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Now that the 2008 filing season is over, it is time to shift our focus to 2009 and 2010 tax planning. There are several items in the Recovery Act as well as an opportunity to roll your Traditional IRAs into Roth IRAs in 2010 that you should review so you can take full advantage of anything that may apply to you.

Understanding the provisions of the Recovery Act:

The Recovery Act passed in February by President Obama includes a number of beneficial, though temporary, tax changes for individuals. In other words, these tax breaks will apply in 2009 only (or in some cases, in 2009 and 2010).

1. Making Work Pay Credit:

I sent out information on this during tax season but thought it was important to review it again: Instead of mailing lump-sum stimulus checks to individuals and families like the federal government did last year, this year all employed individuals will receive a refundable credit of the lesser of 6.2% of their earned income or \$400 (\$800 MFJ). This will be issued in the form of adjusted withholding by employers so that employees receive more take-home pay in their paychecks.

The credit will be phased out for individuals with AGI between \$75,000 and \$95,000 (\$150,000-\$190,000 MFJ). The IRS issued new wage withholding tables on March 17, and you should have already noticed that the amount of federal income tax withheld from your paychecks has decreased.

2. Economic Recovery Payment

This payment may not apply to all of my clients but I am sharing it in case you have family or friends that may want to know more about it. The law provides for a one-time payment of \$250 for certain individuals who receive Social Security, Supplemental Security Income (SSI), Railroad Retirement and Veterans benefits. If you were eligible for one of these benefits at any time during the months of November 2008, December 2008 or January 2009, you may be eligible for the one-time payment.

The one-time payment should be received by the end of May 2009 and will be delivered the same way you currently receive your Social Security or SSI benefit. If you receive your monthly benefit by check, you will receive your one-time payment by check. If you receive your benefits by direct deposit or Direct Express debit card, you will receive the one-time payment the same way. Please note that the one-time economic recovery payment will be made **separately** from the regular Social Security or SSI benefit; it will not be included with the monthly benefit payment.

Key to note with regard to this payment: People drawing Social Security are not eligible for both the Social Security payment and the Making Work Pay tax credit. Congressional and IRS officials say taxpayers cannot double-dip into both programs. If you are getting extra Social Security money and benefit from a lower withholding in your paycheck, you do not get to keep the \$250 if you are working enough to get the full \$400 tax credit. The two will have to be reconciled when you file your 2009 tax returns in 2010. You can get up to \$400 total between the Social Security payment and the Making Work Pay tax withholding, but it can't be more than that

3. First-Time Homebuyer Credit

This credit amends the Housing Recovery Act of 2008, which provided a tax “credit” to first-time homebuyers that had to be repaid to the federal government over a period of 15 years. The new credit, which has been raised to \$8,000, does not have to be repaid as long as the home is not sold within three years. The credit is phased out for individuals with AGI between \$75,000 and \$95,000 (\$150,000 – \$170,000 MFJ).

To qualify, individuals must have either: 1) never owned a home before or 2) not owned or co-owned a home during the three years preceding the closing date. In addition, the home purchase must occur on or after January 1, 2009 and before December 1, 2009. For the purposes of the tax credit, the purchase date is the date when closing occurs and the title to the property transfers to the home owner. Finally, the home must be used as a principal residence.

One last caveat: individuals who sell, transfer or stop using the home as their primary residence may trigger a recapture of the entire remaining unpaid balance of the refundable credit.

4. American Opportunity Tax Credit

The Act renamed the HOPE education credit and expanded tax breaks for college education. In 2009 and 2010, individuals can receive a tax credit of up to \$2,500 of the cost of tuition and related expenses paid during the tax year. It is available to cover the first four years of post-secondary education in a degree or certificate program, with 40 percent of the credit refundable. The credit is phased out for individuals with AGI between \$80,000 and \$90,000 (\$160,000 – \$180,000 MFJ).

5. Expansion of Refundable Child Tax Credit

Previously, the \$1,000 credit taxpayers receive for each qualifying child under the age of 17 was refundable only to a limited extent. The Act reduces the earned income threshold from \$8,500 to \$3,000 in 2009 and 2010, which will result in the credit being refundable for more individuals and families.

6. Extension of AMT Relief

Two provisions of the Act will help shield more than 26 million families from having to pay the AMT this year: 1) increasing the AMT exemption amount by \$46,700 for individuals (\$70,950 MFJ) in 2009, and 2) allowing nonrefundable credits to offset AMT as well as regular tax.

