Internal Revenue Code lists specific types of property that are protected from seizure, including clothing and necessary household furniture and belongings.

In other words, the IRS is not taking our clients' clothing, televisions, beds, dressers,

tables, or Christmas ornaments. Currently, IRC Sec. 6334(a)(2) protects \$8,940 in value of household goods and personal effects per taxpayer. These restrictions on IRS' power to seize should be remembered and utilized when it is OIC time. Good practice requires a claim on Form 433-A to exclude up to \$8,940 in household goods and personal effects.

As to clothing, Sec. 6334(a)(1) of the Internal Revenue Code allows our clients to keep all their necessary clothing. Bear in mind that the tax code uses the word "necessary" in describing the clothing that is exempt from IRS collections, meaning that the IRS can technically take clothing that is not necessary. It is likely the IRS' opinion that furs, for example, are not protected from seizure.

IRM 5.8.5.11 incorporates IRC Sec. 6334(a)(2) into IRS policy, and specifically instructs offer investigators to apply the statutory exemptions from seizure for furniture,

personal effects, and clothing as value exclusions in an offer in compromise.

In valuing clothing, household goods, and personal effects, garage sale valuations control as the equivalent of fair market value—in other words, what is the charitable donation value of the property?

**Example:** Your client has a three bedroom house, with a living room, family room, and kitchen. All items in the house are more than ten years old and have no antique value. A good faith estimate on the value is \$3,500.

**Result:** Household goods are reported on Form 433-A, Line 19a, Personal Assets, and have no added value to the compromise as they are fully excluded pursuant to IRC Sec. 6334(a)(2) and IRM 5.8.5.11, as shown in Table 4.

**Example #2:** Household goods are valued at \$12,000 for a single taxpayer.

**Result:** As the \$12,000 value is over the excluded amount of \$8,940, the equity for purposes of the compromise would be \$3,060,

**Table 3. Calculating Net Realizable Equity for Smaller Business Equipment**

Description	Purchase Date	Fair Market Value	Loan Balance	Payment	Equity
Hand tools, small equipment	Various	\$5,700	N/A	N/A	\$90
<b>Equity calculation:</b> FMV is \$5,700. QSV is \$4,560 (20% reduction), less \$4,470 exclusion per IRC Sec. 6334(a)(3) and IRM 5.8.5.16 = \$90 net realizable equity.					

**Table 4. Calculating Net Realizable Equity for Household Goods, Example #1**

Description	Purchase Date	Fair Market Value	Loan Balance	Payment	Equity
Household goods	Various	\$3,500	N/A	N/A	Excluded
<b>Location:</b> 21 Holiday Rd, Warren, Ohio. All household goods and personal effects claimed as excluded under IRC Sec. 6334 and IRM 5.8.5.11.					





calculated as follows: \$12,000 FM less 20 percent QSV = \$10,000 less \$8,940 exemption = \$3,060 net realizable equity. Note the claim on Form 433-A, Line Item 19a, Personal Assets, and how you calculated the equity, as shown in Table 5.

If Example #2 had joint taxpayers, there would be no net realizable equity as each taxpayer would be able to claim an \$8,940 exclusion, which is greater than the value of the property. **EA**

#### ENDNOTE

<sup>1</sup> It is the author's experience that the IRS accepts either the Form 433-A or Form 433 (OIC) as a collection information statement in an OIC. Accordingly, references for purposes of this article are to Form 433-A.

**Table 5. Calculating Net Realizable Equity for Household Goods, Example #2**

Description	Purchase Date	Fair Market Value	Loan Balance	Payment	Equity
Household goods	Various	\$12,000	N/A	N/A	\$3,600

**Location:** 21 Holiday Rd, Warren, Ohio. Household goods and personal effects claimed as excluded under IRC Sec. 6334 and IRM 5.8.5.11 up to \$8,940, resulting equity is \$3,060 (\$12,000 – \$8,940).

#### About the Author:

**Howard S. Levy** is a former trial attorney for the IRS and an instructor at NTPI. He has over 20 years' experience in IRS collection proceedings, Tax Court litigation, IRS administrative appeals and the use of bankruptcy to resolve IRS controversies. Howard is a member of Voorhees & Levy LLC in Cincinnati, Ohio. He can be contacted at howard@voorheeslevy.com or at www.howardlevyirslawyer.com.

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# TAX LAW WRAPUP FOR 2014

By David Mellem, EA

Congress has done very little this year when it comes to tax law changes affecting most taxpayers. In fact, Congress has done very little to interfere with our tax-planning abilities *except* that Congress has not extended many temporary tax provisions. This inaction causes us to tax plan “based on current law.”

We are confident Congress will retroactively extend many of these extender items, and we are also confident Congress will not do so until after the November elections, which means we will again have delays in submitting returns to IRS since it will have to reprogram its software.

### Reminders

**Health Insurance:** Individuals must have health insurance coverage or meet an exemption. This has been discussed in prior issues of the *EA Journal*, so is not discussed here. (See the Nov/Dec 2013 and the Jan/Feb 2014 *EA Journals* for a thorough discussion on Obamacare.) Look for an update on ACA in the Jan/Feb 2015 *EA Journal*.

**Repair Regulations:** There are new repair regulations in effect for tax years beginning on or after January 1, 2014. For an in-depth review of the changes, see the Sept/Oct 2014 *EA Journal* article “Repair Regulation Update.”

Common items that expired include:

- Bonus depreciation: Effective for assets placed in service after December 31, 2013
- Sec. 179: The higher \$500,000 amount and the opportunity to use it for certain real estate improvements and off-the-shelf software no longer exists for assets placed in service in tax years beginning after December 31, 2013. The current limitation is \$25,000, with a phaseout beginning at \$200,000 of purchases.
- The fifteen-year MACRS life for qualified leasehold improvement property, restaurant building improvements, and retail improvements no longer exists for tax years beginning after December 31, 2013. These now fall back into their normal category, which is probably thirty-nine years.
- The seven-year MACRS life for motorsports entertainment facilities no longer exists for tax years beginning after December 31, 2013.

- The accelerated depreciation for business property on an Indian reservation no longer exists for tax years beginning after December 31, 2013.
- The sales tax deduction in lieu of the state and local income tax deductions is no longer available effective for tax years beginning after December 31, 2013.
- The mortgage insurance premium deduction is no longer available effective for tax years beginning after December 31, 2013.
- The exclusion from debt discharge income for qualified home mortgage indebtedness
- Tuition deduction
- Educator expense deduction
- Energy credit for energy-efficient home improvements (insulation, storm windows, etc.)
- Energy efficient home builder credit (\$1,000 or \$2,000)
- Employer wage credit for activated reservists
- Indian employment tax credit
- Railroad truck maintenance credit
- Mine rescue team training credit
- New markets tax credit
- Research credit
- Work Opportunity Credit for new hires
- S corporation recognition period for built-in gains of five years (instead of the normal ten years)
- Limited basis adjustments to a shareholder's stock for S corporations making charitable contributions of property
- The provision permitting tax-free distributions from IRAs directly to charities for taxpayers age 70½ or older

### What Else Is New?

#### Form 1023-EZ Streamlined Application Is Now Live

IRS previously announced it was developing a streamlined application process for organizations applying for Sec. 501(c)(3) status. Now the forms, instructions, and Revenue Procedure 2014-40 are available, and the application process is live.

The new Form 1023-EZ (Streamlined Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code) is three pages instead of the much longer Form 1023. This streamlined

application is generally available to U.S. organizations with assets of \$250,000 or less and annual gross receipts of \$50,000 or less. It can only be filed electronically by creating an account at [www.pay.gov](http://www.pay.gov) and then entering the term “Form 1023-EZ” in the search box. Before completing the application online, you will need to determine if the organization qualifies to use the streamlined form by using the worksheet in the Form 1023-EZ instructions. If the organization is eligible, you can then begin the application process.

The user fee required to be paid with the application is \$400. (Form 1023 filing fees are \$400 if not more than \$10,000 in annual receipts, and it is \$850 for those over \$10,000.)

There are some organizations that are not eligible to use the Form 1023-EZ and must use the normal Form 1023. There is a worksheet in the Form 1023-EZ instructions that should be used to determine if the organization is eligible to use Form 1023-EZ.

