



LGT

FINANCIAL FOCUS



Lane Gorman Trubitt, L.L.P.
Accountants & Advisors

Your Accounting for a New Economy

President Signs the HIRE Act: What It Means For You!

Legislative Watch--

President signs HIRE Act into law, fixing effective date of many new law provisions

On March 18, President Obama signed H.R. 2847, carrying the Hiring Incentives to Restore Employment (HIRE) Act, into law as P.L. 111-47. The President's signature sets the effective date for numerous HIRE Act provisions with an effective date geared to the March 18, 2010, date of enactment. For example, under the payroll tax holiday provision (Code Sec. 3111(d)(1), as amended by Act Sec. 101(a)), the OASDI tax on employers doesn't apply to wages paid by a qualified employer with respect to employment during the period beginning on Mar. 19, 2010 (day after enactment) and ending on Dec. 31, 2010, of any qualified individual for qualifying services. In addition, the up-to-\$1,000 credit for "retained workers" under Act Sec. 102, applies for any tax year ending after Mar. 18, 2010.

Business tax changes in the 2010 HIRE Act

Extension of enhanced small business expensing (Section 179). The new law gives a one-year lease on life to enhanced expensing rules, which allow qualifying businesses the option to currently deduct the cost of business machinery and equipment, instead of recovering it via depreciation over a number of years. For tax years beginning in 2010, the maximum amount that a business may expense is \$250,000, and the expensing election begins to phase out when a business buys more than \$800,000 of expensing-eligible assets. These dollar limits are the same as those that were in effect for 2008 and 2009.

Payroll tax holiday and up-to-\$1,000 credit for employers who hire unemployed workers. To help stimulate the hiring of workers by the private sector, the new law exempts any private-sector employer

that hires a worker who had been unemployed for at least 60 days from having to pay the employer's 6.2% share of the Social Security payroll tax on that employee for the remainder of 2010. A company could save a maximum of \$6,621 if it hired an unemployed worker and paid that worker at least \$106,800-the maximum amount of wages subject to Social Security taxes-by the end of the year. As an additional incentive, for any qualifying worker hired under this initiative that the employer keeps on payroll for a continuous 52 weeks, the employer is eligible for an additional non-refundable tax credit of up to \$1,000 after the 52-week threshold is reached, to be taken on their 2011 tax return. In order to be eligible, the employee's pay in the second 26-week period must be at least 80% of the pay in the first 26-week period.

Workers hired after the date of introduction of the legislation (Feb. 3, 2010) are eligible for the payroll tax forgiveness and the retention bonus, but only wages paid after the date of the new law's enactment receive the exemption for payroll taxes.

Here are some additional features of the new hiring incentive:

- The tax benefit of the new incentive is immediate. It puts money into a business' cash flow immediately, since the tax is simply not collected in the first place.
- The tax benefit generally applies only to private-sector employment, including nonprofit organizations-public sector jobs are generally not eligible for either benefit. However, employment by a public higher education institution would qualify.
- There is no minimum weekly number of hours that the new employee must work for the employer to be eligible, and there is no maximum on the dollar amount of payroll taxes per employer that may be forgiven.
- For workers that would otherwise be eligible for the "Work Opportunity Tax Credit," the employer must select one benefit or the other for 2010-no double dipping.
- An employer can't claim the new tax breaks for hiring family members.
- A worker who replaces another employee who performed the same job for the employer is not eligible for the benefit, unless the prior employee left the job voluntarily or for cause.
- For the hiring to qualify, the new hire must sign an affidavit, under penalties of perjury, stating that he or she has not been employed for more than 40 hours during the 60-day period ending on the date the employment begins.
- The incentive is not biased towards either low-wage or high-wage workers. Under the measure, a business saves 6.2% on both a \$40,000 worker and a \$90,000 worker.
- The payroll tax holiday does not apply with respect to wages paid during the first calendar quarter of 2010, but the amount by which the Social Security payroll tax would have been reduced under the payroll tax holiday provision during the first calendar quarter is applied against the tax imposed on the employer for the second calendar quarter of 2010.
- The Act creates a similar new set of rules permitting a payroll tax holiday for railroad retirement tax purposes.

- The credit for retaining qualifying new hires is the lesser of \$1,000 or 6.2% of the wages paid by the taxpayer to the retained worker during the 52-consecutive-week period. Thus, the credit for a retained worker will be \$1,000 if, disregarding rounding, the retained worker's wages during the 52-consecutive-week period exceed \$16,129.03. However, the credit is not available for pay not treated as wages under the Code (e.g., remuneration paid to domestic workers).

Direct payment option for certain tax credit bonds. State and local governments have the ability to issue special purpose tax credit bonds for school construction, energy conservation and renewable energy. The federal government subsidizes these tax credit bonds by providing investors in these bonds with a federal tax credit in place of interest that would otherwise be payable on the bond. In lieu of providing investors with federal tax credits, the new law allows issuers of qualified school construction bonds, qualified zone academy bonds, clean renewable energy bonds, and qualified energy conservation bonds to elect to receive a direct payment from the federal government equal to the amount of the federal tax credit that would otherwise be provided for these bonds.

