

# **Evaluation of Year End Tax Changes and More.....**

*Updated November 2009*

**Presented by:**

*Sincerely, The Experts, Corp.*

**STE** ACCOUNTING  
INCOME TAX

## **“Worker, Homeownership and Business Assistance Act of 2009”**

***New legislation signed in to law on Nov. 6<sup>th</sup>, 2009 (effective date Nov.7<sup>th</sup>, 2009) extends and expands the First-Time Homebuyer Credit allowed by previous Acts. The new law:***

*Extends deadlines for purchasing and closing on a home*

Credit for the first time buyers in the amount of up to **\$ 8000** (\$ 4000 if MFS) **EXTENDED THRU APRIL 30<sup>th</sup>, 2010**. (Previous exp. date Nov.30<sup>th</sup>, 2009)

**New rule!** Property does not have to be actually purchased by April 30<sup>th</sup>, 2010. As long as a taxpayer enters into a written binding contract by the above date, he has until July 1<sup>st</sup>, 2010 to close on the purchase.

*Authorizes the credit for long-time homeowners buying a replacement principal residence*

**Effective Nov.7<sup>th</sup>, 2009 new credit in the amount of \$ 6500 (\$3250 if MFS) for existing homeowners buying replacement principal residence.**

To qualify taxpayer must have lived in the same principal residence for any 5 consecutive years in previous 8 years (8 year period ends on the date when the replacement property is purchased). Replaced principal residence may be sold, become vacant, converted to vacation or rental property.

*Raises the income limitations for taxpayers claiming the credit*

People with higher incomes can now qualify for the credit. The new law raises the income limits for homes purchased after Nov. 6<sup>th</sup>, 2009. The credit phases out for individual taxpayers with modified adjusted gross income (MAGI) between \$125,000 and \$145,000 or between \$225,000 and \$245,000 for MFJ. (Before Nov.6<sup>th</sup> limits MAGI phase-outs of \$75,000 to \$95,000 or \$150,000 to \$170,000 for MFJ)

*Implements other changes:*

**Effective Nov.7<sup>th</sup>, 2009**

- Credit available for home purchased for \$ 800,000 or less (before Nov.7<sup>th</sup> – no limitation)
- Credit not available for taxpayer under 18 years. A married taxpayer is treated as meeting the age requirement if the taxpayer or the spouse meets the age requirement. (Before Nov. 7<sup>th</sup> – no age limitation)
- Credit not available if property purchased by a taxpayer who is a dependent of another taxpayer. (Before Nov. 7<sup>th</sup> - no limitation)
- Credit is not allowed if copy of properly executed( means signed) settlement statement used to complete the purchase is not attached to the relevant tax return.
- \$ 8000 credit for principal residence purchased after Dec.31<sup>st</sup>, 2008 must be repaid only if the home ceases to be principal residence (sold or converted) within 36 month. After 36 months there are no recapture requirements.

-For principal residences purchased after December 31<sup>st</sup>, 2008 taxpayer can elect to treat the purchase as made on December 31<sup>st</sup> of the calendar year preceding the purchase for purposes of claiming the credit on the prior year's tax return, For example: principal residence purchased January 2010- taxpayer may elect to claim the credit of \$ 8000/\$6500 on 2009 income tax return.

Other important parts of the new ACT:

*1. Unemployment benefits extended:*

*From previous Act"American Recovery and Reinvestment Act" signed in Feb. 2009 -First \$2400 of unemployment benefits are not taxable in 2009.*

The extension provides for 14 weeks of extended unemployment benefit coverage for every state and an additional 6 weeks, for a total of 20 weeks, in high unemployment states where unemployment is over 8.5%.

Illinois qualifies for the full 20 weeks of extension- unemployment rate approx. 10%.

*2. Increased S-Corporation and Partnership Penalties*

Under the new law penalties for late-filing tax returns for S-corporations and partnerships, including LLCs treated as partnerships or corporations are increased. The late-filing penalty has more than doubled, from \$89 to \$195 per month per shareholder or partner for each month that a return is filed after the deadline (including extensions). It applies to returns for taxable years beginning after December 31st, 2009(when filing 2010 income taxes in 2011).

