



**ALLIED TAX PLANNERS
SPECIAL REPORT**

Obama Tax Changes – What to Expect for 2009

By Matthew Haupt

Beginning with the “Sub-Prime Mortgage Meltdown,” there have been a lot of recent changes in our economy, to put it mildly. Now, with our new president, there are more changes, but how are these changes going to affect YOU? This report will detail the tax changes we can expect from the recent economic stimulus act, as well as the president’s proposed budget for 2010.

Why should you read this report? A lot of folks are going to get an April 15th surprise next year. *Don’t make the mistake of assuming that these changes won’t impact you.* Arm yourself with some knowledge and make changes NOW to dodge any big tax hits.

I’ll spend most of this report writing about new laws, but I’ll also delve into some future proposals. Some of those proposals may not survive economic and political reality, so I’ll also discuss how the current economy may affect these proposals.

On February 17, President Obama signed the “American Recovery and Reinvestment Act,” or economic stimulus act. We could debate for days about whether the act will actually stimulate the economy, but the act includes nearly \$300 billion in tax breaks that are already law. These are developments you can literally take to the bank.

Economic Stimuli in the Economic Stimulus Act

- Making Work Pay credit
- American Opportunity credit
- First-Time Home Buyer credit
- New car sales tax deduction
- Expanded tax breaks for “going green”
- Business tax breaks

As you can see, there’s a lot going on here. On top of this, Obama has proposed big tax reforms, such as a “flat tax” or national sales tax.

You realize that puts us out of business, right?

Well, we’re not worried. The new administration certainly appears to favor tax credits over broad-based reform. And while tax credits may be a more efficient way to target benefits for specific taxpayers, it also creates the sort of complexity that led former President Jimmy Carter to call the Tax Code “a disgrace to the human race.”

The most immediate change, for those of you who collect a paycheck, is the new “Making Work Pay” credit.

“Making Work Pay” Credit

- \$400 for individual filers
- \$800 for joint filers
- Fully “refundable”
- Phases out at \$75,000/\$150,000
- 2009-2010 only

Right now, you pay a 6.2% Social Security tax on earned income up to the “Social Security wage base.” For 2009, that amount is \$106,800. If you’re self-employed, you pay both halves. You also pay a 1.45% Medicare tax on *all* your earned income. Again, if you’re self-employed, you pay both halves.

The new “Making Work Pay” credit is intended to offset the Social Security tax on the first \$6,500 or so of income. For single filers, the credit is \$400. For married couples filing jointly, it’s \$800. The credit is “refundable,” which means that even if you don’t pay any tax, you get the credit.

Of course, we can’t be giving tax breaks to “the rich.” If you’re single, the credit phases out if your Adjusted Gross Income, which is the number at the bottom of Page 1 of your Form 1040, tops \$75,000. If you’re married, it phases out if your adjusted gross income tops \$150,000. I’ll leave it to you to decide if \$75,000 a year makes you “rich,” but that’s how the law is written.

The economic stimulus act authorizes the “Making Work Pay” credit for just two years. However, the budget proposal, which we’ll discuss in a little bit, proposes making the credit permanent.

The best news is, you don’t have to wait until you file next year’s taxes to start getting the money! The IRS has issued new withholding tables for employers to start including the credit in your paycheck no later than May 1.

Paying for college is a lot of families’ worst nightmare. Have you ever found yourself wishing your kid wouldn’t get such good grades . . . So you won’t have to send them to an expensive college?

Paying for College?

- American Opportunity Tax Credit
- Replaces Hope Scholarship Credit
- Available for 4 Years of College
- 100% of 1st \$2,000 + 25% of next \$2,000
- 40% “refundable”
- Phases out at \$80,000/\$160,000 joint

The economic stimulus act includes a couple of changes to the college tax credit rules. Under the old law, you could claim a “Hope Scholarship” tax credit for your child’s first two years of post-secondary school. The credit itself was 100% of the first \$1,200 in expenses, plus 50% of the next \$1,200 in costs, for a total of \$1,800 per student per year. It phased out once your adjusted gross income topped \$40,000 for single filers and \$80,000 for joint filers. And after two years of school, you had to settle for a less-generous “Lifetime Learning” credit of just \$1,000 per student.

