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New Tax Breaks in the Stimulus Law

The new economic stimulus law just passed by Congress—titled the American Recovery and Reinvestment Act of 2009—provides wide-ranging tax benefits for individual and business taxpayers alike. Here is a brief summary of several key provisions in the new law.

❖ For 2009 and 2010, an employee or a self-employed individual may be entitled to a “Making Work Pay credit” of the lesser of 6.2% of earned income, or \$400 for single filers or \$800 for joint filers. This credit begins to phase out for an adjusted gross income (AGI) of \$75,000 or more for single filers and \$150,000 for joint filers.

❖ The alternative minimum tax (AMT) for individuals is “patched” again for 2009. The new law extends the use of personal credit offsets and increases the exemption amounts for AMT purposes.

❖ The maximum Hope education credit, renamed the “American Opportunity Tax Credit,” is increased to \$2,500 and allowed for all four years of college, instead of just two. Also, the credit will begin to phase out at a higher level of \$80,000 of AGI for single filers and \$160,000 for joint filers.

❖ The maximum first-time homebuyer’s credit is increased to \$8,000 for home purchases after December 31, 2008, and before December 1, 2009. Also, the homebuyer is not required to repay the credit over 15 years if he or she lives in the home for at least 36 months. But the credit for 2009 still begins to phase out for an AGI over \$75,000 for single filers and \$150,000 for joint filers. This is a refundable credit on either your 2008 or 2009 tax return, but not both.

❖ An individual can deduct sales and excise taxes attributable to the first \$49,500

of the price of a new vehicle purchased after February 16, 2009, and before January 1, 2010. This new deduction is phased out for an AGI above \$125,000 for single filers and \$250,000 for joint filers.

❖ A business may currently deduct up to \$250,000 of qualified property placed in service in 2009 under Section 179. This enhanced write-off was scheduled to revert to lower levels after 2008. The threshold for the amount of new property a business may place into service and still be eligible for the Sec. 179 deduction also remains at \$800,000 for 2009. The new law extends the 50% bonus depreciation deduction for qualified property placed in service in 2009. However, the State of North Carolina has not conformed to the federal law and requires an addback equal to 85% of the federal depreciation.

❖ Instead of carrying back net operating losses (NOLs) for only two years, the carry-back period is extended to five years for NOLs sustained by a small business in tax years beginning or ending in 2008. A “small business” is defined as one with average gross receipts of \$15 million or less for the three tax years ending with the year in question.

❖ The holding period for the built-in gains (BIG) tax that may apply when a C corporation converts to S corporation status is shortened from ten years to seven for gains realized in tax years beginning in 2009 and 2010. This change in the BIG tax gives certain business owners more flexibility.

❖ For those individuals who lose their jobs between September 1, 2008 and January 1, 2010, the new law allows them to pay 35% of their COBRA coverage and have it treated as paying the whole amount. The

New Rules for Required Minimum Distributions

The new Worker, Retiree, and Employer Recovery Act of 2008—signed into law in the waning days of 2008—provides greater flexibility to retirees who normally must take required minimum distributions (RMDs) from their IRAs and qualified retirement plans. But this special relief is only available for the 2009 tax year.

Background: A participant in an IRA or qualified retirement plan, such as a 401(k) plan, is generally required to begin taking RMDs by April 1 of the year following the year in which he or she turns age 70½. However, someone who is still working and does not own 5% or more of the company may postpone distributions from a qualified plan until actual retirement. This exception does not apply to IRA distributions.

The amount of the required distribution is based on IRS-approved life expectancy tables and the balance in the account on the last day of the prior year. This can result in a disproportionately higher tax when the participant's account value decreases during the year. Many plan and IRA participants suffered this fate in 2008 due to the stock market decline, while volatility has continued into the early part of 2009.

The penalty tax for failing to take the required distribution is equal to 50% of the amount of the shortfall. Therefore, it is imperative to observe the rules in this area.

New law change: The rule for RMDs is suspended, but only for 2009. As a result, IRA and plan participants do not have to take a distribution this year, unless they choose to do so. The

intention is to help retirees avoid additional erosion to their accounts from distributions. It can also position them for increased savings if the stock market rebounds.

Note that a similar rule applies to beneficiaries who inherit amounts from IRAs and qualified plans. If the plan participant has not started taking RMDs, the beneficiary is generally required to receive distributions over a five-year period. The new law also waives this requirement for the 2009 tax year.

However, despite calls for retroactive relief, the new law did not suspend RMDs for the 2008 tax year. The IRS has also indicated there will be no changes that would affect 2008 RMDs.

Example: An IRA or plan participant who turned age 70½ in 2008 is still required to take a distribution for 2008 by April 1, 2009. The participant can then skip the distribution for 2009 and resume taking RMDs in 2010. Conversely, a participant who turns age 70½ in 2009 does not have to take a distribution by the April 1, 2010 deadline for 2009, but then he or she must take an RMD for 2010 by December 31, 2010.

The actual required minimum distribution is based upon a sliding scale. The older you are, the higher a percentage you have to take out. For example, for tax year 2008, a 71 year-old person has to take out an amount equal to the value of his account divided by 26.5. For a 71 year-old person with \$100,000 in their account, this amount would equal to \$3,774. Please consult with a professional adviser for further details.

Estate Planning: Alternate Valuation Date

A special estate-planning technique can save thousands of estate-tax dollars in the wake of recent stock market woes.

