THE VOS VOICE

July 2017

"Because Accounting Matters And We Know It"

VOS CPAs, PLLC 30 Wall Street, NY, NY 10005 * 80 Orville Drive, Bohemia, NY 11716 * 41 Park of Commerce Way, Savannah, GA 31405
www.voscpas.com

Inside This Issue

Good Construction CPA's are "Money"

A certified public accountant (CPA) firm that specializes in construction is critical to the success of the financial management of any contractor's business. Construction companies experience strong economic cycles and work in complex business environments. It is imperative for a construction company to be surrounded by a solid team of advisors in order to sustain profitability, and that team includes a construction-oriented CPA. All long-term successful contractors share this positive characteristic.

Construction accounting is unique. There are different methods of reporting income for tax purposes that are available to contractors. Surety companies prefer to see a financial statement where revenues are recognized on a percentage- of- completion basis of accounting, and a good construction-oriented CPA firm will provide this. The CPA firm should understand the complex accounting and tax issues required of contractors. A CPA firm that does not focus on contractors may not fully recognize all of the tax implications to a construction company, or the strategies to mitigate taxes that are available to a contractor. Simply put, if the CPA is not construction-oriented, the result could be the contractor paying taxes the business does not owe.

A construction-oriented CPA is well versed in the nuances of construction accounting. This will become increasingly more important considering the guidance by Financial Accounting Standards Board (FASB) regarding new revenue recognition standards. The objective of the new guidance is to establish the principles to report useful information to users of financial statements about the nature, timing, and uncertainty of revenue from contracts with customers. A CPA firm that understands these kinds of changes will bring value to the relationship and is crucial to obtaining the optimum level of surety credit.

A construction-oriented CPA firm will also be a valuable consultant when choosing a software program for contractors. A sophisticated contractor will use an accounting system that can produce timely and accurate financial information. It is of great benefit for the contractor to have an internal accounting system that closely mirrors the CPA's financial reports. A construction-oriented CPA firm will make recommendations for software programs that accomplish this goal. The CPA firm should also be available to help implement the system, recommend when upgrades to the system are beneficial, and easily provide temporary support for vacationing accounting staff.

The timing of the CPA's financial reports is critical for surety support. A surety company expects to review the contractor's fiscal year end report within 90 to 120 days after fiscal year end. A construction-oriented CPA firm will ensure the reports are promptly available to the surety, bank, and any other party that requires financial information to help support the contractor's operations. If the CPA's fiscal year end report takes more than 120 days to complete, the surety is required to make decisions regarding the contractor's surety credit based on out of date information. This will limit the contractor's surety bond capacity.

Most construction companies, particularly subcontractors, require the use of a bank-line of credit to help cash flow their operations. Even general contractors, that do not normally require it, often have a bank-line of credit facility in place for the occasional short-term need for cash. A construction-oriented CPA firm that prepares the fiscal year end financial statement could be beneficial to a contractor's banking relationship. Just like a construction-oriented CPA firm provides comfort to the surety that the financial information is accurate and appropriately prepared, a banker should also receive the same level of comfort from the CPA's financial information. Since borrowing ability is important to the business operations of most contractors, a construction-oriented CPA firm can only help when qualifying for bank credit.

The benefits from hiring a good construction-oriented CPA firm are numerous. Keys to a successful CPA/Contractor relationship are respect and trust, clear communication, mutual commitment, responsiveness, and availability. Finding a good construction-oriented CPA firm can come from referrals from surety bond agents and by surety companies. Various industry associations can also be good resources. Strategically, using a construction-oriented CPA firm should be a priority for a construction company that wants to minimize their taxes, values their banking relationship, and wants to increase their surety capacity.

