# TAX LAW: CHANGES, UPDATES, & REMINDERS

**By: Tammy Wishowski, CPA**
**Scribner, Cohen and Company, S.C.**

Table of Contents:



In these uncertain times one thing is certain, changes have occurred in the tax law. As a result there are tax planning strategies that taxpayers and businesses can take advantage of. This issue of our newsletter will highlight the changes to the tax laws and includes reminders and information for individuals that have foreign holdings.

On October 3, 2008, President Bush signed into law the most recent of the tax law changes, the "***Emergency Economic Stabilization Act of 2008***." This Act is one of the largest tax bills in recent years and includes over 100 tax provisions and over $150 billion in separate tax breaks.

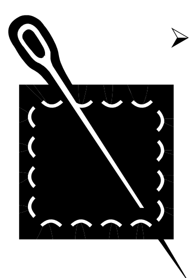
One of the main provisions was the financial markets rescue plan. Two of the tax-related provisions of the rescue plan are as follows:

- ***Executive Compensation:*** The government took a two part approach in curbing excessive compensation. In a direct purchase situation, the Treasury Department will set the compensation standards. The rescue package also limits the deductibility of compensation to $500,000 for CEOs, CFOs, and other executives of qualifying companies in TARP auctions, if the company has sold $300 million or more in troubled assets.

- ***Extended Exclusion for Homeowners:*** The rescue plan extends a temporary rule for cancellation of indebtedness income. The Act extended a provision in the Mortgage Forgiveness Debt Relief Act of 2007 which stated that discharging debt of up to $2 million secured by a principal residence is not taxable. This rule is extended through 2012.

The tax provisions of the Act will affect both individuals and business by not only giving tax relief to some, but increasing taxes for others.

## INDIVIDUALS



- ***AMT Patch:*** The AMT exemptions for 2008 are $69,950 for married couples filing jointly and surviving spouses, $46,200 for single taxpayers and heads of households, and $34,975 for married couples filing separately. This "patch" is only for 2008. Hopefully, in 2009 Congress will pass a permanent solution instead of a "patch" each year.

The "patch" also allows taxpayers to take some nonrefundable personal credits to reduce their AMT liability such as the dependant care credit and the education tax credits.

Finally, the AMT "patch" provides relief to individuals holding worthless stock options and have a large tax bill based on AMT calculations. If you are involved in incentive stock options (ISOs), with either an unpaid tax liability or a paid ISO AMT liability, relief may be available to you.

## EXTENDERS

- ***State and Local Sales Tax Deduction***: The law which allowed individuals to deduct state and local general sales taxes in lieu of state and local income taxes was extended through December 31, 2009.

- ***Higher Education Tuition Deduction***: The above-the-line higher education tuition deduction has been extended through December 31, 2009. The maximum deduction is $4,000 when adjusted gross income does not exceed $130,000 for joint filers. However, the deduction phases out completely after $160,000 for joint filers.

> Please note: The Lifetime Learning Credit or Hope Credit may be more beneficial to you depending on your tax situation.

- ***Additional Standard Deduction for Real Property Taxes***: Congress authorized a maximum $500 additional standard deduction ($1,000 for joint filers) in the *Housing Assistance Act of 2008* for the year 2008. The deduction is in addition to the standard deduction.

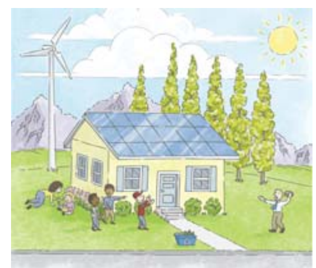
  The Act extends the additional standard deduction for real property taxes for non-itemizers through 2009.

- ***Teachers' Classroom Expense Deduction***: The law extended through 2009 the ability for teachers and other education professionals to take an above-the-line deduction of up to $250 of certain out-of-pocket classroom expenses.

> *Note*: Expenses that exceed $250 and non-classroom supplies may be deducted as an employment related miscellaneous itemized deduction subject to 2% floor for taxpayers who itemize.

- ***Tax-Free Distributions from IRAs for Charitable Purposes***: The new Act extended the law to allow some taxpayers to make tax-free distributions from IRAs for charitable purposes through December 31, 2009. The maximum contribution limit is $100,000.

Energy Credits:



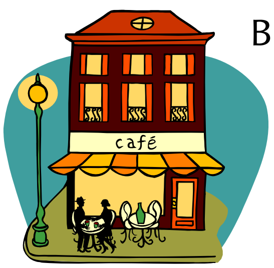
- A tax credit is available to individuals who add solar energy equipment or fuel-cell equipment to their residences. The new law extends this credit through 2016.

