Tax Outlook Under New Casualty Loss Rules

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Furthermore, the new law allows nonitemizers to deduct personal casualty losses in disaster areas, in addition to claiming the usual standard deduction. This change applies to tax years beginning after 2007.

Reminder: Make sure you claim the maximum tax deduction you are entitled to when you file your 2008 return. Professional tax assistance is recommended.

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Eight New Items on Your 2008 Return
Key changes in store for tax filers

It has been a tumultuous year on the tax front. Several significant new laws and a flood of new regulations and rulings in 2008 have contributed to more than 500 revisions in the federal tax code. Keeping that in mind, here is a roundup of eight key changes on 2008 returns.

1. Homebuyer's tax credit: For the first time ever, a homebuyer may claim a credit equal to the lesser of $7,500 or 10% of the home's purchase price. The credit is available for a principal residence purchased after April 8, 2008, and before July 1, 2009. Note: If a home purchased in 2009 qualifies, you can claim the credit on your 2008 return.

2. Zero-percent capital gains rate: Previously, the maximum 15% capital gains tax rate for net long-term capital gain and qualified dividends was reduced to only 5% for taxpayers in the regular 10% and 15% tax brackets. But this 5% rate drops to 0% for 2008. Currently, the 0% rate is scheduled to remain in effect through 2010.

3. Kiddie tax: Beginning in 2008, the kiddie tax generally applies to unearned income above a specified annual threshold received by a child who is younger than 19 years of age (up from age 18 years for 2007) or a full-time student younger than age 24 years. For 2008 returns, unearned income above $1,800 is taxed at the top tax rate of a child's parents.

see **Eight New Items on Your 2008 Return,** page 4

Facts and Figures
Timely points of particular interest

Checking on Rebates -
The economic stimulus checks handed out in 2008 were based on data from 2007 tax returns. But some taxpayers were short-changed because they lost their jobs last year or their income in 2008 declined for other reasons. In that case, a rebate credit may be available when an individual's 2008 federal tax return is filed. Check with a tax professional if you are unsure of your status.

Gift-tax Exclusion -
The IRS recently announced that the annual gift-tax exclusion has increased from $12,000 per recipient for 2008 to $13,000 per recipient for 2009. A married couple can jointly give gifts of up to $26,000 exempt from gift tax this year. For example, by giving the maximum gifts to ten family members for five consecutive years, you can reduce your taxable estate by $1.3 million.

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2009 - A New Year Filled with Challenge

This is a moment in our history in which along with the change in leadership in Washington, as well as the turmoil in our financial markets, every one is left with the uncertainty of what it all means, especially to them. From the standpoint of our clients, a few pertinent observations can be made.

In general, the government will be more involved in our lives. This will be manifested in several ways that impact our clients:

First, given the financial climate, there will be more government regulation impacting business in general. Historically, this means complication rather than simplification of the business process---more laws, regulations and filing of more mandatory reports.

Secondly, given the anticipated growth of government, at some point, most taxes impacting the vast majority of our clients will be going up. This includes income taxes, estate and gift taxes and likely a variety of payroll taxes. Also, since most states are in as bad a situation as the federal government, the financial impact will be compounded.

Given the anticipated effect on our clients, Hood & Strong LLP is committed to keeping our clients informed of the specifics of new laws and regulations, along with what these may mean to you and your financial situation. In addition our planning will be focused on mitigating any negative result to the greatest extent possible. At the same time, it is imperative for you to stay current on the specifics of what is going on in the world and plan with us to insure the most favorable possible outcomes for you personally.

During this period of governmental transition and uncertain financial and banking relations, the partners and staff of Hood & Strong LLP intend to be proactive in communicating with you on a regular basis. We want you to feel confident that we are here for you when you seek support and expert advice. Together we will work through the financial uncertainties we are facing to make this year not only one of challenge, but also one of opportunity.

Robert J. Raffo
Managing Partner

Tax Outlook Under New Casualty Loss Rules
New law includes significant modifications

providing a special tax break for victims in disaster areas.

Starting point: The tax regulations say that you can qualify for a casualty loss deduction if damage is caused by an event that is "sudden, unexpected or unusual." This includes not only natural disasters such as tornadoes, hurricanes and earthquakes, but also automobile collisions and frozen pipes bursting. The same basic rules apply to theft of your property.

