

PENNSYLVANIA ACCOUNTANT

THE MAGAZINE OF THE PENNSYLVANIA SOCIETY OF TAX & ACCOUNTING PROFESSIONALS

[WWW.PSTAP.ORG] FEBRUARY 2015

68TH ANNUAL MEETING

June 18-21, 2015

Mohegan Sun at
Pocono Downs - Wilkes Barre

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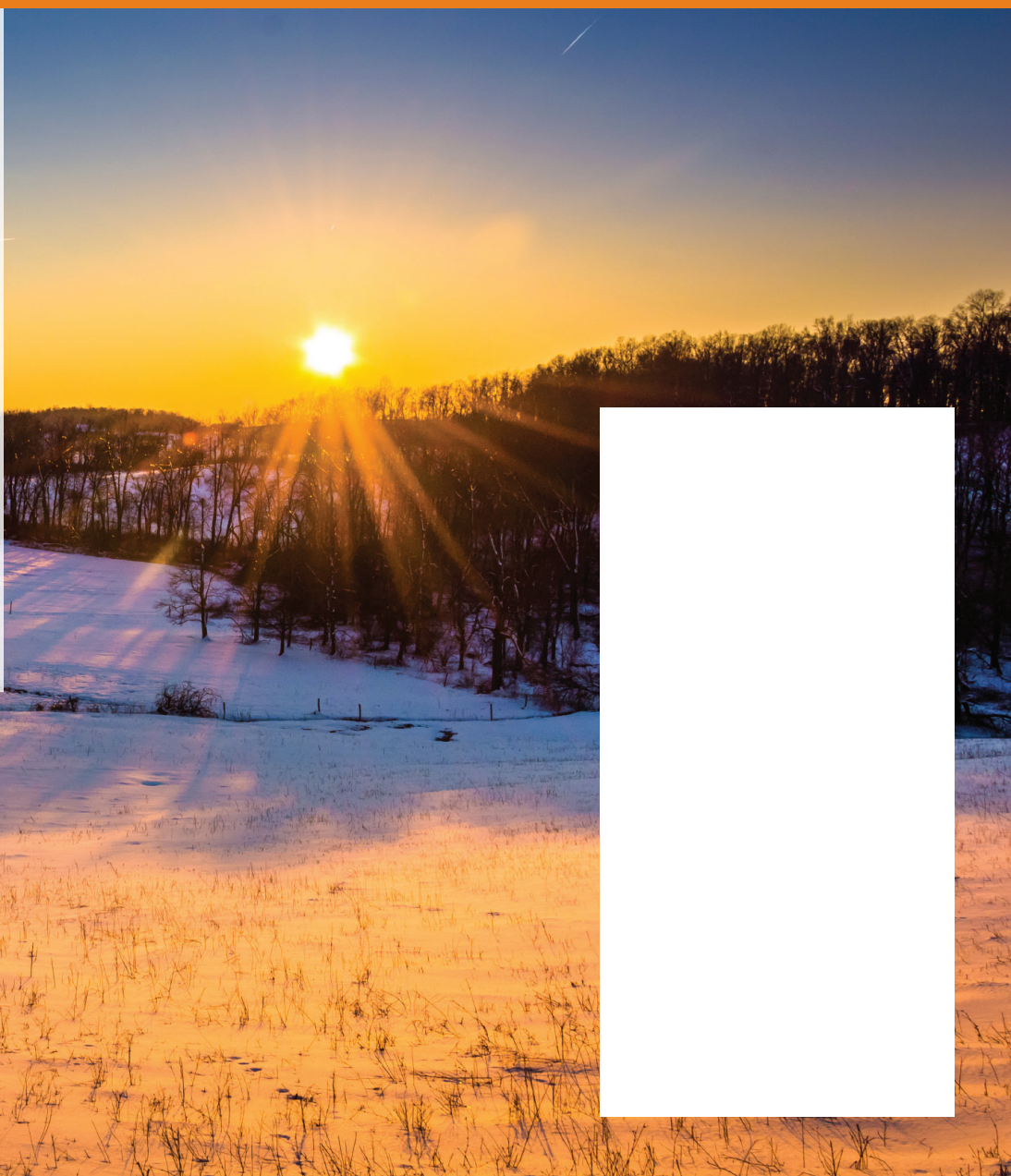
PSTAP's 1st Annual Practice
Management Retreat

June 17 & 18, 2015

Mohegan Sun at
Pocono Downs - Wilkes Barre

PA DEPARTMENT OF REVENUE

2014/2015 Q&A Meeting
Transcript Inside This Issue



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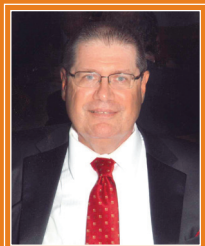
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Pennsylvania Society of Tax
& Accounting Professionals
20 Erford Road, Suite 200A
Lemoyne, PA 17043
1 (717) 737-4439
1 (800) 270-3352
www.pstap.org

A MESSAGE FROM THE PRESIDENT



I hope this message finds each of you in the midst of a healthy and prosperous 2015 as we embark on what is sure to be another challenging tax filing season.

It is already the half way point of my term and I have managed to visit most of the Chapters. I really enjoyed meeting members both old and new. All Chapters were terrific hosts and I extend my thanks.

working with our lobbyist and staff to explore potential legislation for the organization to pursue. I invite you to contact the PSTAP Executive Office and speak to our Executive Director, Sherry DeAgostino if there is a legislative issue that you think PSTAP should pursue for the benefit of our members.

PSTAP members will soon be introduced to a new listserv/email discussion group. I would like to thank Mary Lew Kehm, CPA (Lehigh Valley Chapter) for her work as the Chair of the Technology Committee. We will continue to make changes and upgrades to our website in

Chapters had another successful Seminar Season and the State sponsored seminars with the Pennsylvania Department of Revenue were very well attended and more locations are scheduled to be added.

I would like to extend an invitation to all members to attend the Annual Convention to be held at the Mohegan Sun at Pocono Downs in Wilkes-Barre, PA from June 18-21 2015. The committee is planning a good time for all around the necessary business meetings.

I REALLY ENJOYED MEETING MEMBERS BOTH OLD AND NEW. ALL CHAPTERS WERE TERRIFIC HOSTS AND I EXTEND MY THANKS.

ON THE STATE FRONT:

We had a very successful annual Q&A meeting with the Pennsylvania Department of Revenue. Committee Chair, Richard Kelly, CPA (Southeast Chapter) did an outstanding job at bringing your concerns before the Department. The meeting transcript with all of the questions and the corresponding answers from the Department of Revenue are included in this issue of the Magazine.

We conducted an Enrolled Agent Review Cram Course this winter, and our pass rate among the attendees has been excellent. Frank Kelly, EA (South Central Chapter) was the course facilitator and he did an outstanding job. We plan to offer another review course in the spring. Our Legislative Committee is currently

the coming months, and I applaud the efforts of Frank Cellini, EA (Southeast Chapter) for his guidance throughout this project.

Our Committee on Cooperation with the Internal Revenue Service continues to do a great job in sometimes difficult situations. Paul Cannataro who serves as Chairman of NSA Federal Tax Committee keeps us informed on what is happening on the National front.

The State continues to implement the ideas of the long Range Planning Committee.

Our membership continues to grow thanks in large part to our membership committee, Chairman Richard Brasch and our Executive Director Sherry DeAgostino.

We are also planning a Practice Management Retreat to be held on June 17th preceding the convention at the same location.

Remember the Executive office is always available to help and serve members. They certainly make my job as President a lot easier.

Best wishes for a successful tax season.

Respectfully Submitted,

A handwritten signature in dark ink, appearing to read "Neil C. Trama".

Neil C. Trama
PSTAP President

ANNOUNCEMENTS, UPDATES AND GENERAL INFORMATION

PSTAP 68TH ANNUAL MEETING

Mark Your Calendar & Plan to Join Us in Northeastern Pennsylvania!

June 18-21, 2015

Mohegan Sun at Pocono Downs - Wilkes Barre, PA

Priced Right at Just \$900 per couple!

(fee includes 3 night hotel stay from June 18-20, 2015, 3 dinners, three breakfasts, cocktail reception, group activities, admission fees and entertainment, welcome gift and all taxes and gratuities.)

This year's annual meeting venue, **The Mohegan Sun at Pocono Downs**, is one of the most distinctive and spectacular entertainment, gaming, shopping and dining destinations in Pennsylvania... all under one roof. Situated on 400 acres near Wilkes Barre, Pennsylvania, it features a 238-room hotel with a luxurious on-site spa, a beautiful state of the art pool, a convention center as well as 82,000 square feet of gaming space including 87 live table games, 2,300 slot machines, electronic gaming tables and live harness racing.

Additional details and registration information will be posted on our website within the next 6-8 weeks.

1ST ANNUAL PRACTICE MANAGEMENT SEMINAR

Retreat with PSTAP to Grow Your Practice and Move it Forward

June 17-18, 2015

Mohegan Sun at Pocono Downs - Wilkes Barre, PA

This new event is being held the day preceding the start of PSTAP's 68th Annual Meeting. An all-star team of industry experts is being convened and will present 12 hours of practical CPE designed for principal owners. Break-out sessions will allow attendees to choose the segments most applicable to his/her firm.

