

CLIENT REPORT:

2009 First Quarter Federal Tax Developments

Dear Client:

The first three months of 2009 have seen a flood of new federal tax developments. We'd like to highlight some of the more important federal tax developments for you. As always, please give our office a call or send us an e-mail if you have any questions about these developments.

2009 Recovery Act

In February, Congress passed a nearly \$800 billion economic stimulus package with significant tax incentives for individuals and businesses. Many of the incentives are temporary so taxpayers need to be proactive this year not to miss them. The Economic Recovery and Reinvestment Act of 2009 (2009 Recovery Act) gives individuals an extended and enhanced first-time homebuyer tax credit, a new Making Work Pay credit, a new vehicle sales and excise tax deduction, improved energy efficiency tax breaks, and more. The 2009 Recovery Act gives businesses extended bonus depreciation and Code Sec. 179 expensing, many expanded energy tax incentives and an expanded net operating loss carry back for small businesses. Since President Obama signed the 2009 Recovery Act into law on February 17, the IRS has issued guidance on many of the tax incentives.

Making Work Pay Credit

Effective April 1, 2009, employers have started withholding at reduced rates to reflect the Making Work Pay credit. The credit is automatic and many individuals will see an immediate increase in their take home pay. However, married couples whose combined incomes place them in a higher tax bracket and individuals with more than one job may want to submit a revised Form W-4 to their employers to ensure that enough withholding is held. Our office can help you determine if you should submit a revised Form W-4 to your employer.

Economic Recovery Payments

The 2009 Recovery Act authorizes one-time payments of \$250 to individuals receiving Social Security benefits, disabled veterans and others on fixed incomes. The Social Security Administration, which will be sending the bulk of the one-time payments, has announced it will start making the one-time payments by mail and direct deposit in May 2009.

Help for Taxpayers

IRS Commissioner Douglas Shulman announced in January that the agency will be sensitive to taxpayers stung by the recession. The IRS will consider suspending collection actions, granting short-term extensions of time to pay, allowing taxpayers to miss a payment under an installment agreement, and revisiting offers-in-compromise to help distressed taxpayers. The IRS chief has also said that help will only be given to taxpayers who ask and taxpayers must have a history of compliance.

Net Operating Losses

The 2009 Recovery Act allows an eligible small business to carry back its 2008 net operating loss (NOL) for three, four or five years. For fiscal year taxpayers, this applies to the NOL for the tax year either beginning or ending in 2008. To qualify for the new carry back provision, a small business must have no greater than an average of \$15 million in gross receipts over a three-year period ending with the tax year of the NOL. The IRS issued guidance on the new carry back in March and reminded taxpayers about some special elections to take advantage of the new provision.

Offshore Accounts

In March, the IRS invited individuals and businesses to disclose unreported assets in foreign bank accounts. In exchange for full disclosure by taxpayers not already under investigation, the IRS will agree not to criminally prosecute tax evaders. Taxpayers must pay all back taxes plus interest and penalties, although the IRS will waive the 75 percent fraud penalty.

Cost-Sharing Arrangements

At year-end 2008, the IRS issued temporary regulations making some taxpayer-friendly changes to the cost-sharing arrangement rules under Code Sec. 482. A cost-sharing arrangement is an agreement where the parties share the costs of developing one or more intangibles in proportion to their shares of the reasonably anticipated benefits from their individual exploitation of the interests in the intangibles assigned to them under the arrangement. The IRS has identified the transfer of intangibles outside the U.S. as an area of potentially high noncompliance with the tax laws.

First-Time Homebuyer Credit

The first-time homebuyer credit gives eligible individuals as much as \$8,000 when they purchase a residence. The \$8,000 refundable credit is only available for purchases between January 1, 2009 and December 1, 2009. In a taxpayer-friendly move, the IRS announced that individuals who purchase a home in 2009 may claim the \$8,000 credit on their 2008 returns. If the home is purchased after April 15, 2009, a taxpayer may request an extension to file or file an amended return to claim the credit. Alternatively, they can wait to claim the credit when they file their 2009 returns in 2010. The IRS also announced liberal rules for allocating the credit among unmarried taxpayers.

President Obama's Budget Proposals

President Obama proposed a \$3.5 trillion fiscal year (FY) 2010 federal budget in February. The president proposed several tax incentives targeted to middle-income individuals, including a permanent Making Work Pay credit and a long-term alternative minimum tax (AMT) patch. Higher-income individuals, however, would pay more if Congress agrees to allow tax cuts enacted in 2001 to expire. The president has indicated that increased taxes on higher-income individuals will pay for health care reform. More details about the president's budget proposals are expected to be released in May.

COBRA

The 2009 Recovery Act provides a special subsidy to help individuals pay for COBRA continuation coverage. Eligible individuals pay only 35 percent of their COBRA premiums and the remaining 65 percent is reimbursed to the employer or other coverage provider through a payroll tax credit. Additionally, an individual generally must have been involuntarily terminated from employment between September 1, 2008 and December 31, 2009 and fall within certain income limitations. A limited retroactive window is also available. The IRS posted information about the COBRA subsidy on its website in March and issued guidance in April.

Unemployment Benefits

Individuals receiving unemployment benefits in 2009 can exclude the first \$2,400 from their incomes. The IRS reminded taxpayers about the exclusion (which, unlike other tax incentives has no income limitations) in March. The exclusion is only available for 2009. Individuals who are receiving unemployment compensation can elect to have income tax withheld. Our office can help you determine if withholding will be beneficial for you.

Broker Basis Reporting

In 2008, Congress passed the Emergency Economic Stabilization Act which, among other things, requires mandatory broker basis reporting. Brokers must report the adjusted basis of publicly-traded securities when reporting sales transactions and indicate whether gain is long-term or short-term. Reporting will be effective for stock acquired in 2011, mutual funds acquired in 2012, and other

securities acquired in 2013. The IRS announced in February that it was developing guidance on broker basis reporting and requested comments from interested parties.

Automatic Enrollment

The Obama Administration is touting automatic enrollment in 401(k)s and similar plans as an effective way to encourage workers to save for retirement. In February, the IRS issued final regulations to facilitate automatic enrollment in 401(k)s, 403(b) tax sheltered annuities and 457(b) government deferred compensation plans.

Private Tax Collection

Several years ago, the IRS hired private collection agencies to handle certain collection cases. The move was immediately controversial. Supporters argued that these were cases that the IRS would otherwise not be working. Opponents argued that IRS employees and not private entities should be contacting taxpayers about their tax debts. In March, the IRS announced that it was ending the private collection initiative. The IRS collected about \$70 million from the program over two years.

Ponzi Scams

Ponzi and similar scams have victimized taxpayers for years. Recently, a prominent investment advisor pleaded guilty to a massive Ponzi scheme involving securities fraud, money laundering and mail and wire fraud. The IRS released guidance in March clarifying the tax treatment of fraudulent investment scams. Among other things, the investor may be entitled to an ordinary theft loss rather than just a capital loss.

These are just some of the many federal tax developments so far this year. Please contact our office if you have any questions about these or other developments.

Sincerely yours,

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