

# Stimulus Act Provides Substantial Tax Breaks for Businesses and Individuals

The American Recovery and Reinvestment Act of 2009 (ARRA), signed by President Obama on Feb. 17, provides close to \$300 billion in tax breaks for businesses and individuals, and hundreds of billions more for spending projects designed to stimulate our nation's flagging economy.

Below is an overview of the more widely applicable tax changes affecting businesses, individuals and families in the new law. If you would like more detailed information about this new tax law, please give us a call. We would be glad to help you determine exactly how ARRA will affect your tax liability — and what you should do to take full advantage of the act.

## *Changes Affecting Businesses*

■ **Reduced estimated tax payment requirements.** For 2009, ARRA reduces the estimated tax payment requirements for many small business owners. Owners generally will qualify for the reduced payments if their adjusted gross income (AGI) for 2008 was less than \$500,000 and if more than 50 percent of their 2009 gross income is generated from a "small business," which is defined as a business that, on average, had fewer than 500 employees during 2008.

■ **Deferral of income from cancellation of debt.** Taxpayers generally must recognize cancellation-of-debt income (CODI) when they cancel — or repurchase — debt for an amount less than its adjusted issue price. In certain situations, ARRA allows businesses to defer CODI generated from repurchasing business debt after Dec. 31, 2008, and before Jan. 1, 2011, until calendar year 2014 and then report the income ratably over the 2014 through 2018 tax years.

■ **Shortening of S corporation built-in gains period.** Although a C corporation conversion to an S corporation isn't a taxable event, the S corporation normally must hold on to its assets for 10 years to avoid tax on any built-in gains that existed at the time of the conversion. For conversions occurring in 2009 and 2010, however, ARRA reduces this holding period to seven years.

*The act also expands some important tax breaks for businesses:*

■ **Net operating loss carryback.** A net operating loss (NOL) generally may be carried back two years to generate a current tax refund, providing a cash infusion in times of loss. For 2008 (not 2009), ARRA extends the maximum NOL carryback to five years for small businesses with gross receipts of \$15 million or less.

■ **Work Opportunity credit.** Employers can claim a credit equal to 40 percent of the first \$6,000 of wages paid to employees in certain target groups, such as ex-felons, food stamp recipients and disabled veterans. ARRA expands the eligible target groups to include unemployed veterans and disconnected youth. This expanded benefit applies to such workers hired in 2009 and 2010.

■ **Depreciation breaks extended.** To spur additional investment, ARRA extends the increase in the Section 179 limit for initial year expensing to \$250,000 (from \$125,000 indexed for inflation). The expensing election begins to phase out dollar for dollar when total asset acquisitions for the tax year exceed \$800,000 (up from \$500,000 indexed for inflation). The new higher limit applies for calendar year 2009 or a business' fiscal year that begins in 2009.

Another depreciation-related provision extends the special allowance for certain property, generally if acquired in 2009. For eligible property, the special depreciation amount is equal to 50 percent of its adjusted basis. For passenger automobiles that are eligible property under the 50 percent bonus depreciation rules, the \$8,000 increase for the first-year limit on depreciation also is extended to new vehicles placed in service in 2009.

Last year, corporate taxpayers were also allowed to accelerate their alternative minimum tax (AMT) and research and development (R&D) credits in lieu of taking the 50 percent bonus depreciation. That break has now been extended through 2009.

■ **Energy-related breaks for businesses expanded.** ARRA creates or expands several energy-related breaks for businesses, such as the:

- Advanced energy investment credit
- Renewable electricity production credit
- Alternative fuel pump tax credit.

## *Changes Affecting Individuals and Families*

### ● **“Making Work Pay” Credit**

The new law provides an individual tax credit in the amount of 6.2% of earned income not to exceed \$400 for single returns and \$800 for joint returns in 2009 and 2010. The credit is phased out at adjusted gross income (AGI) in excess of \$75,000 (\$150,000 for married couples filing jointly). The credit can be claimed as a reduction in the amount of income tax that is withheld from a paycheck, or through a credit on a tax return. Under the credit, workers can expect to see perhaps \$13 a week less withheld from their paychecks starting around June. Next year, the extra take-home pay will go down to around \$7.70 per week.

### ● **Economic Recovery Payment**

The new law provides for a one-time payment of \$250 to retirees, disabled individuals and Social Security beneficiaries and SSI recipients receiving benefits from the Social Security Administration and Railroad Retirement beneficiaries, and to veterans receiving disability compensation and pension benefits from the U.S. Department of Veterans' Affairs. The one-time payment is a reduction to any allowable Making Work Pay credit.

### ● **Refundable Credit for Certain Federal and State Pensioners**

The new law provides a one-time refundable tax credit of \$250 in 2009 to certain government retirees who are not eligible for Social Security benefits. This one-time credit is a reduction to any allowable Making Work Pay credit.

● **Unemployment compensation exclusion.** A provision temporarily suspends federal income tax on the first \$2,400 of unemployment benefits received by a recipient in 2009.

● **Expanded earned income tax credit.** The new law provides tax relief to families with three or more children and increases marriage penalty relief. The changes apply for 2009 and 2010.

● **Expanded child tax credit.** A measure increases the eligibility for the refundable child tax credit in 2009 and 2010 by lowering the AGI threshold to \$3,000 (from \$8,500 in 2008).

● **Expanded and revised higher education tax credit.** The new law creates a \$2,500 higher education tax credit that is available for the first four years of college. The credit is based on 100% of the first \$2,000 of tuition and related expenses (including books) paid during the tax year and 25% of the next \$2,000 of tuition and related expenses paid during the tax year, subject to

a phaseout for AGI in excess of \$80,000 (\$160,000 for married couples filing jointly). 40% of the credit is refundable. The new credit temporarily replaces the Hope credit.

● **Computers as an education expense.** A provision permits computers and computer technology to qualify as qualified education expenses in 529 education plans for tax years beginning in 2009 and 2010.

● **Expanded credit for first-time home buyers.** Last year, Congress provided taxpayers with a refundable tax credit that was equivalent to an interest-free loan equal to 10% of the purchase of a home (up to \$75,000) by first-time home buyers. The provision applied to homes purchased on or after April 9, 2008 and before July 1, 2009. Taxpayers receiving this tax credit were required to repay any amount received under this provision back to the government over 15 years in equal installments (or earlier if the home was sold). The credit phases out for taxpayers with adjusted gross income in excess of \$75,000 (\$150,000 in the case of a joint return). The new law enhances the credit by eliminating the repayment obligation for taxpayers that purchase homes on or after January 1, 2009. It also extends the credit through the end of November 2009, and bumps up the maximum value of the credit from \$7,500 to \$8,000.

● **Tax break for new car purchasers.** The new law allows taxpayers to deduct State and local sales taxes paid on the purchase of a new automobile, including light trucks, SUVs, motorcycles, and motor homes. The tax break phases out starting with taxpayers earning \$125,000 per year (\$250,000 for joint returns). The deduction is allowed to both those who itemize their deductions as well as to nonitemizers. However, the deduction cannot be taken by a taxpayer who elects to deduct State and local sales taxes in lieu of state and local income taxes.

● **Alternative minimum tax (AMT) patch.** To hold the number of taxpayers subject to the AMT at bay, the new law increases the AMT exemption amounts for 2009 to \$46,700 for unmarried individuals, to \$70,950 for joint returns, and to \$35,475 for married individuals filing separate returns, and allows the personal credits against the AMT.

  
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