Revenue offsets. To pay for the tax incentives, the Act includes revenue offsets consisting of: (1) a comprehensive set of measures to reduce offshore noncompliance by giving IRS new administrative tools to detect, deter and discourage offshore tax abuses; and (2) a three-year delay (through 2020) of implementation of worldwide allocation of interest—a liberalized rule for allocating interest expense between U.S. sources and foreign sources for purposes of determining a taxpayer's foreign tax credit limitation.

Payroll tax holiday and up-to-\$1,000 credit for companies hiring unemployed workers in the 2010 HIRE Act

To help stimulate the hiring of workers by the private sector, the new law exempts any private-sector employer that hires a worker who had been unemployed for at least 60 days from having to pay the employer's 6.2% share of the Social Security payroll tax on that employee for the remainder of 2010. A company could save a maximum of \$6,621 if it hired an unemployed worker and paid that worker at least \$106,800—the maximum amount of wages subject to Social Security taxes—by the end of the year. As an additional incentive, for any qualifying worker hired under this initiative that the employer keeps on payroll for a continuous 52 weeks, the employer is eligible for an additional non-refundable tax credit of up to \$1,000 after the 52-week threshold is reached, to be taken on their 2011 tax return. In order to be eligible, the employee's pay in the second 26-week period must be at least 80% of the pay in the first 26-week period.

Workers hired after the date of introduction of the legislation (Feb. 3, 2010) are eligible for the payroll tax forgiveness and the retention bonus, but only wages paid after the date of the new law's enactment receive the exemption for payroll taxes.

Here are some additional features of the new hiring incentive:

- The tax benefit of the new incentive is immediate. It puts money into a business' cash flow immediately, since the tax is simply not collected in the first place.
- The tax benefit generally applies only to private-sector employment, including nonprofit organizations- public sector jobs are generally not eligible for either benefit. However, employment by a public higher education institution would qualify.
- There is no minimum weekly number of hours that the new employee must work for the employer to be eligible, and there is no maximum on the dollar amount of payroll taxes per employer that may be forgiven.
- For workers that would otherwise be eligible for the "Work Opportunity Tax Credit," the employer must select one benefit or the other for 2010-no double dipping.
- An employer can't claim the new tax breaks for hiring family members.
- A worker who replaces another employee who performed the same job for the employer is not eligible for the benefit, unless the prior employee left the job voluntarily or for cause.
- For the hiring to qualify, the new hire must sign an affidavit, under penalties of perjury, stating that he or she has not been employed for more than 40 hours during the 60-day period ending on the date the employment begins.
- The incentive is not biased towards either low-wage or high-wage workers. Under the measure, a business saves 6.2% on both a \$40,000 worker and a \$90,000 worker.
- The payroll tax holiday does not apply with respect to wages paid during the first calendar quarter of 2010, but the amount by which the Social Security payroll tax would have been reduced under the payroll tax holiday provision during the first calendar quarter is applied against the tax imposed on the employer for the second calendar quarter of 2010.
- The Act creates a similar new set of rules permitting a payroll tax holiday for railroad retirement tax purposes.
- The credit for retaining qualifying new hires is the lesser of \$1,000 or 6.2% of the wages paid by the taxpayer to the retained worker during the 52-consecutive-week period. Thus, the credit for a retained worker will be \$1,000 if, disregarding rounding, the retained worker's wages during the 52-consecutive-week period exceed \$16,129.03. However, the credit is not available for pay not treated as wages under the Code (e.g., remuneration paid to domestic workers).

Offshore anti-abuse provisions in the 2010 HIRE Act

To pay for the hiring incentives in the recently enacted "Hiring Incentives to Restore Employment Act" (the 2010 HIRE Act), Congress passed several offsetting revenue raisers, including a comprehensive set of measures to reduce offshore noncompliance by giving IRS new administrative tools to detect, deter and discourage offshore tax abuses. Here is a brief overview of the new offshore anti-abuse provisions.

Increased disclosure of beneficial owners

Reporting on certain foreign bank accounts. The Act imposes a 30% withholding tax on certain income from

U.S. financial assets held by a foreign institution unless the foreign financial institution agrees to disclose the identity of any U.S. individual with an account at the institution (or the institution's affiliates) and to annually report on the account balance, gross receipts and gross withdrawals/payments from such account. Foreign financial institutions would also be required to agree to disclose and report on foreign entities that have substantial U.S. owners. Congress expects that foreign financial institutions will comply with these disclosure and reporting requirements in order to avoid paying this withholding tax. These provisions are effective generally for payments made after 2012.

Reporting on owners of foreign corporations, foreign partnerships and foreign trusts. The Act requires foreign entities to provide withholding agents with the name, address and tax identification number of any U.S. individual that is a substantial owner of the foreign entity. Withholding agents are to report this information to the U.S. Treasury Department. The Act exempts publicly-held and certain other foreign corporations from these reporting requirements and provides the Treasury Department with the regulatory authority to exclude other recipients that pose a low risk of tax evasion. Any withholding agent making a withholdable payment to a foreign entity that does not comply with these disclosure and reporting requirements is required to withhold tax at a rate of 30%. These provisions are effective generally for payments made after 2012.

