

MarketWise



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Current Tax Law Changes & Planning for the Future

Earlier this month, I attended a seminar hosted by Mercy Medical Hospital Planned Giving Foundation in Boise, ID and the most enlightening session was on Current Tax Law Changes and Planning for the Future by Trevor Gunstream, MBA, CPA.

Trevor's presentation on the current tax law changes and the number of tax initiatives that are scheduled to expire brought home to me the need to be working with your tax advisor now, this year, sooner than later, especially if you are a business owner, or if you have a significant tax event in 2009 or are contemplating a significant taxable transaction in the next couple of years such as the sale of a business or real estate that is not your personal residence.

The thing that really caught my attention is the number of temporary tax laws that have been passed since 2001 listed below. There have been 23 major tax initiatives since 2001. In 8 years, the US Government has averaged almost 3 tax initiatives per year so how does the average tax payer or business owner keep current? I don't think you and I can – and what we don't know can cost us money! Trevor's next point that hit home with me is that most of the federal tax initiatives were temporary income tax laws and there are no significant tax provisions scheduled to expire in 2009 and 2010 – 113 tax provisions scheduled to expire by the end of 2010.

Trevor made the point that if the federal government allowed all of the tax initiatives to expire, it would generate significant extra federal tax revenue, something the federal government needs given the financial events of the past few years that need to be paid for. His point was that one should not assume an

existing tax credit will still be there when you execute your transaction, so seek tax advice and plan ahead!

Of course tax strategy is something you should work on with your CPA firm. I wanted to make you aware of all the changes coming. It's too easy to go from day to day and then all of a sudden be blindsided by something that you just weren't aware of. I think it is your CPA's responsibility to keep you advised about your financials for both your company and personal financial health.

Major Initiatives Since 2001

1. Economic Growth and Tax Relief Reconciliation Act of 2001
2. Victims of Terrorism Tax Relief Act of 2001
3. Job Creation and Worker Assistance Act 2002
4. Jobs and Growth Tax Relief Reconciliation Act of 2003
5. Military Family Tax Relief Act of 2003
6. Tax Provisions of the Medicare Act of 2003
7. Pension Funding Equity Act of 2004
8. Working Families Tax Relief Act of 2004
9. American Jobs Creation Act of 2004
10. Tax Provisions of the Energy and Transportation Acts of 2005
11. Gulf Opportunity Zone and Katrina Emergency Tax Relief Acts of 2005
12. Tax Increase Prevention and Reconciliation Act of 2005
13. Pension Protection Act of 2006
14. Tax Provisions of the Tax Relief and Health Care Act of 2006
15. Small Business and Work Opportunity Tax Act of 2007
16. AMT Patch, Mortgage Relief, Energy, Technical Corrections, and Other Late 2007 Tax Acts
17. Economic Stimulus Act of 2008
18. Heroes Earnings Assistance and Relief Tax Act of 2008

19. Heartland, Habitat, Harvest, and Horticulture Act of 2008
20. Housing Assistance Tax Act of 2008
21. Emergency Economic Stabilization, Energy Improvement and Extension, and Tax Extenders and AMT Relief Acts of 2008
22. Worker, Retiree, and Employer Recovery Act of 2008
23. American Recovery and Reinvestment Act of 2009

Simplification?

- 1992 Calendar Year – 21 tax provisions set to expire during that year
- 2009 Calendar Year – 73 tax provisions set to expire during the year
- 2010 Calendar Year – 40 tax provisions set to expire during that year (One being the entire 2001 tax act)
- That's 113 provisions set to expire by the end of next year!

NOL Carryback

- Extension of NOL carryback period
- For small businesses with receipts of <\$15 million
- For year ending in 2008 or for year beginning in 2008 (by election)
- Tip: Fiscal year taxpayers have some flexibility on application

First-time Homebuyer Credit

- Set to expire November 30, 2009
- 2008 purchase: 10% of price, \$7,500 max, 15 year payback
- 2009 purchase: 10% of price, \$8,000 max, no payback
- 2009 purchaser can elect to place on 2008 tax return
- Tip#1: Closing must occur first to claim the credit
- Tip#2: Beware of short sale purchases started in late summer/early fall

Credits Allowed Against AMT

- Set to expire December 31, 2009
- Example: Education credits, child care credit, dependent care credit, etc.

- Since 2001 – reduce both regular and AMT taxes
- After 2009 – will only reduce regular tax
- Tip: Be aware that this can impact those individuals who don't pay AMT but are on the AMT bubble!

AMT Exemption

- Set to expire December 31, 2009
- \$70,950 for joint filers (up \$1,000 from 2008)
- The 2009 amount has been set way ahead of historical standards.
- Still no provision to index for inflation

Deduction: Sales Taxes

- Set to expire December 31, 2009
- Allows deduction of sales taxes in lieu of state income taxes
- Application: those individuals in "non-income tax" states (Washington, Nevada, etc.)

