

2008 Tax Legislation Highlights & Reminders

By: Christopher J. Loughran, Perkins & Company, P.C.

Hopefully as you read this the election is in the rear view mirror, and the financial and stock markets are rebounding for all of us. We can all refocus before year end on the real important things: Thanksgiving, turkey, football, Greg Oden's right leg ... *and taxes.*

The most recent tax legislation enacted was included in the Emergency Economic Stabilization Act of 2008 (the Act), signed into law October 3, 2008, which contained a myriad of tax changes along with the "bailout" provisions that were its primary focus. Many of the tax related items provide retroactive benefits for 2008 not previously available, as well as substantial benefits for 2009. The summary below will only address the tax provisions contained in the Act that have fairly broad application to individuals and businesses. In addition, we have included pertinent reminders from prior legislation that are effective for 2008, including special bonus depreciation provisions and section 409A deferred compensation plan compliance. We recommend you meet with us or your tax advisor to discuss how the specifics may affect you.

Individual Provisions

Extension of \$100,000 Nontaxable IRA Transfers to Charity

The Act retroactively extended this expired provision to make it available for 2008 and 2009. Under this provision, taxpayers at least age 70 1/2 can exclude up to \$100,000 of distributions per year from gross taxable income that would otherwise be taxable IRA distributions. To qualify, the IRA distribution must be made directly to a qualifying charity or qualifying donor advised fund, and otherwise qualify for a charitable deduction (without accounting for charitable deduction percentage limitations). A qualifying distribution, while not taxable, does count toward required minimum distributions.

Itemized Sales Tax Deduction

For Washington residents (and others residing in states without an income tax), the Act extends to 2008 and 2009 the ability to elect to claim sales taxes as itemized deductions (in lieu of state and local income tax deductions).

Credit for Purchase of Residential Energy Property

The Act reinstated the section 25C residential energy property credit for property placed in service in 2009. A maximum credit of \$500 is available for items such as insulation, exterior windows, skylights and exterior doors that meet qualified energy efficiency standards.

Alternative Minimum Tax (AMT) Relief for Individuals

The Act increases the AMT exemption for 2008 only (since it is not indexed for inflation), to \$69,950 for jointly filing married taxpayers and \$46,200 for single filers. The net result is merely to avoid additional taxpayers being reached by the AMT, not necessarily to remove you from it if you were in AMT for 2007. There is a special retroactive break which may be significant for a smaller group of taxpayers who were subject to AMT in pre-2008 years because of exercising incentive stock options (ISOs) which subsequently decreased in value significantly. Tax relief is available if the pre-2008 AMT tax related to the ISO remained unpaid as of October 3, 2008.

Debt Forgiveness Income Exclusion Extension

Taxpayers may exclude up to \$2 million (\$1 million for married taxpayers filing separately) of debt relief income under section 108, relating to foreclosures of principal residences. This provision previously expired at the end of 2009, and is now extended through the end of 2012, and contains additional benefits for mortgage workouts/restructurings, deeds in lieu of foreclosure and short sales.

Business Provisions

Research Credit Extension and Modification

The Act retroactively extends the research credit so that it applies for all amounts paid or incurred through December 31, 2009. It also removes the election for the alternative incremental research credit effective for tax years beginning after December 31, 2008, and increases the alternative simplified research credit rate to 14% (from 12%) for years ending after December 31, 2008.

Depreciation of Leasehold Improvements, Restaurant and Retail Improvements

The Act extends for two years, thus including property placed in service through December 31, 2009, the 15 year write off for qualified leasehold improvement property and qualified restaurant property (rather than 39 year recovery). With certain exceptions, a qualified leasehold improvement is an interior improvement to a building that qualifies for first year bonus depreciation. Qualified restaurant property relates to property in service more than three years and more than 50% devoted to on-site meal preparation and consumption. The Act also provides for a new category of assets placed in service between January 1, 2009 and December 31, 2009, called "qualified retail improvement property" which is depreciated over a 15 year straight-line MACRS life. This new category includes specified nonresidential retail property improvements, also placed in service more than three years after the related building was first in service.

S Corporation Contribution Basis Adjustment Extension

The Act retroactively extends to tax years beginning before January 1, 2010, the provision that expired at December 31, 2007, which allows an S corporation shareholder to reduce the basis in their S corporation stock by the adjusted tax basis of items contributed to charity by the S corporation, which amount is normally lower than the fair market value of the item (fair market value being the normal basis reduction amount).

Other Contributions

The Act extends through December 31, 2009 the enhanced deductions available to businesses for contributions of food to charitable organizations, as well as contributions of books and computer equipment to qualifying schools.