Topics & Speakers Are Still Being Developed, but here is what we have so far:

- Trends in Billing/Pricing/Collections
- Technology: Software & Applications
 1. Microsoft Tips and Tricks
 2. Windows 10 & the Next Generation of Office
 3. The Cloud

- Marketing Your Practice for Growth
 1. New standards of client care - how to make your clients raving fans
 2. Promotional Marketing - how to develop referrals through constant contact, seminars, lunches, webinars, direct mail, collateral material and phone contact
 3. Social Media Marketing - how to use linked-in, Facebook, Twitter, Yelp to drive your marketing and get people to your website.
- Practice Continuation & Succession Planning
 1. Succession Planning For Success
 2. Valuing an Accounting Firm
 3. Partner Agreements that Protect the Firm
 4. Succession Options
- Employment Law for Small Firms
 1. Compliance Pitfalls All Small Firms Should Know
 2. Hiring and Firing and Everything in Between
 3. Employee Management

Additional information including pricing as well as a list of speakers and the course agenda will be posted on our website in the coming weeks. **SAVE THE DATE - YOU WON'T WANT TO MISS OUT ON THIS IMPORTANT INFORMATION.** Let Us Help YOUR firm succeed!

CFP CREDIT REPORTING

Those members who requested that CFP credits be reported to the *Certified Financial Planner Board* please be advised that all credits for the 2014 Gear Up 1040, the 2014 Jennings 1040 and the 2014 Business Entities courses were reported before December 31, 2014. Please check your individual account to make sure that the credits have been posted properly to your account. If the credits are not showing on your account please contact our office immediately at 1-800-270-3352.

IRS CPE CREDIT REPORTING

Please be advised that credits for all 2014 PSTAP sponsored seminars and chapter meetings were reported to the IRS on or before January 6, 2015. Credits were reported for ALL attendees of these

courses as long as we have a valid PTIN number. If you have any questions about your credits, the PTIN number that we have on file for you, or the courses that qualified for federal credit please contact our office at 1-800-270-3352.

CPE SEMINAR ATTENDANCE CERTIFICATES


Certificates of completion for all PSTAP CPE events for the 2014 calendar year have been posted to the PSTAP website. If you have not already done so, you can download your certificate(s) using your **'PSTAP ID Number'** and **'password'** and then clicking on the **'CPE History'** link. Your CPE certificates beginning with the 2008 calendar year to present will remain in this location on our website for your future reference. We attempt to have all certificates posted 5-7 days following the completion of each program.

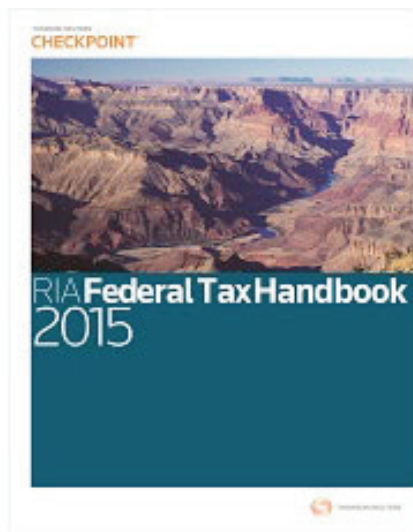
PSTAP EMAIL DISCUSSION LIST (FORMERLY THE PSTAP LISTSERV) HAS A NEW ADDRESS!

Those members formerly subscribed to the PSTAP Listserv have been informed about the change via email and were provided with the new address to use when posting a question to the email discussion group. The new address is: pstap@mail-list.com.

We have changed the hosting company for this very popular member benefit to offer you an improved user experience. Members are subscribed to receive each individual email by default, but the new software will allow you to personally change your status to receive the daily digest if that is your preference simply by clicking on the bottom of any message. You can also choose to suspend delivery for a period of time (vacation mode) or change your email address to which the email discussion list thread is sent.

If you are not currently subscribed to the listserv, subscribe today by sending an email to: pstap-on@mail-list.com.

This is a great tax season resource - Join Us Today! 



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PSTAP COMMITTEE ON COOPERATION WITH THE PENNSYLVANIA DEPARTMENT OF REVENUE

ANNUAL Q&A - December 9, 2014

DEPARTMENT OF REVENUE KEY PERSONNEL

Acting Secretary of Revenue	Eileen McNulty	(717) 783-3680
Chief Counsel	Gretchen Wisehart	(717) 787-1440
Communications Office	Elizabeth Brassell	(717) 787-6960
Legislative Liaison Office	Vacant	(717) 787-1007
Lottery	Silvan Lutkewitte	(717) 702-8009
Taxpayer Advocate	Marva Patterson	(717) 772-9347
Integrated Tax System (ITS)	Donald Sheridan	(717) 783-9566
Voluntary Disclosure Liaison	Alicia Danner	(717) 787-9832
Business Trust Fund Taxes	Thompson Young	(717) 783-5470
Corporation Taxes	Tom Bordner	(717) 787-8211
Individual Taxes	Meggan Swisher	(717) 787-8346
Motor Fuel Taxes	Jim Dehnert	(717) 783-9191
Taxpayer Service & Information Center	Don Bianchi	(717) 772-9201
Deputy Secretary for Administration	Charles Erdman	(717) 783-3691
Administrative Services	Pam McGranahan	(717) 787-8293
Fiscal Management	Melanie Rhine	(717) 787-6737
Human Resources	Linda Miller	(717) 787-7315
Imaging & Document Management	Bernard Stakem	(717) 787-8117
Deputy Secretary for Compliance & Collections	Robert Coyne	(717) 783-3690
Collections & Taxpayer Services	Thomas Scott	(717) 787-6611
Compliance	Mary Hubler	(717) 787-3847
Criminal Tax Investigations	Anthony Beccone	(717) 783-9685
Pass Through Business Office	Suzanne Leighton	(717) 346-0018
EPAD	Kevin Milligan	(717) 783-5571
Deputy Secretary for Tax Policy	C. Daniel Hassell	(717) 787-4099
Audits	Jason Weimer	(717) 783-1731
Board of Appeals	Lauren Zaccarelli	(717) 783-3664
Research	Amy Gill	(717) 787-6300
Chief Information Officer	Robert Donaldson	(717) 772-1731
Information Systems	Ron Wilt	(717) 787-2300

1 As you are aware, there was much confusion and unrest among the practitioner community regarding PA Department of Revenue's policy change as it pertained to unreimbursed employee expenses this year. In many cases, the deduction was not worth the administrative burden/cost to the taxpayer to respond and provide additional documentation to obtain the deduction.

a. Please address this issue, the background for the policy change and how the Department plans to handle these expenses in the future.

ANSWER

As part of the recently implemented Refund Fraud Project, the Department placed additional efforts on the review of all refund returns including those that included deductions for unreimbursed employee (UE) business expenses (Attachment B). Through new analytical measures that identify fraudulent and erroneous filings, the Department is making improvements in sending accurate refunds to only their rightful owners.

Department personnel, during the review of selected returns, either denied in whole or in part the expenses claimed or requested additional information to substantiate the type and the amount of the expenses being claimed. The larger effort is improving our return selection process so that tax examiners are looking at returns more likely to be fraudulently or erroneously claiming refunds and then manually or stopping those refunds. This is not a policy or procedure change, we're simply improving our flagging capabilities, looking at more suspicious refunds and making adjustments accordingly.

In an effort to address the concerns raised from taxpayers and various professional organizations:

- The Bureau of Individual Taxes (BIT) will improve the notices that are issued to taxpayers with the goal of providing a better explanation of the exact adjustment that was made, as well as more details on how to respond to the notice.
- A review of the criteria used to select accounts for examination of UE expenses is being done to reduce the number of accounts suspended for occupations that should have allowable expenses.
- Additional education on allowable UE and areas that accountants should be

cognizant of is being provided during the PIT portion of the Fall Tax Seminars.

- Review of the FAQ's regarding UE has been done to insure that additional details are added regarding disallowance of certain expenses and documentation that should be provided to substantiate those expenses.
- BIT is planning to only utilize seasoned tax examiners to review certain UE suspended returns this processing season instead of temporary staff which will lessen the amount of erroneous adjustments being made. Prior to the start of the upcoming processing season, additional UE focused training will be provided to those staff members who are designated to review these suspensions.

b. Does Pennsylvania have a Taxpayer Bill of Rights (similar to IRS Publication 1)?

ANSWER

Handout provided at the meeting is the Pennsylvania Taxpayers' Bill of Rights.

c. Upon responding to notices with supporting documentation, in some cases it took more than 8 weeks to receive anything back from the Department. With all of the cuts etc., is this policy a good use of the Department's limited resources based on the fact that many of the expenses were approved in prior years?

ANSWER

The Department did experience a backlog in reviewing correspondence this tax season as in previous years. However, steps were taken to expedite review of correspondence during the year and measures have been taken to ensure we do not have as large of a back log in the review of correspondence during the next tax season.

c. Do you have comparative annual statistics about how much revenue was generated this year vs. prior years as a result of the policy change?

ANSWER

As part of the new effort, the Department adjusted (either partially or wholly), 58,283 refunds totaling \$11 million in savings.

e. As an organization we like to think that we have established a

good working relationship with the Department. Any communication/information that can be shared prior to such a drastic policy change benefits both the Department and the practitioner community and ultimately the taxpayer. We welcome this communication regarding issues such as this that we can in turn disseminate to our membership.

