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With 2009 soon coming to a close, it is a good time to review some of the tax changes that may affect your 2009 income tax returns as well as take a look at some of what 2010 will bring tax-wise.

## **2009 Tax Changes and Planning Ideas:**

### **1. First-Time Homebuyer Credit**

You can ignore the warnings that you've been hearing recently that the first-time homebuyer tax credit is about to expire. You no longer need to rush out and close that deal for a new home by November 30, 2009. The homebuyer tax credit is alive and well--in fact, better than ever!

With the backdrop of a weak economy (and pressure from the homebuilding and real estate industries), Congress could not resist the temptation to extend its generosity to homebuyers. As a result, Congress has enacted a law not only to extend the expiration date of the homebuyer tax credit through April 2010, but to expand its availability to a whole new set of potential homebuyers.

Under the provisions of the law, first-time homebuyers will continue to be eligible for the 10 percent tax credit of up to \$8,000 on the purchase of a principal residence through April 30, 2010. The tax credit was previously scheduled to expire on November 30, 2009, so the new law revives the credit for an extra five months. It also provides that if a binding written contract for purchase is entered into by the deadline, the homebuyer can have until June 30, 2010 to complete the purchase transaction.

In addition to the time extension, Congress added a few enhancements to the tax credit. Most significantly, the measure extends eligibility for the tax credit (limited to a maximum amount of \$6,500) to current homeowners who purchase a new principal residence. To be eligible, the homeowner must have owned and lived in their current home for five consecutive years in the time leading up to the purchase of the new home.

The new law also eases the income limits for tax credit eligibility. Under the new law, the tax credit phases out between income levels of \$125,000 and \$145,000 for individuals and \$225,000 and \$245,000 for joint filers. Under the prior law, the tax credit phased out between income levels of \$75,000 and \$95,000 for individuals and \$150,000 and \$170,000 for joint filers.

Some limitations have also been added to the tax credit eligibility standards: The credit can now be claimed only on a home that is purchased for \$800,000 or less; the homebuyer claiming the credit must be at least 18 years of age; some home purchases from related persons will not qualify for the credit; the credit cannot be claimed by a taxpayer who is a dependent of another taxpayer; and the credit will be

disallowed unless the HUD-1 settlement form (closing statement) is attached to a return where the credit is claimed as proof of the completed home purchase.

The IRS has also advised taxpayers to expect delays in the processing of returns where the first time homebuyer credit is being taken. As such, if you expect to claim the credit either this year or next, you may want to adjust your withholding so you avoid a penalty but owe taxes with your return so you are not left with a long wait for your refund.

One last caveat: individuals who sell, transfer or stop using the home as their primary residence within 36 months may trigger a recapture of the entire remaining unpaid balance of the refundable credit.

## **2. Making Work Pay Credit:**

In 2009 and 2010 all employed individuals will receive a refundable credit on their income tax return of the lesser of 6.2% of their earned income or \$400 (\$800 MFJ). The credit will be phased out for individuals with AGI between \$75,000 and \$95,000 (\$150,000-\$190,000 MFJ).

You are not likely to see any benefit from this on your return, however, as the tax tables were adjusted earlier in the year to give you the money back during the year instead of having to wait for tax time to get it.

## **3. Real Estate Tax Deduction for Non-Itemizers**

Taxpayers who pay real estate taxes on personal residences but do not itemize may now take a deduction of the lesser of the taxes paid or \$1,000. This will be calculated on the new Schedule L and will be added to the standard deduction. Please note that foreign property taxes do not qualify.

## **4. 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.

## **5. 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.

## **6. Personal Energy Property Credit**

The new law increases the energy tax credit for homeowners who make energy efficient improvements to their existing homes. The credit is now 30% of the cost of all qualifying improvements and raises the maximum credit limit to \$1,500 for improvements placed in service in 2009 and 2010. Taxpayers can take advantage of this credit even if they have already met the \$500 cap previously imposed.

The credit applies to improvements such as adding insulation, energy efficient exterior windows and energy-efficient heating and air conditioning systems.

Be aware that the standards are now higher than the standards were for the credit that was previously available. You can check on [www.energystar.gov](http://www.energystar.gov) to see if the products you are considering qualify.

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 tax return.

### **7. Illinois Property Tax Credit**

Illinois will continue to provide a 5% real estate tax credit for taxes paid on your principal residence. However, in order to claim the credit on your 2009 tax return, you will need to include your property identification number (PIN). This is listed on your real estate tax bill so be sure to keep a copy of the bill with your other tax documents so you will have it readily available at tax time.