Extending bearer bond tax sanction to bearer bonds designed for foreign markets. Bearer bonds (i.e., bonds that do not have an official record of ownership) allow individuals seeking to evade taxes with the ability to invest anonymously. Recognizing the potential for U.S. individuals to take advantage of bearer bonds to avoid U.S. taxes, Congress took a number of steps in the 1980's to eliminate bearer bonds in the United States. First, they prevented the U.S. government from issuing bearer bonds that would be marketed to U.S. investors. Second, they imposed sanctions on issuers of bearer bonds that could be purchased by U.S. investors. The Act extends many of these sanctions to bearer bonds that are marketed to foreign investors and prevents the U.S. government from issuing any bearer bonds. These provisions apply to debt obligations issued after the date which is two years after the new law's enactment date.

Foreign financial asset reporting

Disclosure of information with respect to foreign financial assets. The new law requires individuals to report offshore accounts and other foreign financial assets with values of \$50,000 or more on their tax returns. Individuals who fail to make the required disclosures are subject to a penalty of \$10,000 for the tax year; an additional penalty can apply if Treasury notifies an individual by mail of the failure to disclose and the failure to disclose continues. These provisions apply for tax years beginning after the new law's enactment date.

Penalties for underpayments attributable to undisclosed foreign financial assets. For tax years beginning after the new law's enactment date, the Act imposes a penalty equal to 40% of the amount of any understatement that is attributable to an undisclosed foreign financial asset (i.e., any foreign financial asset that a taxpayer is required to disclose and fails to disclose on an information return).

New 6-year limitations period. For returns filed after the new law's enactment date as well as for any other return for which the assessment period has not yet expired as of the new law's enactment date, the Act imposes a new six-year limitations period for omissions of items from a tax return that exceed \$5,000 and are attributable to one or more reportable foreign assets. The Act also clarifies that the statute of limitations does not begin to run until the taxpayer files the information return disclosing the taxpayer's reportable foreign assets.

Other disclosure provisions

New reporting rule for PFICs. Effective on the new law's enactment date, activities with respect to passive foreign investment companies (PFICs) are subject to a new reporting rule. Unless otherwise provided by IRS, each U.S. person who is a shareholder of a PFIC must file an annual information return containing such information as IRS may require. A person that meets this new reporting requirement could, however, also have to meet the new reporting rule requiring disclosure of information with respect to foreign financial assets (see above). It is anticipated that IRS will exercise its regulatory authority to avoid duplicative reporting.

Electronic filing. For returns the due date for which (determined without regard to extensions) is after the new law's enactment date, the Act creates an exception to the general annual 250 returns threshold for electronic filing: IRS will be permitted to issue regs requiring filing on magnetic media for any return filed by a financial institution with respect to any taxes withheld by it for which it is personally liable. Thus, IRS will be authorized to require a financial institution to electronically file returns with respect to any taxes withheld by the financial institution even though the financial institution files less than 250 returns during the year.

Provisions related to foreign trusts

Clarifications with respect to foreign trusts. Under present law, a U.S. person is treated as the owner of the property transferred to a foreign trust if the trust has a U.S. beneficiary. Under current Treasury regulations, a foreign trust is treated as having a U.S. beneficiary if any current, future or contingent beneficiary of the trust is a U.S. person. Notwithstanding this requirement, some taxpayers have taken positions that are contrary to this regulation. In order to enhance compliance with this regulation, the Act codifies this regulation into the statute. This provision is effective on the new law's enactment date. The Act also clarifies that a foreign trust will be treated as having a U.S. beneficiary if (1) any person has discretion to determine the beneficiaries of the trust unless the terms of the trust specifically identify the class of beneficiaries and none of those beneficiaries are U.S. persons or (2) any written oral or other agreement could result in a beneficiary of the trust being a U.S. person. As a final clarification, the Act clarifies that the use of any trust property will be treated as a payment from the trust in the amount of the fair market value of such use.

Presumption with respect to transfers to foreign trusts. For transfers of property after the new law's enactment date, the Act provides that if a U.S. person directly or indirectly transfers property to a foreign trust (other

than a trust established for deferred compensation or a charitable trust) IRS may treat the trust as having a U.S. beneficiary unless such person can demonstrate to the satisfaction of IRS that under the terms of the trust, (1) no part of the trust may be paid or accumulated during the year for the benefit of a U.S. person, (2) that if the trust were terminated during the year, no part of the trust could be paid to a U.S. person (3) and that such person provides any additional information as IRS may require with respect to such transfer.

Minimum penalty with respect to failure to report on certain foreign trusts. Under pre-Act law, a taxpayer that fails to file an information return with respect to certain transactions involving foreign trusts (e.g., the creation of a foreign trust, the transfer of money or property to a foreign trust, or the death of a U.S. owner of a foreign trust) is subject to a penalty of 35% of the amount required to be disclosed on such return. If IRS uncovers the existence of an undisclosed foreign trust but is unable to determine the amount required to be disclosed on such return, it is unable to impose a penalty. The Act strengthens this penalty by imposing a minimum penalty of \$10,000 on any such failure to file. This provision applies to notices and returns required to be filed after Dec. 31, 2009. Notwithstanding this minimum penalty, in no event may the penalties imposed on taxpayers for failing to file an information return with respect to a foreign trust exceed the amount required to be disclosed on the return.

