

# CPA

Peters & Assoc., CPA's, P.C.  
731 James Street, Ste. 400  
Syracuse, NY 13203

MAY 2009

# Client Bulletin

BUSINESS & TAX PLANNING IDEAS *for* OUR CLIENTS *and* FRIENDS

## Faster, Slimmer Stimulus Payments

In the Economic Stimulus Act of 2008 (Stimulus Act), most taxpayers were given stimulus payments of \$600 each to spur a sputtering economy. Generally, they received another \$300 for each child under age 17. Some low-income retirees received \$300. In 2009, with the U.S. economy still struggling, the American Recovery and Reinvestment Act of 2009 (Recovery Act) provides another round of stimulus payments. There are some key differences in this year's law.

### Making work pay

The new law provides two years of stimulus payments for most workers and their spouses. In 2009 and 2010, working individuals get a refundable tax credit of up to \$400, while married couples filing jointly get a refundable tax credit up to \$800. (There are no tax credits for children.)

Technically, this tax credit is calculated at a rate of 6.2% of earned income: 6.2% is the amount of tax withheld from workers' paychecks for Social Security. Thus, this tax credit effectively offsets a worker's contributions to Social Security. The tax credit generally will be distributed to workers via reduced paycheck withholding on the first \$6,452 of earnings (\$12,904 for married couples filing joint tax returns). You probably have seen this increase in your paychecks already because the federal government wanted the economic stimulus to take effect as soon as possible. With \$800 in annual savings, a married couple will have about \$65 per

### IN THIS ISSUE

**SPECIAL ISSUE:**  
*Report on the American Recovery and Reinvestment Act of 2009*

**Faster, Slimmer Stimulus Payments**  
PP. 1-2

**Raising Tax Relief for Higher Education**  
P. 2

**First Time Homebuyers Get a Real Tax Credit**  
P. 3

**Auto Buyers Get a Break, Too**  
PP. 3-4

**Another Patch for the AMT**  
P. 4

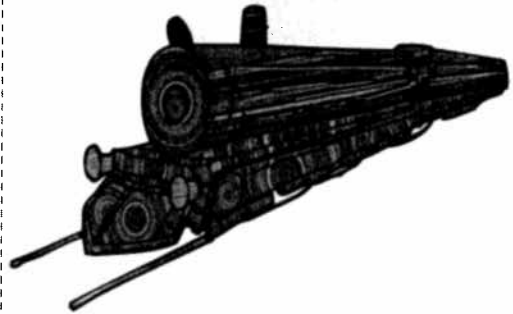
**A Bigger Incentive to Invest in Small Companies**  
PP. 4-5

**Encouraging Equipment Expenditures**  
P. 5

**Turning Losses Into Gains**  
P. 5

**Health Care Help for Former Employees**  
P. 6

month in extra take-home pay. (New withholding tables for employers are available at [www.irs.gov/pub/irs-pdf/n1036.pdf](http://www.irs.gov/pub/irs-pdf/n1036.pdf).)



Self-employed individuals and other workers who do not receive paychecks will not get these stimulus payments via withholding. Instead, they can claim the tax credits on their 2009 and 2010 tax returns. If you pay quarterly estimated income tax, contact our office for help in adjusting your payments to account for this tax savings.

The Stimulus Act's payments were not extended to high-income taxpayers, and this year's law has similar constraints. The new tax credits phase out for taxpayers with modified adjusted gross income (MAGI) in excess of \$75,000 (\$150,000 for married couples filing jointly). If your MAGI is over \$95,000 (\$190,000 on joint returns), you will get no tax credit. Also, nonresident aliens, estates, trusts, and people who are claimed as dependents on someone else's tax return will not get these making work pay tax credits.

### Payout to pensioners

Recipients collecting Social Security, Supplemental Security Income, Railroad Retirement benefits, and Veterans' Disability

CPA<sup>SM</sup>

America Counts on CPAs

continued on page 2

## C P A

## Client Bulletin

*continued from page 1* — **Faster, Slimmer Stimulus Payments**

Compensation benefits will get a one-time payment of \$250 (\$500 to married couples if both spouses qualify) in 2009. Similarly, federal and state pensioners who are not eligible for Social Security retirement benefits will receive a one-time refundable

tax credit of \$250 in 2009. These \$250 payments won't be withheld from paychecks, so they'll be distributed in the same manner (generally, direct deposit) as the 2008 stimulus payments.

The payout will be limited to \$250 per person, even for those who receive

more than one of the benefits listed in the preceding paragraph. What's more, people who get this one-time \$250 benefit will get a \$250 reduction of any making work pay tax credit to which they would be entitled.