The amount you can deduct each year depends on whether the property damaged is personal or business property. For personal property, the deduction on a 2008 return is limited to the excess above 10% of your adjusted gross income (AGI) after subtracting a $100 "floor" per casualty or theft event. For example, if your AGI for 2008 was $100,000 and you suffered a $20,000 loss to personal property last year, the deduction is limited to $9,900 ([$20,000 - $100] - [10% of $100,000]).

In contrast, there are no such limits for business property. The full amount of the eligible loss can be deducted on the company's return.

The amount that is eligible for the deduction is the lesser of (1) the difference in the property's value before and after the casualty or (2) the adjusted basis in the property. Of course, you must reduce the deductible amount by any insurance proceeds received.

Finally, there is a special tax break if a loss is suffered in an area designated as a federal disaster area. You can elect to claim the deductible loss on your tax return for the year prior to the year in which the loss occurred.

New rules: The floor for each casualty and theft loss is increased from $100 to $500, but for 2009 only. Going back to our previous example, your deduction would be reduced to $9,500 for a $20,000 casualty loss occurring in 2009. On the other hand, the new law completely eliminates the 10%-of-AGI limit for losses in federal disaster areas. Thus, if you suffer a $20,000 loss in a disaster area in 2009, you would be able to deduct $19,500 ($20,000 - $500), no matter what your AGI is. The change is effective for tax years beginning after 2007 and before 2010.

see **Tax Outlook Under New Casualty Loss Rules,** page 8

Should You Skip Bonus Depreciation?

If your business placed qualified assets in service in 2008, it can claim a 50% "bonus depreciation" tax break for the assets. But there is a potential drawback for some business operations.

Reason: A business may not derive tax benefits if it shows a loss for the year. This is a common occurrence in the current economic environment.

Instead, a business may elect to forego bonus depreciation on its tax return. With this approach, the business can treat unused alternative minimum tax and research credits as being refundable, freeing up cash.

Caution: The rules in this area are extremely complex. It is recommended that you seek professional guidance for your company's situation.

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Dip in the Standard Mileage Rate

The IRS increased the standard mileage rate in the middle of last year. Now it has found a middle ground.

The standard mileage rate may be used in lieu of deducting actual business-related expenses of a vehicle. It was 50.5 cents per business mile traveled (plus related tolls and parking fees) for the first six months of 2008. Then the IRS raised the rate to 58.5 cents for the last six months. The IRS recently announced that this figure has declined to 55 cents per business mile for 2009.

Note: Even if you use the standard mileage rate, you still must keep records showing the date, place, mileage and business purpose of all your trips.

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Eight New Items on Your 2008 Return

cont. from page 1

4. Small-business deductions: If you own a small business, you can take advantage of an enhanced Section 179 deduction and 50% "bonus depreciation" for qualified assets placed in service last year. The maximum Section 179 allowance-the amount you can currently deduct-is increased to $250,000 for 2008 (up from $125,000 for 2007).

5. Property-tax deduction: Prior to 2008, state and local taxes could be deducted only by filers who itemized their tax deductions. But a law change enables nonitemizers to deduct the lesser of $1,000 ($500 for single filers) or property taxes actually paid on a 2008 return. Note: This special deduction was recently extended for the 2009 tax year.

6. Standard mileage rates: In an unusual move, the IRS adjusted the standard mileage rate for business driving midway through the year. The initial rate of 50.5 cents per business mile plus related tolls and parking fees (up from 48.5 cents per mile for 2007) was increased to 58.5 cents per business mile for the last six months of 2008. Note: The rate drops down to 55 cents per mile for 2009 (see Dip in the Standard Mileage Rate).

7. Itemized deductions: Itemized deductions are reduced for high-income taxpayers with an adjusted gross income (AGI) above a specified level. The reduction for 2008 begins if AGI exceeds $159,950 for joint filers (up from $156,400 for 2007). For 2008, you forfeit only one third of the amount that would otherwise be lost, as opposed to two thirds in 2007.