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**More Tax News for individuals for tax year 2009**

***Making Work Pay Credit***

New credit in the amount of up to \$ 400 will be available in 2009 and 2010. Most wage earners will benefit immediately — or already have — with a larger paycheck as a result of the changes made to the federal income tax withholding tables to implement the Making Work Pay tax credit. Some people may find that the changes built into the withholding tables result in less tax being withheld than they prefer. Self-employed individuals can also benefit now from the Making Work Pay tax credit by evaluating their expected income tax liability, allowing for this tax credit if they are eligible, and making the appropriate adjustment in the amount of their regularly scheduled estimated tax payments.

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## ***Exclusion for Unemployment Compensation***

Recipients of unemployment compensation are allowed to exclude from income up to \$ 2400 of unemployment compensation benefits received in 2009.

## ***New vehicle Sales Tax Deduction***

“The American Recovery and Reinvestment Act” permits taxpayers to take a deduction for state and local sales and excise taxes paid on the purchase of new cars, light trucks, motor homes and motorcycles. The deduction is available on new vehicles purchased **from Feb. 17, 2009, through Dec. 31, 2009**. In states that don't have a sales tax, the law provides a deduction for other taxes or fees paid. This deduction is available whether or not a taxpayer itemizes deductions on Schedule A.

The deduction is limited to the taxes and fees paid on up to \$49,500 of the purchase price of an eligible vehicle. The deduction is reduced for joint filers with modified adjusted gross incomes (MAGI) between \$250,000 and \$260,000 and other taxpayers with MAGI between \$125,000 and \$135,000. Taxpayers with higher incomes do not qualify.

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## ***American Opportunity Tax Credit (expended Hope Credit)***

Under “The American Recovery and Reinvestment Act” the Hope Credit is modified and renamed to “American Opportunity Tax Credit” for tax years 2009 and 2010.

### ***Tax year 2009 & 2010***

Available for first 4 years of post secondary education

Maximum credit \$ 2500

Up to 40 % is refundable (up to \$1000)

Cost of books and related materials needed for the course no matter where purchased or if a condition of enrollment or not

### ***Tax year 2008***

Available for first 2 years

Maximum credit \$ 1800

Non refundable

Cost of books & related materials only if paid to the institution as a condition of enrollment

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## ***Eligible Expenses Under 529 Plans***

### *What is a 529 plan?*

They are investment accounts designed to help families pay for future expenses associated with college or other qualified post-secondary training.

“The American Recovery and Reinvestment Act of 2009” added computer technology to the list of college expenses (tuition, books, etc.) that can be paid for by a 529 plan. For 2009 and 2010, the law expands the definition of qualified higher education expenses to include expenses for computer technology and equipment or Internet access and related services to be used by the designated beneficiary of the 529 plan while enrolled at an eligible educational institution. Software designed for sports, games or hobbies does not qualify, unless it is predominantly educational in nature. It is effective for expenses paid of incurred after December 31<sup>st</sup> 2008.

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## ***Mortgage Relief Act***

The law originally applied to debt forgiven in 2007, 2008 or 2009. The law has been extended and now it applies to debt discharged after 2006 and before 2013. Debt reduced through mortgage restructuring, as well as mortgage debt forgiven in connection with a foreclosure, may qualify for this relief. Normally, debt forgiveness results in taxable income. Under the “Mortgage Relief Act” taxpayers may exclude debt forgiven on their principal residence if the balance of their loan was less than \$2 million. The limit is \$1 million for a married person filing a separate return. Debt must be used to buy, build or substantially improve the taxpayers’ principal residence and must be secured by that residence. Debt used to refinance qualifying debt is also eligible for the exclusion, but only up to the amount of the old mortgage principal, just before refinancing.

Debt forgiven on second homes, rental property, business property, credit cards or car loans does not qualify for the exclusion from income under this act (but other provisions may apply).

