



March 1, 2010

Dear Client:

While you may be concerned about your 2009 tax return, right now is a good time to start thinking about 2010. Beginning in 2010, new tax provisions have been enacted, some have been extended that were set to expire, while others have disappeared. This letter serves as an outline of the major tax law changes you should be aware of to minimize taxes.

Please note that some of the changes below could be altered again by Congress this year.

New for 2010

- *No estate tax:* For decedents dying after 2009, the estate tax is repealed. With this repeal, the stepped-up basis at-death transfer rule is also eliminated. However, this rule is alleviated somewhat with special elective step-up rules.
- *Roth IRA conversions:* Regardless of income, taxpayers can convert traditional IRA accounts to Roth IRA accounts. Previously, taxpayers with modified adjusted gross income over \$100,000 could not make the conversion. Also, married persons filing separate returns are now eligible to make the conversion. Note that the converted amounts are includible in income, however, for conversions taking place in 2010, a taxpayer can elect to ratably include the amount over two years in 2011 and 2012.
- *Recapture of first-time homebuyer credit:* For first-time homebuyers who purchased a principal residence before Jan. 1, 2009, and took the then-\$7,500 credit, 2010 marks the first year of recapture, in what amounts to a \$500 repayment.
- *Phaseouts of itemized deductions and personal exemptions:* The overall limitation on itemized deductions for taxpayers with AGIs above a threshold amount does not apply. The phaseout for personal exemptions for higher income taxpayers also does not apply.

Expiring in 2010

- *Education credit:* The American Opportunity Credit replaced the Hope Education Credit for 2009 and 2010 only. The benefits of the new credit are: (1) required course materials, such as books qualify; (2) the credit is increased to up to \$2,500; (3) income level phaseouts are higher; (4) forty percent of the credit is refundable.
- *Nonbusiness energy property credit:* A 30% credit (up to \$1,500, less if any credit was taken in 2009) is available if you make certain energy efficient improvements to your home. Such improvements include high-efficiency heating and air conditioning systems, water heaters, windows, skylights, doors, insulation and roofs. The improvements must be made to an existing principal residence. A manufacturer's certificate must accompany the qualifying property.
- *Residential energy efficient property credit:* Taxpayers receive a 30% credit for installing solar electric systems, solar hot water heaters, geothermal heat pumps, wind turbines, and fuel cell property. The property can be purchased for both an existing principal residence and for new construction. A manufacturer's certificate must accompany the qualifying property.

- *First-time homebuyer credit:* First-time homebuyers (including long-term residents) are eligible for the tax credit if the purchase contract is entered into before May 1, 2010, and closing takes place before July 1, 2010. These dates are extended by one year for members of the military on extended active duty.
- *Lower capital gains rates:* The 15% capital gains rate (0% for taxpayers below the 15% tax bracket) will increase to 20% in 2011. Qualifying dividends taxed at reduced capital gains rates will be taxed at ordinary income rates beginning in 2011.
- *Increased first-year asset expensing:* For 2010, the amount eligible for asset expensing is \$134,000. Beginning in 2011, the amount is reduced to \$25,000 (indexed for inflation).
- *Expanded NOL carrybacks:* Businesses may carryback NOLs for up to five years for losses incurred in taxable years beginning after Dec. 31, 2007, and beginning before Jan. 1, 2010, but can only elect for one taxable year, not two. Businesses are able to offset 50% of the available income from the fifth taxable year preceding the loss, and 100% of all income in the remaining four carryback years.
- *Refundable portion of child tax credit:* The earned income formula for the determination of the refundable child credit applies to 15% of the taxpayer's earned income in excess of \$3,000. This allows more earned income to qualify in order to determine how much of the credit is refundable. Beginning in 2011, the amount will be considerably higher.
- *Higher earned income tax credit:* The temporary increase in the EITC percentage from 40% to 45% for families with three or more qualifying children ends in 2010. Additionally, the marriage penalty relief, through an increased threshold phaseout amount for married couples filing joint returns, expires.
- *Lower income tax rates:* Legislation in 2001, reduced the tax rates on ordinary income through 2010. The current rates of 10%, 15%, 25%, 28%, 33%, and 35% could all change beginning in 2011.
- *Child tax credit dollar amount:* The \$1,000 per qualifying child credit amount is set to be reduced to \$500 beginning in 2011.

Expired in 2009

- *Sales taxes paid on new vehicle purchases:* If you purchased a new car after Feb. 17, 2009, and before Jan. 1, 2010, the sales tax paid on up to \$49,500 of the purchase price was deductible. The deduction phases out for higher income taxpayers.
- *Increased AMT exemption amounts:* For 2009, the AMT exemption amounts were \$70,950 for married filing jointly, \$35,475 for married filing separately, and \$46,700 for singles and heads of household. For 2010, the exemption amounts are significantly lower (unless Congress acts to adjust): \$45,000 for married filing jointly, \$22,500 for married filing separately, and \$33,750 for singles and heads of households.
- *Waiver of required minimum distributions (RMDs) for IRAs and other retirement savings plans:* When a taxpayer turns 70½, he or she is required to take a distribution from his or her retirement account. However, for 2009, that rule was eliminated. Beginning in 2010, the RMD rule returns.
- *Unemployment compensation:* 2009 marked the only year that the first \$2,400 of unemployment compensation received was not includible in income.
- *Tuition deduction:* An above the line deduction for qualified tuition and related expenses, up to \$4,000, depending on income.
- *Research credit:* The tax credit for research and experimentation expenses.
- *Bonus depreciation:* The additional first-year depreciation for 50% of basis of qualified property.
- *Deduction for state sales taxes:* The election to deduct as an itemized deduction state and local sales taxes instead of state and local income taxes.
- *Charitable contributions from IRA accounts:* The ability to distribute up to \$100,000 tax free to charity from an IRA maintained for an individual whose has reached age 70½.
- *Educator expense deduction:* The \$250 above the line deduction for qualifying educators for expenses paid for books and supplies used in the classroom.
- *Increased first-year asset expensing:* For 2009, the amount eligible for asset expensing was \$250,000.
- *D.C. first-time homebuyer credit:* Purchases made before Jan. 1, 2010, qualify for the \$5,000 D.C. first-time homebuyer credit.
- *Nonrefundable personal credits offsetting AMT:* Only through 2009 could nonrefundable personal credits offset a taxpayer's alternative minimum tax. However, this rule does not apply to the adoption credit, the child tax credit, the saver's credit, the residential energy efficient property credit, and the American Opportunity credit, among others.

While there are other minor changes that have taken place from 2009 to 2010, the above list represents tax changes that most likely will impact your 2010 taxes. You also should be aware that Congress is in the middle of deliberations that could lead to the extension of some of the above-mentioned expired or expiring tax

provisions. If that happens, we will notify you of those changes.

Please do not hesitate to contact Kurt A. Alter or Karin Vickers if you have any concerns about how any of the tax law changes would affect you.

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