



## **21 Things You Need to Know About the 2009 Tax Laws**

We are only one year away from perhaps the most interesting, most experimental year in the history of the tax code: 2010. But before we get there, we have a host of little adjustments in tax law for 2009. Let's take a look at the notable changes. While we're at it, we will also include a couple of tax provisions enacted during 2008 that are still applicable in 2009. (For those of you wondering exactly where the last minute falls on your calendar, April 15 is a Wednesday this year.)

## 1) No mandatory taxable withdrawals from tax-deferred retirement accounts in 2009.

Late last year, President Bush signed a new law suspending all Required Minimum Distributions (RMDs) from IRAs, 401(k)s and 403(b)s for 2009. If you are 70½ or older, you can skip your RMD this year without a tax penalty.<sup>1</sup>

- *Did you turn 70½ in 2008?* You have until April 1, 2009 to take your RMD for the 2008 tax year, calculated using your account balance as of December 31, 2007. (You may have taken that first RMD in 2008.)<sup>2</sup>
- *Will you turn 70½ in 2009?* You have no requirement to take a 2009 RMD, but you will need to make a 2010 RMD by December 31, 2010, which the IRS will officially count as your "second" distribution from your retirement account, even though you didn't take a "first" one the year before.<sup>2</sup>
- *Do you have an inherited IRA?* You can skip your mandatory withdrawal in 2009. Effectively, this gives you another year toward the five-year deadline you face to withdraw all the funds in that IRA. (In fact, you may not have to face this deadline. If the original IRA owner died after his or her Required Beginning Date or RBD, which is generally April 1 of the year after turning 70½, the timetable for withdrawals is longer. If the initial IRA owner designated a beneficiary, the IRA custodian may permit stretch IRA planning, whereby the beneficiary may receive payments based on their own life expectancy.)<sup>3</sup>
- *Are you taking regular 72(t) withdrawals from a retirement plan?* You still have to take your required withdrawals; you cannot skip them in 2009.<sup>4</sup>
- *Do you have a defined benefit plan?* Sorry – this new law only applies to defined contribution plans. You still have to take your required withdrawals.<sup>4</sup>

## 2) Many retirement plan contribution limits rise.

The contribution limits on 401(k) and 403(b) plans have risen by \$1,000 – you can put up to \$16,500 in either a 401(k) or 403(b) in 2009. Catch-up contributions (permitted if you are age 50 or older) also increase by \$500 for both 401(k) and 403(b) plans to a maximum of \$5,500 for 2009.<sup>5</sup>

Contribution limits on SIMPLE plans are also raised by \$1,000 to \$11,500 in 2009. Compensation amounts for simplified employee pensions (SEPs) go up from \$500 to \$550 in 2009. The contribution limits on 457 plans rise from \$15,500 to \$16,500.<sup>6</sup>

The IRS has not raised annual contribution limits on traditional and Roth IRAs. The annual contribution limits for both types of IRAs remain \$5,000 or your taxable compensation for 2009, whichever will be smaller. Generally, up to \$1,000 in additional catch-up contributions may be made by those 50 and older.<sup>5</sup>

### **3) MAGI limits affecting traditional IRA and Roth IRA contributions increase.**

**Traditional IRAs:** if you have a retirement plan at work, your deduction for contributions to a traditional IRA will be reduced (phased out) if your MAGI falls within these ranges.

