# 2009 Economic Stimulus Act

On February 17, President Obama signed into law the "American Recovery and Reinvestment Act of 2009" (the 2009 Economic Stimulus Act). This new legislation was passed to aid our ailing economy and includes a wide variety of tax provisions, many of which will affect both individuals and small businesses. Included below are highlights of the more prominent provisions.

## INDIVIDUAL PROVISIONS

**Plug-In Electric Vehicle Credit -** For vehicles bought after February 17, 2009 and before January 1, 2012, the Recovery Act creates a new 10% nonrefundable personal credit for low-speed vehicles, motorcycles, and three-wheeled vehicles that meet the criteria of a qualified plug-in electric drive motor vehicle. The maximum credit for these vehicles is $2,500. If the vehicle is also used in business, the business portion of the credit is treated as a general business credit. Four-wheel vehicles purchased after January 1, 2009 also qualify for this credit based on a law passed in 2008. There are additional qualifications, so please call for further details.

**Unemployment – Partially Tax-Free** – Although some states don't tax unemployment compensation, it is taxable income for Federal purposes. Under the new law and for 2009 only, there is no federal income tax on the first $2,400 of unemployment benefits. However, the balance is taxable. The benefit of this provision depends upon your tax bracket. For example, if you are in the 15% tax bracket, this will save you up to $360 in taxes.

**AMT Patched Again** – For yet another year, Congress has applied a patch to the alternative minimum tax (AMT) to prevent middle-income taxpayers from getting hit by a punitive tax that was originally enacted to counter tax shelters of the wealthy.

- AMT Exemption Amount Increased - The AMT exemptions have been increased for 2009 to: $70,950 for married individuals filing jointly, $46,700 for unmarried individuals, and $35,475 for married individuals filing separately. The AMT phase-out rules remain unchanged.
- AMT Relief for Nonrefundable Personal Credits - Nonrefundable personal credits will offset the AMT for 2009. Those credits include the dependent care credit, elderly and disabled credit, education credits, adoption credit, child tax credit, mortgage credit, saver's credit, certain residential, home energy credits, first-time homebuyer credit, and plug-in electric vehicle credit.

**One-Time Payment to Retirees -** Retirees, disabled individuals and Social Security beneficiaries and SSI recipients receiving benefits from the Social Security Administration or Railroad Retirement Board, and disabled veterans receiving benefits from the U.S. Department of Veterans' Affairs will receive a one-time payment of $250 in 2009. The one-time payment will reduce any allowable *Making Work Pay* credit. Thus, taxpayers receiving any of the benefits mentioned above who are working will be required to reduce any otherwise allowable *Making Work Pay* credit by the $250 one-time payment. At press time, no date was specified for release of the payments, although the new law specifies payments be made within 120 days of enactment. Presumably payments will be made in conjunction with the taxpayer's SS, RR or Veterans payments.

Government retirees who are not eligible for Social Security will also receive the $250, but in the form of a credit on their 2009 tax return, which will reduce any otherwise allowable *Making Work Pay* credit for 2009.

**Computers and 529 Education Plans –** Section 529 Education Plans are tax-advantaged savings plans that permit contributions of large sums of money to be used for the education of a designated beneficiary, and investment earnings generated by these plans are tax-free if the funds are used for qualified education expenses. Qualified education expenses include tuition, room & board, mandatory fees and books. For 2009 and 2010, computers and computer technology purchases qualify as qualified education expenses, provided the technology, equipment, or services are to be used by the plan beneficiary or his family during any of the years the beneficiary is enrolled at an eligible educational institution.

**Break on Small Business Stock Capital Gains –** To encourage the risk of forming new small businesses (sales of $50 million or less), the tax code (Sec. 1202) has for some time allowed taxpayers to exclude fifty percent (50%) of the gain from the sale of certain small business stock held for more than five years. The amount of gain eligible for the exclusion is limited to the greater of 10 times the taxpayer's basis in the stock, or $10 million in gain from stock in that small business corporation. This provision is limited to individual investments and not the investments of a corporation. The non-excluded portion of section 1202 gain is taxed at the lesser of ordinary income rates or 28 percent, instead of the lower capital gains rates for individuals. A provision in the Recovery Act allows a seventy-five percent (75%) exclusion for individuals on the gain from the sale of certain small business stock held for more than five years. This change is for stock issued after the date of enactment and before January 1, 2011. There are also some alternative minimum tax implications associated with the sale; please call this office for additional information.

**Expanded Child Tax Credit** – A credit of $1,000 is available to taxpayers for each qualifying child under age 17 for 2009 and 2010. This credit is phased out depending on income and the number of qualifying children. Taxpayers with "earned" (not investment) income whose child credit exceeds their regular and alternative minimum taxes are eligible for a refundable credit. This credit is 15% of the taxpayer's earned income in excess of a threshold amount, which was to be $12,550 for 2009. However, for 2009 and 2010, the threshold amount has been reduced to $3,000, potentially expanding the number of taxpayers who may qualify for the refundable portion of the credit.