> ***Take Note***: For 2008, you can claim a tax credit of 30% of the cost of equipment that uses solar energy to generate electricity, up to a $2,000 maximum credit
>
> After 2008, there's no dollar limitation on the credit. Therefore, the credit is 30% of the cost of the equipment.

  Additionally starting in 2008, the new law makes the credit available for more exotic energy generating/retaining equipment: wind turbines; and geothermal heat pumps.

- A tax credit was available prior to 2008 for energy savings improvements to your principal residence. The new law brings back that credit for 2009.

The credit depends on the type of improvement (e.g., 10% of the cost of energy efficient building envelope components, such as insulation and windows, and an up to $150 credit for natural gas, propane, or oil furnace or hot water boiler) and there's an overall $500 lifetime dollar limit for all improvements.




## BUSINESSES

- *Leasehold and Restaurant Improvements:* Qualifying restaurant and leasehold improvements and certain improvements to retail space will be eligible for the 15 year cost recovery rather than a 39-year period through December 31, 2009.

- ***Charitable Contributions from Businesses***: The Tax Code gives businesses enhanced deductions for contributions of food to charitable organizations as well as contributions of books and computer equipment to qualifying schools. The law was extended through December 31, 2009.

- ***Energy Credits***: The Act also extends a host of energy tax incentives for consumers as well as for producers and manufacturers.

- ***Transportation Fringe Benefit***: Employees can exclude certain employer provided transportation fringe benefits from income, such as transit passes and van pooling.

- ***Disaster Relief***: There are many different tax incentives provided for the Midwestern and Hurricane Ike disaster area along with Natural Disaster Relief areas. Please contact a tax professional for more details.

Since you usually can not have tax decreases without tax increases, the following is one of the new law changes to increase taxes.

- ***Broker Basis Reporting***: Reporting by brokers has been expanded. Brokers will have to report the adjusted basis of publicly-traded securities when reporting sales transactions and indicate whether a gain is long-term or short-term.

  Reporting will take effect for stock acquired in 2011, for mutual funds acquired in 2012, and for other securities acquired in 2013.

On July 30, 2008 the President signed into law the ***Housing and Economic Recovery Act of 2008***. The Act is in reaction to the continuing decrease in housing sales along with rising unemployment numbers and weakness in the credit markets.

- ***First-Time Homebuyers Tax Credit***: The Housing Act gives first time home buyers nationwide a temporary refundable tax credit equal to 10% of the purchase price of a home up to a maximum credit of $7,500 ($3,750 for married individuals filing separately).

  The credit begins to phase out for taxpayers with adjusted gross income in excess of $75,000 ($150,000 for joint filers).

  The credit is effective for homes purchased on or after April 9, 2008 and before July 1, 2009. However, unlike other credits, the first-time homebuyer credit must be repaid in equal installments over 15 years, essentially making it an interest free loan from the government.

  A first time homebuyer is a person who had no ownership interest in a principal residence during the three year period before the new home is purchased. If the taxpayer sells or no longer uses the home as his or her principal residence before repaying the credit, the unpaid balance becomes due in the year in which the **residence is sold or is** no longer used as the taxpayer's principal residence.

> *Note:* Special rules apply for when a taxpayer dies, for a residence transferred in a divorce, and for an involuntary conversion.

The Act also contained some provisions which could produce tax increases.

- ***Credit Card Information Reporting***: Banks and other processors of merchant payment card transactions will be required to report the merchant's annual gross payment card receipts to the IRS and to the merchant. The new treatment is effective for sales made on or after January 1, 2011.

  *Exception:* If the aggregate value does not exceed $20,000 for the calendar year or the aggregate number of these transactions does not exceed 200.

- ***Reduced Home Sale Exclusion***: Gain from the sale of a principal residence home will no longer be excluded from gross income for periods that the home was not used as the principal residence.

  The new income inclusion rule applies to home sales **after** December 31, 2008 and is based on nonqualified use periods that begin on or after January 1, 2009.

On May 22, 2008 the House of Representatives and Senate voted to override the President's veto, and, therefore, the ***Heartland, Habitat, Harvest, and Horticulture Act of 2008*** was enacted into law, otherwise known as the "Farm" bill.

There are many provisions of the "Farm" bill which are tax related, such as:

- Enhanced Like-Kind Exchange rules to permit the exchange of water rights in the form of mutual ditch, reservoir and irrigation company stock.

- Tax Credit for Protecting Agricultural Chemicals.

- Enhanced Depreciation for Race Horses over a three year period regardless of age.