Dividend equivalent payments

Dividend equivalents treated as dividends. For payments made on or after the date that is 180 days after the new law's enactment date, the Act treats a dividend equivalent as a dividend from U.S. sources for certain purposes, including the U.S. withholding tax rules applicable to foreign persons. A dividend equivalent is any substitute dividend made pursuant to a securities lending or a sale-repurchase transaction that (directly or indirectly) is contingent upon, or determined by reference to, the payment of a dividend from sources within the U.S. or any payment made under a specified notional principal contract that directly or indirectly is contingent upon, or determined by reference to, the payment of a dividend from sources within the U.S. A dividend equivalent also includes any other payment that IRS determines is substantially similar to a payment described in the preceding sentence. Under this rule, for example, IRS may conclude that payments under certain forward contracts or other financial contracts that reference stock of U.S. corporations are dividend equivalents.

How the Temporary Extension Act of 2010 affects the COBRA premium subsidy rules

On Mar. 2, the President signed into law the "Temporary Extension Act of 2010" (the Act), which, among other provisions extends the COBRA continuation premium subsidy for one month and makes a number of other clarifying and substantive changes to it. Here's an overview of the major changes to the COBRA premium subsidy rules:

Extension of COBRA 65% subsidy. In 2009, Congress created a temporary 65% COBRA premium subsidy in

response to a major recession that added millions to the unemployment rolls and would have left many without health insurance coverage because they couldn't afford to pay COBRA premiums on their own. The way the subsidy works is that, if a company has a group health plan that is subject to the Federal COBRA continuation coverage requirements or to similar requirements under State law, and the company receives a 35% payment from someone eligible for the subsidy, it must make the remaining 65% premium payment. The company is then "paid back," either by offsetting its payroll tax deposits or claiming the subsidy as an overpayment at the end of the payroll quarter. Eligible individuals can receive this subsidy for up to 15 months. However, under pre-Act law, to qualify for premium assistance, a worker had to be involuntarily terminated between Sept. 1, 2008 and Feb. 28, 2010. That meant that if there had not been an extension, workers involuntarily terminated after Feb. 28 wouldn't have been eligible for the COBRA subsidy. The new law extends the deadline for one month, so that workers who are involuntarily terminated between Sept. 1, 2008 and Mar. 31, 2010 are eligible for up to 15 months of COBRA subsidies. (I should also note that another bill currently being considered by the Senate would extend the 65% COBRA premium subsidy to apply for involuntary terminations through the end of 2010.)

New election for those terminated after a reduction in hours. The new law clarifies the treatment of COBRA continuation that results from reductions in hours followed by termination of employment. Evidently, there was some concern under pre-Act law regarding COBRA continuation coverage for workers who (1) were hit by a reduction in hours, (2) did not make a timely COBRA continuation election or made the election and later dropped COBRA continuation coverage (e.g., because it was too expensive), and (3) are ultimately involuntarily terminated. Under the new law, if an individual did not make a COBRA continuation coverage election when his or her hours were reduced (or made an election but then discontinued COBRA coverage), if the individual is then involuntarily terminated from employment, that will be treated as a qualifying event for COBRA continuation coverage purposes. The period of the individual's COBRA continuation coverage is determined as though the qualifying event were the reduction in hours of employment. However, affected individuals will not be required to make a payment for COBRA continuation coverage for the period between their reduction in hours of employment and their involuntary termination.

Tax changes affecting businesses in the Worker, Homeownership and Business Assistance Act of 2009

On Nov. 6, 2009, President Obama signed the "Worker, Homeownership, and Business Assistance Act of 2009" (the 2009 Assistance Act) into law. In addition to providing an extension of unemployment benefits for the longtime jobless, the 2009 Assistance Act includes tax changes for businesses, including liberalized rules for net operating losses and toughened penalties for partnerships and S corporations. I'm writing to give you an overview of these new provisions. Please call our offices for details of how the new changes may affect your business.

Five-Year Carryback of NOLs Extended to Include 2009 NOLs and to Apply to Most Businesses. A net operating loss (NOL) is the excess of business deductions (computed with certain modifications) over gross

income in a particular tax year. The loss can be deducted, through an NOL carryback or carryover, in another tax year in which gross income exceeds business deductions. In general, NOLs may be carried back two years and forward 20 years. The NOL is first carried back to the earliest tax year for which it's allowable as a carryback or a carryover, and is then carried to the next earliest tax year. A taxpayer may elect to forego the entire carryback period for an NOL and instead carry it forward.

Stimulus legislation passed earlier this year allowed eligible small businesses (with average annual gross receipts of \$15 million or less for 2006-2008) to elect to carry back NOLs from 2008 for 3, 4 or 5 years rather than the standard 2 years. A taxpayer with a fiscal year (i.e., other than a calendar year) was entitled to choose the extended carryback period for the tax year that began or ended in 2008.