### Unused ITINs Will

#### Expire After Five Years of Nonuse

In News Release 2014-76, IRS announced an individual taxpayer identification number (ITIN) will expire if it is not used on a federal income tax return for five consecutive years. To give everyone time to adjust to this change and to give IRS time to reprogram its systems, IRS will not begin deactivating ITINs until 2016.

Back in November 2012, IRS announced ITINs issued after January 1, 2013, would automatically expire after five years, even if used properly and regularly by taxpayers. This would have required these taxpayers to reapply starting in 2018.

This older policy from November 2012 has been replaced by the new policy announced in News Release 2014-76, and is effective for all ITINs.

Here's to a happy, successful, stress-free tax season. **EA**

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### About the Author:

**David Mellem, EA**, is an enrolled agent who has been practicing for more than twenty years. He and his wife Mary own Ashwaubenon Tax Professionals in Green Bay, Wisconsin. David also consults and teaches for other tax professionals throughout the country.

To learn more about this topic, visit the *NAEA Forums*.





BY ALAN PINCK, EA & ANN E. KUMMER, EA, CPA

### Introduction

If your practice includes audit representation, you may encounter a situation in which you are representing a client with a cash-intensive business. If you prepare returns for business clients, you should know this process as well. You will find these are quite unlike typical audits; the auditors are generally much more prepared and organized than in other audits. You will detect the inherent assumption by the auditor (and, by extension, IRS) that the taxpayer did not report all income. Consequently, the auditor approaches the examination with that belief. The auditor's goal, therefore, is to substantiate it.

This is an area the IRS believed its auditors needed guidance in, so they developed the *Audit Technique Guide (ATG)*<sup>1</sup> for it. In the event you are engaged in a case involving such a business, be sure to read this guide, as it will help you understand why the auditor is asking for information not typically requested in other types of examinations.

### The Process

The key to effectively representing your clients is to know as much about them and their business as you can. Anticipate problem areas with some legwork ahead of the exam appointment.

- **Prepare a cash T-analysis (described in the ATG).** Be sure that the auditor will

already have prepared the analysis using national industry standards. By having the actual numbers, you can determine whether you have an issue and how large it may be. Having previously discussed those issues with your client will help you refute or explain discrepancies during your interactions with the auditor.

- **Observe and absorb the business operations.** Spend time in the business, watching the day-to-day transactions and interactions, as well as understanding all that is involved. You should be able to concisely explain what services are provided or products manufactured and be able to knowledgeably describe all business functions, especially the financial areas.
- **Consider having the taxpayer present at the interview.** As a rule, I do not have the client present during the interview process, but, in this type of audit, it *may* be beneficial. Having the client present may help expedite the interview process as he or she will be able to best explain the internal controls of the operation. As much as we interview our clients to prepare for the audit, we cannot always think of every question the auditor may ask. If you decide to do this, schedule the business walk-through at the same time as the interview to limit the client's exposure to the auditor.

Be sure to prepare your client well so that he or she understands the process and the extensive questioning that will occur. People have a habit of providing too much information and not keeping their answers on point, so beware. Not every client is a good candidate for this option, so contemplate this choice carefully.

- **Do your homework.** As previously mentioned, the auditor will have done his. Know *all* the client's assets, both business and personal. Learn about the client's prior business history, both in the current industry and in other dissimilar businesses. These can be indicators that the client may be hiding something. For example, if the client was successful in a manufacturing business and is losing money or breaking even in a liquor store business, there will be an assumption that not all income is reported. A good business person will tend to be successful in other ventures. All industries have average costs, and the auditor will be familiar with those for the business in question. If your client is not in line with industry averages, be prepared to explain why.<sup>2</sup>

### Evaluation Methods

The auditor will be scrutinizing everything for signs that your client has underreported

income. One such mark is a lack of proper internal controls. The more levels involved, then presumably, the more control there is, thus decreasing the opportunity to underreport income and circumvent the system. The auditor will examine how many people (and who) have access to the cash register, who counts the cash at the end of the day, who makes the deposits, who books the receipts to the ledger, how overages and shortages are accounted for, and the list goes on.

Another method of evaluation the auditor will employ is to compare purchases with sales. Do not be surprised to learn the auditor has summonsed a supplier for all invoices to perform a comparison between supplier records and taxpayer ledgers. The auditor will use a percentage markup approach to be sure the income is reported correctly. For example, if the audit involves a laundromat, the auditor will compare the number of gallons of water used per wash to the number of gallons of water used in a water billing cycle. For a bar or tavern, the auditor will evaluate the number of bottles purchased, the number of shots per bottle, and the average cost of drinks.

The auditor will prepare a bank deposit analysis (BDA), and any overages and shortages will need a detailed explanation. Shortages in a cash business will trigger more questions, since they may indicate that not all income was deposited. If so, it will fortify the auditor's suspicion that not all income was accurately reported. If there is a reasonable explanation for the shortages, be sure to have as much supporting documentation to illustrate it was reported.

Conversely, you will need explanations and support to explain any overages in the BDA. If your client obtained loans, all the documentation should be available for the auditor. If the loans were from private parties or family members, they *will* be subject to higher scrutiny. If you are not in the habit of preparing your own BDA for this type of audit, you should incorporate this practice into future cash-intensive business examination engagements in order to have answers to these questions, because they will be asked. The ATG mentioned earlier goes into great detail with regard to loans sourced from offshore family members. Auditors are interested in the original currency, the conversion rate used, and, of course, observing that the proper FinCEN declarations were made.

## Other Businesses

While your client's business history is meaningful, so is her concurrent business activities. The auditor will also investigate whether your client currently operates any other businesses. There is a theory that taxpayers in cash businesses tend to favor other cash businesses. The client may not believe he or she has another business as it is "casual." For example, the client with the convenience store may also buy and resell used cars, or perhaps she likes to purchase items at garage sales and then resell them at the local flea market. As these are often handled solely in cash, the client may perceive these transactions as unreportable and not as the additional business ventures they truly are. How about that hobby that generates a little income? In a typical audit of your average tax client, you would not think to look into this as deeply, but the ATG reminds the auditor to explore these areas. You should, too.

When we think of a cash-intensive business, we do not always take into consideration the underground economy. I am not necessarily referring to illegal activities but to the "temporary laborer" or local handyman. You may observe this in your practice, perhaps with a client who may not appear to make much money in his job but has managed to accumulate assets. Possibly you will see this when representing a client with what appears to be only moderate W-2 income, yet she owns three rental properties. These observations should trigger a conversation between you and your client; rest assured the auditor will likely stumble upon this and open up a whole other issue. As practitioners, we need to work with our eyes wide open so that we can foresee what may be coming next.

## Things to Consider

In the event that the audit does not go well and you intend to go further to Appeals, be sure to do an FOIA request. The FOIA request will yield you both the work papers and the auditor's notes, among other documents and support. The information provided in response to the FOIA request could be invaluable at deciding whether to proceed to Appeals and while in Appeals, as you will know on what basis the auditor made his decisions.

## Form 8300

Although in most cash-intensive businesses there would not be many sales that would warrant the filing of Form 8300 (Report of Cash



Payments Over \$10,000 Received in a Trade or Business) for cash transactions of \$10,000 or more, we need to be mindful of the requirement. This will be something the auditor will be looking for if your client is in a business that deals in high-dollar cash transactions.

## Conclusion

When taking on this type of engagement, you must be prepared to be patient and to let it take its course. These are not simple cases, and they take a considerable amount of time and organization. Be upfront with the client and make him or her aware that the auditor is going to start with the assumption of unreported income which he'll be searching to identify. No stone will be left unturned. Be sure to stay on top of every request and provide it in a timely manner; any delay will be thought of as a lack of records.

Most importantly, understand your client's business so that you can prevent the necessity of a meeting between the auditor and the taxpayer. These are challenging cases to work on, but they can also be very gratifying and enlightening when you successfully represent a client with a cash-intensive business under IRS scrutiny. **EA**

## About the Authors:

**Alan Pinck, EA**, has more than 25 years of tax preparation experience in the San Francisco Bay Area. He has built a practice specializing in individual, small business tax preparation, and audit representation.