**Raising Tax Relief for Higher Education**

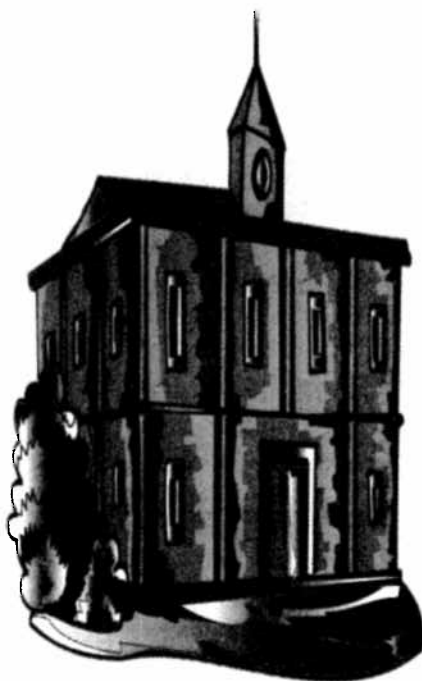
The American opportunity tax credit is in effect for 2009 and 2010. For those years, most taxpayers who pay tuition and related expenses for post-high school education can claim a tax credit of up to \$2,500. The tax credit will be equal to 100% of the first \$2,000 of higher education expenses and 25% of the next \$2,000 of those expenses. Outlays for course materials such as books are included among the costs eligible for the credit.

The American opportunity tax credit is actually an enhanced 2009–2010 substitute for the Hope education tax credit, which has been in effect for many years. While the Hope tax credit has a maximum of \$1,800 per year and is limited to the first two years of college, the two-year temporary American opportunity tax credit has a \$2,500 annual maximum for expenses incurred in up to four years of college. Also, the Hope tax credit doesn't cover expenses for course materials.

Taxpayers who don't owe enough tax to take the full credit can get a refund of up to 40% of the credit for which they qualify.

**Example:** Laura Lancaster qualifies for a \$2,500 American opportunity tax credit in 2009. However, Laura's federal income tax liability is only \$1,500 this year. Thus, the American opportunity tax credit completely

offsets her tax liability, with \$1,000 left over. Laura will receive a \$1,000 refund (40% of her \$2,500 tax credit) from the IRS.



The American opportunity tax credit is subject to a phaseout for taxpayers with modified adjusted gross income in excess of \$80,000 (\$160,000 for married couples filing jointly).

If you're paying higher education bills in 2009, 2010, or both, you probably can choose among the American

opportunity credit, the lifetime learning credit, and an above-the-line tuition deduction. You'll typically enjoy the greatest tax benefit by selecting the American opportunity credit; our office can help you with that decision.

**Laptop largesse**

Another two-year tax break (2009 and 2010) applies to computers bought for higher education. This year and next, you can take tax-free withdrawals from 529 college savings plans for the purchase of computers and related equipment, as well as for Internet access for students and their families. In prior years (and in years after this provision expires), such outlays qualify for tax-free 529 plan withdrawals only if they're required by the college as a condition of enrollment or attendance.

Even before this new law was passed, the federal government had been trying to make 529 plans more user friendly. For example, the IRS issued Notice 2009-01, which permits investors in 529 plans to switch the investment options on their existing contributions twice each year. This notice applies only to 2009; otherwise, 529 account owners may switch investment options only once per year. In 2009, at least, 529 plan investors have more flexibility to help them cope with difficult market conditions.

## First Time Homebuyers Get a Real Tax Credit

In last year's Housing and Economic Recovery Act of 2008, Congress provided certain home purchasers with a "tax credit" of 10% of the home's price, up to \$7,500. Homebuyers who had not owned and occupied a house as a principal residence in the three years before the purchase were eligible (see *CPA Client Bulletin*, Nov. 2008).

In reality, this tax break was not a true tax credit. Instead, qualified homebuyers received an interest-free loan from the federal government. That is, they received up to \$7,500 up-front in tax savings, an IRS refund check, or both. However, taxpayers receiving that \$7,500 were scheduled to repay that amount in higher taxes—\$500 per year for 15 years. If those taxpayers sold the house within 15 years, repayment would be accelerated.

### Raising the cap, forgiving repayment

The Recovery Act modifies the homebuyers tax credit. The cap is now \$8,000 on qualified home purchases over \$80,000. (For less expensive homes, the tax credit is 10% of the price.) In addition, qualified homebuyers will not have to repay the \$8,000 tax credit as

long as they stay in the house as owners for at least 36 months. This credit amounts to an \$8,000 discount on the home's price, courtesy of the federal government.