- Married Filing Jointly or Qualifying Widow: \$89,000-\$109,000
- Single or Head of Household: \$55,000-\$65,000
- Married Filing Separately: \$0-\$10,000 (no change from 2008).<sup>7</sup>

If your AGI is above \$176,000 in 2009, you cannot claim a deduction for contributions to a traditional IRA.<sup>7</sup>

**Roth IRAs:** Roth IRA contribution limit phase-outs are as follows.

- Married Filing Jointly or Qualifying Widow: \$166,000-\$176,000
- Single or Head of Household: \$105,000-\$120,000
- Married Filing Separately and living with your spouse at any time in 2009: \$0-\$10,000 (no change from 2008).<sup>7</sup>

### **4) The estate tax exemption rises dramatically.**

The estate tax exemption is \$3.5 million for 2009, as opposed to \$2 million in 2008. The estate tax rate is still 45% for 2009.<sup>8</sup>

### **5) The gift tax exclusion increases.**

For 2009, it is \$1,000 higher – rising to \$13,000.<sup>8</sup>

### **6) Personal exemption values rise by \$150.**

In 2009, each personal and dependency exemption you claim will be worth \$3,650, up from \$3,500 in 2008.<sup>8</sup>

## 7) Standard deductions increase.

For TY 2009, standard deduction amounts rise by \$250-500 depending on your filing status.

- Married Filing Jointly or Qualifying Widow: \$11,400
- Single or Head of Household: \$8,350
- Single or Married Filing Separately - \$5,700<sup>8</sup>

## 8) Tax bracket thresholds have been adjusted for inflation.

Here's where the brackets kick in for 2009.

- Single Taxpayers:
  - 25% bracket @ \$33,950
  - 28% bracket @ \$82,250
  - 33% bracket @ \$171,550
  - 35% bracket @ \$372,950
- Married Filing Jointly or Qualifying Widow:
  - 25% bracket @ \$67,900
  - 28% bracket @ \$137,050
  - 33% bracket @ \$208,850
  - 35% bracket @ \$372,950
- Married Filing Separately:
  - 25% bracket @ \$33,950
  - 28% bracket @ \$68,525
  - 33% bracket @ \$104,425
  - 35% bracket @ \$186,475
- Head of Household:
  - 25% bracket @ \$45,500
  - 28% bracket @ \$117,450
  - 33% bracket @ \$190,200
  - 35% bracket @ \$372,950<sup>9</sup>

## **9) AMT exemption amounts go way down.**

Congress will likely intervene at the end of 2009 to counter this, but if they don't come up with an AMT patch, AMT exemption amounts will be really low.

- Single or Head of Household: \$33,750
- Married Filing Jointly or Qualifying Widow: \$45,000
- Married Filing Separately: \$22,500<sup>9</sup>

## **10) Mileage deduction rates increase.**

In TY 2009, business miles can be deducted at \$0.55 per mile. Miles accumulated for medical travel or for purposes of moving can be deducted at the rate of \$0.24 a mile. Lastly, miles driven while performing charitable services can be deducted at \$0.14 per mile.<sup>10</sup> (A 2008 note: business miles driven from July 1, 2008 through the end of 2008 can be deducted at a rate of \$0.585 per mile; before June 30, the deduction was \$0.505 cents per mile.<sup>11</sup>)

## **11) A higher tax exclusion for taxpayers working outside the U.S.**

The exclusion is \$91,400 for 2009.<sup>12</sup>

## **12) Less of a capital gains tax break when it comes to the sale of vacation homes, second homes and certain rental properties.**

Say goodbye to a great tax loophole. In years past, the IRS allowed owners of principal residences to take advantage of a \$250,000 capital gains tax exemption when they sold or exchanged said residences (the exemption was \$500,000 for those married and filing jointly). To qualify, a home had to be the owner's principal residence for just two of the five years ending on the date of the sale or exchange.