**Ann E. Kummer, EA, CPA**, is the tax manager at Kirshon & Company, P.C. in Poughkeepsie, New York. She has nearly two decades of experience in tax preparation and representation.

To learn more about this topic, visit the NAEA Forum

## ENDNOTES

<sup>1</sup> Find the guide at [www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Cash-Intensive-Businesses-Audit-Techniques-Guide-Table-of-Contents](http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Cash-Intensive-Businesses-Audit-Techniques-Guide-Table-of-Contents).

<sup>2</sup> The following are sources for you to use when researching industry standards: [www.bizstats.com](http://www.bizstats.com), Dunn & Bradstreet, Robert Morris & Associates periodicals, and Bureau of Labor Statistics ([www.bls.gov](http://www.bls.gov)).





# PREVENTING THE PIERCING

# OF THE CORPORATE VEIL

BY JEFF KEENAN



**It can be a challenge for tax professionals to convey to their clients the importance of adhering to corporate formalities, especially for single-owner corporations. It is not uncommon for an individual to form a corporation or LLC without sufficient tax and legal advice and without any understanding of what they created or how it works. Lack of understanding and adherence to corporate formalities can produce compliance headaches, as well as undermining the reason for incorporating in the first place.**

### **Corporate Characteristics**

A corporation is often described as an “artificial person.” A corporation has independent legal status, can own property, can conduct business, pay taxes, and can sue or be sued. Ownership of a corporation is represented by shares of stock owned by shareholders, and ownership can be transferred by sale of stock. Corporations are formed under state laws and fall under special rules under the Internal Revenue Code for federal tax purposes.

### **Limited Liability**

Historically, one of the primary reasons for the existence of corporations is to encourage innovation and commerce by allowing individuals to pool their resources to operate a business while being protected from extended liability. If a corporation is set up and operated properly, the shareholder’s risk of loss is limited to the amount invested in stock and amounts loaned to the corporation. For example, if a corporation becomes liable for monetary damages, theoretically, the liability does not extend to shareholders, even if the damages exceed the value of the corporation. If the corporation becomes defunct, the shareholder is not liable for additional damages in excess of the amount invested. However, especially in small corporations, shareholders often do not understand and adhere to the necessary corporate formalities, and they put themselves at risk for “piercing the corporate veil” in the event of a lawsuit.

### **Exceptions to Limited Liability**

Personal liability may exist for a shareholder who:

- personally guarantees a debt for the corporation on which the corporation defaults
- personally injures someone
- commits fraud
- fails to deposit payroll taxes withheld from employees

### **Limited Liability Companies (LLCs)**

The same principles apply to limited liability protection for LLCs, and it can also apply to maintaining the benefits of a partnership structure. These business entities must be operated as separate legal entities to ensure the tax benefits and limited liability aspects of forming a separate business entity.

### **Tax Issues**

Under federal tax rules, corporations generally fall into one of two groups: C corporations and S corporations. Since S corporation status is an election made at the federal level, legal liability under state law is generally the same whether the entity is a C corporation or an S corporation.

### **C corporations**

A C corporation computes taxable income and pays tax in a similar manner to an individual. After-tax corporate earnings, known as earnings and profits (E&P), are distributed to shareholders in the form of dividends, which are taxable to the shareholders. A C corporation’s ability to retain corporate earnings is limited to the amount needed for bona fide business reasons. A C corporation is subject to an accumulated earnings tax for retaining earnings beyond the business needs of the entity. Generally, accumulated earnings up to \$250,000 are considered to be within the reasonable needs of a corporation without a specified reason for the need to accumulate a higher amount.

One benefit of a C corporation treated as a separate tax-paying entity is the ability for shareholders to benefit from tax-preferred fringe benefits. These tax incentives are not available to partners or shareholders who own more than 2 percent of an S corporation. Failure to adhere to corporate formalities can cause taxation of benefits that would otherwise be tax-free.

## S corporations

Although an S corporation may be subject to payroll taxes or other taxes in the form of fines or penalties, an S corporation is not subject to federal income tax. Instead, earnings from an S corporation flow through directly to shareholders on Schedule K-1, Form 1120S. State laws vary on taxation of S corporations. An S corporation can provide tax benefits for shareholders, including avoidance of double taxation that exists with a C corporation and reduced FICA tax on earnings as compared to a general partner. Adhering to corporate formalities, including strict rules on distributions to shareholders, is necessary to ensure the S corporation status is maintained.

## The Corporate Mentality

Taxpayers must think and behave differently when acting in the capacity of a shareholder. Failure to comply with even the simplest of corporate formalities can jeopardize the tax benefits and liability protection sought by the shareholder.

## Capitalization

A corporation must be funded by contributions to capital. A corporation that does not have sufficient operating capital can be subject to having the corporation ignored by the courts and the IRS. In cases where a taxpayer does not properly separate the finances between personal funds and funds belonging to the corporation, capitalization issues can arise.

## Corporate Name

The corporate name or properly registered DBA should be used on invoices, receipts, checks, company documents, business cards, advertising, etc., so that third parties know they are dealing with a corporation. Contractual agreements should be made in the corporation's name, rather than in the name of an officer or shareholder. All too often, a new corporation continues to use the preceding sole proprietorship's name, checks, and invoices as though incorporation had not occurred.

## Asset Ownership

All corporate assets should be held in the

name of the corporation, including bank accounts, equipment, real estate, insurance policies, etc. Assets that are transferred to the company (such as equipment acquired before incorporation) should be retitled. The corporation's commercial insurance policy can include a "non-owned automobile" rider to provide liability protection in the event that an employee or contractor has an accident in a personally-owned car while conducting company business.

## Separate Legal Entity

A corporation shareholder must understand the concept of having created a separate legal entity. Sometimes referred to as "creating a next-door neighbor," the shareholder must understand the fiduciary concept of issues, such as acting as a payroll administrator who issues a paycheck to himself or herself, then accepting and cashing the paycheck as the shareholder.

The concept of corporate formalities can seem silly to the single shareholder of a corporation, especially the need to have board meetings, but it is necessary to maintain the integrity of the corporation and benefits the corporation can provide. Failure to do so can create a mess and can make the taxpayer vulnerable to recharacterization by the IRS and the courts.

## Piercing the Corporate Veil

In the event of litigation for damages, plaintiff attorneys are likely to attempt to pierce the corporate veil in situations involving small corporations. If the court agrees to pierce the corporate veil, the liability protection offered by the corporation vanishes, and the shareholder(s) is held personally liable for damages. Note that piercing the corporate veil is not a danger for publicly traded corporations because of the large number of shareholders and the adherence to corporate formalities. Lack of adherence to corporate formalities is a primary reason why courts pierce the corporate veil.

## Court Actions

Courts have had a long-standing tradition of adhering to a strong set of principles when considering piercing the corporate veil. The New Jersey

Supreme Court, for example, has explained:

*"The purpose of the doctrine of piercing the corporate veil is to prevent an independent corporation from being used to defeat the ends of justice, to prevent fraud, to accomplish a crime, or to otherwise evade the law."*  
(Rospond, T.C. Summary 2012-47)

## Intermingling Funds

A common problem with single-owner and other small corporations is intermingling of funds. This occurs when a corporate shareholder uses his or her personal checking account for corporate deposits or payment of corporate expenses.

Separation of funds can be a key in preserving the liability protection of the corporate veil. Courts can pierce the corporate veil by finding that the corporation is an "alter ego" of the shareholder, essentially stating that the corporation is not separate and distinct from the individual as evidenced by the intermingling of finances.

On the other hand, a shareholder who deposits personal funds or pays personal expenses from the corporate checking account is intermingling funds. For the same reasons as the reverse, courts can cite this as evidence that the corporation is not a separate and distinct entity from the individual.

## Tax Problems Caused by Intermingling Funds

Unintended tax consequences can occur when personal and corporate funds are intermingled. When a shareholder provides funds to or on behalf of a corporation, there are different types of tax treatment that may apply, depending on the circumstances. For example, when a shareholder provides funds to a corporation, it can be classified as one of the transactions below:

- capital contribution
- loan to the corporation
- repayment of a loan from the corporation
- expense reimbursement
- purchase

When a shareholder purchases an item for the corporation from his or her personal

funds, that shareholder is considered to have provided funds, or made a contribution, to the corporation. Classification is determined by how the transaction is structured and the circumstances surrounding the transaction. Providing funds to corporations without careful planning can cause unintended tax consequences.