ANSWER

The Department understands your concerns and will communicate issues and changes so that there is appropriate time to disseminate to your membership.

f. Is it possible for the Department to provide a Pennsylvania vs. Federal comparison for UE expenses that could be made available on the website?

ANSWER

The Department has created additional FAQ's (Attachment B) to address confusion over what are allowable UE expenses. While it is not a comparison of Pennsylvania (PA) vs. Federal, the FAQ's do provide guidance to taxpayers on what is acceptable for PA. The Department will research the feasibility of adding comparison information to the web site.

2 Does the Department of Revenue have any new audit initiatives and/or policy changes that will go into effect this year that practitioners/taxpayers should be aware of? Once again, if there is any information that can be distributed to the practitioner community regarding such initiatives/changes please advise us. The IRS does communicate various audit initiatives to their stakeholder groups which assists collection and implementation.

ANSWER

Effective November, 2014, Pennsylvania joined the Multistate Tax Commission (MTC) joint income tax audit program for corporate net income and capital stock/foreign franchise taxes. In addition to many other functions, the MTC serves as an operating arm for 24 states which are currently participating in the Income Tax Audit program.

The MTC is an intergovernmental state tax agency working on behalf of states and taxpayers to administer tax laws that apply to multistate and multinational

enterprises. The MTC was created in 1967 as a result of the Multistate Tax Compact, the Commission is charged by this law with:

- Facilitating the proper determination of State and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes;
- Promoting uniformity or compatibility in significant components of tax systems;
- Facilitating taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration;
- Avoiding duplicative taxation.

Participating states pool their resources to select candidates for corporate tax audits. The Commission's audit staff will perform the audits as if they were part of Pennsylvania's own audit staff and forward their findings and recommendations to Pennsylvania for assessment at the completion of the audit. Participating states maintain control of the program through selection of the audit candidates, providing guidance on key issues, and independently deciding whether to act upon audit results.

An audit of a consolidated group will be completed on a separate company basis thereby broadening the Department's ability to ensure compliance with the laws and regulation of the Commonwealth. A significant benefit of the joint audit program is that a single MTC audit takes the place of separate and duplicative audits by member states, thereby providing obvious economies of scale to the states. This program will also reveal inconsistent reporting to different states by multistate taxpayers. Taxpayers benefit from a MTC joint audit in that it relieves them of the burden of multiple ongoing audits by individual states.

The Pass Through Business Office will be starting a sales and use tax desk review program. Initially, the Office will focus on nonfilers for sales tax and potential underreporters for use tax. Eventually, the program will expand to sales tax underreporting.

3 If a divorce agreement/QUADRO allows for the spouse to receive 1/2 of taxpayer's 401K and then the spouse withdraws some of the money, is her basis 1/2 of the taxpayer's basis for Pennsylvania?

ANSWER

Income from a 401K is always the income of the account owner spouse even if a divorce agreement or QUADRO provides that the other spouse gets some or all of it. Any distribution from the 401K is a distribution to the 401K account owner spouse even if the money goes to the other spouse. The account owner spouse must report the income from any distribution. The account owner spouse gets to use cost recovery for any distribution.

4 Does PA have a back-up withholding requirement? If so, are we required to withhold back up withholding for a foreign resident or corporation, if so at what rate?

ANSWER

Pennsylvania has no provisions for backup withholding.

5 In August 2014, *Notices of Assessment* were sent to business entities that previously timely electronically filed the 2013 RCT-101 and were subject to Corporate Net Income tax. The liability indicated on the notices is exactly double the actual tax liability per return. Why is this systematic return processing error occurring?

ANSWER

The errors were primarily due to minor programming glitches and user error. Both have been addressed and corrections have been made to many accounts. If you experience this issue please contact the Bureau of Corporation Taxes Accounting Division at (717) 705-6225 or via email at: RA-RVNOTICEOFADJUSTM@pa.gov.

6 Why would PA Department of Revenue increase the PA wages to Medicare wages when the W-2 clearly shows what the amount of PA wages? This is also occurring with part-year residents (those who moved into PA from another state). Why is the Department not asking for wage reconciliation documentation before assessing extra tax for the part-year resident?

ANSWER

The department's normal procedures for compensation verification is to use the

information on the W-2 to reconcile the wages between federal and state wages using information provided on the W-2. When the information is not present on the W-2 the department's normal procedures are to adjust the wages to the Medicare wages. Beginning with the 2012 tax year, our normal procedure was to adjust the wages without requesting the reconciliation document. For 2013 tax year, there were significantly more taxpayers (including nonresident taxpayers) where this adjustment occurred as a result of our work with Revenue Solutions Inc.

Although the Department did not send a letter requesting the information after receiving the returns, the department has provided notice that the W-2RW is needed if the Medicare wages are greater than PA wages for several years in the PA-40IN booklet and by covering the issue during discussions of the most common errors with individual returns during one or more Fall Tax Seminars.

In an effort to reduce the number or notices that may need to be sent for 2014 tax year, the department is making the W-2 RW Reconciliation Worksheet an optional part of its electronic filing specifications for 2014 electronically filed returns. It is recommended that preparers contact their software vendor to determine if that document will be supported in their software packages.

7 In a prior year a taxpayer qualified and received a PA property tax rebate. However, due to a recent IRS notice it was discovered that income from a Form 1099 was previously not included in the taxpayer's taxable income. With the inclusion of the Form 1099 income, the taxpayer's income for rebate purposes would now exceed the maximum \$35,000 limit. Please advise as to the best way to handle this situation.

ANSWER

A letter of explanation should be submitted along with the supporting documents that reflect the additional income. A payment can be remitted along with this letter made payable to the PA Department of Revenue or if the claimant is unable to pay the balance in full, contact information should be provided so payment arrangements can be established. The letter should be mailed to:

PA Department of Revenue
Property Tax/Rent Rebate Division
Attention: Anita Bullock, Division Chief
P.O. Box 280600
Harrisburg, PA 17128-0600

8

Why is the Department of Revenue delaying refunds for clients that

have had PA income tax withheld on IRA or pension distributions which were withheld in error? Practitioner reports that he has had five clients where refunds were delayed for a period of time exceeding 6 months. The practitioner received a letter from the Department of Revenue requesting copies of the 1099Rs and W-2s to verify the tax withheld. Once the requested information was submitted by the practitioner it took the Department 6 months or longer to process the refund.

ANSWER

The department requires alternative procedures and documentation whenever tax is withheld on income that is generally not taxable for PA personal income tax purposes such as retirement pay. These steps are taken to attempt to prevent fraud on the amount of tax withholding being claimed. In prior years, the department has discovered cases where the tax withheld claimed by a taxpayer was not paid to the department by the payer listed on the 1099-R. Therefore, the department requires an actual copy of the 1099-R provided to the taxpayer by the payer be included with the e-filed return via DEX-93 or attached as a pdf file. In addition, the department can request verification of the payment by the payer with the Bureau of Trust Fund Taxes. In some cases, these additional steps require more time.

If a return is received without the information, the department must make a request for that information. If the response to the request for the 1099-R is provided to the department via a letter received by U.S. Postal Service, there are multiple other factors that can further delay a refund of the taxes withheld. If a response to a notice is received via DEX-93, the department is able to provide a more timely review of the correspondence it receives.

9

Will the Department of Revenue continue to accept the federal 15% depletion expense against natural gas royalty income?

ANSWER

PA PIT law does not include a provision for the allowance of percentage depletion. Although the department does have a regulation (125.51) allowing percentage depletion, most taxpayers cannot meet all the specifications of the regulation. The department does allow cost depletion. However, the owner of the property has to be able to clearly show that the cost of the mineral rights for the property were included by separate allocation of the total purchase price of the property and that a study has been conducted to determine the amount of the reserves.

The department is focusing resources on accounts where expenses against royalty income for the 15% percentage depletion deduction. In addition, the department has noted in its examinations of the depletion expense issue that many taxpayers are also including non-deductible surface rights expenses such as interest, real estate taxes, cleaning and maintenance and travel.

10

Why does the system reject corporation extensions filed under Etides when entered on the 15th of the month?

ANSWER

E-Tides does not reject extensions on the 15th. If there are any instances where the taxpayer is unable to make an extension payment on the 15th of the month, it is most likely because of their fiscal year history in the ITS. We have over 500 extension requests in e-Tides with the date filed occurring on the 15th of a month for 2014 alone. I would suggest if a taxpayer is not able to make an extension request on the 15th of the month that they call into the Bureau of Corporation taxes and have their fiscal year history reviewed and corrected/changed as needed.

11

If you own a vacation home (original cost of \$300k) and sold it for \$500k, can the basis of this property be increased by mortgage interest and property taxes paid?

ANSWER

Personal income tax does not allow for adjustments to basis for mortgage interest and property taxes paid.

12

Practitioner each year files partnership returns which happen to have investments in many other partnerships; some of the partnerships issue PA RK-1s and some do not. For the last 3 years, the practitioner/taxpayer received a PA Department of Revenue *Notice of Adjustment*, but the notice offered no explanation on the adjustment that was made by the Department.