- Conservative Reserve Program Payments are excluded from self-employment income.

- Conservation Easements charitable deduction was changed so that individuals could take an immediate deduction for the donation of conservation property up to 50% of their "contribution base," rather than being restricted to the normal 20%.

- Credit for Production of Cellulosic Biofuel.

- Deduction for Endangered Species Recovery Expenditures.

- Limitation of Excess Farm Losses.

- Reduction in the current tax credit for Ethanol production.

On June 17, 2008 the President signed into law the *Heroes Earnings Assistance and Tax Relief Tax Bill of 2008*. This new bill targets members of the U.S. Armed Forces (active and reserve) and their families.

- ***Economic Stimulus Payments***: The bill allows couples who file a joint return but only one spouse has a valid social security number to receive the Economic Stimulus Payment.

- ***Combat Pay as Earned Income***: The temporary provision that allows tax free combat pay to be treated as earned income solely for the purpose of maximizing the Earned Income Credit has been made permanent.

- ***Retirement Plan Withdrawals***: The new law makes permanent the allowance for military reservists called to active duty for more than a short tour to make penalty-free withdrawals from IRAs, 401(k)s, and other arrangements. Reservists on active duty would still be subject to income tax on the **withdrawals;**

however, reservists have up to two years to repay these withdrawn contributions.

- ***Flexible Spending Accounts****:* The new law allows reservists called to active duty penalty-free access to unused amounts from flexible spending arrangements sponsored by their employer for any purpose, not just for medical or child care expenses. This new law takes effect after June 17, 2008.

- ***Employer Tax Credit***: Small employers will be eligible for a temporary differential pay tax credit. The credit equals 20% of the sum of the eligible differential wage payments (up to $20,000) for each qualified employee on active military duty during the tax year. The credit is allowed from June 17, 2008 through 2010. The amount taken as a credit by the employer may not also be taken as deductible compensation.

- ***Volunteer Fire Fighters****:* If some states and localities provide benefits to volunteer fire fighters or emergency medical responders to recruit and retain qualified professionals, these payments were originally excluded from gross income for federal tax purposes due to the Mortgage Debt Forgiveness Act of 2007.

  The new law excludes these benefits from FICA and FUTA as well.

On February 13, 2008, the President signed into law the *2008 Economic Stimulus Act* with rebates and business incentives.

- ***Economic Stimulus Rebate****:* The new law allowed a refundable credit against tax to low and middle income individuals for 2008 which was known as the economic stimulus rebate.

  After 2008, those who missed out on the rebate or received a partial rebate get a second chance when they file their 2008 return in 2009.

***Section 179****:* The new law also doubles the amount of deductible Code Section 179 expensing for 2008 to $250,000 and increases the threshold for reducing the deduction up to $800,000. It applies to property purchased and placed into service in tax years beginning in 2008.

The new law does not make changes to the general rule for the types of property that are eligible. Property must be tangible personal property, which is actively used in the taxpayer's business for which a depreciation deduction would be allowed. The property must be used more than 50% for business and must be newly purchased property. The existing exception for computer software applies to the enhanced expensing amounts.

- ***Temporary Bonus Depreciation****:* To be eligible to claim bonus depreciation, property must be 1) eligible for the modified accelerated cost recovery system (MACRS) with a depreciation period of 20 years or less, 2) water utility property, 3) computer software (off the shelf) 4) qualified leasehold property.

  The property must be purchased and placed into service in 2008.

- ***Luxury Autos****:* The new law also raises the luxury auto limitations on depreciation. Originally the first year limitation on depreciation for luxury autos was $3,060. However, this limit was increased to $8,000. If bonus depreciation is taken than the limit could potentially be $11,060.

As you have seen, there were several law changes that occurred in 2008. We have only highlighted some of the law changes for 2008. Therefore, please consult your tax advisor to discuss the full spectrum of credits available to you.

## YEAR END TAX PLANNING

We do not know what will happen in the future, but based on current law there are several strategies that you might want to utilize to take advantage of the tax savings that would result.

- If you had set aside too little this year, you can increase the amount you set aside for next year in your employer health flexible spending account (FSA).

- Realize losses on stock as long as it coincides with your investment strategy. (You should consult your financial advisor as well as your accountant.)

- Postpone income until 2009 and accelerate deductions in 2008 to lower your 2008 tax bill, i.e. postpone a possible bonus for 2008 to 2009, pre-pay expenses with a credit card so that those expenses are deductible in 2008.

- Possible conversion of a traditional IRA into a Roth IRA

- If you own a pass-through entity that has a loss in 2008 and not enough basis to take the loss, you might want to consider increasing your basis so that you can take the loss.