New law. The 2009 Assistance Act provides an election for most taxpayers (not just small businesses) to increase the carryback period for an applicable NOL to 3, 4, or 5 years from 2 years. An applicable NOL means the taxpayer's NOL for any tax year ending after Dec. 31, 2007, and beginning before Jan. 1, 2010. A taxpayer with a fiscal year may effectively choose from among three taxable years, i.e., any taxable year beginning or ending in 2008 or 2009, as the loss year eligible for the extended carryback period.

Taxpayers electing a 5-year carryback can use the NOL to offset up to 50% of taxable income for the 5th tax year preceding the loss year, and 100% of taxable income in the remaining 4 carryback years. The amount of the NOL otherwise carried to tax years after the 5th preceding tax year is adjusted to take into account that the NOL could offset only 50% of the taxable income for the 5th year. That is to say, unlike previous versions of this proposal which were not included in the final legislation, there is no "haircut" for the amount by which the NOL is limited in the 5th preceding year.

In addition, the Act suspends the 90% limitation on the use of an NOL deduction for alternative minimum tax purposes, for alternative tax NOLs attributable to carrybacks for which the extended carryback is elected.

Generally, an extended carryback period election may be made for only one tax year. However, small businesses that have already elected an extended carryback for a 2008 NOL may also elect to extend the carryback for NOLs from 2009.

A similar extended carryback period is available for the loss from operations of a life insurance company.

The election of an extended carryback period must be made by the due date (with extensions) for filing the tax return for the taxpayer's last tax year beginning in 2009. Once made, the election is irrevocable. If the taxpayer had previously elected to forego the carryback of an NOL from a tax year ending before Nov. 6, 2009, the taxpayer may revoke that election before the due date (including extensions) for filing the taxpayer's 2009 return.

The right to elect an extended carryback period does not apply to any taxpayer that has received or will receive financial assistance under the Emergency Economic Stabilization Act of 2008 in the form of an equity infusion or acquisition of a warrant (or other right).

Increased Penalty for Failure to File Partnership or S Corporation Returns. Under pre-Act law, the penalty for the failure to file a partnership or S corporation return is \$89 per partner or shareholder for each month or portion of a month the return is not filed, up to a maximum of 12 months. The Act increases the penalty to \$195 per month per shareholder or partner, effective for returns for tax years beginning after December 31, 2009.

Additional FUTA Surtax Is Extended Through June of 2011. The Act provides that the 6.2% FUTA tax rate continues to apply through June of 2011, and the 6.0% rate applies for the remainder of calendar year 2011 and for later years. That is, the temporary 0.2% surtax is extended for 1½ years through June 30 of 2011. Delay the Application of the Worldwide Interest Allocation Election. The Act delays for seven years (through 2017) an election, previously effective for tax years after Dec. 31, 2010, that would let U.S. multinational companies allocate and apportion interest expense on a worldwide basis.

Corporate Estimated Tax Payments. The Act provides that for large corporations, the required payment of estimated tax otherwise due in July, August, or September of 2014 will be increased by 33%. The amount of the next required installment will be appropriately reduced to reflect the amount of the increase in the earlier installment. This will have the effect of accelerating government revenue for the affected fiscal year.

Expansion of Magnetic Media Filing by Return Preparers. The Act mandates that IRS require tax return preparers who reasonably expect to file more than ten income tax returns for individuals, trusts, or estates to file the tax returns on magnetic media, effective for tax returns filed after December 31, 2010.

Expansion of five-year carryback election for NOLs in the Worker, Homeownership and Business Assistance Act of 2009

Background. A net operating loss (NOL) is the excess of business deductions (computed with certain modifications) over gross income in a particular tax year. The loss can be deducted, through an NOL carryback or carryover, in another tax year in which gross income exceeds business deductions. In general, NOLs may be carried back two years and forward 20 years. The NOL is first carried back to the earliest tax year for which it's allowable as a carryback or a carryover, and is then carried to the next earliest tax year. A taxpayer may elect to forego the entire carryback period for an NOL and instead carry it forward.

Stimulus legislation passed earlier this year allowed eligible small businesses (with average annual gross receipts of \$15 million or less for 2006-2008) to elect to carry back NOLs from 2008 for 3, 4 or 5 years rather than the standard 2 years. A taxpayer with a fiscal year (i.e., other than a calendar year) was entitled to choose the extended carryback period for the tax year that began or ended in 2008.

New law. The 2009 Assistance Act provides an election for most taxpayers (not just small businesses) to increase the carryback period for an applicable NOL to 3, 4, or 5 years from 2 years. An applicable NOL means the taxpayer's NOL for any tax year ending after Dec. 31, 2007, and beginning before Jan. 1, 2010. This means the election may be made for a tax year beginning or ending in either 2008 or 2009.

Taxpayers electing a 5-year carryback can use the NOL to offset up to 50% of the available taxable income for the 5th tax year preceding the loss year, and 100% of all taxable income in the remaining 4 carryback years. The amount of the NOL otherwise carried to tax years after the 5th preceding tax year is adjusted to take into account that the NOL could offset only 50% of the taxable income for the 5th year. That is to say, unlike previous versions of this proposal which were not included in the final legislation, there is no "haircut" for the amount by which the NOL is limited in the 5th preceding year.