Practitioner is referred to the 'pass through unit' when contacting the Department of Revenue where he provides various documentation, letters, schedules in order to obtain a spreadsheet of the K-1s. Upon reviewing the information on the spreadsheet, the practitioner discovers that the changes are not from the K-1s where there was no PA RK-1, but rather, the Department of Revenue used the Federal K-1 in lieu of the filed PA RK-1, because they did not believe the PA RK-1 as filed, was accurate.

Practitioner questioned the Department of Revenue employee regarding how they can simply change figures without an audit or even making any further inquiry back to the practitioner or taxpayer and was told that "they don't have the resources to perform those procedures". In every case, the filed PA RK-1 had lower figures because of the *Keystone Opportunity Zone*, which was properly disclosed with the filed returns. Eventually the state reversed its position on the adjustment.

a. Is it really the policy of the Department of Revenue for the pass-through unit to change figures on a filed PA RK-1 without audit or question, simply because they believe it is incorrect because it doesn't match the federal form?

ANSWER

No, this is not the policy of the Department nor of PTBO. Act 52 of 2013 states that the individual owner of a pass through entity must report income on their PA-40 consistent with the RK-1 or NRK-1.

b. Is there a way that the notices can be improved to provide meaningful information about the specific adjustments that are being made by the Department?

ANSWER

When PTBO adjusts a PA20S/PA-65, a letter is sent to the entity notifying it of the change. This letter is sent prior or at the same time the owner is assessed.

c. Is there some way to communicate with the proper level at the Department of Revenue rather than try to work with a phone operator who struggles at best to handle these complicated matters?

ANSWER

If the caller calls the TS&IC general phone line (717-787-8201) and our agent sees that case was worked by the PTBO, there standard operating procedure is to explain to the caller the situation and transfer the caller to the PTBO. If the case isn't a PTBO item and the adjustment was made by BIT. TS&IC agents will do their best to quickly review any notes or documents with the account and do their best to assist the caller. Please understand that the phone agents are not the one who made the adjustments to the account; they are only customer service representatives that are here to help our customers.

In these situations if the preparer has reviewed the notice/adjustment and determined what has happened. I would encourage them to respond to the notice with a written explanation of the situation and copies of any documents that supports their assertions.

When an analyst in PTBO reviews an entity or individual return, the correspondence they send should have their name and phone number on it. In addition, when the phone unit in PTBO receives a call regarding an analyst case, the call is transferred to the analyst.

If the above described scenario occurs, please call Suzanne Leighton at 717-346-0018.

13 On taxpayers who file a joint return, what is the maximum IRC 179 depreciation allowed?

ANSWER

The maximum Section 179 deduction for PA PIT purposes is \$25,000 on a joint return. See Informational Notice 2012-05 - IRC Section 179 Expense Deductions for more information regarding the limitations and how to apply them to PA personal income tax.

14 If a taxpayer sells a business on a 5 year installment sale for a gain, and the buyer defaults on year 4, how should the taxpayer report the default in year 4 when PA required the full gain to be recognized during the year sold?

ANSWER

PA personal income tax law does not include a claim of right doctrine provision similar to the IRS's provision that permits a loss to be reported in the year of the default. If the statute of limitations is closed on the tax year in which the sale occurred, the taxpayer is precluded from filing an amended return to adjust the sales price. However, if the sale agreement included provisions that a default on the agreement caused the property to revert back to the taxpayer, the taxpayer would be able to adjust their basis in the property for the gain less the default amount plus the tax paid on the gain.

In addition, if the taxpayer had used the cost recovery method to report the gain on the sale of the intangible property which is permitted if the purchase price paid to the seller is paid over more than one tax year, the taxpayer would not have the default issue and subsequent adjustment of sales price as a concern. However, in order to report the sale of property using the cost recovery method, the sales agreement and corresponding note would have to contain clauses that the proceeds for the sale and corresponding note are not assignable (i.e., can't be used as collateral).

15 If an extension is filed by a tax preparer for a client, but the client subsequently has another preparer complete the return and is unable to obtain a copy of the filed extension, can PA determine if a valid extension existed upon e-filing the corporate return?

ANSWER

In cases where a client taxpayer changes tax practitioner(s) and the former possesses documentation that subsequently needs to be filed with the Department such as copy of the Federal Form 7004, 4868, Application for Automatic Extension of Time. However, due to unfortunate situations such document(s) are not made available to the taxpayer or upon request of the new successor tax practitioner, a "Statement/Affidavit" explaining such circumstances

shall be included with the filing of the next ensuing tax report filing affected by the absent document(s).

This statement should be attached in lieu of the normal required FF7004 or 4868 in the proper sequence for paper submitted filings or be made an attachment in "pdf" format as accommodated for electronic filing, or MEF Fed/State e-filing.

In situations as described above, special attention should be paid to insure that the "Extension" Block is properly marked when filing the PA Corporate Annual Tax report(s) ie RCT-101. Failure to properly mark/code the tax reporting instrument, paper or electronic transmission will result in the imposition of "Late Filing Penalties" upon submission of the subject report(s).

16 How are licensing authorities (such as the PLCB) made aware when only a federal extension is granted?

ANSWER

The Department's policy has been to not look for the 2013 corporation tax returns due to anticipated backlogs in their processing. The only way the Department would look for a current year return at this point is if it involved a special credit such as KOZ, KIZ, NIZ, R & D, REAP and Film Credits.

17 What are the new late filing penalties for business entities and who are affected by them?

ANSWER

For tax years beginning on January 1, 2014 or after, Act 52 of 2013, imposed a \$500 penalty plus an additional 1% for every dollar of tax determined to be due in excess of \$25,000 for the failure to file a corporate tax return.

18 If a Single Member LLC converts to an S Corporation, does the 5 year earnings history carryover?

ANSWER

61Pa. Code § 155.26 (f) reads as follows (emphasis added):

Average net income does not include net income or loss of the corporation for a period of time prior to incorporation, such as net income or loss of a partnership prior to incorporation.

Net income or loss of a predecessor corporation may not be attributed to a successor corporation. In the case of a mere change in identity, form or place of organization of one corporation, net income or loss prior to the change shall be utilized in determining average net income. Net income or loss may not be adjusted in the event of a change in corporate structure, but to the extent that a change occurs as a result of a tax evasion motive, net income or loss may be adjusted to negate the effects of the change in corporate structure. The following examples demonstrate the application of this subsection with respect to mergers, consolidations and reincorporations. Where there is evidence of a tax evasion motive, average net income will be determined based on the substance of the transaction.

This is a change in form so the history of earnings will continue.

19 If ABC Inc was a PA S Corporation that owns an interest in a PA LLC taxed as a partnership, and subsequently the owner moved to another state, would ABC Inc become a foreign corporation exempt from CS/FF because the only PA activity is in owning part of a PA LLC?

ANSWER

Unless ABC, Inc. reincorporates in a different state, it is still a domestic corporation.

20 If a parent company and its subsidiary file separate PA corporation returns, and the parent company dissolves and passes its assets to its subsidiary, can the subsidiary continue to exist or must a new company be created?

ANSWER

The subsidiary is a separate company from the parent. As long as the subsidiary continues to operate under that corporate charter, it is no necessary to form a new corporation.

21 Does Pennsylvania recognize a *Foreign Earned Income Exclusion* (Similar to IRS Form 2555) for military personnel who live abroad for 330 days or more in a calendar year?

ANSWER

No. The only exemption PA has is that "compensation" does not include income derived from the US Government for active duty outside the Commonwealth as a member of the armed forces.

22 If a Pennsylvania resident owns a business incorporated and operating in Maryland, must a PA corporate return be filed?

ANSWER

As long as there is absolutely no business conducted in PA the corporation is not required to file a PA Corporate Tax Report.

23 When PA Department of Revenue leaves a message on an answering machine of a preparer, why is only a return phone number left without identifying taxpayer name, EIN/SSN, and naming individual leaving message or identification number so that a preparer can efficiently resolve issue?

ANSWER

The security of taxpayer information is always a key concern of the Department. Therefore leaving specific taxpayer information on an unknown voice mail is not something the Department will normally do. Since the scenario laid out in this question seems to be in reference to one of our automated (robo) calls. They call back to the number we left, one of our helpful agents can help them out. Also, we don't leave the name of an individual calling, because we don't have case ownership and the person leaving the message is most likely NOT going to be the one who answers if they do as requested and call us back.

In another scenario if a caller leaves a message on our TSIC voice mail. When our friendly and helpful Agents call back and are put into a voice mail, they will leave a message that identifies them, lets the person know we are returning their call. Similarly, if we are calling a preparer back; they will leave a message that identifies themselves and let the preparer know that they are calling back concerning X taxpayer.

24 Has there been an increase in the use of the tax practitioners email hotline from the prior year?

ANSWER

No, actually the use of the Tax Practitioner email has decreased about 34% when compared to the same time last year. 2013 - 202 emails for the year, 192 at this time, vs 127 so far in 2014.

25 Follow up from 2013. We inquired about the possibility of confirmation receipts of information that is requested by and received by the Department as well as confirmation that an issue was resolved. It was indicated on the Department's responses that while this was not in the initial plans, that this would be considered as a suggestion. Please advise of the status.