Deduction: Vehicle Sales Tax

- New provision
- Set to expire December 31, 2009
- Above the line deduction for sales tax paid on vehicles, motorcycles, and motor homes purchased in 2009
- Deduction allowed for sales taxes paid on amounts up to \$49,500
- Weight must not exceed 8,500 pounds
- **IRA Distributions for Charity**
- Original enactment in 2006
- Set to expire December 31, 2009
- Allows for exclusion of income for IRA distributions sent directly to charity
- Up to \$100,000 per year

Required Minimum Distributions

- Set to expire December 31, 2009
- There is a complete waiver of RMD rules for the 2009 calendar year
- Applies to:
 - Defined Contribution Plans
 - 457(b) State Deferred Compensation Plans
 - Individual Retirement Plans
- Tip #1: Applies to well-to-do retirees
- Tip #2: Retirees living month-to-month

Provisions of the 2001 Act (Bush Policy)

- All provisions, unless modified, will expire December 31, 2010
- Examples:
 - Capital Gains back to the 20%/10% rates
 - Dividends back to ordinary income
 - Tax brackets revert to old law (no 10% bracket, 39.6% bracket reinstated)
 - Energy credits
 - Alternative motor vehicle credits
 - Marriage penalty (various forms)
 - Estate tax exemption back to \$1 million

Farm Assets

- Set to expire December 31, 2009
- Allows a 5 year life instead of 7 on farm machinery and equipment
- For assets placed in service between January 1 and December 31
- Original use language is present
- Excluded assets: Grain bins, cotton ginning assets, fences, and land improvements
- Tip: This provision is not sensitive to fiscal year taxpayers – the placed in service dates are firm

Real Property Depreciation

- Set to expire December 31, 2009
- 15-year recovery period for:
 - Leasehold improvements
 - Restaurant buildings and improvements
 - Retail improvements
- This was effective for 2008!

50% Bonus Depreciation

- Set to expire on December 31, 2009
- Qualified original use property placed in service in 2008 or 2009
- Allows for 50% depreciation of the cost before consideration of other regular depreciation
- Available for most property with 20 years or less life

Section 179 Expense

- Allows for immediate write off of qualified assets
- The current \$250,000/\$800,000 limits expire on December 31, 2009
- Once expired the limits return to the \$125,000/\$500,000 limits until December 31, 2010

- Without an extender by the end of 2010...the limits are \$25,000/\$200,000.

Charitable Conservation Contributions

- Set to expire December 31, 2009
- Allowed conservation real property contributions to offset 50% of AGI (instead of 30%)
- Allowed unused contribution to be carried forward for 15 years (instead of 5)
- Exception: Farming businesses (including C-corps) were allowed a 100% from AGI offset and 15 year carry forward

Real Property Gifts from S-Corps

- Set to expire December 31, 2009
- Appreciated real property given to charity
- Shareholder allowed a deduction for FMV
- Shareholder only required to reduce stock basis for the amount of the basis in the gifted property.
- Limited in application...but good to know.

Federal COBRA Subsidy

- Origin date: February 17, 2009
- Set to expire December 31, 2009
- Allows individuals who elect COBRA continuation coverage to only pay for 35% of the premium
- The employer pays for the remaining 65% and claims a dollar for dollar reduction in payroll taxes

Estimated Taxes

- Set to expire December 31, 2009
- Prior law: Estimates required for 100% of prior year tax or 90% of current year tax (lesser)
- New law: Estimates required for 90% of prior year tax or 90% of current year tax (lesser)
- Observation: only reduces estimated tax penalties, not ultimate tax burden

Business Debt Discharge Income

- Set to expire December 31, 2010
- Allows for 100% deferral of discharge income for 5 years
- Allows for 5 year ratable inclusion of discharge income for the following 5 years

- Observation: Should allow some companies to survive and stay out of bankruptcy.

Built-in Gains Recognition Period

- Set to expire in 2010
- 10 year window reduced to 7 years for 2009 and 2010
- Tip: Those S-corporations sitting on BIG tax problems need to be reviewed for possible forward planning possibilities

Pending legislation...

- Required minimum distributions
 - Extend the waiver of the RMD rules to 2010
 - Increase the age for RMD to 75 (from 70 ½)
 - Pending legislation...
- First-time homebuyer credit
 - Change name to “home purchase credit”
 - Change credit to include all purchasers of residences
 - Additional credit for refinancing costs paid to refinance residence acquisition debt
 - Extend the provisions of the credit for a full year longer for active members of the military
- “Education tax deduction for all”
 - Above the line deduction allowed for each child in grades K-12
 - Public school children – deduction is 25% of the average cost of education per pupil in that state
 - Private school children (including home schooled children) – deduction is 100% of the average cost of education per pupil in that state
- NOL carryback act
 - To extend the 5 year carryback provisions to years ending or beginning (by election) in 2009
- Kids IRA Act (“K-IRA”)
 - Roth type account is established for an individual under the age of 26
 - The contributor can take a deduction for 20% of the contribution, not to exceed \$5,000
 - Very healthy phase out limits (\$300,000 of AGI for married couples)
- Medical reform

- Elimination of the itemized deduction for medical expenses
- Raising of the 7.5% AGI limitation for medical expenses
- Taxing employer contributions to Health Savings Accounts and Health Reimbursement Arrangements.
- Allow sole proprietors to deduct medical insurance for themselves and their families on Schedule C (Taxpayer advocate)
- Payroll Tax Reform
 - Imposition of payroll tax on previously exempt persons
 - i.e., college students performing part-time work at their schools
 - Imposition of Medicare on employees of state and local governments
- Capital loss reform
 - To allow capital losses in excess of capital gains to be deducted in the amount of \$10,000 each year (from \$3,000)
 - In some bills, the applicable date is 2010
 - In other bills, the applicable date is to apply retroactively to all of 2009
- S-corporation officer compensation
 - 2007 Report indicated that nearly 1,000,000 S-corporations with one shareholder paid no officer compensation in the year 2005.
 - If the profitable S-corporations in the 1,000,000 above had been Schedule C’s (sole proprietor), they would have paid \$4.9 billion in self-employment taxes.
 - Several bills introduced and brewing political winds indicate that there is a movement that would subject ALL S-corporation earnings of service or professional service entities to self-employment taxes

Financial Firepower Management Roundtable

October 29-30 in Scottsdale, Arizona

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