**Example:** Mark and Claire Collins buy their first home for \$100,000 and qualify for an \$8,000 tax credit. Without this tax credit, they would have owed \$1,000 when they filed their federal income tax return. The \$8,000 tax credit completely offsets their \$1,000 tax obligation, so they'll owe no income tax with their return. In addition, they'll get a \$7,000 refund from the IRS for a total tax savings of \$8,000.

### Sooner or later

Now that two laws have included a tax credit for homebuyers who have not owned and occupied a principal residence in the previous three years, there are two sets of tax benefits:

- *For qualified home purchases that closed from April 9, 2008–December 31, 2008.* Taxpayers in this category can get a credit up to \$7,500. They must repay the amount received under this provision over 15 years, or sooner if they sell their home.

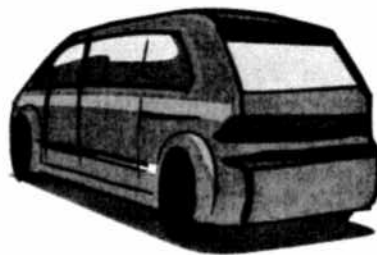
- *For qualified home purchases that closed or will close from January 1, 2009–November 30, 2009.* Taxpayers in this category can get a credit up to \$8,000. They will have no repayment obligation after they have owned and occupied the home for 36 months. (If they sell or move out within 36 months, they must repay the amount received under this provision.)

Taxpayers in either of these two categories face the same income limits. To get the full credit, a single taxpayer can have modified adjusted gross income (MAGI) no higher than \$75,000; married couples filing joint tax returns can have MAGI up to \$150,000. With MAGI up to \$95,000 (\$170,000 on joint returns), qualified homebuyers can get partial credits.

All qualified taxpayers may claim the appropriate credit on their 2008 tax return. If you have already filed your 2008 return and have not claimed the credit, our office can help you file an amended return. Alternatively, you can wait until you file your 2009 return to claim this tax credit.

## Auto Buyers Get a Break, Too

Congress not only enhanced the tax benefit offered to first time homebuyers, it also added a tax incentive for most purchasers of new vehicles. If you pay state or local sales and excise taxes, you may get a federal income tax deduction for the amount you pay. You can take such a deduction "above the line," meaning that it goes on the front page of your tax return. Such deductions reduce your adjusted gross income, which may help you claim more credits and deductions elsewhere on your tax return. You can take above-the-line deductions even if you don't itemize deductions on Schedule A of



your 1040. The above-the-line sales tax deduction for a vehicle purchase can reduce your alternative minimum tax (see related article on page 4) as well as your regular income tax.

The above-the-line deduction for vehicle sales tax applies to tax paid on

the purchase of new cars, light trucks, and motorcycles weighing no more than 8,500 pounds; this deduction also applies to new motor homes. You must purchase or have purchased the vehicle from February 17, 2009–December 31, 2009. You won't get an above-the-line sales tax deduction for leasing a vehicle.

### Over the limit

You may deduct the sales tax you pay on a purchase price up to \$49,500; if you pay more for the vehicle, you'll get a partial deduction.

**Example:** Jerry Harris pays \$60,000 for a sports car plus \$2,400 (4%) in sales

*continued on page 4*

## C P A

## Client Bulletin

continued from page 3 — **Auto Buyers Get a Break, Too**

tax. Jerry can deduct \$1,980 (82.5% of \$2,400) because \$49,500 is 82.5% of \$60,000.

This deduction is phased out for taxpayers with modified adjusted gross income (MAGI) over \$125,000 (\$250,000 for married couples filing a joint return). If your MAGI is over \$135,000 (\$260,000 filing jointly), you can't use this above-the-line tax break. If you

qualify, you can claim it on your 2009 tax return. However, you won't be able to take the above-the-line deduction if you also claim an itemized deduction for state and local sales taxes.

On the other hand, if you do claim an itemized deduction for state and local sales taxes, you can deduct the sales tax paid for a vehicle on Schedule A,

and this deduction won't be subject to the limits previously mentioned. Typically, you'll find the standard sales tax you can deduct, based on your income and place of residence, in an IRS table, and then add the sales tax paid on certain big-ticket items to get your total itemized sales tax deduction.

## Another Patch for the AMT

Virtually every year, Congress raises the amount of income that's exempt from the alternative minimum tax (AMT). The Recovery Act raises the AMT exemption amounts for 2009 to \$70,950 for joint filers and \$46,700 for single taxpayers. In 2008, those numbers were \$69,950 for joint filers and \$46,200 for single taxpayers.