The new law expands the “Hope Scholarship” credit and renames it the “American Opportunity” credit. Now you get 100% of your first \$2,000 in costs, plus 25% of your next \$2,000 in costs, for a total credit of \$2,500. The extra \$700 is nice, but the *real* benefit is a higher phaseout. Now the credit doesn’t start phasing out until your adjusted gross income tops \$80,000, or \$160,000 if you’re married filing jointly. And the credit is good for four years. And now you get the more generous credit for *four* years of school, not just two.

The new credit is even 40% “refundable,” which means that if you owe no other tax, you can still claim 40% of the credit by filing your return.

Some of you may be using “Section 529” plans to save for your kids’ college. These plans let you set money aside for college, and withdraw earnings tax-free if you use them for qualified college costs. The new law now lets you use withdrawals for computers and computer equipment, including online access. You can feel better knowing your kids are surfing “Facebook” using tax-free dollars.

College Costs

- Section 529 plan withdrawals now available for computers and computer technology purchases (including internet access)



With markets where they are right now, you may actually have less in your 529 plan than you initially invested. It may be possible to claim a tax break for those losses. If you shut down the account, you can deduct the loss as a “miscellaneous itemized deduction. But there’s a special limit to this deduction based on your adjusted gross income, and you can’t claim it if you’re subject to the Alternative Minimum Tax. So if you’ve put money in a 529 plan and watched your account value go down, talk to an advisor at ATP to discuss whether this might make sense.

The real estate market is obviously a cornerstone of our economy, and Washington is scrambling to do everything they can to keep home values up. So last year’s economic stimulus act included a new “first-time homebuyer” credit. You’re a first-time homebuyer if neither you nor your spouse have owned your primary residence for the last three years.

Buying a New House?

- Enhanced “First-Time Home Buyer” Tax Credit
- 10% of purchase price up to \$80,000
- No repayment after 36 months
- Purchases between 1/1/09 and 11/30/09
- Phases out at \$75,000/\$150,000 joint

The old law gave you a credit equal to 10% of the home’s purchase price, up to \$75,000, for a \$7,500 credit. *But* - and this is a *big* but - you had to repay that credit in equal installments over the next 15 years. So it wasn’t really a credit; it was more like an interest-free loan.

This year’s economic stimulus act expands and extends that credit. Now you can claim 10% of your new home’s purchase price up to \$80,000, for an \$8,000 credit. You have to buy by November 30, 2009. But now there’s no repayment requirement so long as you occupy the home as your primary residence for at least 36 months. So if you’re currently renting, and you’re looking to buy a home, this may be a great time to buy.

Of course, Washington doesn’t want to subsidize McMansions. So there’s an income limit. In this case, the credit starts phasing out as your adjusted gross income tops \$75,000, or \$150,000 if you’re married filing jointly.

Our auto industry is another cornerstone of our economy. Washington wants us to buy cars, and lots of them; so the economic stimulus act includes a new deduction for state and local sales tax you pay to buy a brand-new car.

Buying a New Car?

- “Above the line” deduction for state sales or excise tax 2009 new car purchase
- Qualifying cars, light trucks, SUVs, or motorcycles up to \$49,500
- Phases out at \$125,000/\$250,000

This is an “above-the-line” deduction, which means you get it even if you don’t itemize. You can deduct tax you pay on up to \$49,500 of car, light truck, SUV, motorcycle, or RV, so long as it’s not more than 8,500 pounds.

Yes, there’s an income phaseout here too – but it’s not as bad as some of the others. In this case, the deduction for new-car sales tax starts phasing out as your adjusted gross income tops \$125,000, or \$250,000 if you’re married filing jointly.

Now let me write about some breaks for small business. This is where lots of the action lies because small business creates most of the wealth in the country and small business creates most of the jobs in the country. You may think of Microsoft as a typical

corporate giant, but it started out as a couple of computer geeks spotting an opportunity to sell a program called “DOS” long before it made Bill Gates the richest man in the world.

Running a Business?

- Extend \$250,000 “first-year expensing” (2009)
- Extend 50% “bonus depreciation” (2009)
- Carry back NOL
- Cut tax for investments in small business

We’ll start with business equipment. Businesses generally don’t get to *deduct* equipment they buy for their operations. They have to *depreciate* it over a specified period ranging from 3 years to 39 years depending on its useful life. But there’s a special provision called “first-year expensing” that lets businesses deduct part or all of the equipment they buy. The theory here is that by giving buyers tax breaks, they’ll buy more, which grows the economy faster than without the tax breaks.