On the other hand, if an individual takes funds from a corporation checking account, the transaction can be classified as the following:

- taxable dividend
- nontaxable distribution
- nontaxable expense reimbursement
- wages
- loan to the shareholder
- repayment of a loan from the shareholder

Failure to carefully structure transactions when taking disbursements from a corporation can result in otherwise nontaxable transactions becoming taxable, in addition to opening the corporation up for a court to pierce the corporate veil.

#### Court Case

A taxpayer operated a tax preparation business as a sole proprietor. The taxpayer later incorporated but continued to have clients make checks out to him personally, and treated funds received from the business as his own. No evidence of any employment agreement existed between the taxpayer and his corporation. The court ruled that the taxpayer operated his business as a sole proprietor and the income earned should be treated as earned not by the corporation but by the individual and be subject to self-employment tax. (*Reginald Jarrett, et al*, T.C. Summary 2008-94)

#### Personal Use of Corporate Assets

A similar situation with intermingling funds occurs when personal assets are used by the corporation and vice versa. If corporate assets are used for personal purposes, the IRS can reclassify expenses reported on the corporation tax return as expenses attributable to the shareholder, rather than the corporation. On the other hand, if a corporation uses personal assets owned by the shareholder, this could

indicate a lack of separation between the shareholder and corporation, opening up the possibility of having the corporate veil pierced.

#### Court Case

The taxpayer was engaged in several business activities, including real estate, entertainment services, and interior design. She incorporated her business in New York under the name Real Services, Inc. The taxpayer's books were not well-kept, and she frequently used the corporation checking account to intermingle funds. Business deposits were made into the account, but checks were written for items such as birthday presents for family members, tuition costs for the daughter of a friend, and contact lenses for her friend. The taxpayer was audited by the IRS, and taxes were assessed on unreported income.

The taxpayer argued she was not individually liable for the taxes. Instead, her corporation, Real Services, Inc., should be liable because the corporation received the funds in question. The court decision determined the corporation was a sham and stated the corporation had the characteristics of an alter ego, including:

*“The intermingling of corporate and personal funds, undercapitalization of the corporation, failure to observe corporate formalities, such as the maintenance of separate books and records, failure to pay dividends, insolvency at the time of a transaction, siphoning off funds by the dominant shareholder, and in the inactivity of other officers and directors.”*  
(*Zabetti Pappas*, T.C. Memo 2002-127)

#### Reasonable Compensation

Reasonable compensation in the form of wages is required of corporate shareholders who perform services for the corporation. Factors involved in determining reasonable compensation are different for C corporations as compared with S corporations.

#### Reasonable Compensation for a C Corporation

Wages are deductible by a corporation in computing taxable income, but dividends are

“

PROVIDING FUNDS  
TO CORPORATIONS  
WITHOUT CAREFUL  
PLANNING  
CAN CAUSE  
UNINTENDED TAX  
CONSEQUENCES.

”

not. In a small corporation, the owners might decide to take dividends in the form of salary in order to avoid the corporate income tax.

The Internal Revenue Code allows a business to deduct from its taxable income a reasonable allowance for salaries or other compensation for personal services actually rendered. If a corporation pays an employee who is also a shareholder a salary that is unreasonably high considering the services actually performed, the IRS may deem the excessive part of the salary to be a constructive distribution to the shareholder-employee.

Reasonableness is determined based on the facts and circumstances that exist when the services are contracted. In determining reasonable compensation, courts rely heavily on the amount that an unrelated party



“

**THE IRS CAN RECLASSIFY A LOAN AS A TAXABLE DIVIDEND IF IT DETERMINES THAT THE LOAN IS ACTUALLY A DISTRIBUTION OF PROFITS OR DOES NOT HAVE THE CHARACTERISTICS OF AN ARMS-LENGTH TRANSACTION.**

”

would be paid for similar work at a similar company. Factors considered are:

- duties performed by the employee
- volume of business handled
- character and amount of responsibility
- complexities of the business
- amount of time required
- cost of living in the locality
- ability and achievements of the employee performing the service
- pay compared to the gross and net income of the business and distributions to shareholders
- policy regarding pay for all employees
- history of pay for each employee

A common scenario for the reclassification of salary as dividends is of a small corporation with shareholders who all draw salary but do not all perform services for the company.

The form or method of figuring the pay does not affect its deductibility. Bonuses and commissions based on sales or earnings, and paid under an agreement made before the services were performed, are both deductible.

#### **Reasonable Compensation for an S Corporation**

Many S corporations are set up for the primary purpose of avoiding self-employment tax and payroll taxes on wages for shareholders. The structural process is straightforward. Instead of taking profits as wages, the person can form an S corporation and take income as S corporation earnings not subject to payroll tax. Considering that a sole proprietor with \$90,000 or more in net profit will pay over \$11,000 in Social Security tax, the incentive to convert the earnings away from FICA is clear. However, this approach does not comply with tax law, and the IRS continues to crack down on such “tax planning” techniques.

#### **Court Case**

The taxpayer and his wife each owned separate S corporations under which they ran a tax preparation business and realty business, respectively. Each taxpayer assigned payments received for their services to their respective corporations. Neither corporation paid either taxpayer wages for their services. Since there was

not an employer-employee relationship, nor any contract between the corporation and the taxpayer giving the corporation the right to instruct or control the taxpayer’s actions, the court upheld the IRS’ position that the S corporations themselves did not earn the income. Rather, the taxpayers personally earned the income outside the corporation and, thus, were subject to self-employment tax. (*Arnold*, T.C. Memo 2007-168)

#### **Loans**

A shareholder can receive a loan from a corporation. However, the loan must be bona fide. The IRS can reclassify a loan as a taxable dividend if it determines that the loan is actually a distribution of profits or does not have the characteristics of an arms-length transaction.

A shareholder can also loan money to a corporation and receive interest payments. However, if the loan is not properly structured, the interest payments by the corporation can be recharacterized by the IRS as return of capital, which eliminates the corporation’s deduction for interest.

Factors considered by the IRS in determining whether a loan to a shareholder is bona fide:

- Extent to which the shareholder controls the corporation.
- Whether security was given.
- Is the shareholder in a position to repay the loan?
- Are there adequate earnings and profits?
- Certificate of indebtedness given to the corporation.
- Is there a repayment schedule or an attempt to repay?
- Is there a set maturity date?
- Whether the corporation charges interest.
- Whether the corporation has made systematic efforts to obtain repayment.
- Magnitude of the advances.
- Whether a ceiling exists to limit the amount the corporation can advance.
- Dividend history of the corporation.

#### **Constructive Dividends**

A common IRS adjustment for C corporations with earnings and profits is reclassifying distributions to shareholders as constructive dividends. If a distribution is made to a shareholder

and reported as nontaxable, and the amount is reclassified as a constructive dividend, it becomes taxable to the shareholder.

The following items are examples of what may be treated as constructive dividends:

- **Below-market loans.** If a corporation gives a shareholder a loan with interest below the applicable federal rate, the interest may be treated as a constructive dividend taxable to the shareholder.
- **Cancellation of shareholder's debt.** If a corporation cancels a shareholder's debt, the amount of debt cancelled is treated the same as a cash distribution to the shareholder.
- **Transfers of property to shareholders for less than FMV.** If the FMV of property on the date of sale or exchange exceeds the price paid by the shareholder, the excess may be treated as a taxable distribution to the shareholder.
- **Unreasonable rents.** If a corporation pays a shareholder higher rent than what the shareholder would charge an unrelated party, the excess rent can be classified as a constructive dividend.
- **Unreasonable compensation.** If shareholder compensation is determined to be unreasonable, the excess amount is reclassified as a constructive dividend and is not deductible by the corporation.