ANSWER

Though it is acknowledged that this was taken as practical modernization suggestion, the Department is still only partially through developing the required functionality as documented in the original project plan. It is not clear when this functionality will be achieved. For PIT and PTRR individuals and preparers can use our online or automated telephone systems to check on the status of a return.

26 Follow up from 2013. Once again, we are very interested in working with the Department to identify an appropriate threshold for a standardized installment payment agreement. It was indicated on the Department's response that *"several technical issues would need to be discussed and resolved prior to the deployment of a self-service deferred payment plan (DPP). Much of it will hinge on how sales, employer, and personal income taxes are integrated into the ITS."* Can you provide an update on this issue?

ANSWER

The department remains committed to expanding self-service options for taxpayers. This includes the ability to create a DPP via the department's website. The department has not finalized the exact parameters for a self-service DPP. However, in general the department would follow what other state revenue departments have instituted as parameters. For example, a taxpayer that owes less than \$5,000 and is able to make a 20% down payment and then have six installment payments via either an automatic withdrawal from a bank account or a reoccurring credit card

charge would most likely be able to set up this DPP online. Assuming timely payments are made, no follow-up collection action would be required by the department with the taxpayer regarding the delinquent account. Again, no final decisions have been made regarding the parameters.

Resource limitations at this time do not allow the department to provide an accurate estimate as to when a self-service DPP would be functional. The department is finalizing plans for the next self-service option for taxpayers from a compliance perspective, which will be online lien certificate requests. The department receives almost 20,000 lien certificate requests per year and automating this process will make the department more efficient. It is anticipated that the infrastructure used to build an online clearance request system will be available for eventual use in administration self-service DPPs.

The department developed several Q&As on deferred payment plans in late April of 2014. However, they have not yet been posted to the department's website. (Attachment C) is a copy of the latest version of the Q&A.

27 Follow up from 2013. This question was regarding e-filed PA 41 and the fact that there were only three software vendors willing to develop a state only software product. It was indicated that once the Department becomes part of the MeF platform fed-state fiduciary e-filing program beginning with the filing of 2014 fiduciary tax returns more software vendors may offer the PA-41 e-filing product. Do you have an update on this?

ANSWER

The Department is currently in the process of testing electronic filing of the PA41 through the Fed/State e-file platform and plan to be in production in January of 2015. The Department has provided software vendors with our specifications and notified them that we are ready for testing.

28 Under an employer payment plan, an employer reimburses or pays health insurance premiums (for an employee's substantiated premiums) directly to the insurance company for non-employer sponsored health insurance.

IRC Section 106 Rev ruling 61-146 excludes the payments from the employee's gross income. The Affordable Care Act states this a group plan and does not meet the market reform and has to be included in gross income now. Are these payments by employers for various employees considered taxable PA compensation?

ANSWER

The payment is taxable as compensation for PA PIT purposes as it considered to be made pursuant to a cash or deferred arrangement under which an employee may unilaterally elect to have the employer make payments to such third party or fund for the benefit of the employee or to the employee directly in cash and it is not part of an IRC Section 125 plan.

WHAT ARE UNREIMBURSED BUSINESS EXPENSES?

Answer ID 3201 | Published 10/28/2014 02:38 PM | Updated 10/28/2014 03:41 PM

A taxpayer may use PA Schedule UE to report allowable unreimbursed business expenses which can be excluded from compensation on Line 1A. For an expense to be allowable, it must meet the following conditions:

1. The **actual** amount paid must be reported. Expenses may not be estimated or guessed.
2. The expenses must be **reasonable**. The amount of expense should not be excessive in relation to income, type of expenditure or purpose of expense.
3. The expenses must be **necessary** for the employee to do the duties of the job. Costs may not be incurred to make the job more convenient for the employee or to make the job more productive.
4. Only **ordinary** expenses are allowable. The expenses must be similar to those incurred by other employees in the same trade or profession.
5. The expenses must be **directly related** to the employee's present trade, business, or profession. Expenses from a previous job or incurred for a future occupation may not be taken as Unreimbursed Expenses.
6. The expenses **must be unreimbursed**. Only expenses for which the employee receives no reimbursement or is only

partially reimbursed may be on a PA Schedule UE.

WHAT ARE ACCEPTABLE DEDUCTIONS ON A PA SCHEDULE UE?

Answer ID 3202 | Published 10/28/2014 02:45 PM | Updated 10/29/2014 03:45 PM

The following is a list of deductions that may be claimed on the PA Schedule UE:

1. Union dues, agency fees, or initiation fees
2. Work clothes not suitable for street wear that are required to be purchased. This includes cleaning, altering, and repairs of such clothing
3. Small tools and supplies
4. Professional license fees, malpractice insurance and fidelity bond premiums where required by law.
5. Travel and mileage
6. Moving expenses into PA; provided the transfer is from one permanent duty station to another and the difference in mileage between the residence and the old duty station and the original residence and the new duty station is 35 miles or more (the 35 mile rule is waived for military residence and their families). The expenses must be limited to those incurred in moving family, self and household goods from point of departure to point of arrival including lodging the night of arrival. Not allowed if moving out of PA and not allowed for non-residents.
7. Educational expenses, if required by law or employer to maintain or improve skills in present job
8. Office work area expenses
9. Miscellaneous expenses such as breakage fees, cash shortages, costs incurred to pay readers for blind employee, business gifts and W-2 fees that must be paid back to the employer such as jury duty where an employer continues full wages and requires repayment of monies received for jury duty

I WORKED FOR SEVERAL EMPLOYERS CAN I JUST COMPLETE ONE PA SCHEDULE UE?

Answer ID 3203 | Published 10/28/2014 02:48 PM | Updated 10/28/2014 03:41 PM

No, a separate PA Schedule UE must be completed for each taxpayer and for each employer and occupation.

WHAT TYPE OF EXPENSES CAN BE CLAIMED ON PART A OF THE PA SCHEDULE UE?

Answer ID 3204 | Published 10/28/2014 03:02 PM | Updated 10/28/2014 03:42 PM

Union dues: An employee may deduct union dues, union initiation fees and assessments when such payments are a condition of continued membership in the union, and membership is related directly to your present job or such payments are a required wage deduction under an agency shop agreement.

Work clothes and uniforms:

An employee may deduct special or protective clothing only when the special clothing is required as a condition of employment and the clothing is not suitable for everyday use. Allowable items include hard hats, special gloves, special shoes, protective goggles, etc. The cleaning, altering and repairs to such clothing would also be an allowable expense.

Small tools and supplies: An employee may deduct small tools when required as a condition of employment but not provided by the employer. Depreciation is the annual deduction you must take to recover the cost of business property having a useful life beyond the tax year. If any of these tools or supplies has a useful life of more than one year, you depreciate or amortize the cost in Part G.

Professional license fees: An employee may deduct these expenses if required as a condition of employment or by law. These expenses include malpractice insurance payments and fidelity bond premiums.

WHAT TYPE OF EXPENSES CAN BE CLAIMED ON PART B OF THE PA SCHEDULE UE?

Answer ID 3205 | Published 10/28/2014 03:03 PM | Updated 10/29/2014 10:27 AM

Regular expenses commuting back and forth to work or from one job to another job **cannot** be deducted on the PA Schedule UE. The expenses listed below should be used when your employer

requires you to travel and you are not reimbursed for any of these expenses.

Standard mileage rate: A taxpayer can use the figure shown on his/her federal Form 2106 or 2106-EZ for these expenses, or he/she can enter the total business miles and multiply by the federal standard mileage rate for the particular year.

Vehicle expenses: Actual Travel and Mileage Expenses: A taxpayer can use the figure shown on his/her federal Form 2106, but should make the necessary adjustment for the inclusion amount. Actual expenses include the cost of gasoline, oil, finance charges, repairs, sales tax, depreciation, etc. If the car is not used exclusively for business, the business percentage must be determined (number of business miles divided by the total miles).

Parking fees, tolls, and

transportation: A taxpayer can take any expenses paid for parking, tolls, or any transportation expenses for buses, cabs, etc. for business use. Travel expenses while away from home overnight: A taxpayer may claim:

1. Lodging and hotel expenses
2. Baggage charges
3. Convention expenses
4. Displays and samples
5. Tips, telephone, telegraph, laundry, etc.

Away from home means away from the employee's place of business, employment or post of duty, regardless of where the employee maintains his residence. These must be actual expenses and the federal per diems are not permitted.

Meals and entertainment expenses:

Meals must be claimed while traveling overnight. Meals cannot be claimed by a taxpayer that is working late and we do not accept the federal per diem rates. A taxpayer may claim entertainment that is ordinary and necessary to the trade of business or profession, and directly related to the active conduct of business or immediately precede or follow the active conduct of the business. Theatre or sporting event tickets may be entertainment if the employee accompanies the business associate, or gifts, if given to the business associate for their use.

WHAT TYPE OF EXPENSES CAN BE CLAIMED ON PART C OF THE PA SCHEDULE UE?