**American Opportunity Credit** – The Hope education credit, which provides a tax credit up to $1,800 for qualified higher education, has been enhanced and renamed for 2009 and 2010. For these two years, it will be called the *American Opportunity* tax credit. Where the Hope credit only applied to the first two years of post-secondary education, the *American Opportunity* credit will be available for four years of college, and the maximum credit per student increases to $2,500. The credit will be based on 100% of the first $2,000, and 25% of the next $2,000, of tuition, fees and course material (including books) expenses paid during the tax year. 40% of the credit is refundable, provided the taxpayer is not a child under the age of 18 or under the age of 24, a full-time student and is not self-supporting.

For higher-income taxpayers, this credit begins to phase out for AGI in excess of $80,000 ($160,000 for married couples filing jointly), an increase from the previous phase out thresholds of $50,000/$100,000.

**Expanded Earned Income Tax Credit (EITC)** – EITC is a refundable tax credit that rewards lower-income individuals for working. The credit, based upon the amount of the individual's earned income, is determined through a complicated computation, where the credit increases until the earned income reaches a predetermined apex and then begins to decrease as the amount of earned income increases. As a result the credit becomes zero when the taxpayer is no longer considered a low-income individual. The amount of the credit is based upon the number of the taxpayer's qualifying children. Previously, the categories for the number of children were none, one and two or more. Under the new stimulus legislation for 2009 and 2010, a new category of three or more children has been added and, for that category, the credit will be based on 45% of the earned income instead of the 40% which applies to the category for two children. This, in effect, temporarily increases the otherwise allowable EIC for taxpayers with three or more children and provides a maximum credit in 2009 of $5,657 when the taxpayer's earned income is $12,750.

Joint filing taxpayers will also benefit by having the point at which the EITC phases out for them increased by $1,880 of earned income, to $5,000 for 2009, and to be inflation-adjusted for 2010.

**Home Energy-Efficient Purchases** – Previous tax law included a 10% tax credit for the cost of home energy-efficient purchases, such as energy-efficient furnaces, hot water boilers, windows, doors, roofing, insulation and other qualified energy-efficient property, and included complicated cost limits on each category along with lifetime caps. Effective for qualifying items purchased in 2009 and 2010, the credit rate has been increased to 30% with an aggregate cap of $1,500.

**Tax Credit Cap Removed for Home Energy Systems** – Through 2016, individuals are allowed to claim a 30% tax credit for the cost of qualified solar water heating property (capped at $2,000), qualified small wind energy property (capped at $500 per kilowatt of capacity, up to $4,000), and qualified geothermal heat pumps (capped at $2,000). Under the new law, beginning in 2009, the dollar caps for each of these properties is removed.

**Making Work Pay Credit** –For 2009 and 2010, we have the new "Making Work Pay" credit which the Obama administration says will cut taxes for more than 95% of working families in the United States. It provides a refundable credit of 6.2% of a taxpayer's earned income not to exceed $400 for individuals and $800 for joint filing couples. This credit phases out at the rate of 2% of modified AGI, starting at $75,000 for individuals and $150,000 for joint filers. It is fully phased out at $95,000 for individuals and $190,000 for joint filers. Taxpayers can receive this benefit through a reduction in the amount of income tax that is withheld from their paychecks, or through claiming the credit on their tax returns.

**Above-the-Line Sales Tax Deduction for New Car Purchases** – Taxpayers that itemize their deductions have the option of deducting state income tax or sales tax. However, if the standard deduction is taken, there is no income tax benefit received from the sales tax that was paid for a vehicle. Under a provision that applies only to 2009, taxpayers will be allowed to deduct the sales tax paid on the purchase cost of a new motor vehicle, up to a cost of $49,500 ($24,750 if filing married separate). The deduction will be claimed "above-the-line," thus providing taxpayers with a tax benefit for the tax paid, even if they don't itemize deductions. Let's say the vehicle cost $30,000, sales tax was 8% and the taxpayer was in the 15% tax bracket. He or she would save $360. This deduction is not available to taxpayers who elect to deduct sales tax in lieu of income taxes as an itemized deduction.

To keep higher-income taxpayers from benefiting from this deduction, it phases out ratably for a taxpayer with modified AGI between $125,000 and $135,000 ($250,000 and $260,000 on a joint return).

Qualifying vehicles for this deduction are new cars, SUVs, light trucks, or motorcycles weighing no more than 8,500 pounds, and motor homes.

