RECAP OF SIGNIFICANT DEVELOPMENTS THAT OCCURRED IN THE THIRD QUARTER OF 2005

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 for more information about any of these developments and what steps you should implement to take advantage of favorable developments and to minimize the impact of those which are unfavorable.

- **New energy tax breaks**.

  On August 8, 2005, the "Energy Tax Incentives Act of 2005" was signed into law. It contains $14.5 billion in tax incentives designed to improve energy production, transportation and efficiency. These tax breaks generally first apply in 2006 and include tax credits for:

  - Builders to construct energy efficient homes (plus deductions to design and build energy efficient buildings);
  - Individuals to make energy saving improvements to their residences;
  - Individuals to buy vehicles powered by alternative fuels;
  - Manufacturers to make energy saving dishwashers, clothes washers and refrigerators; and
  - Businesses to buy fuel cell power plants and microturbine power plants.

  It also has a host of tax incentives designed to stimulate the production of energy, particularly from alternative sources. These include accelerated write-offs for expenses and new and expanded tax credits for producers.

- **Legislative and administrative Hurricane Katrina tax relief.**

  On September 23, 2005, the Katrina Emergency Tax Relief Act of 2005 ("KETRA") was signed into law. It contains a number of tax breaks for victims of Hurricane Katrina, some for relief workers, and a few for charitable-minded individuals all across the country including:

  - Eased rules for IRA and qualified retirement plan distributions,
  - Eligibility to take a larger loan from a retirement plan without adverse tax consequences,
  - A credit for hiring workers who are victims of Hurricane Katrina,
  - Eased limits on deductions for casualty and theft losses,

- A limited exemption for housing Katrina victims,
- Eased charitable deduction limits,
- Increased cents per mile deduction for charitable use of an auto,
- Increased deductions for charitable contributions of food and book inventory,
- Opportunity to use income from last year to achieve larger earned income and child credits for this year,
- Longer replacement period for deferring gain on involuntarily converted property, and
- Extension of IRS-extended deadlines and deadlines for deposits of employment and excises taxes through February 28, 2006, for affected taxpayers.

This legislative relief is in addition to numerous tax-related deadlines which have been extended by the IRS acting alone or in concert with other governmental agencies, such as the Department of Labor.

- **Taxpayers lose in an important family limited partnership (FLP) case.**

Individuals sometimes transfer assets to an FLP in the hope of achieving large estate tax discounts for the assets which would not otherwise be available if the assets were retained in outright ownership. The huge discounts, in turn, can result in substantial estate tax savings. However, in order to achieve the desired result, the individual must give up control of the transferred assets or the property will be brought back into his estate under a complex statutory provision. That's exactly what happened in a very important case decided this past summer in the IRS's favor. This case, which started out as *Estate of Strangi* (the individual who created the FLP) and ended up as *Gulig* (his son-in-law and attorney) found that there was an “implied agreement” between Mr. Strangi and his relatives for him to retain possession of the property after he transferred it to the FLP. This case, which is famous in estate planning circles, shows what not to do when structuring an FLP to achieve estate tax savings.

- **New form for qualified vehicle donations.**

Under new rules which first apply for post-2005 contributions, the deduction for “qualified vehicles” (motor vehicles, boats and planes which aren't inventory or held for sale in the ordinary course of business) contributed to charity for which the claimed value exceeds $500 is dependent on the charity's use of the donated property. If the charity sells the vehicle without any “significant intervening use” or “material improvement,” or transfers it to other than a needy person at a price significantly below fair market value in furtherance of its charitable purpose, the donor's charitable deduction can't exceed the charity's gross proceeds from the sale. The IRS has released new Form 1098-C, Contributions of Motor Vehicles,

Boats, and Airplanes. Donee organizations must use Copy A of this form to report donations of qualified vehicles with a claimed value of more than $500 to the IRS. In addition, they can use Copy B and C of the form to provide a contemporaneous written acknowledgment to donors, who must attach Copy B (or any alternative acknowledgment provided by the donor) to their Federal income tax return in order to claim a charitable deduction for such qualified vehicle donations. Copy C can be retained by the donor.

- **Standard mileage rates increase for last four months of 2005.**

  In response to the high cost of gasoline, the IRS increased the standard mileage rates for business use of an auto to 48.5¢ a mile for business miles driven between September 1, and December 31, 2005. This is 8¢ a mile more than the 40.5¢ per mile rate that applies for business miles driven between January 1, and August 31, 2005. The IRS also increased the standard mileage rate for computing deductible medical or moving expenses to 22¢ a mile for miles driven between September 1, and December 31, 2005. This is 7¢ a mile more than the 15¢ per mile rate which applies during the first eight months of 2005.

- **Open assessment period for some responsible persons.**

  The IRS recently asserted a "responsible person" liable for the trust fund recovery penalty is subject to the same assessment period which applies to the employer's return. Thus, where the employer has committed fraud, willfully attempted to evade tax, or failed to file an employment tax return, an unlimited assessment period applies to the responsible person. Due to the enormous potential for substantial liability, anyone who is responsible for collecting, accounting for and paying payroll taxes (e.g., officers, directors, accountants or shareholders) must be constantly vigilant the proper employment taxes are paid. This is especially so under the recent IRS position which, if sustained, will continue the period of exposure indefinitely in a good number of cases.

- **Increased S corporation compliance.**

  The IRS announced the launch of a new study to assess the reporting compliance of S corporations, which have grown significantly in number in recent years. The study will examine 5,000 randomly selected S corporation returns from tax years 2003 and 2004.

- **More guidance and new form for repatriation of foreign earnings.**

  The IRS issued more guidance and released Form 8895 (One-Time Dividends Received Deduction for Certain Cash Dividends from Controlled Foreign Corporations) for U.S. companies planning to repatriate earnings from overseas subsidiaries at a reduced tax rate which is available through a special dividends received deduction for a single tax year.

- **Advance look at some of next year's tax figures.**

  Inflation data which is finalized each August is used by the IRS to compute the following year's standard deductions, exemptions, tax brackets and other key items. While the IRS has not yet released its “official” computations (it has until December 15 to do so), a reputable publisher of tax law information has calculated the figures for 2006. It has determined, among other items, the standard deduction will increase to $10,300 for joint filers and $5,150 for singles and separate filers (from $10,000 and $5,000 for 2005) and the personal exemption will rise to $3,300 (from $3,200 for 2005). The income levels at which high income taxpayers lose exemptions and deductions also will increase for 2006. However, under a law change which goes into effect next year, a taxpayer will only lose two-thirds of the exemptions and deductions he would otherwise lose under these rules. On the education front, for 2006, the Hope credit will be 100% of up to $1,100 (up from $1,000 in 2005) of qualified higher education tuition and related expenses plus 50% of the next $1,100 (up from $1,000 in 2005) of such expenses. There also is good news for gift givers - the gift tax annual exclusion will increase to $12,000 from $11,000.

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