**S Corporations: One-Class-of-Stock Rule**

A corporation that has more than one class of stock does not qualify as an S corporation. A corporation is treated as having only one class of stock if all outstanding shares of stock confer identical rights to distributions and liquidation proceeds. Differences in voting rights are disregarded in determining whether a corporation has more than one class of stock. The determination of whether stock confers identical rights is based on the corporation's governing provisions, which are defined in regulations as the corporate charter, articles of incorporation, bylaws, applicable state law, and binding agreements.

Any time distributions are made to shareholders, each shareholder should receive a distribution in proportion to the percentage of stock owned. Distributions that differ in timing or amount, depending on the facts and circumstances, may be deemed to create a second class of stock and terminate the S corporation status.

**Loans as a Second Class of Stock**

Instruments, obligations, or arrangements, regardless of whether designated as debt, will be treated as a second class of stock if:

- The instrument, obligation, or arrangement constitutes equity or otherwise results in the holder being treated as the owner of stock.

- A principal purpose of issuing or entering into the instrument, obligation, or arrangement is to avoid the rights to distribution or liquidation proceeds conferred by the outstanding shares of stock or to avoid the limitation on eligible shareholders.

**Prevent the Piercing of the Veil**

Almost anything a shareholder of a small corporation does has the potential to pierce the corporate veil and destroy the reasons for creating the corporation in the first place. Using the wrong stationery, taking a loan from the corporation, using personal funds to buy office supplies, or failing to pay reasonable compensation can cause a court to destroy the protection a shareholder seeks. The best prevention of problems is for the taxpayer to understand the formalities that must be followed prior to establishing the corporate entity. **EA**

**About the Author:**

**Jeff Keenan, BSB**, is an author for TheTaxBook™ line of publications, published by Tax Materials, Inc. He is the proprietor of Keenan Tax Service in Minneapolis, Minnesota, providing services as a tax consultant and independent financial representative for individuals and small businesses. E-mail Jeff at [jeff@thetaxbook.com](mailto:jeff@thetaxbook.com).

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2014	-	Uk					-	-	not found
2013	Original	MFJ	10/15/14		No		\$10,657.58	\$12,113.66	7/10/2013
2012	Amended	HOH			No	06/14/13	\$16,975.95	\$18,523.26	7/10/2013
2011	SFR	S	10/15/12	12/21/12	08/23/13	Closed	\$7,668.22	\$7,975.44	7/10/2013

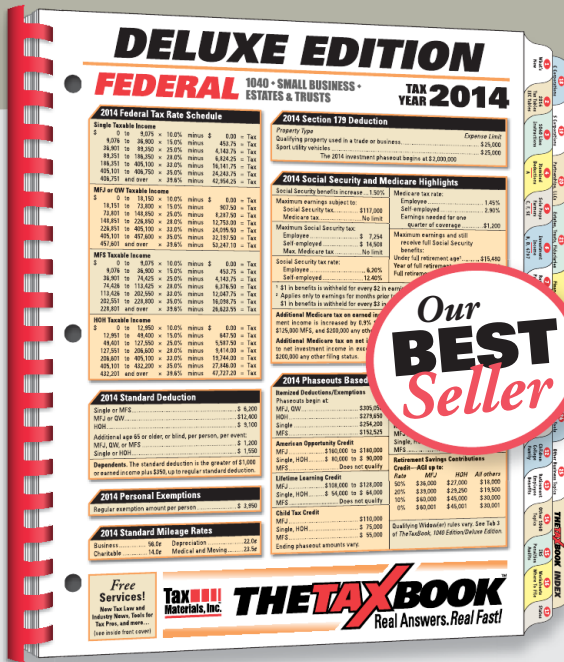
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# Tax Appointment Worksheet

The Tax Appointment Worksheet is a tool to help you gather the needed information for new and returning clients for the 2014 tax year. This year's worksheet has been enhanced to reflect the changes in tax law.

This year will be the first year that you will need to report whether you are covered by health insurance or meet an exception. For those who have received a government subsidy for the purchase

of health insurance, there will be a reconciliation of that subsidy. For those who were eligible to take the subsidy but opted to receive the credit, the credit will be calculated on this year's return.

EVENT		DOCUMENTS OR INFORMATION NEEDED	EVENT		DOCUMENTS OR INFORMATION NEEDED
1	Married, divorced, or separated in 2014	<ul style="list-style-type: none"> <li>• Married – prior year's returns of both spouses</li> <li>• Divorced – finalized date; copy of the divorce decree</li> <li>• Separated – copy of the separate maintenance agreement</li> <li>• Community property income allocation</li> <li>• Alimony paid or received</li> </ul>	9	Social Security benefits	<ul style="list-style-type: none"> <li>• Form 1099-SSA</li> </ul>
			10	Sale of stocks, bonds, etc.	<ul style="list-style-type: none"> <li>• Form 1099-B or other sale documents</li> <li>• Basis or original costs</li> </ul>
2	Birth or adoption	<ul style="list-style-type: none"> <li>• Social Security cards and adoption papers</li> </ul>	11	Purchase of stocks, bonds, etc., personal residence, or other real estate	<ul style="list-style-type: none"> <li>• Purchase documents, closing papers</li> </ul>
	Adoption Credit	<ul style="list-style-type: none"> <li>• Date and amount of expenses, date of adoption, special needs certification</li> </ul>	12	Inheritance	<ul style="list-style-type: none"> <li>• Will, K-1 from the estate</li> <li>• Decedent's basis of property if death occurred in 2010</li> </ul>
3	Death of child or spouse	<ul style="list-style-type: none"> <li>• Date of death</li> </ul>		Gifts made or gifts received	<ul style="list-style-type: none"> <li>• Cash or property in excess of \$14,000 per person</li> <li>• Description of property given, basis, donee name</li> <li>• Property – basis of donor</li> </ul>
4	Additional members of household	<ul style="list-style-type: none"> <li>• Date of occupancy and relationship</li> </ul>	13	Trade any property	<ul style="list-style-type: none"> <li>• Date of trade, property given up and property received, basis and FMV</li> <li>• Qualified intermediary sales agreements or closing papers</li> </ul>
5	Job change	<ul style="list-style-type: none"> <li>• Start date</li> <li>• Name of new employer</li> <li>• W-2s from new and old employers</li> <li>• Job-related moving expenses</li> </ul>	14	Start or end a small business (Schedule C, LLC, S or C Corp, partnership)	<ul style="list-style-type: none"> <li>• Formation or termination dates</li> <li>• Property contributions or distributions</li> <li>• K-1s, if applicable</li> </ul>
6	Unemployment	<ul style="list-style-type: none"> <li>• Unemployment Form 1099-G</li> </ul>		Business income/ expenses	<ul style="list-style-type: none"> <li>• 1099-Ks received for use of credit cards</li> <li>• Inventory numbers, if applicable</li> <li>• Mileage information</li> </ul>
7	Retirement contribution	<ul style="list-style-type: none"> <li>• Type of plan</li> <li>• Amount of contribution</li> </ul>			
8	Retirement distributions	<ul style="list-style-type: none"> <li>• Form 1099-R</li> <li>• Rollovers</li> <li>• RMD information if 70½ or older</li> </ul>			