Qualified Environmental Remediation Expenses

The ability to currently deduct certain qualified environmental remediation expenditures under section 198 is retroactively extended to cover such expenses paid or incurred from January 1, 2008 through December 31, 2009.

Transportation Fringe Benefits

Exclusions from employee income for commuter fringe benefits such as transit passes and van pooling were extended by the Act to bicycle commuters. The exclusion is \$20 per month for tax years beginning after December 31, 2008.

Energy Efficiency

The section 179D deduction for certain energy efficient costs for commercial buildings is extended through December 31, 2013. As under prior law, the deduction for the qualifying costs is capped based on a dollar amount per square foot.

FUTA Surtax

The Act extends the .2% FUTA surtax for one year through 2009.

Other Items of Interest

Preparer Standard Synchronization

The Act eliminates retroactively the 2007 change to section 6694 which required that tax return preparers must achieve a "more likely than not" level of certainty for any tax position in a return not specifically disclosed to the IRS, subject to certain transition rules. Except for tax shelters and other reportable transactions, the Act modifies the preparer standard to be based on "substantial authority" which effectively makes the preparer subject to the same standard as the taxpayer.

Bonus Depreciation for 2008 and Election Out

The Economic Stimulus Act of 2008, passed in February, allowed businesses to claim a bonus first year depreciation of 50% for most (new) machinery, equipment and software acquired and placed in service after December 31, 2007 and before January 1, 2009. Bonus depreciation is allowed for regular tax and AMT purposes. The 2008 Housing Act was signed into law on July 30, 2008 - it added that for tax years ending after March 31, 2008, corporations otherwise eligible for bonus depreciation may instead elect to claim additional research credits or certain minimum tax credits. Making the proper decision likely will require some detailed projection work in order to select the best approach for your business.

2008 Housing Act Credit Rules

The 2008 Housing Act allows the low income housing credit (for buildings placed in service after 2007) and the rehabilitation credit (for costs incurred post 2007) to offset the alternative minimum tax. These credits previously were only available to offset regular tax.

2008 Housing Act Section 179 Expensing Allowance Increase

The 2008 Housing Act also increased the section 179 expensing maximum from \$128,000 to \$250,000 for tax years beginning in 2008. Similarly, the investment limit, over which the allowance is phased out, was increased from \$510,000 to \$800,000 for tax years beginning in 2008. Note that as under prior law, there is no AMT adjustment for section 179 expenses (unlike certain depreciation deductions).

Section 409A Compliance Deadline of December 31, 2008 for all Deferred Compensation Plans

While not a subject of recent legislation, we wish to take this opportunity to remind you that the final deadline for written plan compliance under section 409A, which has been pushed back for several years, is December 31, 2008. All plans which have the effect of deferring compensation, to employees or contractors, are subject to the rules. Failure to comply results in significant cost to the affected individuals, including complete taxation (regardless of whether cash is received or not), penalties and interest, potentially for all amounts due under the plan. The rules cover all nonqualified deferred compensation plans, which can cover typical executive plans, but can also apply to general bonus, severance or other plans. If you have not reviewed your compliance under section 409A, you should do so with a qualified employee benefit plan/409A specialist as soon as possible and as far in advance of December 31, 2008 as possible in the event plan modifications or other actions are appropriate.

A Final Note

If something here interests you or raises some questions about your best course of action, please contact any of the Perkins tax shareholders listed below to discuss further - we are eager to help you understand the changes and make the right decisions for your situation.

| | | |
|----------------|---------------|---------------------------------|
| Chris Loughran | (503)221-7565 | cloughran@perkinsaccounting.com |
| Tim Kalberg | (503)221-7511 | tkalberg@perkinsaccounting.com |
| David Uslan | (503)221-7597 | duslan@perkinsaccounting.com |
| Roy Abramowitz | (503)221-7500 | roya@perkinsaccounting.com |
| Keith Meyers | (503)221-7579 | kmeyers@perkinsaccounting.com |

This bulletin is a summary and is not intended as tax or legal advice. You should consult with your tax advisor to obtain specific advice with respect to your fact pattern.

Based on the most recent "best practice" standards for tax advisors issued by the Treasury Department, commonly referred to as Circular 230, we wish to advise you that this bulletin has not been prepared to be used, and cannot be used, to provide assurance that penalties which may be assessed by the IRS or other taxing authority (including specifically section 6662 understatement penalties) will not be upheld.



+ 1211 SW Fifth Avenue, Suite 1000
+ Portland, Oregon 97204-3710

PRSR STD
U.S. POSTAGE
PAID
PERMIT NO. 11
PORTLAND, OR