**First-Time Homebuyer Credit -** The original first-time homebuyer credit enacted in 2008 provided what was essentially a $7,500 interest-free, fifteen-year loan. The credit has been enhanced for 2009 by raising the credit amount to $8,000 ($4,000 married separate) and removing the repayment requirement, except in cases where the home is sold or ceases to be the taxpayer's principal residence within 36 months of its purchase. The home must be purchased between January 1, 2009 and before December 1, 2009. It must be located in the U.S, and not purchased from a close relative. The taxpayer can choose to claim the credit on either his or her 2009 return or the original or amended 2008 return. Taxpayers wishing to take advantage of this provision should act quickly.

A taxpayer is considered a first-time homebuyer if he (or spouse, if married) had no present ownership interest in a principal residence in the U.S. during the three-year period before the purchase of the home to which the credit applies.

The purpose of the credit is to assist lower-income individuals in acquiring their own home. Thus, the credit is reduced or eliminated for higher-income taxpayers. For a married couple filing a joint return, the phase-out range is $150,000 to $170,000. For other taxpayers, the phase-out range is $75,000 to $95,000.

## BUSINESS PROVISIONS

**Bonus Depreciation Extended -** Businesses are allowed to recover the cost of capital expenditures over time according to a depreciation schedule. Last year, Congress temporarily allowed businesses to recover the costs of capital expenditures made in 2008 faster than the ordinary depreciation schedule would allow, by permitting these businesses to immediately write-off 50% of the cost of depreciable property (e.g., equipment, tractors, wind turbines, solar panels, and computers) acquired in 2008 for use in the United States. This temporary provision has been extended through 2009.

**Extension of Enhanced Small Business Expensing -** In order to help small businesses quickly recover the cost of certain capital expenses, small business taxpayers may elect to write-off the cost of these expenses in the year of acquisition in lieu of recovering these costs over time through depreciation. This is commonly referred to as the Sec. 179 deduction. Until the end of 2010, small business taxpayers are allowed to write-off up to $125,000 (indexed for inflation) of capital expenditures subject to a phase out once capital expenditures exceed $500,000 (indexed for inflation). Last year, Congress temporarily increased the amount that small businesses could write-off for capital expenditures incurred in 2008 to $250,000, and increased the phase-out threshold for 2008 to $800,000. Those increased amounts have been extended to 2009.

**Five-Year Carryback of Net Operating Losses** – Under current law, net operating losses (“NOLs”) may be carried back to the two taxable years before the year that the loss arises (the “NOL carryback period”) and carried forward to each of the succeeding twenty taxable years after the year that the loss arises. For NOLs for any tax year beginning or ending in 2008, the bill extends the maximum NOL carryback period from two to five years for small businesses with gross receipts of $15 million or less.

**Work Opportunity Credit** – This provision provides a credit to an employer for qualified wages paid to members of targeted groups. The credit, except for long-term family assistance recipients and summer youth employees, equals 40% (25% for employment of 400 hours or less) of qualified first-year wages ($6,000 cap) for a maximum credit of $2,400. For employment beginning in 2009 and 2010, wages paid to two new targeted groups – unemployed veterans and disconnected youth – count towards the credit.

An individual will qualify as an unemployed veteran if they were discharged or released from active duty from the Armed Forces during the five-year period prior to hiring, served on active duty for more than 180 days or was released from active duty due to a service-connected disability, and received unemployment compensation for not less than four weeks during the year before being hired. An individual qualifies as a disconnected youth if they are between the ages of 16 and 25 and have not been regularly employed or attended school in the past 6 months.

**S Corp Built-In Gain Holding Period Shortened Temporarily to Seven Years -** Under current law, if a taxable corporation converts into an S corporation, the conversion is not a taxable event. However, following such a conversion, an S corporation must hold its assets for ten years in order to avoid a tax on any built-in gains that existed at the time of the conversion. The bill temporarily reduces this holding period from ten to seven years for sales occurring in 2009 and 2010.

**Repeal of Treasury Section 382 Notice -** Last year, the Treasury Department issued Notice 2008-83, which liberalized rules in the tax code that are intended to prevent taxpayers that acquire companies from claiming losses that were incurred by the acquired company prior to the taxpayer’s ownership of the company. The bill would repeal this Notice prospectively.

**Vehicle 50% Bonus Depreciation** – Some years ago, to prevent higher-income taxpayers from creating large tax writes-offs from expensive vehicles, Congress implemented the "Luxury Auto Limitations," which places a cap on first-year depreciation. The provision that extends the 50% first-year bonus depreciation to 2009 purchases (mentioned elsewhere in this article) also extends the increased dollar cap for new vehicles placed in service in 2009 by $8,000. The regular luxury auto depreciation caps for 2009 have not yet been announced by the IRS. For 2008, the regular cap was $2,960 but was increased to $10,960 when the 50% bonus depreciation was claimed. The 2009 amount will likely be similar.