7. Sales Tax Deduction for Vehicle Purchases

Individuals will receive a deduction for state and local sales and excise taxes paid on the purchase of **new** cars, light trucks, RVs and motorcycles bought between February 17 and December 31, 2009. Purchases of used cars do not qualify. The deduction is limited to the tax paid on up to \$49,500 of the purchase price, and is phased out for individuals with AGI between \$125,000 and \$135,000 (\$250,000 – \$260,000

MFJ). Note that this deduction is generally available regardless of whether you itemize or claim the standard deduction.

8. Suspension of Tax on Unemployment Benefits

Federal taxes on the first \$2,400 of unemployment benefits will be suspended in 2009—unemployment benefits in excess of \$2,400 will be taxable.

9. Larger Earned Income Tax Credit

Families with three or more qualifying children can claim an EITC of 45 percent of earnings up to \$12,570 in 2009, resulting in a maximum credit of \$5,656.50.

10. Federal Subsidy for COBRA Continuation Coverage for the Unemployed

The federal government will provide involuntarily terminated workers with a 65% COBRA premium subsidy for up to 9 months. In other words, these individuals can continue to participate in their former employers' group health plans at a cost of only 35% of their normal COBRA premium.

To qualify, you must have been involuntarily terminated from your job between Sept. 1, 2008 and Dec. 31, 2009. However, if your AGI is greater than \$125,000 (\$250,000 MFJ) you must pay back all or part of the subsidy when they file your income tax returns.

11. Personal Energy Property Credit

The Act provides a non-refundable credit in 2009 and 2010 equal to 30 percent of the cost of certain energy efficiency upgrades (insulation, doors, windows, electric heat pumps, etc.) and renewable energy systems (e.g., solar, wind, geothermal). The previous 10 percent credit was scheduled to expire in 2009.

If you do improvements that will create a credit, keep in mind that you can lower your withholding to benefit from the credit now instead of waiting until you file your 2009 tax return.

Other thoughts:

12. Non-cash contributions

Consider cleaning out your home this year and donating all those rarely used items to charity. You can take a charitable contribution for the thrift shop value of what you gave away. I recommend keeping some type of list of what you gave as most people tend to underestimate the value donated.

13. Rolling IRAs into Roth IRAs

In 2010 ONLY, you can roll your traditional IRA into a Roth IRA no matter what your income level. While you will be subject to tax on the amount rolled over (unless some of it was non-deductible and you filed Form 8606 to show that fact), all future withdrawals will be tax-exempt and not subject to mandatory distributions after age 70.

If for some reason you have made non-deductible contributions in the past but haven't submitted a Form 8606 to support them or the number reflected on the current year's 8606 is incorrect, don't worry. The IRS allows you to file this form as a standalone form. Please contact me if this applies to you as it is very important that the IRS have the correct info on file in anticipation of your converting your IRAs to a Roth IRA in 2010.

Because you will need outside funds to pay the tax due on any converted amounts, it is important to note is that if you convert your traditional IRA to a Roth in 2010, the new rules allow a payment plan. Half of the tax will be due in 2011 and the other half will be due in 2012. This is the equivalent of a tax free loan from the US Treasury. This benefit is only available for conversions done in 2010.

You may also want to consider making a non-deductible contribution to your IRA in 2009 so you can roll it over in 2010.

14. Suspension of Required Minimum Distribution (RMS) requirement for 2009 only

One bright spot among all the recent bleak financial news is the suspension of requirements for people older than 70 1/2 to make withdrawals from retirement accounts in the year 2009.

Normally, you're required to take taxable RMDs annually from your tax-deferred retirement savings once you turn 70½ or when you inherit such an account. Legislation enacted in December 2008 waives the distribution requirement for 2009, including first-time distributions that otherwise would have been due by April 1, 2010.

If you're affected by RMDs, this means you can keep money in your retirement accounts this year.

If you or someone you know has already taken their RMD but doesn't need the money, they can re-contribute it within 60 days without any tax implications, subject to IRS rollover rules.

Final Comment:

There are some real opportunities for tax savings in the information above, especially with the IRA conversion opportunity in 2010. As such, it may be beneficial to work together to do a tax projection so you can see the impact on your cash flow. Please contact me if I can help you think through any of these items or if you have any questions related to them.