Last year’s economic stimulus package raised the first-year expensing limit to \$250,000 for 2008. Last year’s law also created a 50% “bonus depreciation” for most tangible property, like vehicles, machinery, and equipment.

The new act extends that limit for 2009 and 2010. This means continued opportunities for those of you looking to buy business equipment or even renovate business premises.

The new law includes a special break for businesses that lost money in 2008. Under regular law, when your business loses money, you get what’s called a “net operating loss.” You can carry that loss back two years to get a refund of taxes you’ve already paid. Or you can carry it forward 15 years to offset future profits.

Under the new law, if your business grosses less than \$15 million and you lost money in 2008, you can carry the net operating loss back 5 years instead of the regular two. The goal, obviously, is to give you more money to lose in 2009 – but at least you’ll be stimulating the economy!

Finally, the new law expands tax breaks for investing in small businesses. Under regular law, when you invest in businesses that qualify under a special section of the tax code, you can exclude up to half of your capital gains from your income when you sell. The new law expands that exclusion to 75% of your gain. Some of you may remember this as the famous “Joe the Plumber” tax break that candidate Obama floated back in September.

If you’re concerned about global warming, you’ll find new incentives to invest in going green.

Going Green?

- Plug-in vehicles
- Energy-efficient home improvements
- Energy-efficient business property



For starters, there's a new deduction for plug-in electrical vehicles. Right now there aren't a lot of plug-in vehicles to buy, but Washington hopes the new credit will help spur development.

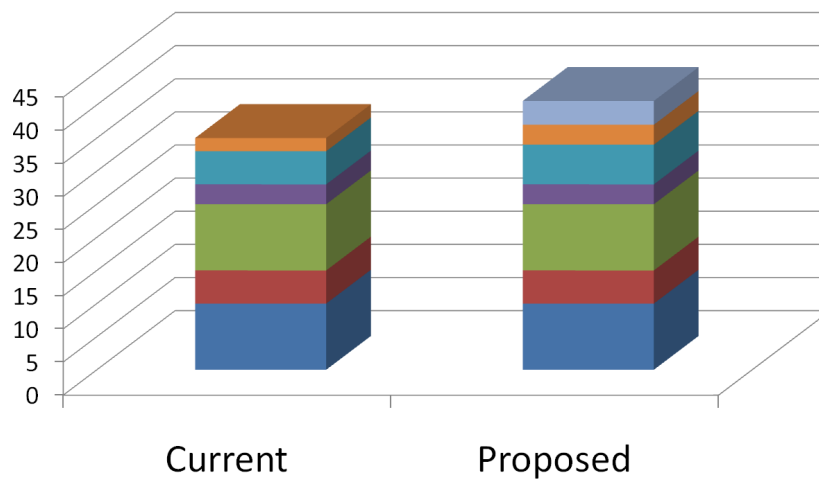
There's also an expanded credit for the cost of energy-efficient home improvements. Under regular law, you could take a credit up to 10% of the cost of those improvements. But the credit was capped at a miserly \$500, with complicated sub-limits for specific types of property like windows, appliances, and insulation. The new law raises the credit percentage to 30% and raises the dollar limit to \$1,500. It won't make you rich – but it can help make “going green” less expensive.

Finally, there are new and expanded credits for solar power systems and energy-efficient business property. Call us if you have any questions about this program.

The Federal Budget and Taxes

Now let's talk about the Obama administration's budget proposals. Most of the talk centers around the raw spending - \$3.55 trillion, with a deficit of \$1.75 billion. But he has proposed several changes that, together, would raise nearly a trillion in new taxes over the next decade.