Background: The estate-tax exemption can effectively shelter up to \$3.5 million of assets from federal estate tax for a decedent dying in 2009 (up from \$2 million for 2008). Although the estate tax is scheduled to be repealed in 2010, it is expected that Congress and the President will keep the exemption around \$3.5 million and not let the exemption return to its previously lower amount. We will continue to update our clients once the final version of this bill is passed.

Generally, the value of assets for estate-tax purposes is based on the date of death. But this rule can create a hardship for families where the decedent owned securities or real estate properties that have declined in value since the date of death.

Possible solution: An executor can elect an alternate valuation date of six months after the date of death. This technique can reduce or even eliminate estate-tax liability for a family.

However, be aware that this is an all-or-nothing proposition. The alternate valuation date generally applies to every asset in the estate. Finally, the special election is available only if it decreases the value of the gross estate and the resulting estate-tax bill.



New Tax Breaks in Stimulus Law

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former employer is required to pay the remaining 65% but will be reimbursed by the government by crediting those amounts against income tax withholding and payroll taxes.

- ❖ The energy incentives in the new law are targeted to both individuals and businesses. These include credits aimed at expanding the development and production of alternative energy sources as well as creating new “green collar” jobs.

- ❖ Finally, there are a multitude of other tax provisions in the new stimulus law, ranging from a one-time \$250 payment to certain retirees to a temporary exclusion of the first \$2,400 of unemployment benefits. Please contact us if you would like further information on the new law.

IRS Sends Signals on Rollover Waivers

A recent trend involving rollovers to IRAs may be a cause for concern. In two new rulings, the IRS denied waiver requests by taxpayers who failed to roll over funds within the allotted time period. This may signal that the IRS will not be as lenient as it has been in prior years.

The change points out the need to comply with the strict letter of the law from the outset.

Whenever possible, the most practical approach is to avoid potential problems by using a trustee-to-trustee rollover.

Background: An individual taxpayer does not have to pay any current tax on amounts rolled over from a qualified plan to an IRA or from an IRA to another IRA, if the rollover is completed within 60 days. But the taxpayer must pay 20% income tax withholding on a distribution from a qualified plan even if he or she intends to meet the 60-day deadline.

The amount withheld cannot be recovered until the individual files his or her tax return for the year of the distribution.

Conversely, if the funds are transferred directly from a qualified plan to an IRA—in other words, the taxpayer never touches the money—the distribution is exempt from withholding. No tax is due until a withdrawal is made from the rollover IRA.

Unfortunately, there are times when a taxpayer may need temporary access to rollover funds. Under a 2002 tax law change, the plan participant may request a waiver if he or she fails to meet the deadline when extenuating circumstances exist. In making its determination, the IRS will consider:

- ❖ Whether any errors were made by the financial institution;

- ❖ If the taxpayer was unable to complete the rollover due to death, disability, hospitalization, incarceration, restrictions imposed by a foreign country or postal error;

- ❖ Whether the taxpayer used the amount distributed; and

- ❖ The length of time since the date of the distribution.

Although the IRS previously has been lenient in approving waivers, the tide seems to have turned.

New ruling #1: A taxpayer received his deceased spouse's interest in a 403(b) plan. The plan administrator withheld the 20% tax on the distribution. Although the taxpayer intended to roll over the funds, he did not deposit the money in an IRA within 60 days. He mistakenly believed that the amount withheld represented the full amount of tax that would be owed.

New ruling #2: A retired taxpayer had established an IRA more than 20 years ago. He notified the IRA provider that he intended to transfer his investment to a financial institution closer to his new retirement residence. The current IRA provider transferred the funds to a non-IRA account. Eventually, the taxpayer deposited the funds in an IRA, but well after the 60-day deadline had passed.

In both of these instances, the IRS attributed the failure to roll over funds in a timely manner to the taxpayer's mistake. Therefore, both waiver requests were denied and the distributions were deemed fully taxable.

It is clear that the IRS is adopting a tougher stance on this issue. Make sure that all the technicalities are observed on rollovers.

Where's My Refund?

Both the federal and NC government have places on their website where you can track the status of your tax refund. You will need to enter your social security number, filing status and amount of refund as shown on your tax return.

- ❖ For the status of your federal refund, go to this website: <https://sa2.www4.irs.gov/irfof/lang/en/irfofgetstatus.jsp>

- ❖ For the status of your state refund, go to this website: <https://eservices.dor.nc.gov/wheresmyrefund/selection.jsp>

The state of North Carolina is taking longer than usual to issue refund checks due to the downturn in the economy. According to the NC Department of Revenue website, the DOR is working with the Office of State Controller on a daily basis to determine how much is available for release each week.

Thomas, Judy and Tucker P.A. in the News

Triangle Business Journal released its rankings of the top accounting firms in the Triangle based upon total number of CPAs and total number of employees. Thomas, Judy & Tucker P. A. improved its ranking by moving up to #6 on the list which included many national and regional accounting firms who do business here in the Triangle.

Congratulations to partners Chris Judy and Jeff Brovet for being recognized as some of the top business leaders in the Triangle. Chris was recently honored by Business Leader magazine as one of 2008/2009 Top Entrepreneurs at the Triangle Hall of Fame Awards. Jeff was selected as one of those individuals who will receive Triangle Business Journal's Top 40 Under 40 Leadership award for 2009.