

Supplement to J.K. Lasser's 1001 Deductions and Tax Breaks 2009 By Barbara Weltman

The tax law is not static and there have been a number of changes affecting 2008 returns, as well as returns in 2009. Since publication of the 2009 edition of *J.K. Lasser's 1001 Deductions and Tax Breaks*, Congress enacted the *Emergency Economic Stabilization Act of 2008*, the *Worker, Retiree, and Employer Recovery Act of 2009*, and the *American Recovery and Reinvestment Act of 2009*. The courts and the IRS have also spoken to many tax items that can impact your 2008 return. Here are key developments, some of which can apply to your 2008 return. Also factor in 2009 changes if they affect your quarterly estimated tax payments for 2009:

Chapter 1 – Your Family

Qualifying children. Under the Fostering Connections to Success and Increasing the Adoptions Act of 2008, the definition of “qualifying child” for purposes of the dependency exemption, child tax credit, earned income credit, and head of household has been changed starting in 2009. A person is a qualifying child only if, in addition to the other requirements for each type of tax break, the child is younger than the taxpayer claiming the benefit.

This change does not apply if the person being claimed as a qualifying child is permanently and totally disabled. A spouse who files a joint return cannot be considered a qualifying child of another taxpayer unless the joint return is filed only as a refund claim.

The tiebreaker rule for claiming a qualifying child has been changed to provide that if a parent and non-parent are both eligible to claim the child as a qualifying child but the parent does not claim the child, the non-parent may do so, but only if his or her adjusted gross income is higher than the adjusted gross income of any eligible parent.

Child tax credit. A portion of the child tax credit is refundable. For 2009 and 2010, the earned income threshold for the 15% refundable portion is \$3,000 (it had been \$8,500 for 2008).

Earned income credit. Those with three or more qualifying children can obtain a larger credit in 2009 and 2010. For these taxpayers, the credit percentage is increased to 45% (those with two qualifying children have a credit percentage of 40%).

Chapter 2--Medical Expenses

COBRA coverage for the unemployed. If you were involuntarily terminated and opt for COBRA under a company plan, the federal government will pay 65% of the premiums for nine months, starting with coverage in March 2009. Also those

who were terminated on or after September 1, 2008, and that did not elect COBRA (perhaps because it was too costly) now have until April 16, 2009, to make the election.

Government-paid coverage phases out for singles with modified adjusted gross income (MAGI) between \$125,000 and \$145,000, and for joint filers with MAGI between \$250,000 and \$290,000.

The payments will be made by having employers pay the premiums equal to the government contribution (the employers will reduce their employment taxes accordingly).

Health coverage credit. Certain individuals can have the federal government pay their premiums, which can be done on an advanced basis. The subsidy increases to 80% (up from 65%) for 2009 and 2010. However, the government is not required to make payments prior to August 17, 2009.

Health savings accounts. The contribution limits for 2009 have increased to \$3,000 for self-only coverage and \$5,950 for family coverage. Those age 55 or older by the end of 2009 can add another \$1,000 for the year.

To contribute to a health savings account, the person must be covered by a high-deductible health plan. For 2009, this means that the plan has a minimum deductible of \$1,150 for self-only coverage and \$2,300 for family coverage.

Chapter 3 – Education Costs

American Opportunity credit. For 2009 and 2010, the Hope credit is replaced by one entitled the American Opportunity credit. It is a better tax break than the Hope credit.

The credit is 100% of the first \$2,000 of qualified expenses, plus 25% of the next \$2,000 of expenses, for a top credit of \$2,500. The credit can be used to offset both regular tax and AMT liability.

The credit is partially refundable; the refundable portion is 40%.

The credit phases out for singles with MAGI between \$80,000 and \$90,000, and for joint filers with MAGI between \$160,000 and \$180,000.

529 plans. For 2009 and 2010, withdrawals from 529 savings plans that are used to pay for computer technology are tax free. Computer technology includes laptops, Internet access fees and software. However, games and entertainment software does not qualify unless it is “predominantly educational in nature.”