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## ***2009 Property Tax Deduction for Taxpayers Who Do Not Itemize***

Property owners who use the standard deduction, rather than itemize their individual deductions when filing their income taxes can take additional property tax deduction, up to \$500 for single taxpayers and up to \$1,000 for married couples filing jointly.

The deduction is determined by whichever of the following is lower: the amount of property taxes paid, or \$500 for single taxpayers or \$1,000 for married, filing jointly.

### ***For state income tax purpose:***

Beginning with tax year 2009 PIN number (available on the property's tax bill) of the principal residence is required in order to be able to claim a deduction for property tax paid on IL. State tax income tax return.

### ***Residential Energy Property Credit***

The new law increases the energy tax credit for homeowners who make energy efficient improvements to their existing homes. The new law increases the credit rate to 30 percent 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. Please note that similar law was in place for 2007, but was not available for 2008.

The credit applies to improvements such as adding insulation, energy efficient exterior windows (including skylights), doors, energy-efficient heating and air conditioning systems, energy efficient water heaters etc.

For full list of qualifying efficient home improvements and the required standards please visit:

[http://www.energystar.gov/index.cfm?c=tax\\_credits.tx\\_index#s1](http://www.energystar.gov/index.cfm?c=tax_credits.tx_index#s1)

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## **Tax news for Businesses for tax year 2009**

### ***Section 179 deduction***

#### ***What is a section 179 deduction?***

Under section 179 businesses can expense business assets placed in service during the tax year and use it as a deduction to lower their tax liability.

Under the new law "American Recovery and Reinvestment Act of 2009" for tax years beginning with 2009 a taxpayer is allowed to annually expense up to \$ 250,000 (\$ 128,000 under the old law). The total investment ceiling limit is \$ 800,000(\$ 510,000 under the old law).

Under this law many small and moderate size businesses will be able to claim full deduction for most depreciable assets purchased in 2009, thus reducing their taxable income. The law has been extended from tax year 2008.

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### ***Additional 50 % first year depreciation business assets placed in service in 2009.***

For qualified business property placed in service in 2009 an additional 50% depreciation deduction of adjusted basis is allowed under the new law "American Recovery and Reinvestment Act of 2009".

#### ***What is a qualified property?***

Qualified property-most types of business properties other than BUILDINGS with a recovery period of 20 years or less.

50 % additional first year depreciation allowance applies to all qualified property and is mandatory unless taxpayer elects out. Election out can be made for any class of property and if made applies to all assets in that class placed in service during the year. That means if taxpayer elects out of 50 % additional depreciation for one business asset, he elects out for all assets in the same class life.

This law has been extended from previous year.

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## ***First year Depreciation for new passenger Autos used in business raised by \$ 8000.***

Under the new law "American Recovery and Reinvestment Act of 2009" first year depreciation limit (if actual expenses are chosen in oppose to standard mileage deduction) for passenger automobiles used in business more than 50% is increased by **\$ 8000**. Then total first year depreciation for a passenger automobile is \$2960+\$ 8000 and for a light truck or van it is \$3160 + \$8000. This law has been extended from previous year.

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## ***Standard mileage rates increased***

Taxpayers may use the deduction based on calculating mileage for business, charitable or medical or moving purposes.

New rates effective as of January 1<sup>st</sup> 2009 are: 55 cents per business mile (\$.505/.585 in 2008), \$. 24 per mile for medical or moving purposes Rates per mile for charitable purposes remain the same at \$.14 per mile.

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The IRS each year makes changes to business deductions that is why it is important to be informed on what new provisions have been introduced or what changes have been made to prior years deductions. The existing provisions for business deductions can be advantageous to your business if you select the most adequate deduction for your business situation.

On the other hand there are new requirements for business that may not seem so business friendly and which may require explanation in order not to complicate the running of your business.

The following are a few examples:

## ***Reasonable compensation for S Corp. shareholder-employee.***

Reasonable compensation for shareholders who perform any services to the corporation is required by IRS under "Revenue ruling 74-44" unless there were no distributions to such shareholder or shareholder performed only minor services.

