

TAX SAVINGS IN THE STIMULUS BILL

The American Recovery and Reinvestment Act of 2009 was signed into law on February 17, 2009 in an effort to stimulate economic development. This bill is one of the largest in history with an expected cost of \$787 billion. Tax relief is the largest component of the bill, with an estimated \$288 billion directed at establishment of new incentives and enhancement of prior credits and deductions. The following summary addresses some of the key tax incentives that may apply to you.

Individual Tax Incentives

Most of the tax incentives in the Act are targeted at immediate economic stimulus to low to middle-income individuals and retirees. There are dozens of individual tax incentives, but many are very narrow in scope. The following are the key incentives that will benefit the general public.

Individual Tax Incentives
◆ “Making Work Pay” credit
◆ Economic recovery payment to retired individuals
◆ Expanded credit for first-time home buyers
◆ Tax break for new car purchasers
◆ Expanded and revised higher education tax credits
◆ Using Section 529 dollars for computers
◆ Extension of credit for energy efficient home improvements
◆ Alternative minimum tax (AMT) patch

“Making Work Pay” Credit

In 2009 and 2010, a new credit against income tax will be allowed in the amount 6.2% of earned income, up to \$400 if you are single and \$800 if you are filing jointly.

If you qualify for this credit, you can either receive it through a reduction in wage withholding or as a lump sum when filing your 2009 tax return.

If you decide to reduce tax withholding, you can expect to see up to \$13 less withheld each week starting around June this year. This extra take-home pay will continue into 2010 but will drop to around \$9 a week next year.

Eligibility: Adjusted gross income (AGI) below \$75,000 (\$150,000 for married couples filing jointly).

Economic Recovery Payment to Retired Individuals

For 2009 only, most retired individuals will receive a one-time payment of \$250. Specifically, you will receive the payment if you are a

1. Social Security beneficiary receiving benefits from the Social Security Administration, or
2. Veteran receiving disability compensation and pension benefits from the U.S. Department of Veterans’ Affairs.

The one-time payment reduces any allowable “Making Work Pay” credit. There is also a replacement credit to certain government retirees who are not eligible for Social Security.

Expanded First-time Homebuyer Credit

There was a \$7,500 first time homebuyer credit enacted in 2008, but individuals are required to pay the credit back over 15 years. The Stimulus Bill increases the credit to \$8,000 and does not require repayment as long as you live in the home for at least three years.

First-time homebuyers from January through November 2009 are eligible for a refundable tax credit equal to 10% of the purchase (up to \$8,000 in credit). Additionally, you can choose to receive this credit now on your 2008 individual income tax return if you purchase the home prior to filing your tax return.

Eligibility: Adjusted gross income (AGI) below \$75,000 (\$150,000 for married couples filing jointly), homebuyers who have not owned a home in previous three years, and a new home purchase or constructed from January 1 – November 30, 2009.

Tax Break for New Car Purchasers

In an effort to help revive the auto industry, Congress added a surprise provision for a deduction of sales tax on the purchase of a new vehicle. You will be able to deduct the state and local sales taxes paid on the purchase of a **new** automobile, which includes light trucks, SUVs, motorcycles, and motor homes. The deduction is “above the line,” meaning you do not need to itemize to receive the deduction. There are no restrictions on the automaker.

*Eligibility: Adjusted gross income (AGI) below \$125,000 (\$250,000 for married couples filing jointly), purchase of **new** vehicle in 2009, generally no more than 8,500 gross weight.*

Expanded and Revised Higher Education Tax Credits

The existing HOPE education credit is expanded in many ways for 2009-2010 only, including the following:

1. Increases maximum credit from \$1,800 to \$2,500.
2. Eligible for all four years of college (previously only first two years).
3. Expands eligible expenses to include course material (e.g. books).
4. Implements more beneficial income restrictions (to \$80,000/\$160,000 single/joint).
5. Makes 40% of the credit refundable, meaning you do not need to have income taxes to receive the benefit.

This new credit is called the “American Opportunity Tax Credit” and temporarily replaces the HOPE credit.

Eligibility: Adjusted gross income (AGI) below \$80,000 (\$160,000 for married couples filing jointly)

Planning Tip

The provision that makes the credit refundable may cause us to rethink whether a parent or child takes the education credit. For most parents with income higher than \$300,000, the dependency exemptions for their children provide little to no tax benefit and they can opt not to claim the children as dependents. Under current law, the student can benefit from education credits even if they are dependents as long as they are not claimed as such. Although there is much in the Act that will be subject to minor changes upon implementation into the Tax Code, the act does not *specifically* change this planning opportunity as it is currently written.