<b>15</b>	Lawsuit settlements	<ul style="list-style-type: none"> <li>• Date received</li> <li>• Reason for the settlement</li> <li>• 1099-MISC</li> </ul>
<b>16</b>	Rental property	<ul style="list-style-type: none"> <li>• Income</li> <li>• Expenses</li> <li>• New property purchased</li> </ul>
<b>17</b>	Prizes	<ul style="list-style-type: none"> <li>• Form 1099-MISC</li> <li>• Value of prizes not included on Form 1099-MISC</li> </ul>
<b>18</b>	Lottery or gambling winnings	<ul style="list-style-type: none"> <li>• Total amount won whether on W-2G or not</li> <li>• Total amount of losses</li> </ul>
<b>19</b>	Health insurance; medical, dental, or drug expenses	<ul style="list-style-type: none"> <li>• Health insurance premiums</li> <li>• Post-tax payments</li> <li>• Totals of other medical, dental, and drug expenses. If the health insurance is pre-tax (i.e. cafeteria plan, Sec. 125, POP), premiums have already been deducted from wages</li> </ul>
	Medical miles (23.5 cents per mile)	<ul style="list-style-type: none"> <li>• Total medical miles driven January–December</li> </ul>
	Health insurance coverage verification	<ul style="list-style-type: none"> <li>• Forms in the 1095 series may be received from your employer or the marketplace or any other relevant information</li> </ul>
	Health savings account contribution/distribution	<ul style="list-style-type: none"> <li>• Forms 5498-SA, 1099-SA</li> </ul>
<b>20</b>	State income taxes; property taxes; sales taxes on vehicles, motorcycles, or homes	<ul style="list-style-type: none"> <li>• Prior year's income tax return</li> <li>• Property tax bills</li> <li>• Closing papers from the purchase or sale of property</li> <li>• Letter from the state regarding any change in a prior-filed return</li> </ul>
<b>21</b>	Refinance a home	<ul style="list-style-type: none"> <li>• Closing papers with amount borrowed</li> <li>• Form 1098</li> <li>• Description of use of money</li> </ul>
<b>22</b>	First-Time Homebuyer Credit	<ul style="list-style-type: none"> <li>• Credit no longer available</li> </ul>
	Recapture of credit taken in 2009 or after	<ul style="list-style-type: none"> <li>• Sale or change of use from principal residence within 36 months of credit</li> <li>• Closing papers if sold</li> </ul>
	Recapture/repayment 2008 credit	<ul style="list-style-type: none"> <li>• Sale or change in use</li> <li>• Record of amount repaid—year 5 of 15</li> </ul>
<b>23</b>	Charitable contributions of money, property, or out-of-pocket expenses	<ul style="list-style-type: none"> <li>• Date, amount, and type of contributions</li> <li>• Knowledge that receipts from the organizations have been received</li> <li>• Statement regarding whether goods and services were received for donation</li> <li>• Mileage log for charitable work</li> <li>• Vehicle donations require Form 1098-C</li> </ul>

	Charitable miles (14 cents/mile)	<ul style="list-style-type: none"> <li>• Total charitable miles driven</li> </ul>
	Transfer of IRA to charity	<ul style="list-style-type: none"> <li>• Brokerage statement showing transfer (may not be allowed for 2014)</li> </ul>
<b>24</b>	Job-related expenses	<ul style="list-style-type: none"> <li>• Meals, lodging, and miscellaneous expense amounts for items related to employment</li> </ul>
	Business miles (56 cents/mile)	<ul style="list-style-type: none"> <li>• Total miles driven per vehicle January–December</li> <li>• Business miles driven per vehicle January–December</li> </ul>
<b>25</b>	Education expenses	<ul style="list-style-type: none"> <li>• Form 1098-T for parent or child (if the child is a student, the form will come to the child)</li> <li>• Actual expense record to verify expenses for credit/deduction purposes</li> <li>• Financial transcript from school needed to show when actual expenses were paid</li> </ul>
	Student loan interest	<ul style="list-style-type: none"> <li>• Interest record for student loans</li> <li>• Form 1098-E</li> </ul>
<b>26</b>	Child or disabled spouse care	<ul style="list-style-type: none"> <li>• Name, address, and ID number of the day-care provider</li> <li>• Amount paid to the provider</li> <li>• If the provider comes into your home, a W-2 may be required</li> </ul>
<b>27</b>	Energy credit	<ul style="list-style-type: none"> <li>• Information regarding the purchase of solar, geothermal, fuel cell, or small wind energy property business or residence</li> <li>• No other residential credit in 2014</li> </ul>
<b>28</b>	Bankruptcy filing	<ul style="list-style-type: none"> <li>• Date filed</li> <li>• Bankruptcy papers to show property rejected/returned by court</li> </ul>
<b>29</b>	Debt forgiveness or abandonment of property	<ul style="list-style-type: none"> <li>• Form 1099-A for abandonment</li> <li>• Date property was taken by the bank or sold in foreclosure</li> <li>• Form 1099-C for cancellation of debt</li> </ul>
<b>30</b>	IRS or state communications	<ul style="list-style-type: none"> <li>• Letters, additional taxes paid, changes in prior-year returns, installment agreements, or offers in compromise</li> </ul>
<b>31</b>	Foreign investments or holdings	<ul style="list-style-type: none"> <li>• Any foreign accounts?</li> <li>• Did value of accounts total more than \$10,000 at any time?</li> <li>• Foreign business interests of stock of \$50,000 or more?</li> <li>• Signature authority over foreign accounts?</li> </ul>



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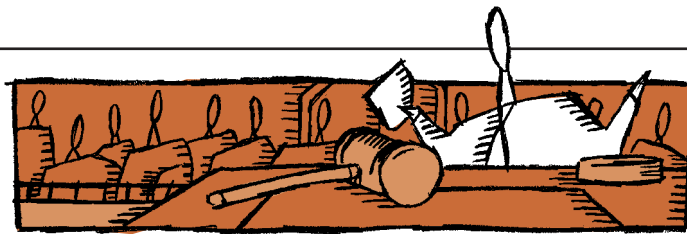
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## TAX COURT CORNER

# Does an IRA Trustee's Policy of Not Allowing Certain Investments Control, Even If the Investments Are Otherwise Allowable?

Guy M. Dabney and Ann V. Dabney, Petitioners

v.

Commissioner of Internal Revenue, Respondent

TC Memo. 2014-108

By Steven R. Diamond, CPA

**G**enerally, amounts distributed from an IRA are included in a taxpayer's gross income. A non-prohibited purchase of an asset inside an IRA or a transfer between IRA trustees is not a taxable distribution.

### FACTS

In 2008, Mr. Dabney rolled over funds from an IRA at Northwest Mutual into a preexisting self-directed IRA that he had with Charles Schwab & Co., Inc. At some point in time after the rollover, he learned of a piece of undeveloped land for sale in Brian Head, Utah, which he believed was undervalued.

On his own, Dabney did some research and concluded that IRAs are permitted to hold real property for investment. He then attempted to have his Charles Schwab IRA purchase the Brian Head property.

Before actually making the purchase, Dabney called the customer service line at Charles Schwab and spoke with whichever customer service representative happened to answer the phone. The customer service representative informed him that Charles Schwab did not allow alternative investments, which included the purchase and holding of real estate.

Dabney also spoke with Vincente Alvarez, a CPA, about whether IRAs could purchase and hold real property. At first, Alvarez told Dabney he did not have experience in retire-

ment accounts and was not certain this type of investment would be allowed. However, Dabney shared his research with Alvarez, and ultimately, Alvarez agreed that it would be possible for an IRA to hold real property.

Based on his conversations with the customer service representative at Charles Schwab, his conversations with Alvarez, and his own research, Dabney arranged what he thought would be a way for his Charles Schwab IRA to purchase the Brian Head property. His plan was to have the funds wired directly from the IRA to the seller of the Brian Head property and to have the title placed in the name of "Guy M. Dabney Charles Schwab and Co., Inc. Cust IRA Contributory." He then planned to resell the property at a gain and contribute the proceeds back to the IRA. Dabney thought that as long as he did not use or enjoy the property, there would be no need for the property to be managed by a trustee.

In February 2009, Dabney signed a contract to purchase the Brian Head property. He then requested a withdrawal of \$114,000

### About the Author

**Steven R. Diamond** is a CPA with a tax practice located in Westport, Connecticut. His practice is limited to compliance issues and representation before the IRS. He has his M.S.M. degree in taxation from Florida International University, and he is admitted to practice before the United States Tax Court. Steven also taught a course preparing EAs and CPAs to take the Tax Court admission exam for non-attorneys.

## On his own, Dabney did some research and concluded that IRAs are permitted to hold real property for investment.

from his IRA by filling out a distribution request form provided by Charles Schwab, and checked the box indicating that the withdrawal was an early withdrawal with no known exception to the early distribution penalty, as he was not yet 59½. The distribution request form did not indicate the requested funds were to be used to invest in real property on behalf of the IRA.

Charles Schwab wired the \$114,000 to the bank account of Chicago Title Insurance Co., the company that was handling the sale of the Brian Head property. Dabney directed Chicago Title to show the owner of the account as “Guy M. Dabney Charles Schwab and Co., Inc. Cust IRA Contributory.” However, the title was incorrectly placed in Dabney’s own name.