### **8. Minimum Withholding or Estimated Tax Payment Requirements**

As your 2009 income may be different from what it was in 2008, you may want to take a quick look at your withholding or estimated tax payments for the year to see if you have paid enough in to avoid an underpayment penalty on your return or have withheld too much and can adjust your withholding for the last few pay periods to have more cash available to you now.

The federal threshold for avoiding an underpayment penalty is the lower of 100% (110% if your 2008 AGI was \$150,000 or above) of your 2008 tax liability or 90% of your 2009 tax liability. The Illinois threshold is the lower of 100% of your 2008 tax liability or 90% of your 2009 tax liability. If you have multiple jobs, keep in mind that each employer is required to withhold social security tax on wages they pay up to \$106,800. Excess social security taxes withheld will be treated as additional federal withholding on your tax return so you may have more withholding than you realize.

### **9. Worthless Stock**

If you own stock or other securities that have lost all their value you may be able to deduct a loss for your adjusted basis (cost). To claim the loss you must show that the security had value on December 31, 2008 and that an identifiable event caused the loss in 2009. The security must be totally worthless to take this deduction and you cannot claim a deduction for any part of the loss for which you were compensated – for example, by insurance.

### **10. Required Minimum Distribution (RMD) Requirement Waived for 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 or someone you know has already taken their RMD but doesn't need the money, they have until the *later* of November 30, 2009, or 60 days after the date the distribution was received, to roll the distribution back into a qualified plan.

### **11. Non-cash contributions**

A good last minute deduction opportunity is to clean out your home and donate 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.

## **12. Flexible Spending Accounts**

If you've covered the basics but still have some remaining funds, check your plan's list of eligible expenses for last-minute ideas. Make sure you use the money that's left in your account by the end of the year, or you'll lose it. It's also enrollment time for 2010 FSAs, so consider whether you've spent all your funds in the past and make any necessary adjustments.

## **2010 Information:**

### **1. Rolling IRAs into Roth IRAs (a review of what I previously shared)**

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.

### **2. Personal Exemptions**

For the first time in as long as I can remember, the personal exemption will not increase in 2010. It will remain at \$3,650. However, while personal exemptions are currently reduced by 2% for each \$2,500 (or fraction thereof) by which your AGI exceeds \$166,800 for those filing single or \$250,000 for those filing jointly, that phase-out is eliminated in 2010 so higher income taxpayers will actually get a tax break.

### **3. Standard Deduction**

The standard deduction amounts will also remain the same in 2010 as they were in 2009 for all filing statuses except Head of Household which will receive a \$50 increase.

### **4. 401(k) limit**

The maximum you can contribute to a 401(k) during 2010 will remain at \$16,500 (\$22,000 for those over age 50).

### **5. Social Security Wage Base**

The social security wage base will remain at \$106,800 in 2010. Social security and Medicare taxes are applied to income before pre-tax deductions such as 401(k) are deducted so once your gross earnings

exceed this level, you will no longer be subject to the 6.2% social security tax. There isn't a wage base for the 1.45% Medicare tax so all earnings are subject to that.

## **6. Social Security Payments**

There will not be an increase in social security income over the next 2 years. However, Medicare premiums are still going up. Those on fixed income will need to plan accordingly.

## **7. FUTA Tax**

For those of you with household employees you will get a small tax break in 2010 when the FUTA tax rate decreases from 6.2% to 6.0%. FUTA is the federal unemployment tax that must be paid if \$1,000 or more in cash wages are paid in any calendar quarter of the current or last year. It applies to only the first \$7,000 of wages paid.

## **8. Estate and Gift Tax**

2010 is the year when the estate tax is eliminated which means that if someone dies during 2010 they will not be subject to any estate tax no matter what the size of their estate. However, this also means that there is not a step-up in basis for assets acquired during 2010 through inheritance so it will be important to gather information related to basis for future use.

The annual gift tax exclusion remains at \$13,000 per recipient in 2010. This is the amount you (and your spouse, if applicable) can give to as many people as you like without incurring any tax liabilities.

## **Final Thought:**

As the holidays are approaching, I wanted to let you know how thankful I am to have the opportunity to assist you with your taxes and financial decisions and how incredibly grateful I am that I get to work with such wonderful clients. I hope we can continue to work together for a long time to come.