- If you have underpaid your income tax liability for 2008, it may be possible to increase your withholding before the end of the year to eliminate or reduce underpayment penalties.

- Depending on your income and deductions, you might find yourself in the alternative minimum tax. By reviewing when you pay state estimated tax payments and real estate taxes, you may avoid or limit your exposure to alternative minimum tax.

- If you are thinking of making energy saving improvements to your home, such as putting in extra insulation or installing energy savings windows, postpone this work until 2009. A credit of up to $500 may be available for such improvements if made next year, but not this year.

- If you are thinking of buying a hybrid vehicle eligible for a tax credit, check to see if it's eligible for the credit, and, if so purchase it before year-end.

- Businesses should consider taking advantage of the increased Section 179 expense deduction in 2008. The amount a business is able to deduct increased to $250,000 for the current year. However, the maximum expensing will drop to $133,000 for assets bought and placed in service next year.

- Businesses should also consider taking advantage of the bonus depreciation offered in 2008. This bonus write-off generally won't be available next year with some exceptions to Presidentially declared disaster areas.

- If you are self-employed and have not done so, set up a self-employed retirement plan.

- You can save gift and estate taxes by making gifts sheltered by the annual gift tax exclusion before year end. You can give $12,000 in 2008 to an unlimited number of individuals but can not carry over unused exclusions from one year to the next.

- If you are age 70 ½ or older, own IRAs or Roth IRAs, and are thinking of making a charitable gift before year-end, consider arranging for the gift to be made directly by the IRA trustee. Such a transfer can achieve important tax savings.

As always, please consult your tax advisor to discuss tax planning strategies that you may be able to take advantage of to save taxes.

# IMPORTANT REMINDERS

- ***Charitable Contributions***:

  Remember: Substantiation is the Key

  To deduct a charitable contribution a donor must retain either 1) a bank record or 2) written communication from the donee showing the name of the donee organization, the date of the contribution, and the amount of the contribution.

  A bank record can include a canceled check, a bank copy of a canceled check, or a bank statement containing the name of the charity, the date, and the amount.

  A one time cash or check contribution of $250 or more must be documented.

- As for non-cash contributions remember that only clothing and household goods that are in "good" used condition can be taken as a non-cash charitable contribution.

- In addition, there are specific rules on the amount of charitable contribution when donating a car or if you are considering making a non-cash contribution in which you believe the value is over $5,000. Please consult your tax advisor for guidance.

- ***Take Note: Kiddie Tax***: Certain children under age 19 and full-time students under age 24 who have unearned income that exceeds $1,800 for 2008 are taxed at the parent's highest marginal tax rate if taxing the income at that rate results in a higher tax.

### MILEAGE RATES FOR 2009

- The standard business mileage rate for 2009 is 55¢ per mile.

- The standard deduction for charitable miles is 14¢ per mile.

- The standard deduction for medical and moving miles is 24¢ per mile.

### GIFT TAX EXCLUSION FOR 2009

- The annual gift tax exclusion is increased to $13,000 per person for 2009.

### RETIREMENT CONTRIBUTIONS

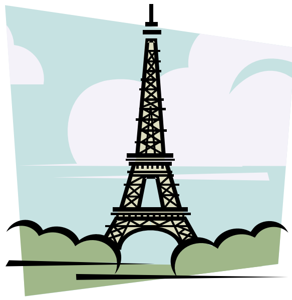
- Retirement plan contribution limits

| Year | 401(k), 403(b), Salary Reduction SEP and 457 Plans | Simple IRAs | Traditional and Roth IRAs |
|---|---|---|---|
| 2008 | $15,500 | $10,500 | $5,000 |
| 2009 | $16,500 | $11,500 | $5,000 |

- **The catch-up contribution limits for an individual age 50 and older are:**

| Year | 401(k), 403(b), and 457 plans | Simples IRAs | Traditional and Roth IRAs |
|---|---|---|---|
| 2008 | $5,000 | $2,500 | $1,000 |
| 2009 | $5,500 | $2,500 | $1,000 |

## FOREIGN HOLDINGS



Unknown to many, there may be additional filing requirements with U.S. taxpayers who own foreign assets, foreign businesses, or receive gifts from foreign individuals. Following are only a few of the possible forms that a U.S. taxpayer may have to prepare regarding their foreign holdings.

- ***Form TDF 90-22.1****:* A U.S. person must report interests in or signature authority over foreign financial accounts on Form TD F 90-22.1 "Report of Foreign Bank and Financial Accounts."