In addition, the Act suspends the 90% limitation on the use of an NOL deduction for alternative minimum tax purposes, for alternative tax NOLs attributable to carrybacks for which the extended carryback is elected. Generally, an extended carryback period election may be made for only one tax year. However, small businesses that have already elected an extended carryback for a 2008 NOL may also elect to extend the carryback for NOLs from 2009.

A similar extended carryback period is available for the loss from operations of a life insurance company.

The election of an extended carryback period must be made by the due date (with extensions) for filing the tax return for the taxpayer's last tax year beginning in 2009. Once made, the election is irrevocable. If the taxpayer had previously elected to forego the carryback of an NOL from a tax year ending before Nov. 6, 2009, the taxpayer may revoke that election before the due date (including extensions) for filing the taxpayer's 2009 return.

The right to elect an extended carryback period does not apply to any taxpayer that has received or will receive financial assistance under the Emergency Economic Stabilization Act of 2008 in the form of an equity infusion or acquisition of a warrant (or other right).

Tax changes affecting individuals in the Worker, Homeownership, and Business Assistance Act of 2009

Homebuyer Credit Extended and Liberalized. You may remember that the stimulus package enacted earlier this year included an up-to-\$8,000 tax credit for first-time homebuyers. This credit was scheduled to expire on November 30, 2009. The new law extends and expands the first-time homebuyer credit by:

- Extending deadlines for purchasing and closing on a home. Under the 2009 Assistance Act, an eligible taxpayer must buy, or enter into a binding contract to buy, a principal residence on or before April 30, 2010

and close on the home by June 30, 2010. For qualifying purchases in 2010, taxpayers have the option of claiming the credit on either their 2009 or 2010 return.

- Authorizing the credit for long-time homeowners buying a replacement principal residence. For the first time, long-time homeowners who buy a replacement principal residence may also claim a homebuyer credit of up to \$6,500 (up to \$3,250 for a married individual filing separately). They must have lived in the same principal residence for any five-consecutive-year period during the eight-year period that ended on the date the replacement home is purchased. One key point is that the replacement home must be a principal residence—vacation homes aren't eligible.
- Raising the income limitations for homeowners claiming the credit. People with higher incomes can now qualify for the credit. The new law raises the income limits for homes purchased after November 6, 2009. The credit phases out for individual taxpayers with modified adjusted gross income (MAGI) between \$125,000 and \$145,000 or between \$225,000 and \$245,000 for joint filers. The pre-2009 Assistance Act MAGI phase-outs of \$75,000 to \$95,000 or \$150,000 to \$170,000 for joint filers still apply to purchases on or before November 6, 2009.
- Providing additional homebuyer liberalizations for service members. The 2009 Assistance Act ensures that recapture of the credit will not apply to service members (including members of the U.S. uniformed services, Foreign Service, and intelligence community) who dispose of a principal residence or cease using a home as a principal residence after December 1, 2008, in connection with Government orders received by the individual or the individual's spouse for qualified official extended duty service. Additionally, in the case of service members serving outside the United States for at least 90 days during the period beginning after December 31, 2008, and ending before May 1, 2010, the credit is extended for one year. This means that the purchase must occur before May 1, 2011 (or July 1, 2011, for taxpayers with binding contracts). This change will allow service members stationed overseas to take advantage of the credit when they return.

However, the 2009 Assistance Act also adds new restrictions on the first-time homebuyer tax credit by:

- Imposing an \$800,000 purchase-price limitation. For purchases after November 6, 2009, the credit cannot be claimed for buying a residence for more than \$800,000. There is no phaseout mechanism. A purchase price that exceeds the \$800,000 threshold by even a single dollar will cause the loss of the entire credit.
- Requiring a minimum age of 18 to claim the credit.
- Prohibiting dependents from claiming the credit.
- Denying the credit for purchases from parties related to the taxpayer's spouse.
- Requiring taxpayers to attach a signed copy of their settlement statement to their return.
- Giving IRS the authority to automatically assess tax and begin collection proceedings in cases where they suspect fraud (thus shortening the time it takes for IRS to collect additional tax through the normal deficiency procedures). This IRS authority (called "math error authority") is retroactive to April 9, 2008, thus giving IRS the ability to quickly address any erroneous refund claims that have been previously filed.

Exclusion from Gross Income of Qualified Military Base Realignment and Closure Fringe. The

Homeowner's Assistance Program (HAP) has long provided payments to certain Defense Department employees and members of the Armed Forces to offset the adverse effects on housing values that result from a military base realignment or closure. These payments are excluded from the recipient's gross income and are not considered wages for FICA tax purposes (including Medicare). The stimulus legislation enacted earlier this year (i.e., the American Recovery and Reinvestment Act of 2009 (ARRA)) expanded HAP to cover, among other things, individuals whose property values were affected by the current real estate slowdown, including wounded Armed Forces members and civilian Department of Defense and Coast Guard employees, and Armed Forces members permanently reassigned from an area at or near a military installation. The new law expands the exclusion from income to cover HAP payments authorized under ARRA, effective for payments made after Feb. 17, 2009 (ARRA's enactment date).