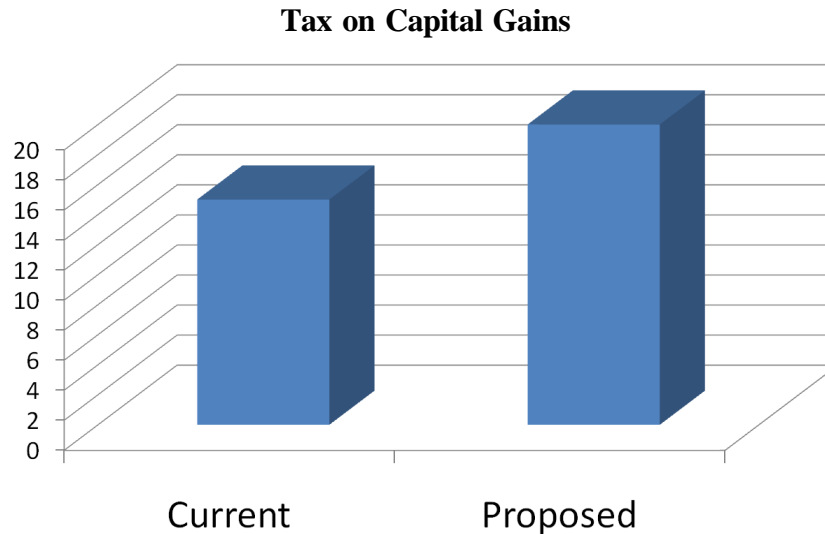
Top Tax Rates



The Bush administration pegged the two top tax rates at 33% and 35%. However, those rates are scheduled to expire after 2010. This would raise the top rates to 36% and 39.6%. Obama's budget proposes to let the top rates expire after 2010, for individuals making over \$200,000 and families making over \$250,000.

Raising taxes in the face of a recession does not seem like a good idea to me, personally. Politicians may argue that the government needs cash after the big bailouts they have given, but I would say the people need their money more, especially at times like this. The bailouts may not have been a good idea in the first place; although they may help with recovery in the short-run, they do not solve the underlying problems of the economy.

Now let's talk about capital gains. These are gains you earn from the sale of property that you've held for longer than 12 months. The key point here is that you don't pay tax until you actually *sell* the property.



It makes sense that rates are lower for capital gains. That's because inflation pushes up the value of your assets, even if they don't grow in "real" terms. We've all heard stories about friends or relatives who bought stock in a company for a few thousand dollars years ago, then cashed out for a few *hundred* thousand. Well, how much of that gain is due to inflation, and how much of that is real appreciation?

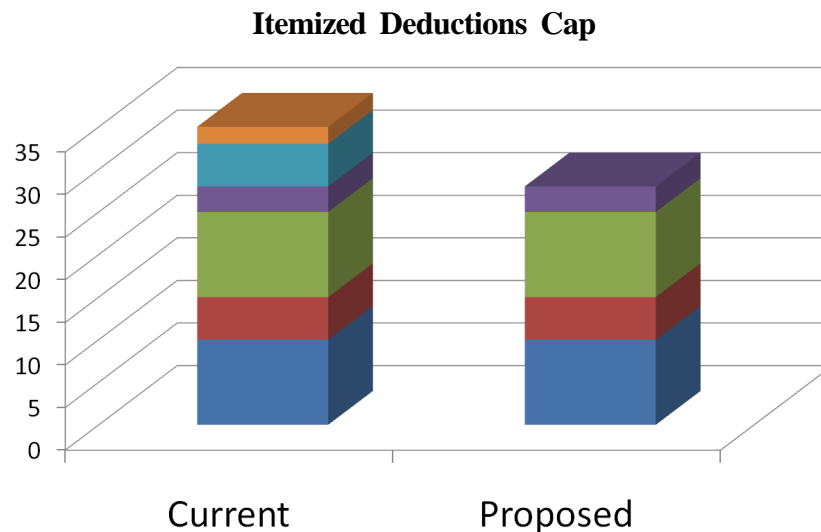
The Bush administration capped tax on most capital gains at just 15%. For 2008 and 2009 only, some gains are taxed at *zero* percent.

Obama proposes to let that 15% cap expire after 2010 for individuals making over \$200,000 and families making over \$250,000. That would raise the rate to 20%.

While those rates may go up, there are still lots of opportunities to use capital gains to cut your taxes. If you own your own business, you have two ways to profit. You can take

income out of the business and pay tax on it today. Or you can grow the value of the business and defer tax until you sell it - or even avoid income tax entirely if you pass it on to your heirs. Lots of sharp business owners plan to sidestep the coming Obama tax hikes by shifting their efforts from growing current income to growing the value of the business. If you're interested, call us and we can set up a time to discuss how you can do this, too.

The 2010 budget includes one last tax hike worth noting. Specifically, the administration proposes capping the value of itemized deductions at just 28%, even if your regular tax bracket is higher. Itemized deductions include medical and dental expenses, state and local taxes, mortgage interest, charitable gifts, casualty and theft losses, and miscellaneous itemized deductions like tax-prep fees, investment management fees, and unreimbursed job costs.