8. Casualty losses: Generally, personal casualty losses are deducted only to the extent they exceed 10% of your AGI. However, beginning in 2008, this 10%-of-AGI limit is eliminated for federal disaster-area losses (see Tax Outlook Under New Casualty Loss Rules).

Of course, this is only an overview of several key changes for 2008 returns. It is recommended that you seek professional assistance for your personal situation.

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Should You Convert to a Roth IRA Now?
Weigh the benefits against future tax break

There's a big tax break looming next year if you want to convert a traditional IRA into a Roth IRA. But you might not want to wait that long.

Basic rules: As with a traditional IRA, you may contribute up to $5,000 to a Roth IRA (less any traditional IRA contributions) for 2008. An extra $1,000 "catch-up contribution" is allowed if you are 50 years of age or older. There is no current income tax on any earnings within the Roth IRA. The deadline for 2008 contributions is your tax return due date (i.e., April 15, 2009).

However, you cannot take advantage of a Roth IRA if your modified adjusted gross income (AGI) exceeds a certain level. For instance, the phaseout for the 2008 tax year occurs between $159,000 and $169,000 of modified AGI for joint filers, and $101,000 and $116,000 for single filers.

Significantly, qualified distributions from Roth IRAs are exempt from income tax. A qualified distribution is a distribution from a Roth IRA in existence at least five years made after age 59½, upon death or disability, or to pay for first-time homebuyer expenses (up to a lifetime limit of $10,000).

If distributions do not meet these requirements, the funds are treated as being withdrawn as follows: contributions first, any amount converted from a traditional IRA second and earnings third. Withdrawals made before age 59½ may also be subject to a 10% penalty. Fortunately, you can choose to convert a traditional IRA to a Roth IRA to secure future tax-free distributions. Of course, you must pay the resulting tax on the conversion. This option is only available to individuals who have an AGI of $100,000 or less.

Key tax break: Beginning in 2010, the $100,000 AGI cap for Roth IRA conversions is removed. Furthermore, for conversions taking place in 2010, you may elect to spread the resulting tax liability ratably over the following two years.

So why would you accelerate a conversion? If you believe your IRA assets are currently valued on the low side, you might opt for a conversion if you are below the $100,000 AGI level for 2009. This reduces your tax liability on the conversion.

Similarly, if you converted within the past year and the value of the assets has declined since then, you can elect to "undo" the conversion. Otherwise, you will have paid tax on the conversion when the assets were at a higher value. The decision to convert to a Roth IRA, and when, is complex. Obtain professional assistance for your situation.❖

The limited liability corporation (LLC) form of business ownership has been gaining in popularity throughout the country, but don't think that this

Facts and Figures
Timely points of particular interest

Higher Per Diems -
The IRS recently announced an increase in the worry-free "per diem rates" for business travelers. Under the method used for travel in specified high-cost areas, the rate increased by $19 to $256 a day. For all other locations (i.e., the low-cost areas), the stated rate rose to $158 a day, an increase of $6. The new per diem rates officially went into effect for business travel beginning on October 1, 2008.

Social Security Tax -
It should come as no surprise that Social Security tax is going up again. The wage base for 2009 is $106,800 (up from $102,000 for 2008). But the tax rate on wages up to the amount of this threshold remains at 6.2%. Also, the 1.45% Hospital Insurance portion of the tax continues to apply to all wages. These tax rates are doubled for self-employment tax purposes, but a self-employed individual can deduct half of the tax.

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Facts and Figures
Timely points of particular interest

Required Minimum Distributions -
Generally, taxpayers 70½ years of age or older must take "required minimum distributions" from IRAs and qualified retirement plans such as 401(k)s each year. However, a new law passed late last year-the Worker, Retiree and Employer Recovery Act of 2008-suspends this requirement for 2009. More related information will be forthcoming.

Student Loans -
In a new case, a lender discharged $3,000 of a consolidated student loan because the borrower had made timely payments for three consecutive years. But the waiver did not qualify as a tax-free gift, nor did the borrower qualify for any special tax law exception. Result: The Tax Court said the $3,000 forgiveness of debt constituted taxable income.