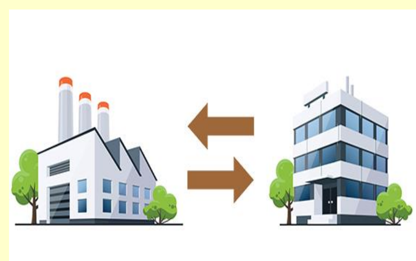
When It Comes to IRS Audits, Be Prepared

If you recently filed for your 2016 income tax return (rather than filing for an extension) you may now be wondering whether it is likely that your business could be audited by the IRS based on your filing. Here is what every business owner should know about the process. Catching the IRS's eye, many business audits occur randomly, but a variety of tax-return-related items are likely to raise red flags with the IRS and may lead to an audit. Here are a few examples: Significant inconsistencies between previous years' filings and your most current filing, Gross profit margin or expenses markedly different from those of other businesses in your industry, and Miscalculated or unusually high deductions. An owner-employee salary that is inordinately higher or lower than those in similar companies in his or her location can also catch the IRS's eye, especially if the business is structured as a corporation. Response measures if you're selected for an audit, you'll be notified by letter. Generally, the IRS will not make initial contact by phone. However, if there is no response to the letter, the agency may follow up with a call. The good news is that many audits simply request that you mail in documentation to support certain deductions you have taken. Others may ask you to take receipts and other documents to a local IRS office. Only the most severe version, the field audit, requires meeting with one or more IRS auditors. More good news: In no instance will the agency demand an immediate response.

You will be informed of the discrepancies in question and given time to prepare. To do so, you will need to collect and organize all relevant income and expense records. If any records are missing, you will have to reconstruct the information as accurately as possible based on other documentation. If the IRS selects you for an audit, our firm can help you: Understand what the IRS is disputing (it is not always crystal clear), Gather the specific documents and information needed, and Respond to the auditor's inquiries in the most expedient and effective manner. Do not let an IRS audit ruin your year — be it this year, next year or whenever that letter shows up in the mail. By taking a meticulous, proactive approach to how you track, document and file your company's tax-related information, you will make an audit much less painful and even decrease the chances that one happens in the first place.

The Section 1031 Exchange: Why It's Such a Great Tax-Planning Tool

Like many business owners, you might also own highly appreciated business or investment real estate. Fortunately, there is an effective tax planning strategy at your disposal: the Section 1031 "like kind" exchange. It can help you defer capital gains tax on appreciated property indefinitely. How it works Section 1031 of the Internal Revenue Code allows you to defer gains on real or personal property used in a business or held for investment if, instead of selling it, you exchange it solely for property of a "like kind." In fact, these arrangements are often referred to as "like-kind exchanges." Thus, the tax benefit of an exchange is that you defer tax and, thereby, have use of the tax savings until you sell the replacement property. Personal property must be of the same asset or product class. However, virtually any type of real estate will qualify as long as it is business or investment property. For example, you can exchange a warehouse for an



office building, or an apartment complex for a strip mall. Executing the deal although an exchange may sound quick and easy, it's relatively rare for two owners to simply swap properties. You will likely have to execute a "deferred" exchange, in which you engage a qualified intermediary (QI) for assistance. When you sell your property (the relinquished property), the net proceeds go directly to the QI, who then uses them to buy replacement property. To qualify for tax-deferred exchange treatment, you generally must identify replacement property within 45 days after you transfer

Please see *Section 1031 Exchange* on page 3

Section 1031 Exchange from page 2

the relinquished property and complete the purchase within 180 days after the initial transfer. An alternate approach is a “reverse” exchange. Here, an exchange accommodation titleholder (EAT) acquires title to the replacement property before you sell the relinquished property. You can defer capital gains by identifying one or more properties to exchange within 45 days after the EAT receives the replacement property and, typically, completing the transaction within 180 days. The rules for like-kind exchanges are complex, so these arrangements present some risks. If, say, you exchange the wrong kind of property or acquire cash or other non-like-kind property in a deal, you may still end up incurring a sizable tax hit. Be sure to contact us when exploring a Sec. 1031 exchange.

> *“All Growth Depends on Activity. There is No Development Physically or Intellectually Without Effort, and Effort Means Work”*
>
> *~Calvin Coolidge*

~ I R S Corner

IRS

Department of the Treasury
Internal Revenue Service

Employee or Independent Contractor? Know the Rules
IRS Small Business Week Tax Tip 2017-02, May 1, 2017

The IRS encourages all businesses and business owners to know the rules when it comes to classifying a worker as an employee or an independent contractor.
An employer must withhold income taxes and pay Social Security, Medicare taxes and unemployment tax on wages paid to an employee. Employers normally do not have to withhold or pay any taxes on payments to independent contractors.