Answer ID 3206 | Published 10/28/2014 03:04 PM | Updated 10/28/2014 03:42 PM

A taxpayer should include the PA allowable expenses that are reported on their federal Form 2106; however, a complete breakdown and itemization of these expenses is required. You cannot just use the figure shown on the federal Form 2106 without itemizing the expenses. Here are some examples of miscellaneous expenses:

1. Breakage fees or cash shortages you must pay to your employer
2. Fees or income included in your PA taxable compensation on your Form W-2 that you are required to pay to your employer as a condition of your employment.
3. Costs incurred by blind employees to pay readers who assist them in performing their job duties.
4. Business gifts that are ordinary, reasonable and actually incurred for business purposes. PA does not follow federal percentage limits on such expenses.

HOW CAN I DETERMINE IF MY OFFICE AND WORK AREA EXPENSES ARE ALLOWABLE EXPENSES ON PART D OF THE PA SCHEDULE UE?

Answer ID 3207 | Published 10/28/2014 03:05 PM | Updated 10/28/2014 03:42 PM

An employee may deduct expenses from their home office only when:

1. The job requires an employee to have a suitable work area.
2. The employer does not provide a suitable work area.
3. The office at home is the principal place of work.

Questions D1, D2 and D3 must be answered yes to qualify for these expenses and you must enter the actual expenses you incurred on Line a through Line h. A statement is required to detail property maintenance and other apportionable expenses from Line f and Line g.

WHAT TYPE OF EXPENSES CAN BE CLAIMED ON PART E OF THE PA SCHEDULE UE?

Answer ID 3208 | Published 10/28/2014 03:06 PM | Updated 10/28/2014 03:42 PM

A taxpayer may deduct moving expenses if the move is more than 35 miles from the old workplace to the new work place. You must continue to work for the same employer to claim this moving expense. You will need to calculate the mileage difference as the change in mileage between the new residence and the old duty station and the original residence and the new duty station. We do not accept the federal Schedule 3903 or 4782.

Allowable expenses:

1. Costs of transporting the employee and immediate family to the new location.
2. Costs of moving household goods if paid directly by the employee.
3. Costs of moving personal belongings and household furnishings, including in-transit storage charges.
4. Travel, meals, and lodging expenses during the actual move from the old home to the new home.

Not allowable expenses:

1. Selling or purchasing a house
2. Breaking a lease or house hunting
3. Securing lodging prior to moving
4. Seeking new employment
5. Moving for your own convenience
6. Relocating to a new job or workplace less than 35 miles farther than your old commute to work
7. Moving anywhere other than within PA

HOW CAN I DETERMINE IF MY EDUCATIONAL EXPENSES CAN BE DEDUCTED ON PART F OF THE PA SCHEDULE UE?

Answer ID 3209 | Published 10/28/2014 03:07 PM | Updated 10/28/2014 03:42 PM

In order to claim educational expenses you must answer yes to the first question listed in Part F.

F1. Did your employer require that you obtain this education or retain your present position or job?

You must answer no to the following questions listed in Part F.

F2. Did you need this education to

meet the entry level or minimum requirements to obtain your job?

F3. Will this education, program or course of study qualify you for a new business or profession?

The name of the educational institution, course of study, the cost of tuition and fees, course materials, and travel expenses must be shown on the PA Schedule UE. A taxpayer may deduct educational expenses only when:

1. The education is specifically required by law or by the employer to keep a job or rate of pay.
2. The education is not the minimum requirement to obtain the job.
3. The education does not qualify the employee for another trade or profession.

PIT PAYMENTS ON ACCOUNT WHEN THE PAYMENTS ARE LESS THAN PAYMENTS IN FULL

I don't have enough money to make the full payment for the amount of taxes due with my PA personal income tax return. Does the PA Department of Revenue have a form similar to the federal 9465, Installment Agreement Request, where I can request to make installment payments for the amount of taxes due on my PA-40 return?

ANSWER

No. The PA Department of Revenue does not have a form that can be filed for establishing an installment or deferred payment plan for payment of taxes due on a return when the return is filed. The department may only establish a deferred payment plan for paying taxes after the taxpayer has been billed, assessed for the taxes and the appeal period for the assessment period has lapsed.

Although no formal plan can be established until the taxpayer's appeal period has lapsed, taxpayers should not wait until that point to make payments

on their tax liability as interest accrues on the tax due through that time period (six to eight months). Taxpayers can always file their returns (returns should always be filed timely), pay what they can at the time of filing and then pay down the amount over the course of time by sending payments to the department as they are able. If a taxpayer is not able to pay the full amount due with their return, a late payment penalty and interest on the unpaid tax amount will also be added to the return.

2 What are the consequences or what is the penalty if I don't make the full payment of taxes due with my return if I file my return without a full payment?

ANSWER

A late payment penalty of 5% of the unpaid tax liability will be added to the amount due for the tax year. In addition, interest on any unpaid tax will accrue as long as there is an outstanding tax liability for the tax year.

3 What are the consequences or what is the penalty if I don't have the money to make the full payment of taxes due with my return and don't file my return until I have the full amount of money to make the full payment?

ANSWER

A late filing penalty of 5% per month or part of a month (up to 25%) will be added to any return filed after the original due date (or extended due date) if additional tax is due with that return. In addition, interest on any unpaid tax will accrue as long as there is tax outstanding for the tax year.

NOTE: It is better to file a return without full payment than to not file a return if full payment of the tax due cannot be made with the return. The minimum penalty in either case is 5%. However, a late filing penalty can be as much as 25% of the unpaid taxes. It is better to file and incur the late payment penalty than to not file and possibly incur a 25% penalty.

4 How do I make payments on my unpaid taxes if I don't have a deferred payment plan?

ANSWER

You should make payments whenever you are able to make them to decrease the amount of interest that accrues on your unpaid tax liability. Payments should be made by making the check or money order payable to the "PA Department of Revenue". You should also write the tax year, PA form number (PA-40 for individual returns) and your Social Security number on the check or money order and mail it to the following address:

PA Department of Revenue
PO Box 280431
Harrisburg, PA 17128-0431

Alternatively, the department will also send taxpayers an initial bill about 30 days after the original due date of the return for any tax return not including full payment of the taxes due. That bill will also include a coupon to make payment of the taxes due on the return. Taxpayers may wish to photocopy the coupon portion of the bill if they will be making multiple payments on their tax liability. By using the coupon, payments

are more likely to be posted to the correct taxpayer's account.

The bill will also include an envelope for sending in the payment to the department. Taxpayers should write this address down for sending in additional payments with the photocopied coupons.

Taxpayers should keep a record of all payments made against their outstanding liability for taxes, interest and penalty as well as the balance for each. A log of the date the payment was made, check number and amount of payment should be kept in the event of a discrepancy between the taxpayer and the department record of payments.

5

How are my payments applied by the department to unpaid tax liabilities?

ANSWER

The department applies payments made by taxpayers in the following sequence: tax, interest, penalties and legal fees. By applying payments in this manner, the

amount of interest that accrues on an outstanding tax liability is minimized if a taxpayer makes regular payments on the outstanding tax liability. In addition, interest only accrues on outstanding tax liabilities. There is no compounding of interest and no interest accrues on penalties. Once a taxpayer pays the tax amount due, interest will stop accruing. Full payment of the penalties and interest can then begin, but the balance due will not increase once full payment of the tax liability is completed (unless payments stop and a lien and lien (legal) fee are added to the balance due).

6

How can I obtain the balance due on my unpaid taxes for a tax year?

ANSWER

Taxpayers can contact the department's Taxpayer Service and Information Center at 717-787-8201 to find out the balance due on their account at any time to avoid overpayment or to make a final payment in the exact amount due. 📞



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THE FINANCIAL REPORTING FRAMEWORK FOR SMALL AND MEDIUM SIZED ENTITIES

RELIEF FOR MAIN STREET

BY ROBERT K. MCCARTT, CPA, MBA



Generally Accepted Accounting Principles (GAAP) are considered the gold standard for financial reporting in the United States. But for years there has been a controversy regarding the application of GAAP to public and private companies. Even a cursory examination of the FASBs pronouncements leaves one with the feeling that these guiding principles were written for the big boys - the Exxon Mobil and the Microsofts of the world.

A common criticism of GAAP by owners and financial managers of privately held companies is that many of the elements of GAAP that apply to public companies are simply too complex or unnecessary and provide little if any decision useful information for their small firms. Let's face it, in many cases we are dealing with small business owners who are still struggling with the distinction between cash and accrual accounting. Trying to explain fully diluted earnings per share to folks of that ilk is like trying to tell a stranger about rock-n-roll. Remember the first time you had to sit down with a small business owner and explain various uncertain tax positions?

The debate has taken the form of a continuing conversation that we have come to know and love as the Little GAAP vs. Big GAAP controversy. In March of 2005 the debate prompted the AICPA to convene a task force to research the issues encountered in private company financial reporting. The task force's report unanimously recommended that processes be established to evaluate GAAP to make it less burdensome to private company financial reporting. In order to address issues identified by the task force the FASB established the Private Company Financial Reporting Committee (PCFRC). The mission of the PCFRC is to help create standards for private companies that will improve the quality and consistency of financial reporting.

The PCFRC was formed in 2008 and in 2010 issued a statement recommending the use of International Financial Reporting Standards for Small and Medium Sized Entities (IFRS for SMEs). IFRS - really? We've just gotten our small business clients comfortable with uncertain tax positions and now they want us to drop IFRS on them. Unless you are practicing in the international arena the very thought of IFRS may make your head explode.

