

**W**elcome to this month's edition of the *Tax and Business Alert*. Our goal is to provide you with current articles on various tax and business topics. The articles are intended to keep you up to date on trends and issues that may impact your business and personal financial affairs. Please contact us if you have questions about any of the issues discussed.

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### **Business Buy/Sell Agreements**

It is important that businesses with more than one owner have a written buy/sell agreement specifying what happens when an owner withdraws from the business.

### **2007 IRS Data Book**

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### **Evaluating Charitable Organizations**

Some charitable organizations may be experiencing a reduction in contributions due to a perceived slowing in the economy. As a result, you may feel compelled to step in and help one or more charitable organizations in this challenging economic environment.

### **IRS's 2008 "Dirty Dozen" Tax Scams**

The IRS recently updated its list of the most notorious tax scams, the "Dirty Dozen." "Taxpayers should be wary of scams and promises to avoid paying taxes that seem too good to be true," Acting IRS Commissioner Linda Stiff said in reference to the Dirty Dozen.

### **Recognizing Worthless Securities Losses**

Taxpayers are allowed a capital loss tax deduction when securities (e.g., common stocks) that are held as capital assets become worthless. The issue of worthlessness can occur where, for example, a taxpayer owns an interest in a small, closely held corporation that is experiencing severe financial problems.



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**2007 IRS Data Book**[Back](#)

The IRS recently released its 2007 Data Book describing activities conducted during Fiscal Year 2007 (FY 2007) from October 1, 2006, through September 30, 2007. The Data Book contains information about returns filed, taxes collected, enforcement, taxpayer assistance, and the IRS budget and workforce. During FY 2007, the IRS collected almost \$2.4 trillion in taxes (net of refunds) and processed over 235 million tax returns. Over 114 million individual income tax return filers received refunds totaling \$248.6 billion. The IRS spent an average of 40 cents to collect each \$100 of tax revenue, which was the lowest in seven years. The IRS examined nearly 1.4 million individual income tax returns in FY 2007.

## Business Buy/Sell Agreements

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It is important that businesses with more than one owner have a written buy/sell agreement specifying what happens when an owner withdraws from the business. A buy/sell agreement is a contract between the owners (or the owners and the business entity itself) that establishes rules and restrictions applicable to changes in ownership.

The typical buy/sell agreement provides that an owner's interest in the business will be sold (or at least offered for sale) at a specified price to the other owners and/or to the business entity itself upon the occurrence of specified events. This prevents unwanted persons from becoming members of the ownership group and ensures a ready market for closely held ownership interests. It also provides liquidity to a deceased owner's family and assures the remaining owners that they will be able to continue the business without interference from the family of the deceased owner. Buy/sell agreements also offer estate planning benefits by establishing a value for the business prior to an owner's death.



Common methods for determining the purchase price under a buy/sell agreement include: establishing a fixed price in the contract; requiring an independent appraisal; or specifying a formula such as a percentage of book value. Events that trigger a buy/sell agreement are specified by the owners in the contract. Generally, buy/sell agreements are triggered by any circumstance that might cause an owner to dispose of an ownership interest such as death, disability, bankruptcy, or retirement.

The best time to establish a buy/sell agreement is now, before a problem develops. If you do not have a buy/sell agreement for your business, we would be happy to discuss their merits with you. Your attorney should be consulted in formulating the terms of a buy/sell agreement, or prior to changing an existing agreement.

Please call us at your convenience if you would like to discuss buy/sell agreements or any tax compliance or planning matter.

## Evaluating Charitable Organizations

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Some charitable organizations may be experiencing a reduction in contributions due to a perceived slowing in the economy. As a result, you may feel compelled to step in and help one or more charitable organizations in this challenging economic environment.

If you would like to evaluate a charity before contributing, you can go to Charity Navigator at [www.charitynavigator.org](http://www.charitynavigator.org). Charity Navigator has gathered information on more than 5,000 of the largest charities, indicating how much of their revenue is expended on their programs, the services they deliver, and how efficient they are.

## IRS's 2008 "Dirty Dozen" Tax Scams

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The IRS recently updated its list of the most notorious tax scams, the "Dirty Dozen." "Taxpayers should be wary of scams and promises to avoid paying taxes that seem too good to be true," Acting IRS Commissioner Linda Stiff said in reference to the Dirty Dozen. "There is no secret formula that can eliminate a person's tax obligations. People should be wary of anyone peddling any of these scams," she indicated. The 2008 list includes the following:



1. *Phishing.* This tactic is used by Internet-based thieves to trick victims into revealing personal information and then using it to access the victim's financial accounts.
2. *Economic stimulus payment scams.* Scam artists trick individuals into revealing personal financial information by making promises related to economic stimulus rebate payments.
3. *Frivolous arguments.* Frivolous scheme promoters encourage people to make unreasonable and unfounded claims to avoid paying the taxes they owe. Taxpayers who file a return or make a submission based on a frivolous position are subject to a \$5,000 penalty.
4. *Fuel tax credit scam.* Some taxpayers are claiming a fuel tax credit when their nontaxable use, occupation, or income level makes the claim unreasonable.
5. *Hiding income offshore.* Some individuals try to avoid paying U.S. taxes by illegally hiding income in offshore bank and brokerage accounts, or using offshore debit cards, credit cards, wire transfers, foreign trusts, employee leasing schemes, private annuities, and life insurance plans. The IRS and state and U.S. possession tax agencies aggressively pursue those using and promoting these scams.
6. *Abusive retirement plans.* The IRS is looking for transactions taxpayers use to avoid the limits on Roth IRA contributions, among other retirement plan abuses.
7. *Zero wages.* Taxpayers file a phony wage or income-related information return to replace a legitimate return as an illegal method to lower the amount of taxes owed.
8. *False claims for refund and abatement requests.* This practice involves filing a false refund or tax abatement claim form.
9. *Return preparer fraud.* Dishonest preparers cause problems for taxpayers falling victim to their schemes.
10. *Disguised corporate ownership.* Domestic shell corporations are used to underreport income and for money laundering, financial crimes, and terrorist financing.
11. *Misuse of trusts.* Unscrupulous promoters urge taxpayers to transfer assets to trusts to save taxes, but don't deliver as promised.
12. *Abuse of charitable organizations and deductions.* Abuses include arrangements to improperly shield income from taxation, attempts by donors to maintain control over donated assets or income from donated property, overvaluation of contributed property, and tuition payments disguised as contributions.



Please contact us if you are approached concerning any of these abusive tax schemes. We remain diligent in our efforts to minimize your tax bill using every possible legal measure within the tax code.

## Recognizing Worthless Securities Losses

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Taxpayers are allowed a capital loss tax deduction when securities (e.g., common stocks) that are held as capital assets become worthless. The issue of worthlessness can occur where, for example, a taxpayer owns an interest in a small, closely held corporation that is experiencing severe financial problems. But, when is a security actually worthless? The IRS says the loss can be taken only when the security becomes wholly worthless; losses for partial worthlessness cannot be claimed. This rule also requires that a taxpayer correctly identify the year a security becomes wholly worthless.

This is important because you can offset capital gains with capital losses, including losses from worthless securities. To the extent there are excess capital losses, up to \$3,000 (\$1,500 for married filing separate returns) can be deducted against your ordinary income. Remaining capital losses can be carried forward indefinitely.

The question of when a security becomes worthless has been the subject of many court cases and IRS rulings. For example, simply because a corporation declares bankruptcy, its shareholders may not be able to claim a loss when it is possible that they will obtain stock in a corporate reorganization. Worthlessness depends on the particular facts of each situation. Generally, a security is considered worthless at the time it first has no liquidation value, and no reasonable hope or expectation exists that the security will become valuable at some future date. A taxpayer may be able to establish worthlessness by showing a fixed and identifiable event demonstrating the worthlessness of the security.

**Example: Timing of worthless stock loss.** Valerie bought 200 shares of ABC Corp. for \$15 per share in 2003. ABC is a publicly traded company. As of the end of 2007, the stock price had declined to \$1.50 per share, and the company was in Chapter 11 bankruptcy.

Valerie cannot take a worthless stock deduction in 2007 for her anticipated loss on ABC stock because the stock is not wholly worthless—as evidenced by its trading value. To establish a deductible capital loss, Valerie must sell her shares or wait for an event that renders her stock worthless. Even if her ownership interest is significantly diluted in the Chapter 11 reorganization, Valerie will be unable to claim a loss as long as she holds securities that have some value—however nominal. If, however, ABC is liquidated in bankruptcy, Valerie should be able to claim a worthless security loss when it is established that her equity holder class will receive nothing in liquidation.



As noted above, it is often difficult to determine if and when a security is wholly worthless. However, the IRS recently issued a final regulation pertaining to abandoned securities which may help in making this determination. The new regulation seems to indicate that a worthless security deduction is available when the taxpayer merely abandons it, even if it has not become wholly worthless. In effect, the worthless securities deduction is available to the taxpayer because, as a result of abandonment, the security is wholly and irretrievably worthless. To prevent abuse of this privilege, the IRS requires a taxpayer to permanently relinquish all title to the security and receive no consideration for it.

This is obviously a tough issue to understand and evaluate. So, please contact us if you have questions pertaining to securities with minimal or no value. We can help determine the most tax-wise and credible way to proceed in the determination of worthlessness or abandonment of investment securities.