Chapter 4 – Your Home

First-time homebuyer credit. The credit for homes purchased after December 31, 2008, and before December 1, 2009, has been modified in several ways from the credit that applies to homes purchased during the qualifying period in 2008. The credit is 10% of the purchase price up to \$8,000 (up from \$7,500). There is no

repayment requirement as long as the home is not sold within 36 months (homes purchased in 2008 generally have a 15-year repayment requirement).

The modified adjusted gross income (MAGI) limits have not been changed. Thus, the credit phases out for singles with MAGI between \$75,000 and \$95,000, and for joint filers with MAGI between \$150,000 and \$170,000. The credit continues to apply only to first-time homebuyers (someone who has not owned a residence within the past three years).

The DC homebuyer credit cannot be claimed if the homebuyer qualifies for the first-time homebuyer credit.

Energy saving improvements. If you add insulation, storm windows, a new furnace or certain other energy-related improvements to a principal residence in 2009 and 2010, you can claim a tax credit in the aggregate up to \$1,500. There is no credit for improvements made in 2008.

The residential credit for adding solar and other alternative energy improvements has been expanded for 2009 and later years. The \$2,000 cap has been removed, so the credit is up to 30% of eligible expenses. These include the cost of heat pumps.

Chapter 7--Your Car

Deduction for taxes on car purchases. If you buy a new vehicle on or after February 17, 2009, and before January 1, 2010, you can deduct state and local sales and excise taxes. The deduction applies only to the cost of a vehicle up to \$49,500. The deduction is allowed even if you don't itemize your other deductions. However, there is an income limit. The deduction phases out for singles with modified adjusted gross income (MAGI) between \$125,000 and \$135,000, and for joint filers with MAGI between \$250,000 and \$260,000.

Chapter 9--Travel

Business travel per diem rates. The maximum federal per diem rate for travel from October 1, 2008, through September 30, 2009, covering lodging, meals and incidental expenses (M&IE) within the continental United States (CONUS) in most locations is \$109 per day (\$70 for lodging and \$39 for M&IE)--the same rate that had applied to the prior 12-month period. However, a number of the rates to certain areas have changed. These rates can be found at www.gsa.gov (click on "Per Diem Rates").

Chapter 13--Insurance and Catastrophes

Disaster losses. The Emergency Economic Stabilization Act of 2008 provides relief for those affected by natural disasters after December 31, 2007, and before January 1, 2010). The relief primarily helps businesses by permitting increased expensing for qualified disaster expenses, special depreciation for qualified disaster property and other specific breaks.

Chapter 14--Your Job

Making work pay credit. A new tax credit for 2009 and 2010 is 6.2% of earned income up to a maximum of \$400 for individuals and \$800 for joint filers. The credit is paid in the form of reduced take home pay; no special forms or actions are required by earners in order to receive the credit.

The credit phases out for singles with modified adjusted gross income (MAGI) between \$75,000 and \$95,000, and for joint filers with MAGI between \$150,000 and \$190,000.

Transportation fringe benefits. Starting in March 2009 and through 2010, the exclusion for monthly transit passes and van pooling is the same as for free parking. For 2009, the monthly exclusion for transit passes and van pooling is \$120 per month for January and February, and then increases in March to \$230 per month, the same as for parking. The exclusions will be indexed for inflation for 2010.

The fringe benefit for bicycle commuters starting in 2009 has not been changed; it remains at \$20 per month.

Unemployment benefits. Usually, all unemployment benefits are taxable. However, the first \$2,400 in unemployment compensation in 2009 is tax free.

Working abroad. The IRS has increased the limit on the foreign housing exclusion for eligible individuals working abroad in 2008. The maximum exclusion or deduction for 2008 is \$12,264. Certain areas, such as Hong Kong, qualify for a special, higher rate. A list of these rates can be found in IRS Notice 2008-107 (found in Internal Revenue Bulletin 2008-50).

