Early Warning Signs!

Periodically most small dealership groups, single point dealerships, suffer some form of breakdown in the accounting department. The breakdown results in unreliable, partial and incomplete accounting records. In this brief article we are not talking about manipulation of the accounting records, but rather things which just happen due to events affecting the lives of the accounting staff. The changes and/or the deficiencies in the accounting records do not happen overnight. There are usually a number of early warning signs that a non accountant or a member of management can detect if they are aware of them and looking for them. Some of these early warning signs include:

- The monthly performance or delivery time table for reports, financial statements and other information is not being met. This does not mean every criteria is deficient but rather one or more items is missing over the course of several months.
- Parties reviewing the financial statements have questions or ask for modification to the monthly balances.
- Unusual balances appear on the financial statements. The amounts which should not be in brackets or have a minus sign all of a sudden do so.
- Accruals, prepaids or other accounts affected by standard monthly entries go without change over several months.
- Reconciliations are not presented on time for management approval.
- Reconciliations presented have a large number of reconciling items or outstanding transactions which have not been cleared from the previous reconciliation.
- Schedules are not being reconciled on a monthly basis. A review of receivables, factory receivables and inventory accounts show small balances not being reconciled and adjusted or show inconsistent balances. For example, a schedule showing new vehicle inventory and the related floor plan financing show a balance in one account but not in the other related account.
- There are unusual balances and descriptions at the end of schedules. For example "to adjust allowance account."
- Fixed asset additions are not put in the appropriate account and the monthly amortization is not adjusted for significant additions.
- Sales tax or other tax accounts are not cleared when returns are filed.
- Income tax provisions or bonus accounts are not updated on a monthly basis.

The list can include many other items but this is an example of the items which should be reviewed periodically by a senior member of management. The existence of the above points or others should result in a more in-depth review to ensure the items in question are not an early warning of a bigger problem.

TAX TIP

2012 YEAR-END TAX PLANNING

A combination of events including possible expiration of some or all of the Bush-era tax cuts after 2012, the imposition of new so-called Medicare taxes on investments and wages, doubts about renewal of many tax extenders, and the threat of massive across-the-board federal spending cuts, have many taxpayers asking how can they prepare for 2013 and beyond…and what to do before then.

In the short run taxpayers should become familiar with the expiring tax incentives and what may replace them after 2012 and plan accordingly.

INDIVIDUAL INCOME TAX RATES

Unless extended, reduced individual income tax rates in place since 2003 will be replaced by higher rates in 2013. The current 10, 15, 25, 28, 33 and 35 percent rate structure would be replaced by the higher pre-Bush 15, 28, 31, 36 and 39.6 percent levels.

CAPITAL GAINS/DIVIDENDS

The current taxpayer-favorable rates-zero percent for taxpayers in the 10 and 15 percent brackets and 15 percent for all other taxpayers will be replaced by pre-2003 rates of 10 percent for taxpayers in the 15 percent bracket and a maximum 20 percent for all others. Dividends will be subject to ordinary income tax rates.

Strategy:

Depending upon the appreciation or losses now locked into a current portfolio, consider the following strategies: (1) accelerate long-term capital gain, which has the certainty of being taxed at 15 percent maximum in 2012, or (2) increase carryover losses into potentially higher rates in years after 2012.

For those in control of C corporations, declaring dividends to be distributed before 2013 may be beneficial if top rates on dividends rise from 15% to 43.4% (39.6% plus 3.8% Medicare surtax).

Shareholders of closely-held corporations may benefit from implementing corporate liquidations before year-end so that resulting distributions are taxed at favorable capital gain rates in 2012.

3.8 PERCENT MEDICARE CONTRIBUTION TAX

Effective January 1, 2013, a 3.8 % Medicare surtax will be imposed on the taxpayer's "net investment income" (NII) and will generally apply to passive income. The Medicare surtax will also apply to capital gains from the disposition of property (unless property was used in a trade or business). For individuals, the Medicare surtax will apply to the lesser of the taxpayer's NII or the amount of "modified" adjusted gross income above specified thresholds ($250,000 for married taxpayers filing jointly or a surviving spouse; $125,000 for taxpayers filing separately; and $200,000 for single and head of household taxpayers).

Strategy:

Since the Medicare surtax will not apply until 2013, taxpayers face several planning decisions:

- Whether to sell off assets and recognize gains in 2012, thus avoiding subjecting them to the surtax in 2013 and thereafter;
- How to reduce NII in 2013 and thereafter; and
- How to reduce modified AGI in 2013 and thereafter

For trusts and estates, the Medicare surtax applies to the lesser of undistributed net investment income for the year, or the amount of AGI that exceeds the dollar amount at which the highest tax rate bracket begins for estates and trusts (estimated at $11,950 for 2013). Thus, the Medicare surtax applies to a much lower amount for trusts and estates than for individuals.

Net Investment Income (NII) for purposes of the 3.8 % Medicare surtax includes:

- Gross income from interest, dividends, annuities, royalties, and rents;
- Gross income from a trade or business that is a passive activity; and
- Net gain from the disposition of property, other than property held in an active trade or business.

ADDITIONAL 0.9 PERCENT MEDICARE TAX

Effective January 1, 2013, higher income individuals will be subject to an additional 0.9 % HI (Medicare) tax. This should not be confused with the additional 3.8% surtax on NII. This additional Medicare tax is applicable to that portion of wages in excess of $200,000 ($250,000 for married couples filing jointly and $125,000 for married couples filing separately) which will be subject to a 2.35% (1.45% plus 0.9%) Medicare tax rate. The additional Medicare tax rate also attaches to self-employed individuals.

There are more year end planning opportunities that may be available for you. Please consult with your ATA representative.