  File this form if you are a U.S. person who has a financial interest in or signature authority over any financial accounts including bank, securities, or other types of financial accounts in a foreign country, if the aggregate value of these financial accounts exceeds $10,000 at any time during the calendar year.

  The form must be filed on or before June 30 of the succeeding year to which it relates. Requests for an extension of time to file Form TDF 90-22.1 are not granted.

> *Penalty:* Civil penalties for a non-willful violation can range up to $10,000 per violation. Civil penalties for a willful violation can range up to the greater of $100,000 or 50% of the amount in the account at the time of the violation.

- ***Form 3520****:* U.S. persons need to file Form 3520 "Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts" to report certain transactions with foreign trusts and receipt of certain large gifts or bequests from certain foreign persons.

- ***Form 5471****:* U.S. citizens and residents who are officers, directors, or shareholders in certain foreign corporations should file Form 5471 "Information Return of U.S. Persons With Respect To Certain Foreign Corporations."

In an international economy, it is very possible that taxpayers and businesses hold interests in foreign bank accounts, brokerage accounts, or have a major ownership interest in a foreign entity. Therefore, you must be aware of the additional filing requirements. Please consult your tax advisor, if any of the above apply to you.

By the Numbers is published by Scribner, Cohen and Company, S.C. as a source of information for clients and business associates. This information is of a technical nature and professional advice should be sought before implementing specific ideas. Please call for more information or if you have any other questions.

Happy

Holidays!

# PAYROLL TAX UPDATES

## PAYROLL TAX RATES AND LIMITS FOR 2009

| | |
|---|---|
| Social Security (OASDI) Wage Base | $106,800 |
| Medicare Wage Base | No limit |
| OASDI Percentage | 6.2% |
| Medicare Percentage | 1.45% |
| Maximum OASDI Withholding | $6,621.60 |
| Maximum Medicare Withholding | No limit |
| Maximum Federal Unemployment Compensation Wage Base | $7,000 |
| Maximum State Unemployment Compensation Wage Base | $12,000 |

2009 Wisconsin
Unemployment Tax Rates

**Firms with less than $500,000 taxable payroll:**

- **Minimum rate - .05%**
- **New employer (construction industry) - 6.6%**
- **All other new employers - 3.25%**

## WISCONSIN UNEMPLOYMENT CHANGES

Beginning October 31, 2008, a new law became effective stating that Wisconsin unemployment tax payments must be *received* on or before the due date to be considered on time. The latest date an EFT payment can be made and still have a settlement date of the due date, is 4:00 P.M. one business day before the tax due date.

Effective January 1, 2009, the unemployment wage base will be increased from $10,500 to $12,000. This means that the first $12,000 of wages earned by each employee for each calendar year will be subject to Wisconsin unemployment taxes.

***Remember to update the Wisconsin unemployment wage base and tax rate in your payroll system.**

## FEDERAL UNEMPLOYMENT TAX (FUTA) DEPOSITS

- No deposit is required if the FUTA tax liability for the quarter is $500 or less.
- If payment is not required for the quarter, the liability incurred is added to the following quarter's liability.
- If the FUTA tax liability for the quarter is greater than $500 (including any unpaid liability from the previous quarter), a deposit is due the last day of the first month following the end of the quarter.

## NEW HIRING REMINDERS

Effective December 26, 2007, *all* employers must use the new Form I-9 for new employees. Within three days of being hired, the employee's identity and employment eligibility must be verified. If copies of documents are made, they must be retained with Form I-9. Employers must retain the completed forms for three years after the date of hire <u>or</u> one year after the date employment ends, *whichever is later*.

The new Form I-9 can be obtained from the internet website at **www.uscis.gov**. These forms can be reproduced, provided both sides are copied. Instructions must be available to all employees completing this form.

Employers are required to report each newly hired employee to the State of Wisconsin within 20 days after the employee starts work. State Form WT-4 or Federal Form W-4 can be used to report via mail or fax. Internet reporting can be completed at **www.dwd.state.wi.us/uinh.**

The WT-4 form can be obtained from the Wisconsin Department of Revenue website at **www.dor.state.wi.us**. The Federal W-4 can be obtained from the internet website at **www.irs.gov**.

**Remember…**

- If you pay bonuses to your employees, deduct FICA from the employee's gross pay at the current 2008 rates of 6.2% and 1.45%. No social security deduction is required if the employee is already over the $102,000 base for 2008.
- **If a noncorporate service provider payee fails to supply you with their taxpayer identification number on Form W-9, you are required to withhold 28% of the payment for federal withholding.**