The number one audit risk for S-Corporations is salary and wages paid to officers of the corporation. The fastest way to get audited as an S-Corporation is to file an 1120S with no amount showing on Form 1120S Line 7 "Compensation of Officers." It is assumed by the IRS that no one works for free, and so the IRS repeatedly said that officers of the corporation must receive wages (reported on line 7). As an owner-employee of the S-Corporation, you must pay yourself a salary, and pay payroll taxes on your salary, even if the business is losing money. You don't have to pay yourself a high salary, but it must be a "reasonable amount" according to the IRS. Please note that the IRS has announced that it will perform more random employment tax audits starting February 2010.

*What is reasonable compensation?*

Compensation of shareholder-employees should be based on the same criteria as salary for non-shareholders. Factors would include general market rates; the individual's knowledge, skills, and abilities; amount of hours worked; and so forth. Salary is reasonable if a non-shareholder would be willing to accept the job at the proposed salary level. Generally, the IRS will grant the S-Corporation a degree of latitude in setting salary compensation for shareholder-employees. However, the salary must be paid, and the level of salary must be appropriate.

*What is unreasonable compensation?*

Zero salary is unreasonable. No one works for free. Salary below minimum wage is unreasonable. You would not persuade a non-shareholder to accept a job offering below minimum wage. Salary far in excess of an appropriate wage is unreasonable. Paying a million-dollar salary when an officer in similar position would expect to make only \$150,000 is also unreasonable.

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***Late filing penalties for businesses***

IRS is getting tougher on assessing penalties for late filing business tax returns.

*Penalty for Late Filing of an S Corporation or Partnership Return*

For tax returns for tax years beginning in 2008 that are required to be filed after 2008 late filing penalty is increased to \$89 for each month or part of a month (up to 12 months) the return is late or does not include the required information, multiplied by the total number of persons who were shareholders/partners.

For taxable years beginning after December 31<sup>st</sup>, 2009(when filing 2010 income taxes in 2011) the late-filing penalty will increase from \$89 to \$195 per month per shareholder or partner for each month that a return is filed after the deadline (including extensions).

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## ***Employee vs. subcontractor***

Under the state law "Employee Classification Act" which went in to effect as of January 1, 2008 businesses in construction industry must re-evaluate how they treat their workers.

*What is construction industry?*

For purpose of this new law construction industry includes but is not limited to public and private construction, residential and commercial buildings, maintenance, renovation and repair work, painting and decorating work, landscaping and the transportation of construction related materials.

Under this law each individual performing service for a business (contractor) must be treated as an employee with only few exceptions.

The exceptions are:

- Individual providing services is not controlled by the contractor
- The service provided by the individual is outside the usual course of services performed by the contractor.
- Individual performing services is engaged in an independently established business (sole proprietor, partnership, corporation, LLC) and is able to proof that the business is a legitimate business by going thru 12 checkpoints.

Please note that only corporations are not required to go thru 12 points in order to proof that the business is legitimate.

Please find few and most important differences between employee and subcontractor.

<b>EMPLOYEE</b>	<b>VS</b>	<b>SUBCONTRACTOR</b>
1. Employed and paid by hours		1. Paid for work completed as As described in a contract
2. Controlled and directed by the Employer		2. Free from control and directions over the performance of the Services
3. Regular working hrs		3. Hrs not regulated by the Contractor
4. When providing service Uses employer's tools and equipment		4. Furnishes the tools and Equipment necessary to provide The service

The Illinois Department of Labor is authorized to enforce the New Law including assessing penalties of up to \$ 1500 for each violation found in first audit and up to \$2500 for each repeat violation within 5 years. Please note that each violation means each day of not correctly classifying workers.

*It is important to say that this law is not really a new law. Same or similar laws are already in place in different departments like IRS and IDES (Illinois Dept. Of Employment Security) and not only in construction industry, but the business industry in general.*

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*These materials were prepared by Sincerely, The Experts, Corp. It contains general tax information for taxpayers. As each tax situation may be different, do not rely upon this information as your sole source of authority. Please seek professional advice for all tax situations.*

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