Without the annual patch, the AMT exemption amounts would drop to much lower levels. Therefore, law-

makers state that this year's version will keep 26 million taxpayers from paying the AMT.

### Tax break for bonds

Some municipal bonds are issued by government agencies to fund private activities such as airports and waste disposal facilities. Investors who hold such private activity municipal bonds must pay tax on the interest if they owe the AMT, even though investors generally receive tax-exempt interest from municipal bonds.

In 2009, Congress excluded the interest paid by private activity housing bonds from the AMT. The new law excludes all other private activity bonds from the AMT as well, if those bonds are issued or (for private activity bonds issued after 2003) refunded during 2009 and 2010. This provision will benefit some investors who own municipal bonds and bond funds while stimulating the issuance of bonds that can fund such private activities.

## A Bigger Incentive to Invest in Small Companies

The tax code includes several incentives to invest in small businesses. Section 1202, one of those incentives, has provided individual investors a 50% tax exclusion on gains from selling certain small business stock. The new law increases the tax exclusion from 50% to 75% on gains from the sale of such stock issued after the date of enactment (February 17, 2009) and before January 1, 2011.

Until the Recovery Act was passed, § 1202 effectively limited the tax rate on qualified sales to 14% (50% of a 28% rate in effect during prior years). Under the new law, with a 75% exclusion, you would owe only 7% in tax

on qualified sales: 25% of that former 28% rate. If you'd rather not pay 7%, you can roll over any gains and defer the tax bill.

**Example:** Cindy Roberts invests \$50,000 in a small company and receives stock issued in 2009. She sells that stock in 2016 for \$150,000. Section 1202 permits Cindy to exclude 75% of her \$100,000 gain: \$75,000. The other \$25,000 of gain will be taxed at 28% under § 1202, so Cindy owes only \$7,000 in tax on her \$100,000 gain. Cindy also has the option of reinvesting her \$100,000 gain in another small company and deferring all tax on her gain.



To get this tax break, you must meet the following conditions:

- You must invest in a domestic C corporation and receive stock in the company's original issue.
- The gross assets of the company can't exceed \$50 million before or right after issuance.
- The company must be in a qualified trade or business. The IRS defines "qualified trade or business" as excluding the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, farming, hotel services, restaurant ser-

vices, and the production or extraction of minerals, oil, or natural gas.

- You must hold the stock for five years before selling.
- The amount of gain eligible for the § 1202 exclusion is limited to the greater of 10 times the investor's basis in the stock or \$10 million.

#### Going for more gains

If you invest in a company that meets the preceding conditions and you hold this qualified small business stock for more than six months, you can roll over any capital gain on a sale of the stock into another qualified small business within 60 days. The tax can

be deferred, and the ultimate sale can qualify for the § 1202 tax exclusion.

The expansion of § 1202 can help small companies attract investors. Therefore, if you start a new business between now and the end of 2010, you should consider choosing C corporation status. You'll give up the tax benefits of an S corporation or a limited liability company, both of which let you avoid corporate income tax and deduct company losses on your personal tax return. With a C corporation, however, you might find it easier to raise needed capital.

## Encouraging Equipment Expenditures

The Recovery Act also extends some tax benefits designed to increase the purchase of business equipment and thus stimulate economic activity. One provision involves § 179 of the tax code, which allows small companies to buy business equipment and take an upfront tax deduction rather than recovering those outlays over several years.

In 2008, Congress increased the maximum first year "expensing" election from \$128,000, indexed for inflation, to \$250,000. This year's Recovery Act retains the \$250,000 cap for 2009; the new law also keeps the 2008 phaseout threshold at \$800,000 for 2009.

**Example #1:** ABC Corp. spends \$350,000 on business equipment in 2009. It can immediately deduct \$250,000.

**Example #2:** XYZ Corp. spends \$1 million on business equipment in 2009. The company's expenditures are \$200,000 over the \$800,000 phaseout

threshold, so its expensing election is reduced by \$200,000, from \$250,000 to \$50,000.

As you can see, if a company spends \$1,050,000 or more on equipment this year, no expensing will be permitted.

#### A bonus for business

In the preceding discussion, ABC Corp. had \$100,000 of equipment purchases in 2009 that it could not deduct via § 179, and XYZ Corp. had \$950,000 of purchases that it could not deduct. The new law extends another tax benefit—"bonus depreciation"—which covers such outlays. Under this provision, property purchased and first placed in service in 2009 for use in the U.S. may qualify for 50% first year depreciation if it can't be expensed.