TAX SAVINGS IN THE STIMULUS BILL

Expanded Education Expenses for Section 529 Plans

Computers and computer technology (including internet access) will qualify as qualified education expenses in 529 education plans. This benefits many students since many universities require computers and internet access. The new law does not have any restriction for personal use as long the computer is used by an eligible student for educational purposes as well.

Extension of Credit for Energy Efficient Home Improvements

The Act increases and expands the “Residential Energy Tax Credit”, including the following changes:

1. Credit increased from 10% to 30% of the cost.
2. Raises maximum cap from \$500 to \$1,500 for 2009 and 2010.
3. Eliminates the \$500 lifetime cap.
4. Expands what qualifies as energy efficient home improvements

The foundation of the credit is to incentivize homeowners to invest in improvements that will reduce energy costs. This primarily includes insulation, windows, doors, skylights, central air conditioning, furnaces, and water heaters.

Eligibility: Purchase of qualifying energy efficient home improvements – no income limitation

Alternative Minimum Tax (AMT) Patch

The AMT exemption amounts for 2009 have been increased to \$46,700 (\$70,950 if you are filing jointly) to make the 2009 calculation in line with 2008.

Additionally, some previous AMT limitations are removed, including the following:

1. Interest on tax-exempt “private activity” bonds issued in 2009 and 2010 is not subject to AMT.
2. The Alternative Motor Vehicle Credit (AMVC) is treated as a personal credit and offset against AMT for years after 2008.

Eligibility: Prevents as many as estimated 26 million middle-income individuals from AMT and reduces AMT for many others. Those affected are likely in the \$100,000-\$350,000 income range.

Summary of Individual Tax Incentives			
Incentive	Description	Eligibility	Timing
“Making Work Pay” Credit	Credit of \$400 single/\$800 married	Income limits of \$75,000 single/\$150,000 married; must have earned income	Starting June 2009 or on 2009 tax return at your option
Payment to retirees	\$250 payment to retirees	Most SSI recipients and government retirees	Expect May-June 2009
First-time homebuyer credit	10% of purchase price up to \$8,000	Income limits of \$75,000 single/\$150,000 married; Haven’t owned in previous 3 years	When filing 2008 tax return if haven’t filed; 2009 tax return otherwise
New car tax deduction	Deduction of sales tax on purchase of new car	\$125,000 single/\$250,000 married; purchase new vehicle	When filing 2009 tax return
Education credits	Increased amount and eligibility for HOPE credit	\$80,000 single/\$160,000 married	When filing 2009-10 tax returns
Computers with \$529 dollars	Can use \$529 dollars for computer	Any qualifying student	Permanent
Home improvement credits	\$1,500 credit (from \$300)	Specific energy efficient home improvements	When filing 2009-10 tax returns
AMT patch	Continuation of AMT exemption from 2008	Reduces/eliminates AMT for some.	When filing 2009 tax return

Business Tax Incentives

There are a few business tax incentives in the Act, with the most significant provisions intended to stimulate small business fixed asset purchases and employment. There are some new provisions that are unlikely to affect most companies and the incentives are predominantly continuation or expansion of prior tax incentives. The following summarizes key provisions that may benefit small businesses.

Business Tax Incentives

- ◆ Extension of bonus depreciation
- ◆ Extension of enhanced small business expensing (Section 179)
- ◆ Estimated tax payment reduction
- ◆ Incentives to hire unemployed veterans and disconnected youth
- ◆ Tax loss carryback period

Extension of Bonus Depreciation

Similar to 2008, most **new** equipment, fixtures and leasehold improvements that your business purchases in 2009 are allowed to have 50% of the cost to be immediately written off as depreciation. Any luxury automobiles are also allowed an additional \$8,000 first year depreciation deduction.

The bonus depreciation does not increase your **overall** deduction, but accelerates much of the tax benefit to the first year to reduce current taxes. Take note that Wisconsin and many other states do not allow the bonus depreciation.

Eligibility: Purchase of qualifying property in 2009, including most equipment, vehicles and fixtures. Also includes leasehold improvements provided the building owner is not a related party.

Extension of Enhanced Small Business Expensing (Section 179)

As a small business, you may elect to write off the costs of certain equipment and other capital expenses that you incur in 2009 up to \$250,000. You may expense this full amount as long as the total assets purchased do not exceed \$800,000 this year.

Similar to bonus depreciation, this provision does not increase your **overall** deduction and Wisconsin still limits the maximum expense to \$25,000 per year.