Dabney was not able to find a buyer for the Brian Head property until 2011. It was then he discovered the property had been incorrectly titled in his own name, and he immediately had Chicago Title issue an affidavit where the company admitted fault for the titling error. Dabney sold the property for \$127,226, and he had the funds wired directly into his Charles Schwab IRA account. The deposit slip with the sale proceeds was marked as a rollover, and Charles Schwab accepted the check.

In 2009, Charles Schwab issued a 1099-R to Dabney for the \$114,000 for the withdrawal he made to purchase the Brian Head property. The 1099-R indicated that this was an early distribution from the Charles Schwab IRA and that no exceptions to the early distribution penalty applied. Petition-

ers did not report the withdrawal on their 2009 federal income tax return.

### OPINION

Generally, amounts distributed from an IRA are includable in a taxpayer’s gross income pursuant to IRC Sec. 72. Mr. Dabney argued that the \$114,000 was not a taxable distribution because it was either a purchase made by an IRA or it was an IRA trustee-to-trustee transfer.

Dabney argued that he acted as a conduit his IRA purchased the Brian Head property through, and since the IRA was the purchaser, it was not a distribution. In *Ancira v. Commissioner*,<sup>1</sup> the taxpayer had a self-directed IRA. In order to direct funds from the IRA to specific assets, the taxpayer made phone requests to the investment advisor of the IRA. One year, the taxpayer requested that the IRA purchase the stock of a particular company. The investment advisor told the taxpayer that the custodian would not purchase the stock because it was not publicly traded, even though the stock could be held as an asset of the IRA. The investment advisor determined that the IRA could make the investment if the custodian issued a check payable to the issuing company and the taxpayer delivered the check to the issuing company.<sup>2</sup>

The custodian sent the check to the taxpayer and the taxpayer forwarded the check to the issuing company. A stock certificate was issued, which stated that the IRA was the owner of the shares. The taxpayer thought that the issuing com-

pany would send the stock certificate to the custodian, but it did not. The error was discovered when the taxpayer received a notice of deficiency. After the error was discovered, the taxpayer directed the issuing company to send the stock certificate to him, and then the taxpayer delivered the certificate directly to the custodian. The Tax Court determined that a distribution did not occur when the custodian delivered the check to the taxpayer. The Court held that because the taxpayer had arranged the purchase, the taxpayer was not in constructive receipt of the check, the taxpayer had acted as an agent for the custodian, and that ownership of the stock was directly assumed by the IRA. Additionally, the Court held that the late delivery of the stock to the custodian was a bookkeeping error and did not transfer ownership to the taxpayer.

Dabney argued that the facts of the *Ancira* case are similar to his. He argued that Charles Schwab’s not permitting its IRAs to invest in real property was a matter of company policy and not due to a statutory prohibition. He also argued that had the title been placed in the name of “Guy M. Dabney Charles Schwab and Co., Inc. Cust IRA Contributory,” as originally intended, the purchase would have been essentially the same as in the *Ancira* case.

The Tax Court noted that Mr. Dabney was correct that IRAs are permitted to hold real property. However, the Court was not aware of any provision in the Internal Revenue Code requiring an IRA trustee to

give the owner of a self-directed IRA the option to invest funds in *any asset* that is not prohibited by statute. IRA trustees and custodians generally have broad latitude to direct or limit the investment of funds in an IRA.

At trial, the operations manager of Charles Schwab's San Diego branch testified that Schwab's policies do not permit IRAs to hold real estate. Dabney did not introduce any evidence that showed this policy violates any statutory provision or the terms of the Charles Schwab IRA trust instrument. The Tax Court determined that Charles Schwab, in its role as an IRA trustee, had the power to prohibit the purchase and holding of real property.

Therefore, even if the Brian Head property had been titled as intended, the Charles Schwab IRA could not hold real property and would not have accepted ownership of the Brian Head property. Therefore, the Tax Court determined that Dabney did not act as an agent on behalf of Charles Schwab, and the IRA did not purchase the Brian Head property.

The Tax Court also noted that the owner of an IRA may direct the trustee to transfer funds directly to the trustee of another IRA. Therefore, had Mr. Dabney done a trustee-to-trustee rollover from his Charles Schwab IRA to an IRA that permitted the purchasing and holding of real property, he would have achieved what he set out to do.

Instead, Mr. Dabney had Charles Schwab wire the funds directly from his IRA to Chicago Title, and Chicago Title is not an IRA trustee. Therefore, the transfer did not qualify as a transfer between IRA trustees. The Tax Court ruled in favor of the IRS on the primary issue presented in this case, although it did find that the petitioner, due to his intentions and beliefs, had reasonable cause and acted in good faith, thereby avoiding the accuracy-related penalty which the IRS wanted to impose on his underpayment of tax. **EA**

#### ENDNOTES

<sup>1</sup> 119 T.C. 135, 136

<sup>2</sup> Id

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- 39. A  B  C  D  E
- 40. A  B  C  D  E

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### ASSET VALUATION AND FORM 433-A

1. In an OIC, the IRS defines the QSV of an asset as:

- A. A reduction of 20% from the FMV
- B. Equal to the FMV
- C. The IRS only uses FMV in valuing assets in a compromise
- D. The asset value if it had to be replaced

2. When valuing an OIC, the IRM permits cash in bank accounts to be reduced by:

- A. All of a taxpayer's monthly living expenses, regardless of whether the expense is allowable
- B. \$1,000
- C. One month's allowable living expenses
- D. Both B and C

3. When completing Form 433-A to accompany an OIC, it is important to:

- A. Know your IRM value exclusions for assets like automobiles, household goods, bank account balances, and business equipment
- B. Avoid claiming asset-value exclusions, and let the IRS figure that out
- C. Show the IRS your work on Form 433-A and demonstrate how a value exclusion resulted in a net realizable equity that is different from the asset's FMV
- D. Both A and C

4. IRM 5.8.5.7 provides an equity exclusion of \$1,000 for the cash balance in a savings account.

- A. True
- B. False



5. The IRM has specific exclusions that can be used to reduce the equity of which asset in an OIC:

- A. Automobile
- B. Business equipment up to \$4,470 in value
- C. Household goods up to \$8,940 in value
- D. All of the above

6. The net realizable equity of an asset in an OIC will always be the same as the asset's FMV.

- A. True
- B. False

7. The IRC prevents the IRS from seizing:

- A. A taxpayer's everyday household goods up to \$8,940 in value
- B. Retirement accounts
- C. A taxpayer's tools and equipment of a trade or business up to \$4,470 in value
- D. Both A and C

8. Restrictions on IRS' power to seize a taxpayer's property can also be value exclusions in an offer in compromise.

- A. True
- B. False

9. To arrive at the net realizable equity of an automobile in an OIC, you should:

- A. Reduce the FMV to QSV
- B. Reduce the QSV by the value exclusion in IRM 5.8.5.12
- C. Subtract any loan balances encumbering the automobile
- D. All of the above

10. The IRS has expressed a general policy against simultaneously including both the net realizable equity in business equipment and the revenue the equipment generates into the value of an OIC.

