2008 Stabilization Act: Tax Changes Affecting Individuals

Dear Client:

On October 3, President Bush signed into law a $ 850 billion financial markets rescue package. The rescue plan is designed to restore liquidity to the financial markets. At the same time, it includes some valuable individual tax incentives we want you to know about. The tax incentives cover a wide spectrum of activities. They are designed to put money back into the pockets of individual taxpayers during these difficult days. In this letter, we highlight some of the key incentives and invite you to discuss them with us in more detail.

AMT. The rescue package has some good news for individuals who are liable for alternative minimum tax (AMT) The AMT was created nearly 40 years ago as an alternative tax to the regular income tax to ensure that very wealthy individuals pay their fair share of taxes. However, the AMT was not indexed for inflation and it is ensnaring middle-income taxpayers. To prevent this, Congress created an AMT "patch." The 2008 patch is similar to past patches but with some important differences.

The 2008 patch raises the AMT exemption amounts to $69,950 for married couples filing jointly and surviving spouses, $46,200 for single taxpayers and heads of household and $34,975 for married couples filing separately. The rescue package also allows taxpayers to take nonrefundable personal credits to reduce their AMT liability. Additionally, and this is a new feature to the patch, the rescue plan abates AMT liability stemming from the exercise of incentive stock options along with interest and penalties on the unpaid amounts. The rescue package also allows individuals, including those who paid their ISO AMT liabilities, to accelerate the refund of the minimum tax credit that has not been used.

Homeowners. When a lender forecloses on property, sells the home for less than the borrower's outstanding mortgage and forgives all or part of the excess mortgage debt, the Tax Code treats the cancelled debt as taxable income to the homeowner. The *Mortgage Forgiveness Debt Relief Act* , enacted in late 2007, excludes from federal tax discharges involving up to $2 million of indebtedness ($1 million for a married taxpayer filing a separate return) secured by a principal residence and incurred in the acquisition, construction or substantial improvement of the residence. The new law extends this treatment from the end of 2009 through 2012.

The rescue package also extends the additional standard deduction for real property taxes. Individuals who do not itemize their deductions may take this deduction in 2008 and 2009. This deduction is not an above the line deduction that lowers your adjusted gross income. It is an addition to the standard deduction, and can reduce your taxable income by as much as $500 ($1,000 for those filing joint returns).

Child tax credit. The rescue package also enhances the child tax credit. Before the new law, the child tax credit was refundable to the extent of 15 percent of the taxpayer's earned income in excess of approximately $12,050 (reflecting inflation adjustments from the original floor of $10,000). Under the new law, the floor falls to $8,500. This treatment will result in an increase in the amount of the refundable credit for more taxpayers. Additionally, the rescue plan changes the definition of a "qualifying child" with respect to age and joint returns, clarifies the tiebreaker rules and ties the child tax credit to the child dependency exemption.

Charity. In 2008 and 2009, an individual age 70 1/2 or older can distribute up to $100,000 of his or her IRA balance to charitable organizations, including churches, without recognizing income and without taking a charitable deduction. This special tax break had expired at the end of 2007. The rescue package also includes some provisions related to donations to charities helping victims in disaster areas.

Energy. Rising fuel costs are pinching many people's wallets. If you install qualifying energy conservation property, such as exterior windows and doors, in your home you may be eligible to a tax break. The new law extends a number of energy conservation tax incentives and creates a new tax credit for individuals who purchase a plug-in electrical vehicle. Significant take breaks for "going solar" are also available in connection with home improvements.

State and local taxes. The rescue package gives individuals who itemize their deductions the option of deducting state and local income taxes or deducting state and local general sales taxes. This election was available in past years but expired at the end of 2007. The new law makes it retroactive to January 1, 2008, and extends it for 2009.

Education. The Tax Code provides many incentives to help individuals with educational expenses. The higher education tuition deduction is one of the most popular. The rescue package extends it but does not make it permanent. Nonetheless, it can be a valuable incentive. As previously, however, the amount of the deduction depends on your adjusted gross income.

Teachers. The Tax Code also gives teachers and other education workers a special deduction. Teachers may deduct up to $250 of qualified classroom expenses above-the-line. This special treatment expired at the end of 2007. The rescue package makes it retroactive to January 1, 2008, and extends it through 2009.

Disasters. Many individuals across the country are recovering from tornadoes, hurricanes and other natural disasters in 2008. The rescue package targets tax relief for individuals affected by flooding and tornadoes in 10 states and also helps victims of Hurricane Ike in Louisiana and Texas. For the first time, Congress authorized temporary national disaster relief.

Broker basis reporting. Starting in 2011, brokers will be required to report to the IRS not only their customers' gross proceeds from the sale of most corporate stocks but also the investor's cost basis in those shares. This will encourage the more accurate computation of capital gains each year. Broker basis reporting is expected to raise $6 billion over 10 years to partially offset the cost of the tax incentives in the rescue package. The reporting requirement takes effect for stocks acquired in 2011, mutual funds acquired in 2012, and other securities acquired in 2013.

We encourage you to call or email our office to discuss these tax breaks and the many other incentives and new tax rules created under the rescue package. You may be able to realize some tax savings this year. Don't put off contacting us; we can help you develop a strategy that maximizes your tax savings.

Sincerely,

ALAN L. GORDON, CPA, P.A.

Alan

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