August 1, 2002

RECAP OF SIGNIFICANT TAX DEVELOPMENTS THAT OCCURRED IN THE SECOND QUARTER OF 2002

The following is a summary of the most important tax developments that have occurred in the past three months which may affect you, your family, your investments and your livelihood. Please call me for more information about any of these developments and what steps you should take to take advantage of favorable developments and to minimize the impact of those that are unfavorable.

WEIGHT LOSS PROGRAMS MAY BE DEDUCTIBLE

The IRS has ruled the unreimbursed cost of participating in a weight-loss program as treatment for a specific disease or diseases (including obesity) diagnosed by a physician qualifies as a medical care expense. The cost of diet foods, however, is not deductible. Individual who might otherwise join a weight-loss program to improve their general health or appearance should first be examined by a physician to see if there is a medical reason for participating, such as to aid in alleviating hypertension, reducing high cholesterol or combating diabetes. If a medical reason exists, and is documented in a written report from the physician, the cost of the program may be deductible. Note that medical expenses, including qualifying weight-loss expenses, are deductible only to the extent they cumulatively exceed 7.5% of adjusted gross income (AGI). Individuals who participate in a company medical flexible spending account may obtain a reimbursement from the account for qualifying weight-loss expenses.

FINAL REGS LIBERALIZE REQUIRED MINIMUM DISTRIBUTION (RMD) RULES

You must begin withdrawing minimum annual distributions from your qualified retirement plan accounts and traditional IRA's no later than April 1st following the year you attain age 70 ½. If you are not a 5% company owner and continue working, the start date for distributions from your employer sponsored qualified retirement plan account is deferred until April 1st following the year you retire. In 2001, the IRS issued proposed regulations overhauling and simplifying the rules for determining these minimum annual amounts, which are called required minimum distributions or RMD's. Now, the IRS has issued final regulations liberalizing the RMD rules even further. The most important changes are as follows:

(1) The expectancy tables used to determine RMD's have been revised to reflect current mortality experience. The net result is that RMD's may be spread over a longer period than under the 2001 proposed regulations.

(2) Liberalized rules apply where the owner of a qualified plan account or IRA dies on or after the date when distributions must begin. Post-death RMD's are distributed over the longer of the IRA owner's remaining life expectancy or the remaining life expectancy of the eldest designated beneficiary. This helps where the IRA owner was younger than the eldest designated beneficiary. By contrast, the rules issued in 2001 required post-death RMD's to be are distributed over the beneficiary's life expectancy even if the IRA owner was younger than the beneficiary.

(3) A designated beneficiary of a qualified plan account or IRA is someone who was (a) named as a beneficiary as of the account owner's date of death and (b) remains a

beneficiary on September 30th of the year following the year of the account owner's death. Under the 2001 rules, the designated beneficiary was determined as of the end of the year following the year of the IRA owner's death. This change means there is slightly less time to do post-mortem tax planning to aid the beneficiaries of the qualified plan account or IRA.

 # FINALIZED RULES ALLOW MORE BUSINESSES TO USE THE CASH METHOD OF ACCOUNTING

The IRS has finalized proposed rules issued in 2001 permitting businesses with average annual gross receipts of up to $10 million to use the cash method of accounting (instead of the accrual method) if their principal business activity is providing services or the fabrication or modification of non-realty property in accordance with customer design or specifications. The business cannot, however, engage in mining, manufacturing, wholesale or retail trade or information industries as its principal business activity. Additionally, the relief does not apply to businesses that are C corporations (or partnerships with C corporation partners having average gross receipts over $5 million), unless they are personal service corporations or farming businesses.

 # LESS PAPERWORK FOR SMALL CORPORATIONS

Starting with the 2002 tax year, the IRS will no longer require small corporations to reveal balance sheet information or complete related reconciliations on their corporate income tax returns. The relief applies to corporations with less than $250,000 of gross receipts and less than $250,000 in assets. For example, on the regular corporate income tax return (Form 1120), these small corporations will no longer have to complete Schedule L (Balance Sheets per Books), Schedule M-1 (Reconciliation of Income (Loss) per Books With Income per Return), or Schedule M-2 (Analysis of Unappropriated Retained Earnings per Books).