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This LLC Is Just for One Person
Single-member format provides personal benefits

trend is limited to large corporations. For instance, a sole proprietor may choose to operate his or her business as a single-member limited liability company (SMLLC).

With an SMLLC, you are entitled to the same protection from personal liability as corporate owners using the LLC format. In other words, creditors generally cannot go after your home or your personal bank holdings. Only the SMLLC assets are exposed to this risk. You also avoid the double taxation problem that applies to regular C corporations.

To qualify as an SMLLC, you must observe the legal formalities required by state law, including drafting articles of incorporation and filing them with the appropriate state agency. Unless you elect otherwise, an SMLLC is treated as a "disregarded entity" that is not subject to double taxation. Like a partnership, all items of income and expense are reported on your personal return. Thus, you can realize the dual benefits of partnership taxation and personal liability protection.

In contrast, the earnings of C corporations are taxed twice-once on the corporate level and again on the personal level when you receive payment as dividends or compensation. This difference is often a key attraction for small-business owners.

If you operate an SMLLC and benefit from partnership-type taxation, you are required to pay self-employment tax on your earnings. For 2009, the self-employment tax is 12.4% on the first $106,800 of earned income (up from $102,000 for 2008). An additional 2.9% tax applies to all earned income. However, you are entitled to deduct half of the self-employment tax you must pay.

State and local taxation is also a consideration for small-business owners. In certain states, an annual franchise tax is levied on LLCs. In contrast, sole proprietorships may be exempt. Check with your tax adviser for the applicable law in your state.

Generally, making a switch from a sole proprietorship to an SMLLC is comparable with setting up an LLC for the first time. But there are complications if you decide to convert a C corporation to an SMLLC. The conversion is treated as a taxable liquidation of the corporation. Therefore, you will probably owe tax if your company owns appreciated assets, including intangibles such as goodwill. In summary, rely on guidance from expert advisers. ❖
The Emergency Economic Stabilization Act of 2008 includes several important tax law modifications for casualty and theft losses. Significantly, the new law increases the deduction floor for 2009 while

IRS Boosts Retirement Plan Limits for 2009
Higher figures reflect higher inflation rate

The IRS recently issued its annual cost-of-living adjustments for certain retirement plan thresholds. Due to low inflation rates during the middle of this decade, the increases have been relatively modest or nonexistent the last few years. However, the new indexed figures for 2009 reflect a few significant jumps as inflation crept higher last year.

Below is a summary of the key retirement plan limits for the past two years.

Note: The dollar limit for catch-up contributions to a SIMPLE (Savings Investment Match Plan for Employees) plan remains unchanged at $2,500. We will feature contribution limits for traditional and Roth IRAs in an upcoming issue.

	Limit for 2008	**Limit for 2009**
Maximum annual dollar benefit for a defined benefit plan	$185,000	$195,000
Maximum dollar limit on additions to a defined contribution plan	$46,000	$49,000
Maximum amount of compensation taken into account for qualified retirement plans	$230,000	$245,000
Dollar limit for definition of "key employee" in top-heavy retirement plan	$150,000	$160,000
Dollar limit for definition of "highly compensated employee" in qualified plan	$105,000	$110,000
Dollar limit for elective deferrals to a 401(k) plan	$15,500	$16,500
Dollar limit for contributions to a SIMPLE plan	$10,500	$11,500
Dollar limit for elective deferrals to deferred compensation plans of state and local governments and tax-exempt organizations	$15,500	$16,500
Dollar limit for catch-up contributions to a SIMPLE plan	$2,500	$2,500
Dollar limit for catch-up contributions to a 401(k), 403(b), 457 or SEP (Simplified Employee Pension) plan	$5,000	$5,500

The Sun Sets on Day-traders

If you are a day-trader in securities, you are generally required to deduct your investment-related expenses as miscellaneous expenses (subject to the usual 2%-of-adjusted gross income floor). The expenses are deductible in full only if your activities qualify as a business.

New case: A couple made a few hundred stock trades a year, but they traded on fewer than half of the days that the stock markets were open. In addition, the taxpayers held onto many of their stock positions for more than 31 days.

The Tax Court determined that these trading activities were too sporadic to be treated as a business. So the expenses were treated as miscellaneous expenses on the couple's joint return.

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