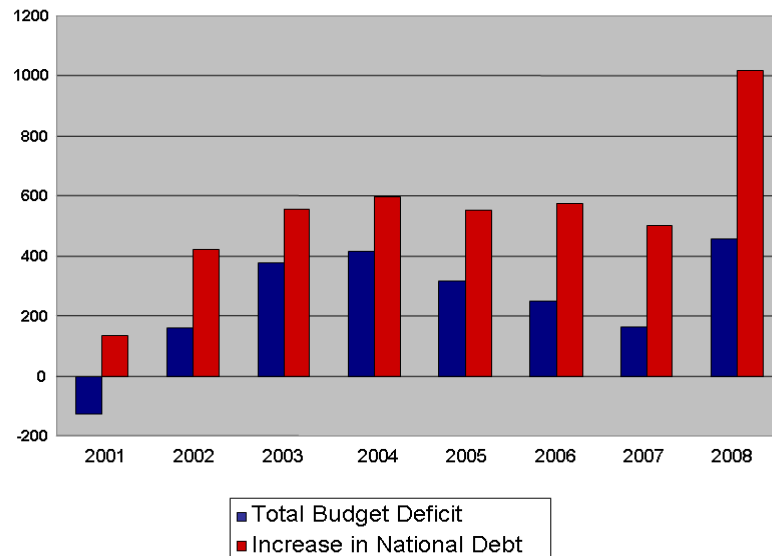
Right now, a dollar of deduction saves different amounts for taxpayers in different brackets. If you're in the 15% bracket, a dollar of deduction saves you 15 cents. If you're in the 35% bracket, that same dollar saves you 35 cents.

There are already several rules that limit the value of these deductions. Medical and dental expenses, for example, are deductible only to the extent they top 7.5% of your adjusted gross income. Miscellaneous itemized deductions have to top 2% of your adjusted gross income. State and local taxes are completely eliminated if you pay Alternative Minimum tax. And all itemized deductions are phased out if your adjusted gross income is above \$159,950.

The new law would simply cap the amount you save as if you were in the 28% bracket. This could amount to a significant increase for many of you with high deductions. It could be especially devastating for charities, which are already feeling the pinch of the poor economy.

President Obama has pledged to cut the deficit in half by the end of his administration. He'll do that by cutting spending, closing corporate tax loopholes, and cracking down on offshore tax evasion. But how *realistic* is this plan? How likely will he be able to *keep* his promise?

Total Deficits vs. National Debt Increases (\$ Billions)



President Bush took office with an actual budget surplus, if you accept the government's own accounting rules. Since then, the combination of lower taxes, higher spending, and an unexpectedly higher defense budget have pushed the deficit up to record levels. For 2009, the Office of Management and Budget is projecting a deficit of \$750 billion. For 2010, we see Obama projects a deficit of \$1.75 trillion. That's over \$5,800 for every man, woman, and child in the country.

What's worse, the economy that produces taxable income has stalled. We're in the worst economy since the Great Depression, and some forecasters still think we've got further to fall. Back when Obama was still campaigning, it was easy to propose tax hikes for Wall Street millionaires. But since then, Wall Street firms have eliminated over 100,000 jobs. That's a lot fewer millionaires to pay tax! And Wall Street is hardly the only employer shedding jobs.

If recent history tells us anything, it's this: be prepared for anything to happen - and happen fast. Who would have expected the Treasury Department to commit \$30 billion to bail out the investment firm of Bear Stearns? Who would have expected them to spend as much to bail out AIG as they did to in the wake of Hurricane Katrina - and actually buy 80% of the company? Who would have guessed, even then, that the government would wind up committing up to \$700 billion to actually buy stakes in banks?

Obama developed his tax plan over the course of a political campaign. But now he faces economic reality. We shouldn't be surprised if the legislation he introduces early in his administration poses new challenges we haven't anticipated.

Here's *your* bottom line. You can't afford to wait until tax time to face the music. You can't afford to risk an April 15th surprise!



The key to beating any future tax changes - *legally* - is planning. It doesn't matter how good I am, or any other accountant is, with a stack of receipts on April 15. If you haven't planned your finances to anticipate the coming changes, you'll wind up paying more than you have to.

I want to invite all of you to call us for a free Tax Analysis. We'll find the mistakes and missed opportunities that may be costing you thousands in taxes now – give you a plan for rescuing those wasted dollars – and position you to respond to the coming tax changes. I guarantee you'll leave with new information and ideas, or we'll donate \$50 in your name to your favorite charity. If you're serious about what I've discussed today, that should be a very easy decision.



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