Changes to first-time homebuyer credit in the Worker, Homeownership, and Business Assistance Act of 2009

You may remember that the stimulus package enacted earlier this year included an up-to-\$8,000 tax credit for first-time homebuyers. This credit was scheduled to expire on November 30, 2009. The new law extends and expands the first-time homebuyer credit by:

- *Extending deadlines for purchasing and closing on a home.* Under the 2009 Assistance Act, an eligible taxpayer must buy, or enter into a binding contract to buy, a principal residence on or before April 30, 2010 and close on the home by June 30, 2010. For qualifying purchases in 2010, taxpayers have the option of claiming the credit on either their 2009 or 2010 return.
- *Authorizing the credit for long-time homeowners buying a replacement principal residence.* For the first time, long-time homeowners who buy a replacement principal residence may also claim a homebuyer credit of up to \$6,500 (up to \$3,250 for a married individual filing separately). They must have lived in the same principal residence for any five-consecutive-year period during the eight-year period that ended on the date the replacement home is purchased. One key point is that the replacement home must be a principal residence—vacation homes aren't eligible.
- *Raising the income limitations for homeowners claiming the credit.* People with higher incomes can now qualify for the credit. The new law raises the income limits for homes purchased after November 6, 2009. The credit phases out for individual taxpayers with modified adjusted gross income (MAGI) between \$125,000 and \$145,000 or between \$225,000 and \$245,000 for joint filers. The pre-2009 Assistance Act MAGI phase-outs of \$75,000 to \$95,000 or \$150,000 to \$170,000 for joint filers still apply to purchases on or before November 6, 2009.
- *Providing additional homebuyer liberalizations for service members.* The 2009 Assistance Act ensures that recapture of the credit will not apply to service members (including members of the U.S. uniformed services, Foreign Service, and intelligence community) who dispose of a principal residence or cease using a home as a principal residence after December 1, 2008, in connection with Government orders received by the individual or the individual's spouse for qualified official extended duty service. Additionally, in the case

of service members serving outside the United States for at least 90 days during the period beginning after December 31, 2008, and ending before May 1, 2010, the credit is extended for one year. This means that the purchase must occur before May 1, 2011 (or July 1, 2011, for taxpayers with binding contracts). This change will allow service members stationed overseas to take advantage of the credit when they return.

However, the 2009 Assistance Act also adds new restrictions on the first-time homebuyer tax credit by:

- Imposing an \$800,000 purchase-price limitation. For purchases after November 6, 2009, the credit cannot be claimed for buying a residence for more than \$800,000. There is no phaseout mechanism. A purchase price that exceeds the \$800,000 threshold by even a single dollar will cause the loss of the entire credit.
- Requiring a minimum age of 18 to claim the credit.
- Prohibiting dependents from claiming the credit.
- Denying the credit for purchases from parties related to the taxpayer's spouse.
- Requiring taxpayers to attach a signed copy of their settlement statement to their return.
- Giving IRS the authority to automatically assess tax and begin collection proceedings in cases where they suspect fraud (thus shortening the time it takes for IRS to collect additional tax through the normal deficiency procedures). This IRS authority (called "math error authority") is retroactive to April 9, 2008, thus giving IRS the ability to quickly address any erroneous refund claims that have been previously filed.

Extended and liberalized homebuyer tax credit rules under the Worker, Homeownership, and Business Assistance Act of 2009

Homebuyer credit basics. Before the new law was enacted, the homebuyer credit was only available for qualifying first-time home purchases after April 8, 2008, and before December 1, 2009. The top credit for homes bought in 2009 is \$8,000 (\$4,000 for a married individual filing separately) or 10% of the residence's purchase price, whichever is less.

Only the purchase of a principal residence (i.e., a main home) located in the U.S. qualifies for the credit. Vacation homes and rental properties are not eligible.

The homebuyer credit reduces your tax liability on a dollar-for-dollar basis. If the credit is more than the tax you owe, the difference is paid to you as a tax refund.

For homes bought after December 31, 2008, you must pay back the homebuyer credit if you dispose of the home or stop using it as your principal residence within 36 months of purchase.

The credit is subject to a phase-out based on your modified adjusted gross income (AGI) for the year of purchase. Before the new law, the credit was phased out at modified AGI between \$75,000 and \$95,000 (\$150,000 and \$170,000 for joint filers).

Your guide to the revised homebuyer credit. The new law makes four important changes to the homebuyer credit, the first three of which make the credit easier to claim:

New lease on life for the homebuyer credit. The homebuyer credit is extended to apply to a principal residence bought before May 1, 2010. The homebuyer credit also applies to a principal residence bought before July 1, 2010 by a person who enters into a written binding contract before May 1, 2010, to close on the purchase of the principal residence before July 1, 2010.

In general, a home is considered bought for credit purposes when the closing takes place. So the extra two months (May and June of 2010) helps buyers who find a home they like but can't close on it before May 1, 2010. They can go to contract on the home before May 1, 2010, close on it before July 1, 2010, and get the homebuyer credit (if they otherwise qualify).

Certain service members on extended duty outside of the U.S. get an extra year to buy a qualifying home and get the credit; they also can avoid the recapture rules under certain circumstances.