- A. True
- B. False

### REPRESENTING CASH-INTENSIVE BUSINESSES

11. It is important to understand your client's business because:

- A. You are acting in place of your client for the interview
- B. You do not want the auditor speaking to your client
- C. You need to be able to answer the auditor's questions in the interview
- D. All of the above

12. When taking the case to Appeals, you want to do an FOIA request so that:

- A. You know the collection process
- B. You understand the appeals process
- C. You know what the auditor has in his notes
- D. You know what the appeals officer will do

13. When dealing with a client who has accumulated assets with no visible means of doing so, you should:

- A. Assume she is deep in debt
- B. Assume she found a money tree
- C. Ignore it altogether
- D. Ask her where the money came from

14. Why should you prepare a Cash T-analysis?

- A. So you know how your client spends his money
- B. To use actual numbers, as the auditor will use national standards
- C. To understand the business operations
- D. To see if your client is lying

15. Why is understanding your client's internal controls important?

- A. To spot any areas that may be seen as weaknesses
- B. To see if the taxpayer is skimming from the sales
- C. To point them out to the auditor
- D. None of the above

16. What is the benefit of having your client present for the interview with the auditor?

- A. The taxpayer can explain his business operations
- B. The auditor can get first-hand knowledge of the business
- C. To show the auditor you want to work with him
- D. All of the above

17. Why would the auditor want to compare the purchases with the sales?

- A. To understand the sales process
- B. To show you and the taxpayer that he is doing his job
- C. To see if the markup percentage being used is legal
- D. To establish that the income was reported correctly

18. Why would the auditor care about the assets the taxpayer has?

- A. To see if the taxpayer can afford to have purchased them based on the reported income
- B. The auditor is curious as to what your client owns because he is jealous
- C. The auditor is thinking of starting his own business and wants to know what he can afford after opening
- D. To establish that the income was reported correctly

19. If the auditor discovers that the deposits are less than the sales after completing his BDA, is this an issue?

- A. No, since the taxpayer reported more than was deposited
- B. No, as long as you have a reasonable explanation
- C. Yes, and you want to point out that the taxpayer overstated his income and is due a refund
- D. Yes, as this will make the auditor believe that there is more income that was not reported

### TAX LAW WRAPUP FOR 2014

20. The maximum amount of Sec. 179 eligible to be claimed on a tax return with a tax year beginning in calendar year 2013 and ending in calendar year 2014 (i.e., a fiscal-year return) is:

- A. \$25,000
- B. \$200,000
- C. \$250,000
- D. \$500,000

21. The maximum amount of Sec. 179 eligible to be claimed on a tax return with a tax year beginning in calendar year 2014 and ending in calendar year 2015 (i.e., a fiscal-year return) is:

- A. \$25,000
- B. \$200,000
- C. \$250,000
- D. \$500,000

22. Bonus depreciation for calendar year 2014 is:

- A. 0 percent
- B. 30 percent
- C. 50 percent
- D. 100 percent

23. The Form 1023-EZ streamlined application has a filing fee of:

- A. \$100
- B. \$400
- C. \$500
- D. \$850

24. Unused ITINS will expire after \_\_\_\_ years of nonuse.

- A. Two
- B. Three
- C. Four
- D. Five

25. The maximum amount of mortgage insurance premium deduction for 2014 is:

- A. \$0
- B. \$1
- C. \$5,000
- D. \$15,000

26. Which of the following is not on the list of extenders expiring after 2013?

- A. Energy credit for storm windows
- B. Tuition deduction
- C. American Opportunity Credit
- D. Sales tax deduction

27. Which of the following is not on the list of extenders expiring after 2013?

- A. Student loan interest expense
- B. The exclusion from debt discharge income for qualified home mortgage indebtedness
- C. The provision permitting tax-free distributions from IRAs directly to charities for taxpayers age 70½ or older
- D. The educator expense deduction

28. Taxpayers whose home mortgage was written off in a foreclosure after 2013 can no longer exclude debt discharge income due to insolvency.
- A. True
  - B. False

**PIERCING THE CORPORATE VEIL**

29. When a court disregards the liability shield provided by a corporation, the action is known as:
- A. Intermingling
  - B. Piercing the corporate veil
  - C. Recharacterization
  - D. Capitalization

30. Which of the following activities is a breach of corporate formalities?
- A. Henry makes a contribution of equipment to the corporation instead of cash
  - B. Susan, a shareholder-employee, issues a paycheck to herself
  - C. Paper, Inc., purchases a life insurance policy on the life of an executive
  - D. Dan's Landscaping, Inc., uses the invoices for Dan's Landscaping before ordering new invoice forms

31. If a corporation gives a shareholder a loan at below-market rates, the IRS may reclassify the loan payment as:
- A. Constructive dividend
  - B. Unreasonable compensation
  - C. Intermingling of funds
  - D. A benefit of incorporating is the ability to receive below-market loans from the corporation

32. The following type of corporation is not in danger of having the corporate veil pierced:
- A. S corporation
  - B. Closely held corporation
  - C. Publicly traded corporation
  - D. C corporation

33. Marsha writes herself a check from the corporation's checking account. This transfer of funds from the corporation to Marsha is treated by the IRS in the following manner:
- A. Taxable dividend
  - B. Loan to the shareholder
  - C. Wages
  - D. Any of the above, depending on the circumstances

34. The term "reasonable compensation" refers to a reasonable amount being paid to a shareholder in the following manner:
- A. Return of capital
  - B. Sale of stock
  - C. Fringe benefits
  - D. Wages

35. The following type of business entity may provide all the same fringe benefits to owner-employees as are available to all other employees.
- A. Partnership
  - B. S corporation (greater than 2% owner)
  - C. C corporation
  - D. LLC taxed as a partnership

36. A corporation is formed in the following manner:
- A. Corporations are formed under state law
  - B. A corporation is formed when it files its first federal tax return
  - C. A corporation is formed when a company files a DBA
  - D. A corporation is formed when the company registers its trademark

37. Generally, a corporation's accumulated earnings are considered to be within the reasonable needs of a corporation up to:
- A. \$150,000
  - B. \$250,000
  - C. \$500,000
  - D. There is no safe harbor

38. The following situation occurs when a court pierces the corporate veil:
- A. Shareholders become personally liable for business debt
  - B. Constructive dividends are declared
  - C. S corporation status is revoked
  - D. Payroll deposit penalties are imposed

**TAX COURT CORNER**

39. Generally, IRC Sec. 72 requires that amounts distributed from an IRA be included in a taxpayer's gross income.
- A. True
  - B. False

40. In the *Dabney* case, the Tax Court:
- A. Conceded it did not have jurisdiction to rule on matters affecting IRA trustees
  - B. Stated that Mr. Dabney's behavior was almost criminal in nature
  - C. Ruled that Mr. Dabney's transfer qualified as a transfer between IRA trustees
  - D. Stated it was not aware of any Internal Revenue Code provision that required an IRA trustee to give the owner of a self-directed IRA the option to invest funds in any asset that is not prohibited by statute

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# National Conference Highlights

**O**ver 600 dedicated tax professionals attended the 2014 NAEA National Conference, held this past August 3–5, and the reviews were overwhelmingly positive! Once again, the National Tax Practice Institute™ provided the best available representation education, and attendees of the Tax Preparation Issues track left feeling fully up to date on changes in the tax code. Social events—such as the opening reception and graduation ceremony, breakfasts, and breaks—provided networking opportunities and good times for conference attendees.

Although classes were challenging, everyone seemed to have the energy to keep going into the night, beginning on Sunday with the NAEA Welcome Reception. Following the reception, attendees enjoyed a keynote address from Sheldon Kay, former IRS chief, Appeals, and current partner in the law firm of Sutherland Asbill & Brennan LLP. Kay's experience with the appeals process on both sides of the table, first with IRS and then representing taxpayers before IRS, allowed him to share a valuable perspective. Kay spoke to conference attendees on representation changes that Circular 230 professionals face in negotiating with today's IRS.

Members engaged in lively discussion at the NAEA Annual Meeting on Monday, as they helped to determine the future direction of the Association. NAEA's members share a dedication to the Association that not many professional societies can claim!

Tuesday night, attendees gathered for the graduation ceremony for this year's NTPI Level 3 class of 147 graduates and the presentation of the 2014 NAEA Annual Awards. The newly minted Fellows and award recipients were feted at a reception following the graduation.

Once again this year, there are a lot of people to thank for making this conference a success. The NTPI Planning Committee, amazing volunteers, instructors, staff, exhibitors, and sponsors all played a role in pulling together this event. And of course, many thanks to the attendees: We couldn't have done it without you!

Be sure to mark your calendar for August 2–4, 2015, when we'll be back in Vegas for another outstanding conference. Remember, tax education that happens in Vegas doesn't stay in Vegas—you take it back to your practice and are a better tax pro because of it!

We'll look for you next year at the Cosmopolitan.



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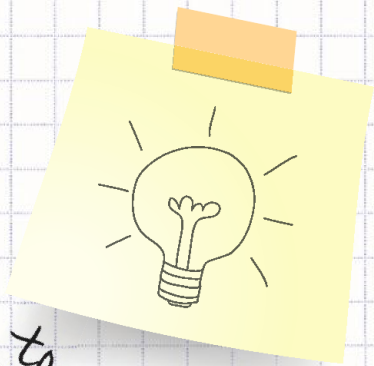
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