Eligibility: Purchase of qualifying property in 2009 less than \$800,000 in total, with benefit reduced dollar for dollar for aggregate purchases in excess of \$800,000.

Estimated Tax Payment Reduction

Many small business owners can reduce the amount of their 2009 federal estimated tax payments without being subject to underpayment penalties. This provision does not reduce your taxes, but it helps cash flow and reduces exposure to penalties.

The requirements are as follows:

1. Income less than \$500,000.
2. Over 50% of income from prior year from a "Small business" (generally 500 or fewer employees)

Incentives to Hire Unemployed Veterans and Disconnected Youth

Tax legislation over the past five years has gradually expanded the Work Opportunity Tax Credit (WOTC) to increase the credit, expand the number of employees in targeted groups, and lessen the restrictions on employer eligibility. Prior law had nine targeted groups, and the 2009 Stimulus adds two more. Employers can claim a tax credit equal to 40% of the first \$6,000 of wages paid to employees in either of the following groups:

1. *Unemployed veterans* – Individuals who were discharged or released from active duty from the Armed Forces during 2008, 2009, or 2010 and received unemployment compensation for more than four weeks during the year prior to hire.
2. *Disconnected youth* – Individuals between the ages of 16 and 25 who have not been regularly employed or attended school in the past 6 months.

Planning Tip

For companies fortunate enough to be growing during this challenging economic time, this provision can be a significant incentive to hire from the targeted groups. Please contact us if you believe you may be hiring and we can discuss the specifics for your situation.

This provision requires some additional clarification of eligible employees and may exclude family members and employees recently employed by a company. Additionally, proprietors, partnerships and S corporations will need to consider the possible impact of alternative minimum tax (AMT), which could reduce or negate the tax benefit.

Tax Loss Carryback Period

The new law expands the period businesses can carry back current year tax losses. Rather than the prior 2 year limit, businesses can carry back the losses as many as five years and can now elect to carry three, four, or five years. This provision includes losses for any tax year beginning or ending in 2008 which could provide immediate benefit to many companies that were hit by economic challenges last year. The normal 2-year carryback period for all businesses is reinstated for losses incurred in 2009.

Planning Tip

Because businesses can now elect which year to offset, you can choose the year where you were in the highest tax bracket. We recommend all businesses that have tax losses in 2008 and 2009 look closely at this planning opportunity and possibly even consider when deciding on Section 179 depreciation vs. bonus depreciation.

Eligibility: Less than \$15 million average gross receipts

State Tax Provisions

Due to state budget restraints, Wisconsin along with many other states have not adopted many federal tax changes in recent years, including most notably the deductions for HSA contributions and depreciation incentives. While state tax rates are much lower than federal rates, we recommend everyone consider the state tax effect of any significant decision that is impacted by federal tax incentives.

Health Insurance Assistance

There is a provision in the Stimulus Act that benefits terminated employees who were eligible to COBRA health insurance coverage from their former employer. The benefit is that the federal government will cover 65% of the COBRA premium and the employee will be responsible for the remaining 35%. There are income limits (\$145,000/\$290,000) at which the employee may be required to pay the government back for a portion of the subsidy.

This provision poses challenges for many businesses in implementation, especially since eligibility is retroactive to employees terminated after September 1, 2008. Employers have the following obligations under the Act:

1. For employees who opted not to take COBRA, employers are required to provide 60 day COBRA notice again prior to April 18, 2009 and these employees will have 60 days from the 2nd notice date to respond.
2. Employees who are covered by COBRA are only required to pay their former employer 35% of their health premium going forward – this provision is effective February 17th and **employers are therefore not required to refund premium** for any coverage prior to that date.
3. Employers will receive a credit on their quarterly payroll tax returns for the 65% portion borne by the federal government.

Because employers will receive the 65% premium reimbursement as a payroll tax offset from the federal government, this provision will complicate tax deposit rules and require the IRS to fast-track a revised form 941. We recommend you do not reduce your tax deposits at this time unless the 65% component is significant. The IRS will issue guidance on proper procedures, but there has simply not been enough time to formalize the process.

Conclusion

The American Recovery and Reinvestment Act of 2009 has over 400 pages and includes a very broad array of incentives in an attempt to revive the economy. There are a handful of relatively straight-forward tax incentives, but most of the Act has complicated parameters that make it nearly impossible for you to understand how the Act will affect you specifically.

As trusted business advisors, we strive to plan proactively for each client's financial situation and long-range plan. This Act has some immediate planning opportunities and we will integrate that planning with our ongoing services to help you achieve your long-term goals.

We will keep you posted as the specifics of the Act unfold – in the meantime, please contact us if you have any questions.