Savvy homeowners often used this capital gains exemption to sell their main home, then move into a vacation home for two or more years and sell that home to reap a similar tax break. The Housing and Economic Recovery Act of 2008 changed things a bit. Now when you sell a vacation home or other secondary residence, the IRS will calculate the amount of capital gains to be excluded from the sale based on the ratio of time after 2008 that the home was used as a second home or rental property to the total time you have owned the home (in IRC terms, "qualified" vs. "non-qualified" use). So beginning this year, you will be eligible for a calculated percentage of the \$250,000/\$500,000 exclusion rather than the full amount.<sup>12</sup> If you want to sell a second home that you rent out, the rule also applies. It will even apply if you make a former vacation home your primary residence.<sup>13</sup>

### **13) A credit for first-time homebuyers.**

If you purchase, or have purchased, a home (personal residence) between April 9, 2008, and June 30, 2009, you could be eligible for a credit of up to \$7,500. This credit is designed for first-time buyers, not people buying income property or trading up. Single filers who earn more than \$95,000 and married taxpayers filing jointly who earn more than \$170,000 aren't eligible for the credit. You are also ineligible if you have owned a home within three years of the qualifying purchase.

Here's the downside of this credit: eventually, it must be paid back. Basically, it's a 15-year interest-free loan dressed up in IRS clothing.<sup>11</sup>

### **14) A Recovery Rebate Credit available to those who didn't get a stimulus check in 2008.**

Not everybody got a check. Some earned too little in 2007, some made too much in 2007. (Eligibility was based on 2007 tax return information.) Did you earn under \$3,000 in qualifying income in 2007? Did you earn more than \$75,000 (single taxpayers) or \$150,000 (married taxpayers) in 2007? If so, you may have received only a partial stimulus payment or none at all in 2008. If you think your 2007 income was abnormally high or low, you can apply for the Recovery Rebate Credit. The IRS can even figure this credit for you, or you can use an online calculator that is supposed to show up online at [irs.gov](http://irs.gov) in February.<sup>11</sup> If your family welcomed a new child last year, you may qualify for an additional credit, even if you got a check in 2008.<sup>14</sup>

### **15) A higher casualty and theft loss limit.**

The IRS says: "a personal casualty or theft loss must exceed \$500 to be allowed for 2009. This is in addition to the 10% of AGI limit that generally applies to the net loss."<sup>15</sup> In 2008, the floor for casualty losses was only \$100.

### **16) Changes regarding the status of a "qualifying child".**

The IRS has introduced some new tests this year.

- A parent must claim an exemption for a child before said child can qualify for the child tax credit.
- If the parents of a child don't claim the child as a qualifying child, no other person can, unless that person's AGI is higher than the highest AGI of any parent of the child.
- A qualifying child cannot be older than you are.
- A qualifying child cannot file a joint return unless the intent of the return is to claim a refund.<sup>15</sup>

## **17) The Earned Income Credit (EIC) increases by \$200, and EIC eligibility limits rise.**

This is a tax break for low- and middle-income families and working families with two or more children. In 2009, the maximum EIC is \$5,028, as opposed to \$4,824 in 2008. Last year, joint return filers with two or more children could take the credit if they came in under the qualifying income limit of \$41,646. For 2009, that qualifying income limit is \$43,415.<sup>16</sup>

## **18) A notable change for the Hope Credit and Lifetime Learning Credit.**

The Hope Credit, sometimes called the Hope Scholarship, helps parents handle expenses for the first two years of a child's college education. For TY 2009, the Hope Credit is \$1,800.<sup>17</sup> (But it may be larger if you live in certain Midwest states – see #21 below.) The Lifetime Learning Credit is intended for continuing education.

Here's the change: in the 2009 tax year, a taxpayer's MAGI will determine the reduction in the amount of the Lifetime Learning Credit and the Hope Credit. Reductions start at \$50,000 for individual filers, and \$100,000 for joint filers.<sup>17</sup>

There may be more change on the way. Under the Obama administration, these credits might be replaced by a single, all-purpose education credit of up to \$2,500, with higher eligibility limits. Part of this \$2,500 credit would even be refundable. We'll see if the unification of these credits advances beyond the House Ways and Means Committee.<sup>18</sup>