For a variety of reasons, many of them economic, there seems to be little appetite for U.S. adoption of IFRS. The IFRS-GAAP convergence movement began in 2007 but adoption of IFRS by U.S. companies has been postponed a number of times. IFRS tends to be principles rather than rules based like GAAP. Detractors argue that principles based standards provide little guidance or structure for exercising professional judgment by preparers and auditors. Could there be another Enron in our future?

Those of us whose practices focus on the small business community have known for years that "Little GAAP" is an idea whose time has come. Yet our clients continue to deal with the burden and cost of issues that have little or no meaning to them. These are folks who focus on cash flow and have little interest in impairment of goodwill or book to tax timing differences. At the end of the day they want to know if they have enough cash to meet payroll and pay the bills and how much their tax bill is going to be.

The FASB has acknowledged the issues that are of concern to the small business operator, but unfortunately - as with justice - the wheels of remediation at the FASB turn slowly.

Help is on the way.

Denizens of the small business community and practitioners who serve them can rejoice. Help has arrived!

In June of 2013, the AICPA launched the Financial Reporting Framework for Small and Medium-Sized Entities (FRF for SMEs). Designed to ameliorate the financial reporting burden of smaller, privately held, owner-managed businesses, FRF for SMEs is intended for businesses that do not need GAAP-compliant financial statements.

Our first response to this news might be it's about time! After all, we are constantly reminded that small businesses are the job creators and the drivers of economic growth. So, isn't it time that we make it easier to do business for these folks who are going to lead us to the economic promised land? Of course it is. But before you get too excited about this, remember it is one small step toward solving a giant financial reporting problem for Main Street.

Who can benefit and why.

First let's look at an overview of the benefits of the Framework and who the beneficiaries are.

The Framework was designed to be responsive to well documented financial reporting issues and concerns among SMEs. It is intended to provide cost effective, comprehensive and relevant information and it is tailored to suit the financial reporting needs of SMEs and users of their financial statements.

Who can use FRF for SMEs? First and probably most important is that the Framework is designed for entities that DO NOT require a GAAP-based financial statement. More on that later. The Framework is designed to benefit small and medium-sized entities that are owner-managed, for profit entities. It can be used by most industry groups and can be used by incorporated or unincorporated businesses.

About this time you may be asking just what is an SME anyway. The answer to that question is that same as the old



accounting joke that asks what's 2 plus 2 ... Clearly the Framework is intended for privately held companies but there is no quantifiable definition of an SME in the United States.

"I shall not attempt to further describe pornography, but I know it when I see it ...
"Justice Potter Stewart,
(*Jacobellis v Ohio*, 1964)

What can the Framework do for you?

The first step in answering that question is to define the audience for financial statements of an SME. The principal audience and their concerns are:

- **Owner-managers.** Typically this group tends to be the same people. They are concerned with profitability, asset and liability valuation, cash flow, taxes and regulatory compliance
- **Lenders.** Lenders tend not to be terribly concerned about internal controls and risk management. This may be short-sighted but at the end of the day, bankers are concerned that there is sufficient cash flow to service the debt and adequate collateral value in the event of a liquidation.
- **Investors.** Typically this group is looking for a conservative view of the company's financial position and performance.

FRF for SMEs is designed to accommodate the needs of these three

primary groups of users of the financial statements. Some of the benefits are:

- A cost beneficial solution for the users of the financial statements.
- Financial statements that are prepared in a consistent and reliable manner.
- The statements and related notes are concise and in plain English.
- Suitable for general use financial statements.
- There are fewer adjustments from book to tax.
- Accounting principles are intended to be appropriate for small businesses based on the needs of the users and cost-benefit considerations.
- Accounting principles are responsive to the well documented issues and concerns that stakeholders encounter when preparing financial statements for small private businesses.

Who's in?

The typical candidate for FRF for SMEs will be a small to medium-sized for profit entity that requires reliable financial statements. This is critical; it must be an entity that does not require GAAP-based financial statements. The Framework applies to most entities and can be employed by both corporate and non-corporate entities.

Characteristics of a typical candidate include:

- No regulatory requirements requiring GAAP.
- No intention of going public.
- People who own a controlling interest are the same people who run the company.
- Management and owners rely on financial statements to confirm their assessments of performance, cash flows and assets and liabilities.
- Entity not in an industry involving specialized accounting.
- Does not engage in overly complicate financial transactions.
- Key users have direct access to management.
- Users are interested in cash flows, strength of financial position and

interest coverage.

- Financial statements support financing applications not solely based on financial statements but also on collateral and similar measures.

The AICPA cannot preclude an entity from using the Framework. It is typically intended for small and medium-sized that meet the characteristics of an SME.

A word of caution

For some time now we have been encouraged to use Other Comprehensive Basis of Accounting (OCBOA) for our small business clients. A couple of problems exist there however. First, OCBOA can mean number of bases of accounting, e.g. cash basis, modified cash basis, tax basis, regulatory basis or contractual basis. Unlike tax or cash bases, the Framework has undergone public exposure and professional scrutiny and contains explicit and comprehensive accounting principles designed to produce reliable and consistent application of the Framework.

But a word of caution. While the Framework is an effort to consolidate and simplify accounting principles for entities that don't require a GAAP financial statement, the Framework is not authoritative. It has been developed by the AICPA's FRF for SMEs taskforce and AICPA staff and was exposed to public comment and professional scrutiny, it has not been approved or disapproved by the senior technical committee of the AICPA or the FASB

Key features

The Framework is especially well suited and relevant to a typical SME and some of the key features include:

- Uses historical cost as measurement basis versus complicated fair value measurements.
- Does not require complicated accounting for derivatives, hedging activities or stock compensation.
- Disclosure requirements are targeted, providing users with relevant information that they need recognizing that users can get additional information from management.
- Policy choice to account for income taxes using either taxes payable

method or deferred income taxes method.

- Only topics that are pertinent and have meaning to most SMEs and their financial statement users are included, e.g. no concept of comprehensive income and no evaluation or accrual of uncertain tax position.
- No impairment assessment of long lived assets.
- Goodwill amortized over 15 years, no impairment testing.
- Focus is on performance, assets, liabilities and cash flows.

What does the future hold?

The FRF for SMEs has been designed to be stable yet nimble. The task force intends to monitor and assess the implementation of the Framework and propose amendments as deemed necessary. Proposed updates will be issued every three or four years based on input from stakeholders and developments in financial reporting. Somebody is finally listening to us.

So now that I've piqued your interest, you may be asking why people aren't flocking to adopt FRF for SMEs. In order to answer that question, let's take another look at the principal users of private company financial information and their respective needs.

First and foremost, are the owner/managers of these entities. These folks are primarily looking for information pertaining to profitability, assets and liabilities and cash flows. Metrics such as earnings per share or fully diluted earnings per share have little utility to this group. Throw in the fact that there may be some economies associated with the adoption of FRF for SMEs and it's an easy sell.

Next let's look at third-party investors.

Typically, this group has invested in an individual and an idea. They are typically interested in accurate, conservative financial information that will enable them to evaluate the performance of the entity in which they have made an investment. So we shouldn't meet with much resistance from this group either. FRF for SMEs is designed to satisfy

their needs.

Now we come to the group that represents the biggest challenge - the lenders. When dealing with private company clients, the need for audited or reviewed financial statements is almost always generated by a loan document of some sort. And to make matters worse, these loan documents almost always make reference to financial statements prepared in accordance with GAAP.

Why does the lending community cling so tightly to the GAAP requirement? That's the way we've always done things or that's what the legal department requires.

The real problem is that lenders tend to be woefully uninformed about FRF for SMEs. A number of years ago I recall being in a meeting with a client and some representatives of a prominent bank where we were negotiating a revolving line of credit. While reviewing the covenants, I noticed a requirement to furnish a GAAP financial statement and asked the bankers if they would be willing to accept an OCBOA financial statement. What, was the response. Other Comprehensive Basis of Accounting, I said. From the look on the banker's faces you would have thought I had started speaking in tongues.

Consider what a lender does with the information contained in these elegantly prepared GAAP financial statements. First they discount things like deferred tax assets and liabilities and impaired good will and then they spread the data in their own model in order to evaluate the loan. At the end of the day what is the lender really concerned with? Basically, that there is adequate cash flow to service the debt and that there is sufficient value in the collateral to make the bank whole in the event of a default.

This is an opportunity for us as practitioners to perform in the role of educators. Educating lenders is a key step in implementation of the Framework. Since adoption represents a change, of course we need to educate our private company owner/managers. But, more importantly, we need to educate the lending community. Arrange meetings with lenders and your clients. Emphasize the fact that FRF for SMEs produces complete and concise financial statements that contain information that they need to evaluate a loan. Host luncheons for the lending

community. Write articles in your local newspaper.

The AICPA has a number of resources designed to educate all parties involved with private company financial statements available at www.aicpa.org/FRF-SMEs. These resources include tool kits for CPAs and CPA firms, financial statement users and small businesses. The tool kits contain pertinent information on topics such as An Introduction to Financial Reporting Framework for Small and Medium-Sized Entities, illustrative financial statements, comparisons of FRF for SMEs to U.S. GAAP, tax basis OCBOA and IFRS for SMEs. There is also a power point presentation that can be used to explain the Framework to larger groups.

