2009 TAX PLANNING GUIDE UPDATE

On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009 (P.L. 111-5) into law. The 2009 Act contains a number of changes that could affect your 2009 tax planning. Below, we highlight several of the 2009 Act's key tax provisions and also discuss an important tax law change made by the Worker, Retiree, and Employer Recovery Act of 2008 (P.L. 110-458). Both laws were enacted after the *2009 Tax Planning Guide* was published.

AMT Relief

Over the years, the alternative minimum tax (AMT) has become an issue not only for the high-income taxpayers it was originally intended to target, but for other taxpayers as well. Lawmakers have responded by enacting temporary AMT "patches" to increase the AMT exemption amounts, typically for only one year. The 2009 Act follows suit by raising the AMT exemptions for 2009 to $70,950 for married taxpayers filing jointly, $46,700 for unmarried taxpayers, and $35,475 for married individuals filing separately. Under another of the 2009 Act's provisions, taxpayers will not have to add tax-exempt interest from "private activity" municipal bonds issued in 2009 and 2010 to their incomes for purposes of calculating AMT.

Enhanced Credit for Higher Education Costs

Parents and students paying for college in 2009 and 2010 stand to benefit from modifications to the Hope Scholarship Credit made by the 2009 Act. The revised credit, which has been renamed the American Opportunity Tax Credit, is equal to 100% of the first $2,000 of qualifying higher education expenses plus 25% of the next $2,000 (maximum credit of $2,500 per student, per year). Although the tax law still places income restrictions on credit eligibility, those restrictions have been relaxed. The American Opportunity Tax Credit phases out for taxpayers with modified adjusted gross income (AGI) between $80,000 and $90,000 ($160,000 and $180,000 if married filing jointly). And, unlike the Hope Scholarship Credit, the new credit is available for all four years of college.

Changes to the First-time Homebuyer Credit

Under the 2009 Act, the first-time homebuyer tax credit is available for qualifying purchases of a principal residence after April 8, 2008, and before December 1, 2009. (Under prior law, purchases had to be made by June 30, 2009.) Home purchases made in 2009 can qualify for a credit of up to $8,000 ($4,000 if married filing separately) that does not have to be repaid to the government. Although most broadly applicable to individuals buying their first homes, the first-time homebuyer credit is also available to taxpayers who have not owned a principal residence in the U.S. during the three years before their home purchase. As under prior law, the credit phases out for taxpayers with modified AGI between $75,000 and $95,000 ($150,000 and $170,000 for joint filers).

New Deduction for Taxes on Vehicle Purchases

Taxpayers who buy new motor vehicles after February 16, 2009, and before January 1, 2010, may be eligible to deduct the state and local sales and excise taxes they pay. The deduction, which is limited to the taxes paid on up to $49,500 of a vehicle's cost, is available for new passenger automobiles, light trucks, and motorcycles (the vehicle must have a gross vehicle rating of no more than 8,500 pounds), and for motor homes. The deduction phases out for taxpayers with modified AGI between $125,000 and $135,000 ($250,000 and $260,000 for joint filers).

Required Minimum Distribution Relief

After reaching age 70½, taxpayers generally must start taking annual required minimum distributions (RMDs) from their tax-deferred retirement accounts — and pay the resulting income taxes. Very generally, the annual RMD is calculated by dividing the account balance at the end of the previous tax year by an age-based factor from an IRS table. In response to the steep slide in the investment markets, the Worker, Retiree, and Employer Recovery Act of 2008 waives RMDs for the 2009 calendar year. Taxpayers who can afford to skip withdrawals from their tax-deferred accounts in 2009 can benefit from an additional year of tax deferral and avoid the need to sell investments, potentially at a loss, to fund their RMDs.

Health Insurance Continuation Subsidy

The 2009 Act lends a helping hand to individuals whose employment has been involuntarily terminated by providing a 65% government subsidy for premiums paid to extend group health coverage. Eligible individuals who elect continuing health coverage under a federal law known as COBRA will have to pay only 35% of the premium for up to nine months. (The employer pays the rest, but is, in effect, reimbursed by the government.) The subsidy is available to workers whose employment terminates from September 1, 2008, through December 31, 2009. There is a payback provision for higher income individuals. Employers can access information about administering the COBRA subsidy on the websites of the IRS (*www.irs.gov*) and the U.S. Department of Labor (*www.dol.gov*).

Breaks for Business Asset Purchases

Instead of claiming depreciation deductions over time, eligible businesses may elect under Section 179 of the tax code to expense qualifying asset purchases in the year the assets are placed in service. The 2009 Act raises the Section 179 expensing limit for the 2009 tax year to $250,000. The $250,000 limit is reduced dollar-for-dollar as the total cost of qualifying assets exceeds $800,000. The 2009 Act also extends through 2009 a tax law provision allowing businesses to claim an additional first-year depreciation deduction on qualifying asset purchases. This depreciation "bonus" is generally equal to 50% of cost.

And More . . .

The 2009 Act also:

- Reinstates and modifies several energy-related tax credits available to individual and business taxpayers
- Expands the definition of qualified higher education expenses that may be paid from a Section 529 college savings account
- Provides a Making Work Pay Credit of up to $400 ($800 for joint filers) in 2009 and 2010
- Calls for a $250 Economic Recovery Payment to be made in 2009 to individuals receiving Social Security retirement, disability, and Supplemental Security Income (SSI) benefits, disabled veterans receiving benefits from the U.S. Department of Veterans Affairs, and Railroad Retirement beneficiaries

- Provides a $250 tax credit for government retirees who are not eligible for Social Security benefits ($500 on a joint return if both spouses are eligible)
- Allows taxpayers to exclude from income up to $2,400 of unemployment benefits received in 2009
- Makes more of the child tax credit refundable to lower income taxpayers
- Expands the Work Opportunity Tax Credit's targeted groups
- Amends requirements related to the payment of estimated taxes by small business owners
- Allows a longer carryback period for the net operating losses (NOLs) sustained by eligible small business taxpayers in taxable years ending in 2008 (alternatively, in taxable years beginning in 2008)
- Increases the maximum monthly exclusion for employer-provided mass transit and van pooling benefits
- Reduces the built-in gains recognition period for certain S corporations originally formed as regular C corporations
- Delays the 3% withholding requirement on certain payments to government suppliers
- Increases the capital gain exclusion for newly acquired qualified small business stock

Many of these changes are temporary, and various requirements and limits apply. We would be happy to discuss these recent tax law changes with you.