Here are two key points for small business owners to keep in mind when it comes to classifying workers:

1. **Control.** The relationship between a worker and a business is important. If the business controls what work is accomplished and directs how it is done, it exerts behavioral control. If the business directs or controls financial and certain relevant aspects of a worker’s job, it exercises financial control. This includes:
    - The extent of the worker's investment in the facilities or tools used in performing services
    - The extent to which the worker makes his or her services available to the relevant market
    - How the business pays the worker, and
    - The extent to which the worker can realize a profit or incur a loss

2. **Relationship.** How the employer and worker perceive their relationship is also important for determining worker status. Key topics to think about include:
    - Written contracts describing the relationship the parties intended to create
    - Whether the business provides the worker with employee-type benefits, such as insurance, a pension plan, vacation or sick pay
    - The permanency of the relationship, and
    - The extent to which services performed by the worker are a key aspect of the regular business of the company
    - The extent to which the worker has unreimbursed business expenses

The IRS can help employers determine the status of their workers by using Form SS-8, Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding. IRS Publication 15-A, Employer's Supplemental Tax Guide, is also an excellent resource.

Important Facts about Filing Late and Paying Penalties

IRS Tax Tip 2017-51, April 20, 2017

April 18 was this year's deadline for most people to file their federal tax return and pay any tax they owe. If taxpayers are due a refund, there is no penalty if they file a late tax return.
Taxpayers who owe tax, and failed to file and pay on time, will most likely owe interest and penalties on the tax they pay late. To keep interest and penalties to a minimum, taxpayers should file their tax return and pay any tax owed as soon as possible.

Here are some facts that taxpayers should know:

1. **Two penalties may apply.** One penalty is for filing late and one is for paying late. They can add up fast. Interest accrues on top of penalties

2. **Penalty for late filing.** If taxpayers file their 2016 tax return more than 60 days after the due date or extended due date, the minimum penalty is $205 or, if they owe less than $205, 100 percent of the unpaid tax. Otherwise, the penalty can be as much as 5 percent of their unpaid taxes each month up to a maximum of 25 percent.

3. **Penalty for late payment.** The penalty is generally 0.5 percent of taxpayers' unpaid taxes per month. It can build up to as much as 25 percent of their unpaid taxes.

4. **Combined penalty per month.** If both the late filing and late payment penalties apply, the maximum amount charged for the two penalties is 5 percent per month.

5. **Taxpayers should file even if they can't pay.** Filing and paying as soon as possible will keep interest and penalties to a minimum. IRS e-file and Free File programs are available for returns filed after the deadline. If a taxpayer can't pay in full, getting a loan or paying by debit or credit card may be less expensive than owing the IRS.

6. **Payment options.** Taxpayers should explore their payment options at IRS.gov/payments. For individuals, IRS Direct Pay is a fast and free way to pay directly from a checking or savings account. The IRS will work with taxpayers to help them resolve their tax debt. Most people can set up a payment plan using the Online Payment Agreement tool on IRS.gov.

7. **Late payment penalty may not apply.** If taxpayers requested an extension of time to file their income tax return by the tax due date and paid at least 90 percent of the taxes they owe, they may not face a failure-to-pay penalty. However, they must pay the remaining balance by the extended due date. Taxpayers will owe interest on any taxes they pay after the April 18 due date.

8. **No penalty if reasonable cause.** Taxpayers will not have to pay a failure-to-file or failure-to-pay penalty if they can show reasonable cause for not filing or paying on time.

Taxpayers should keep a copy of their tax return. Beginning in 2017, taxpayers using a software product for the first time may need their Adjusted Gross Income (AGI) amount from their prior-year tax return to verify their identity. Taxpayers can learn more about how to verify their identity and electronically sign tax returns at Validating Your Electronically Filed Tax Return.

"The Difference Between Ordinary and Extraordinary is That Little Extra"

~Jimmy Johnson