As the Carpenters said, "We've Only Just Begun". FRF for SMEs is not the end of the journey to alleviate financial reporting issues for private companies but it is a big step in the right direction toward "Little GAAP".

Bob McCartt Bio

Bob McCartt is a Certified Public Accountant and practices as a sole practitioner in the New Castle area. Bob is a lifelong resident of New Castle and is a graduate of Robert Morris University with a BSBA in Accounting. He also holds an MBA with a concentration in accounting from Youngstown State University.

Bob's practice focuses on small business and individual clients. He provides accounting, tax preparation and planning and IRS representation for his client base.

Additionally, Bob is an adjunct professor of accounting at the Shenango Valley Campus of Penn State University.

Bob is a past advisor for Junior Achievement and a past member of the Board of Directors of the Beaver-Castle Council of the Girl Scouts of the USA. During his tenure on the board he served as chairman of the finance committee and Vice President of the council.

PRACTITIONER'S CORNER

Pennsylvania Department of Revenue Develops Sales and Use Tax Desk Review Practice

The Department of Revenue has established a sales and use tax desk review practice within the Pass Through Business Office. These reviews may be conducted in tandem with a personal income tax review by the bureau and is separate from any field audits that the department conducts. The desk review process is an economical way for the department to review the filing liability for nonfilers and underreporters.

A review of nonfilers will be done based on information the department receives on individuals and entities that may be responsible for collecting and remitting sales tax. Taxpayers who fail to respond to inquiries by the department will have their cases directed to one of a variety of enforcement efforts. The case may be referred for a field audit. It may be sent to the Discovery division for further review. In other cases, it may be directly assessed.

Taxpayers who are engaged in the sale of taxable services or tangible property within Pennsylvania are encouraged to discuss their liability exposure with their tax practitioner.

The Department will review the filings of businesses that have made purchases of tangible personal property and may not have paid the corresponding sales tax liability. In those cases, the department will inquire regarding the payment of the tax. If sales tax has not been paid, the business will be assessed for use tax. Taxpayers who have purchased business equipment over the internet or from an out of state vendor should review their invoices to determine if the applicable sales tax has been paid. If not, the department may assess them for use tax.

Determination Letters for Qualified Non Profit Health Insurance Issuers

Revenue Procedure 2015-17 sets forth procedures for issuing determination letters and rulings on the exempt status of qualified nonprofit health insurance issuers (QNHIs).

Revenue Procedure 2015-17 will be in IRB 2015-7, dated February 17, 2015.

PA Department of Revenue Issues New Version of REV-1500 Inheritance Tax Return

The PA Department of Revenue released a new version of the REV-1500, Pennsylvania Inheritance Tax Return, on Wednesday, Dec. 17, 2014. The new version is designed to enhance processing efficiency. Form changes include:

Ovals 4 through 11 have been revised, and Ovals 12, 13 and 14 have been added.

- Oval 4 will be used when the estate is claiming an agriculture exemption.
- Oval 11 will be used to report non-probate transfers by the transferee that will not be reported on the probate return. It will be a separate and distinct return from the probate return filed by the estate. This return replaces the Advance Payment Worksheet.
- Oval 13 will be used to indicate that the estate contains business assets, whether an exemption is being claimed or not.
- Oval 14 will indicate that the spouse is the sole beneficiary of an estate whereby the assets pass outright and not in trust.

In addition to the aforementioned changes, the requirement for the Social Security number for the surviving spouse has been eliminated. There is a new

box, which can be data captured, for the date stamp entry. This will enable the department to track returns based on the order in which they were filed. To accommodate the date stamp box, the signature section has been moved to the bottom of the second page.

The current version of the Instruction Book, REV-1501, is being replaced by the new REV-1500a, a seven-page document for the preparation and filing of the Inheritance Tax return, REV-1500. There will be separate instruction sheets available that correspond to most of the individual schedules. The department has also created a new pamphlet, REV-720, containing general information regarding the Pennsylvania inheritance tax.

Forms and schedules are available at www.revenue.pa.gov, or you may order any Pennsylvania tax form or schedule by calling our 24-hour answering service for forms ordering: 1-800-362-2050.

IRS tips on identity theft

The IRS is very concerned about identity theft since a significant amount involves tax refund claims. Here are some tips from the IRS, and a couple of our own.

- Don't carry your Social Security card or any documents that include your Social Security number (SSN) or Individual Taxpayer Identification Number (ITIN).
- Don't give a business your SSN or ITIN just because they ask. Give it only when required.
- Protect your financial information.
- Check your credit report every 12 months. (We suggest more frequently.)
- Review your Social Security Administration earnings statement annually.

- Secure personal information in your home.
- Protect your personal computers by using firewalls and anti-spam/virus software, updating security patches and changing passwords for Internet accounts.
- Don't give personal information over the phone, through the mail or on the Internet unless you have initiated the contact or you are sure you know who you are dealing with.
- Use a strong password-letters, numbers and capital and lower case. Words may be easy to remember, but they're terrible passwords.
- Protect your checking account number. Give it only to trusted businesses.
- Your birthday is a vital piece of information.
- When you get an e-mail, check the source. You can often tell the e-mail is phishing or a scam.
- Check your bank accounts and credit card statements monthly, even for inactive cards. If the accounts are online, check them even more frequently.

Entity liable for filing even if dormant

You may have set up an S or C corporation, partnership, LLC and never "activated" it. The entity has no assets, no bank account, no income or expenses. You'll still have to file a return, even if there's no tax due. For federal purposes you can be liable for a penalty based on the number of K-1s and the number of months a 1065 (partnership return) or 1120S (S corporation return) is late. Many states have similar penalties. In the case of a single member LLC (which would file a Schedule C or Schedule E with a Form 1040) you'll escape a federal penalty, but you may have a minimum fee or tax at the state level. Check the rules. You don't want to incur a significant penalty for failing to pay a \$50 annual fee.

The IRS has recently released updates of a number of forms, instructions and publications

Some of the more important ones include:

- Pub. 3 Armed Forces' Tax Guide
- Pub. 527 Residential Rental Property
- Pub. 530 Tax Information for Homeowners
- Pub. 590-A Contributions to Individual Retirement Arrangements (Pub. 590 has been split into two-590-A and 590-B)
- Pub. 590-B Distributions from Individual Retirement Arrangements
- Pub. 936 Home Mortgage Interest Deduction
- Pub. 5187 The Health Care Law: What's New for Individuals and Families
- Pub. 5199 Tax Preparer Guide to Identity Theft
- Pub. 5027 Identity Theft Information for Taxpayers
- Pub. 5201 The Health Care Law and Your Taxes
- Form 1116 Foreign Tax Credit (Individual, Estate, or Trust)
- Form 4562 Depreciation and Amortization
- Form 5500-EZ Annual Return of One Participant Retirement Plan
- Form 5695 Residential Energy Credits
- Form 5884 Work Opportunity Tax Credit
- Form 8582 Passive Activity Loss Limitations
- Inst 1041 U.S. Income Tax Return for Estates and Trusts
- Inst 4562 Depreciation and Amortization
- Inst 8941 Credit for Small Employer Health Insurance Premiums
- Inst 8960 Net Investment Income Tax for Individuals, Estates, and Trusts
- Inst 8962 Premium Tax Credit
- Inst 8983 Statement of Specified Foreign Financial Assets

Revenue Procedure 2015-13 (IRB 2015-5)

updates and revises the general procedures under Sec. 446 to obtain the advance and automatic consent to change a method of accounting. This procedure is effective for Forms 3115 filed on or after January 16, 2015, for a year of change ending on or after May 31, 2014. This revenue procedure and Rev. Proc. 2015-14 are of particular interest to taxpayers who are changing a method of accounting for depreciation or amortization.

Revenue Procedure 2015-14 (IRB 2015-5)

provides the list of accounting methods to which the automatic change procedures in Rev. Proc. 2015-13 apply. This revenue procedure is effective for a Form 3115 for a year of change ending on or after May 31, 2014, that is filed under the automatic change procedures of Rev. Proc. 2015-13.

Revenue Procedure 2015-15 (IRB 2015-5)

provides the 2015 monthly national average premium for qualified health plans that have a bronze level of coverage for taxpayers to use in determining their maximum individual shared responsibility payment under Sec. 5000A(c)(1)(B) of the Code and Sec. 1.5000A-4 of the Income Tax Regulations. The monthly national average premium for Bronze Plans offered through Exchanges is \$207 per individual or \$1,035 for a shared responsibility family with five or more members. Revenue Procedure 2014-46 is superseded.

Ten-year collection limitation period

The IRS generally has only three years in which to assess income taxes, but there's a 10-year limitation period on collection. For example, the IRS issues a deficiency notice to a taxpayer, but the taxpayer fails to pay. The IRS doesn't follow up immediately. The IRS has 10 years in which to pursue collection. In fact, that limitation period is waived if you have an installment agreement with the IRS to pay the tax. That is, there's no time limit on the IRS. 🚩

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Claim Example

Computer fraud

A hacker gained unauthorized access to an insured's accounts payable in the computer system. Using this access he altered bank routing information on outgoing payments, resulting in \$1 million being transferred to his personal account rather than to the entity which was supposed to be paid. Cyber Liability covers damages caused by the unauthorized entry of data into the insured's computer system.

Coverages Provided

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