**Example #3:** As illustrated, XYZ Corp. buys \$1 million worth of equip-

ment this year. It can expense \$50,000 worth. Of the other \$950,000, it can take another \$475,000 (50%) deduction for bonus depreciation. Of the remaining \$475,000, XYZ can deduct \$95,000 (20%), assuming the property qualifies for a 20% first year writeoff under prior law. Thus, XYZ Corp. can deduct \$50,000 plus \$475,000 plus \$95,000, for a total of \$620,000 out of the \$1 million it spends on equipment in 2009. The Recovery Act also retains the limitation imposed on sport utility vehicles, which have a § 179 expensing limit of \$25,000.

The new law also retains first year writeoffs of around \$11,000 for cars, vans, and light trucks purchased in 2009 and used primarily for business. This is another form of bonus depreciation initiated in 2008.

## Turning Losses Into Gains

In most cases, a company that sustains a net operating loss (NOL) may carry back that loss to the prior two taxable years and use the NOL to offset taxable gains that the company reported. Such a company could recover income tax it had paid for those years. If this

company does not fully use up its NOL with a two-year carryback, it can carry forward the remaining NOL to each of the succeeding 20 taxable years to offset future gains.

The Recovery Act changes the treatment of NOLs incurred in 2008, but only for companies with gross receipts of \$15 million or less. If your

company is in that category, it can carry back a 2008 NOL and recover income tax paid in the previous five years. If your company already has filed its 2008 return showing an NOL, our office can help you start the process to receive a refund of taxes previously paid.

## Health Care Help for Former Employees

With the economy in recession, unemployment has increased. For many people, the loss of a job also means losing health insurance. To help people maintain coverage through their employer after being laid off, the Recovery Act provides a 65% subsidy for Consolidated Omnibus Budget Reconciliation Act (COBRA) continuation premiums for up to nine months. This 65% subsidy applies not only to COBRA, a federal law, but also to any similar laws on the state level.

Under COBRA, if you were a participant in your former employer's health insurance plan, you can extend your group health coverage after leaving the company. You have to pay the entire premium, which might be steep, plus administrative costs. COBRA coverage is generally limited to 18 months. The new law will make it easier for work-

ers who lose their jobs to afford nine months of COBRA payments.



**Example:** William Patterson lost his job in January. He had health insurance for his family through that job. Under COBRA, William is entitled to maintain his health coverage for 18 months if he pays the full price. If the full price of his COBRA is \$1,000 per month (approximately the national average), William can purchase his coverage for 35% of the full price (\$350 per month) for up to nine months. His former employer will be required to pay the remaining \$650

per month (65%) during that period. However, his employer effectively will be reimbursed via federal tax credits against the income tax withholding and payroll taxes it normally remits to the federal government.

To qualify for this subsidy, a worker must be or have been involuntarily terminated from a job between September 1, 2008 and December 31, 2009. Individuals must have modified adjusted gross income (MAGI) of no more than \$125,000 (\$250,000 for joint filers) in any year they receive this subsidy to get the full amount. With MAGI up to \$145,000 (\$290,000 on joint returns), a partial subsidy is available. The subsidy will terminate in fewer than nine months if the worker is offered employer-sponsored health care coverage or becomes eligible for Medicare.

## Tax Calendar

### MAY 2009

#### May 11

**Employers.** For Social Security, Medicare, and withheld income tax, file Form 941 for the first quarter of 2009. This due date applies only if you deposited the tax for the quarter in full and on time.

#### May 15

**Employers.** For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in April if the monthly rule applies.

### JUNE 2009

#### June 15

**Individuals.** If you are not paying your 2009 income tax through withholding (or will not pay enough tax during the year that way), pay the second installment of your 2009 estimated tax.

If you are a U.S. citizen or resident alien living and working (or on military duty) outside the United States and Puerto Rico, file Form 1040 and pay any tax, interest, and penalties due for 2008. If you want additional time to file your return, file Form 4868 to obtain four additional months to file. Then file Form 1040 by October 15.

**Corporations.** Deposit the second installment of estimated tax for 2009.

**Employers.** For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in May if the monthly rule applies.

In accordance with IRS Circular 230, this newsletter is not to be considered a "covered opinion" or other written tax advice and should not be relied upon for IRS audit, tax dispute, or any other purpose.

The CPA Client Bulletin (ISSN 1942-7271) is prepared by AICPA staff for the clients of its members and other practitioners. The Bulletin carries no official authority, and its contents should not be acted upon without professional advice. Copyright © 2009 by the American Institute of Certified Public Accountants, Inc., New York, NY 10036-8775. Printed in the U.S.A. Sidney Kess, CPA, JD, Editor. For AICPA customer service call (888) 777-7077 or visit [www.cpa2biz.com](http://www.cpa2biz.com).