## **19) New energy credits you may be able to take.**

New credits are available for those who drive plug-in electric vehicles in 2009 and those who put "qualifying energy savings items" in service in their homes in 2009.<sup>15</sup> There is now a 30% tax credit that can be used to offset the total cost of putting a solar power system into your home. If you use a wind turbine to generate energy for your business or your residence, or if you use a biomass stove, there are special tax credits available to you this year. The solar and wind residential tax credit can also be claimed against the AMT. Here's another energy-related tax credit: your employer can now reimburse you up to \$20 per month if you commute to work on a bicycle.<sup>12</sup>

## **20) Income caps rise for tax-free EE bonds.**

Are you married? Do you file jointly? You may have a better chance to qualify for a Series EE savings bond used for education purposes this year. The new phase-out range for tax year 2009 is \$104,900-\$134,900 (AGI). The phase-out range for single filers is \$69,950- \$84,950.<sup>12</sup>

## 21) Special tax breaks for Midwesterners affected by the floods, storms and tornadoes in 2008.

The Heartland Disaster Tax Relief Act of 2008, passed last October, offers residents of Iowa, Illinois, and eight other Midwestern states some tax relief. If you lived in a Midwestern county that was declared a “disaster area” by the federal government at some point last year, here are some tax code changes that apply regionally:

- An expanded Hope Credit for students enrolled and paying tuition at eligible schools located in disaster-area counties. Instead of the usual \$1,800 Hope Credit, these students can effectively use a \$3,600 credit in 2009. (For 2009, the Hope Credit is expanded within these geographic areas to 100% of the first \$2,400 in eligible expenses plus 50% of the next \$2,400. Translation: up to \$3,600 credit.)
- Did you suffer casualty or theft losses attributable to storms, floods, tornadoes, or looting that occurred thereafter? If you did, the Heartland Disaster Tax Relief Act lifted certain limits on losses that could be claimed. If you want to take time to itemize, you have the opportunity to deduct the entirety of your unreimbursed losses on your 2008 federal return.
- Did you take anyone in who lost their home in any of these disasters? If you provided housing for a displaced disaster victim, you may be able to claim an additional exemption of \$500 for each displaced individual, to a maximum of \$2,000 on your 2008 return.
- Eligible taxpayers can figure earned income tax credits or refundable child tax credits using their prior year’s earned income, if it results in getting them the higher credit.
- If you had to take 72(t) early distributions from your retirement plan as a consequence of economic hardship brought about by these natural disasters, the HDTRA offers you some tax relief.
- The HDTRA temporarily removes limitations on certain charitable contributions and raises standard mileage rates for taxpayers who used their cars and trucks for charitable services in the wake of the floods and storms.<sup>19</sup>

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To finish up, here are three topics that don’t concern actual 2009 tax law changes yet are definitely worth noting.

**Social Security:** For 2009, the maximum Social Security benefit rises to \$2,399 per month. The cost-of-living adjustment to Social Security benefits for 2009 is 5.8%, well ahead of current inflation. Thankfully, there is no hike in the Social Security tax or Medicare tax for 2009. Social Security benefits will be taxed at 6.2%. The Medicare tax remains at 1.45%.<sup>17</sup>

**The proposed “Making Work Pay” tax credit.** This is a notable feature of the planned stimulus package envisioned by House Democrats and President Obama – a refundable tax credit of up to \$500 for working individuals and up to \$1,000 for working families. (The credit would phase out for individuals with AGI above \$75,000.) The credit would give eligible individuals and families a choice: they could claim it on their federal tax returns, or if they prefer, they could claim it via a reduction in the amount of income tax withheld from their wages.<sup>20</sup>

**The idea of a national sales tax holiday.** You’ve probably heard about this proposal from the National Retail Federation, which is lobbying hard to generate support for the idea. The NRF proposes three national sales tax holidays – not single days, but three 10-day-long periods in March, July and October of 2009. It claims the average family would save \$175 in 2009 as a result of the sales tax suspensions, and many families would undoubtedly be spurred to buy more and save more. Will Congress pick up this ball and run with it? We shall see.<sup>21</sup>

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