Chapter 15 – Your Business

Net operating loss. For losses arising in 2008, small business taxpayers can opt for a longer carryback period. The usual carryback period is two years; for 2008 losses, a taxpayer can choose a three-, four-, or five-year carryback. To qualify the business must have average gross receipts of \$15 million or less.

As soon as the 2008 income tax return has been prepared, eligible taxpayers can file amended returns for prior years or apply for a quick refund on Form 1045 for individuals (e.g., sole proprietors and owners of pass-through entities) or Form 1139 for C corporations.

Standard mileage rate. The IRS announced the standard mileage rate, used in lieu of deducting the actual costs of business driving, for 2009; it is 55¢ per mile.

Those who own their vehicles and use the standard mileage rate must reduce the vehicle's basis by 21¢ per mile.

First-year expensing. The Economic Stimulus Act of 2008 raised the dollar limit to \$250,000 for 2008 and that limit is phased out if total equipment purchases in 2008 exceed \$800,000. The American Recovery and Reinvestment Act of 2009 extends the \$250,000 and \$800,000 limits through 2009.

Bonus depreciation. The Economic Stimulus Act of allows 50% bonus depreciation for certain property placed in service in 2008. This applies to capital equipment (generally equipment and machinery with a useful life of no more than 20 years). The American Recovery and Reinvestment Act of 2009 extends bonus depreciation through 2009.

The extension of bonus depreciation means there is a higher dollar limit on depreciation for vehicles purchased in 2009. The basic dollar limit can be increased by \$8,000 to account for bonus depreciation. This applies only to the purchase of a new (not pre-owned) vehicle.

15-year amortization of qualified leasehold and restaurant improvements. Instead of depreciating these costs over 39 years, they can be amortized over 15 years. This applies to costs in 2008 and 2009. This amortization rule also applies to certain improvements to retail space.

Charitable contributions. Enhanced deductions for business donations of food, books, and computer equipment apply for both 2008 and 2009.

Research credit. The 20% credit has been extended for 2008 and 2009. For tax years ending after 2008, the alternative simplified credit is increased to 14% of qualified research expenses that exceed 50% of the average qualified research expenses for the previous three years. The alternative incremental research credit is repealed for tax years starting after 2008.

Work opportunity credit. For 2009 and 2010, there are two new categories of workers that entitle an employer to this credit: unemployed veterans and disconnected youth (those age 16 to 24 who lack education and basic job skills).

Energy credits. Several energy-related business credits have been extended and new credits designed to stimulate research and investments in alternative energy. For example, there is an expanded credit for small wind energy property.

Chapter 16--Miscellaneous Items

One-time payment to certain taxpayers. The making work pay credit applies only to earners, but recipients of Social Security, Railroad Retirement benefits veterans benefits and SSI receive a one-time payment of \$250 in 2009. No action is required on the part of recipients to receive the payment.

Exemption amounts. The old AMT exemption amounts expired at the end of 2007. Congress increased the exemption amounts for the AMT for 2008 as follows to keep more than 21 million taxpayers from owing this tax:

- \$69,950 for married filing jointly
- \$46,200 for single taxpayers and heads of households
- \$34,975 for married filing separately

These exemption amounts apply only for 2008. For 2009, the exemption amounts have also been increased for one additional year:

- \$70,950 for married filing jointly
- \$46,700 for single taxpayers and heads of households
- \$35,475 for married filing separately

Tax credit offsets. Nonrefundable personal tax credits, such as education credits and the dependent care credit, can be used to offset both regular tax and the alternative minimum tax in both 2008 and 2009. So too, can certain business credits (work opportunity credit and the employer credit for FICA on tips). However, the credit for buying a hybrid vehicle cannot be used to offset AMT; those subject to AMT lose any benefit from this credit.

After 2009, the only nonrefundable personal credits that can offset AMT will be the adoption credit, the child tax credit, the American Opportunity credit, and the retirement saver's credit, unless Congress again changes the law.