Current homeowners who are "long-time residents" can claim credit of up to \$6,500. For purchases after November 6, 2009, you can claim the homebuyer credit if you (and, if married, your spouse) maintained the same principal residence for any period of five consecutive years during the eight years ending on the date that you buy the subsequent principal residence. For example, if you and your spouse are empty nesters who have lived in your suburban home for the past ten years, you may be eligible for the credit if you buy a house in town.

You don't have to sell your current home in order to qualify for a homebuyer credit on the replacement home. You can buy the replacement home to beat the new deadlines (explained above) before you sell the old home. For that matter, you can hold on to your old home in the hope of achieving a better selling price later on. However, the replacement home must be your principal residence.

The maximum allowable homebuyer credit for qualifying existing homeowners is \$6,500 (\$3,250 for a married individual filing separately), or 10% of the purchase price of the subsequent principal residence, whichever is less.

The homebuyer credit is available to higher-income taxpayers. For purchases after November 6, 2009, the homebuyer credit phases out over higher levels of modified AGI, making the credit available to a bigger pool of buyers. For individuals, the phaseout range is between \$125,000 and \$145,000, and for those filing a joint return, it's between \$225,000 and \$245,000.

New home-price limit for the homebuyer credit. For purchases after November 6, 2009, the homebuyer credit can't be claimed for a home if its purchase price exceeds \$800,000. It's important to note that there is no

phaseout mechanism. A purchase price that exceeds the \$800,000 threshold by even a single dollar will cause the loss of the entire credit.

The new purchase price limitation applies whether you are buying a first-time principal residence or are a long-time homeowner purchasing a replacement principal residence.

Other homebuyer credit changes. The new law includes a number of new anti-abuse rules that make it tougher to claim the homebuyer credit. The most important of these are as follows:

- Beginning with the 2009 tax return, the homebuyer credit can't be claimed unless the taxpayer attaches to the return a properly executed copy of the settlement statement used to complete the purchase of the qualifying residence.
- For purchases after November 6, 2009, the homebuyer credit can't be claimed unless the taxpayer is at least 18 years old as of the date of purchase. A married person is treated as meeting this requirement if he or his spouse is at least 18 years old.
- For purchases after November 6, 2009, the homebuyer credit can't be claimed by a taxpayer who can be claimed as a dependent by another taxpayer for the tax year of purchase. It also can't be claimed for a home bought from a person related to the buyer's spouse.
- The new law makes it easier for the IRS to go after questionable homebuyer credit claims without initiating a full-scale audit.

What hasn't changed. The tax law still gives you the extraordinary opportunity to get your hands on homebuyer credit cash without waiting to file your tax return for the year in which you buy the qualifying principal residence. Thus, if you buy a qualifying principal residence in 2009 you can treat the purchase as having taken place on December 31, 2008, file an amended return for 2008 claiming the credit for that year, and get your homebuyer credit cash quickly via a tax refund. Similarly, you can treat a qualifying principal residence bought in 2010 (before the new deadlines) as having taken place on December 31, 2009, and file an original or amended return for 2009 claiming the credit for that year.

Tax relief for military and other service members in the Worker, Homeownership, and Business Assistance Act of 2009

Waiver of Homebuyer Credit Recapture. The first-time homebuyer tax credit must be recaptured (i.e., paid back to the government) if the home is sold (or ceases to be used as a principal residence) within three years of the purchase. A more extensive recapture rule applies to qualifying home purchases in 2008. The 2009 Assistance Act provides that the first-time homebuyer credit does not need to be paid back if, after December 31, 2008, the home is sold (or ceases to be used as a principal residence) by a member of the uniformed services, a member of the U.S. Foreign Service, or an employee of the intelligence community, in connection with a government order received by the individual or the individual's spouse for qualified official extended duty.

Extension of Homebuyer Credit for Service Members Overseas. The first-time homebuyer tax credit was scheduled to expire on November 30, 2009, but the 2009 Assistance Act extends the credit to purchases before May 1, 2010 (July 1, 2010, for taxpayers with binding contracts). For service members serving overseas, the extension is one year longer. The 2009 Assistance Act provides that for service members serving outside the United States for at least 90 days during the period beginning after December 31, 2008, and ending before May 1, 2010, the purchase must occur before May 1, 2011 (July 1, 2011, for taxpayers with binding contracts). The idea behind this additional extension is to allow service members stationed overseas to take advantage of the credit when they return.

Exclusion from Gross Income of Qualified Military Base Realignment and Closure Fringe. The Homeowner's Assistance Program (HAP) has long provided payments to certain Defense Department employees and members of the Armed Forces to offset the adverse effects on housing values that result from a military base realignment or closure. These payments are excluded from the recipient's gross income and are not considered wages for FICA tax purposes (including Medicare). The stimulus legislation enacted earlier this year (i.e., the American Recovery and Reinvestment Act of 2009 (ARRA)) expanded HAP to cover, among other things, individuals whose property values were affected by the current real estate slowdown, including wounded Armed Forces members and civilian Department of Defense and Coast Guard employees, and Armed Forces members permanently reassigned from an area at or near a military installation. The new law expands the exclusion from income to cover HAP payments authorized under ARRA, effective for payments made after Feb. 17, 2009 (ARRA's enactment date).

Source: RIA Newsstand 3/19/2010