 # COUNTRY CLUB CORPORATION'S DISCOUNT TO SHAREHOLDERS TREATED AS DIVIDEND

It is common for suburban, leisure-home or retirement-area country clubs organized as corporations to give their shareholders a discount on dues, fees and restaurant purchases. Now the IRS has ruled privately the excess of the fair market value of the goods and services purchased by country club shareholders, less the amount paid for them, is a taxable distribution to participating shareholders to the extent it constitutes a dividend. A dividend is a distribution of property by a corporation to its shareholders with respect to its stock, out of accumulated or current earnings and profits.

 # IRS EXPLAINS HOW TO CLAIM OR ELECT-OUT OF BONUS FIRST-YEAR DEPRECIATION

The IRS has explained in detail how taxpayers claim or elect not to use the additional 30% first-year depreciation deduction that applies for most types of depreciable tangible personal property (as well as some types of software and leasehold improvements) placed in service after September 10, 2001, and generally before September 11, 2004, (later, for certain classes of property). The new IRS guidance makes it clear the additional first-year depreciation deduction automatically applies to qualifying assets, unless the taxpayer elects not to use it. An election not to use the bonus depreciation allowance may be a good idea if a business has about-to-expire net operating losses, or anticipates being in a higher tax bracket in future years. The IRS also reiterated the additional first-year depreciation allowance applies for both regular tax and alternative minimum tax (AMT) purposes and generally is determined without any proration based on the length of the tax year in which the qualifying property is placed in service.

DIVORCE TRANSFERS OF NON-STATUTORY STOCK OPTIONS AND NONQUALIFIED DEFERRED COMPENSATION NOT TAXED UNTIL EXERCISE OR PAYOUT

The IRS has concluded a person who transfers non-statutory stock options and non-qualified deferred compensation to his former spouse in a divorce isn't taxed on the transfer. Rather, the former spouse is taxed on exercise of the options, and on the deferred compensation when it is paid or made available to the former spouse. A stock option is "non-statutory" if it is not specifically provided for in the tax code or does not meet numerous qualification requirements. A deferred compensation plan is "non-qualified" if it does not meet the detailed rules in the tax code for qualified retirement plans. At the same time, the IRS issued proposed rules on the FICA, FUTA and income tax withholding consequences of the transfers. In general, the employee spouse would be hit with the FICA burden, but income tax withholding on the exercise of non-qualified stock options would apply to the former spouse.

INDEFINITE MORATORIUM ON PAYROLL TAXES ON STATUTORY STOCK OPTIONS

IRS has announced that it is extending a moratorium on payroll taxes on statutory options-incentive stock options or options granted under an employee stock purchase plan-indefinitely until it completes review of comments on recent proposed regs and issues future guidance, which would apply only on a prospective basis. The IRS had earlier announced that statutory options would not trigger FICA or FUTA tax, or income tax withholding before 2003.

IRS EXPLAINS HOW TO CLAIM DEDUCTION FOR PART OF THE COST OF A HYBRID AUTO

A taxpayer may claim an above-the-line deduction for the cost of a qualified clean-fuel (e.g., electricity or natural gas) vehicle. The deduction is taken for the year in which the taxpayer places the vehicle in service (for personal or business use). Through 2003, the deduction is as much as $2,000 for qualifying autos (higher dollar amounts apply to buses, trucks and vans with a gross vehicle weight rating greater than 10,000 pounds). For hybrid vehicles (those propelled by clean-burning fuel and other fuel), only the incremental cost of allowing clean-burning fuel to be used qualifies for the deduction. The IRS recently explained that buyers may rely on a manufacturer's certification of this incremental cost for vehicles propelled by both a gasoline internal combustion engine and an electric motor that is recharged as the vehicle operates. Once certification is established, the IRS says the deduction would apply not only to tax returns for tax year 2002, but also for the previous two years for which such hybrid vehicles were available. The IRS advises taxpayers to file an amended return in order to claim the deduction for a previous year.

TAXPAYERS GIVEN MORE TIME TO GET QUICK REFUNDS FROM NEW 5-YEAR NOL CARRYBACK

Before the Job Creation and Worker Assistance Act of 2002 (JCWAA) was enacted, an NOL (net operating loss) generally could be carried back two years and carried forward 20 years. The JCWAA increased the two year carryback period to five years for NOL's arising in tax years ending in 2001 or 2002. It also allowed a taxpayer to irrevocably elect to forgo the five-year carryback period and instead carry the NOL back 2 years and forward 20 years. The IRS announced it is giving some taxpayers more time to elect the new 5-year net operating loss (NOL) carryback, claim a quick refund as a result of it, and make and undo NOL elections which otherwise would have been barred. The extended deadline for taking action is October 31, 2002.