

CITY SECURITIES WEALTH ADVISORS

Your Life. Your Goals. Your Advisors.

March 10, 2009

Dear clients and friends,

I am writing to brief you on several recent tax changes and assure you that we will be continuing to monitor the many proposed changes to tax law. The American Recovery and Reinvestment Act of 2009 (commonly referred to as the Recovery Act), which was signed into law on Feb. 17, 2009, makes a number of tax changes for individuals. However, most of them are temporary in nature; that means, unless extended by future legislation, they apply for 2009 only, or in a few cases for 2009 and 2010. Here's a review of the more widely applicable provisions that could have an impact on you and your family.

New Making Work Pay Credit. Individuals who work generally get a credit of up to \$400 (\$800 for joint filers). The credit is refundable, meaning you get it even if you owe no income tax. This change applies for 2009 and 2010. The credit is the lesser of 6.2% of your earned income or \$400 (\$800 on a joint return). The credit is phased out for joint filers with modified adjusted gross income between \$150,000 and \$190,000 and other taxpayers with modified AGI between \$75,000 and \$95,000.

You won't be getting a separate check from the IRS, as you did with last year's stimulus payment. Rather, your employer will automatically adjust your withholding so that you will get a little more money in each paycheck. If you have multiple jobs, you may have to adjust your withholding so that too much is not taken out. If you are self-employed, you can effectively receive the credit in advance by reducing your estimated tax payments.

One-time \$250 payment or credit for others. The Recovery Act provides a one-time payment of \$250 in 2009 to retirees, disabled individuals and Social Security Income recipients. It also provides a one-time refundable tax credit of \$250 in 2009 to certain government retirees who are not eligible for Social Security benefits. However, the Making Work Pay Credit is reduced by any \$250 payment or credit received.

New sales tax deduction for vehicle purchases. For 2009, there is a new deduction for state and local sales and excise taxes paid on new cars, light trucks, motor homes and motorcycles purchased after Feb. 16, 2009 and before Jan. 1, 2010. The deduction is generally available regardless of whether you itemize deductions on Schedule A or claim the standard deduction.

The deduction is limited to the tax on up to \$49,500 of the purchase price of an eligible motor vehicle.

The deduction is phased out for joint filers with modified adjusted gross income between \$250,000 and \$260,000 and other taxpayers with modified AGI between \$125,000 and \$135,000.

If you itemize and choose the option to deduct state sales taxes in lieu of state income taxes, you don't get the new deduction. This prevents you from getting a double deduction for the sales taxes on the vehicle but it also involves some tricky planning considerations because different rules apply to the

optional deduction and the new deduction. For example, the new deduction is allowed against the alternative minimum tax, but the optional deduction is not. Additionally, the optional deduction is subject to a limitation that caps the deduction for sales tax on a motor vehicle to the general sales tax rate.

Improved first-time homebuyer credit. Last year's Housing Act included a refundable tax credit for first-time homebuyers equal to the lesser of 10% of the purchase price or \$7,500 for qualifying purchases after Apr. 1, 2008 and before July 1, 2009. The credit is essentially an interest-free loan because it has to be paid back to the government over 15 years.

The Recovery Act has improved the credit for 2009 purchases by (1) eliminating the requirement to pay it back (subject to exceptions), (2) increasing the maximum credit to \$8,000, and (3) making it available for purchases through November 2009.

You can treat a 2009 purchase as having been made on Dec. 31, 2008 and thus get an immediate refund when you file your 2008 taxes by the Apr. 15, 2009 filing deadline. Even if you have already filed your 2008 taxes, you can file an amended 2008 return to get the credit for a 2009 purchase.

You are considered a first-time homebuyer if you (or your spouse, if married) had no present ownership interest in a principal residence in the U.S. during the 3 year period before the purchase of the home to which the credit applies.

The first-time homebuyer credit, whether claimed in 2008 or 2009, phases out for individual taxpayers with modified adjusted gross income between \$75,000 and \$95,000 (\$150,000–\$170,000 for joint filers).

AMT relief. In general terms, to find out if you owe alternative minimum tax (AMT), you start with regular taxable income, modify it with various adjustments and preferences (such as addbacks for property and income tax deductions and dependency exemptions), and then subtract an exemption amount (which phases out at higher levels of income). The result is multiplied by an AMT tax rate of 26% or 28% to arrive at the tentative minimum tax. You pay the AMT only if the tentative minimum tax exceeds your regular tax bill. Although it was originally enacted to make sure that wealthy individuals did not escape paying taxes, the AMT has ensnared many middle-income taxpayers as well. Exemption amounts were scheduled to drop and fewer tax credits were to be available to offset AMT for 2009. The Recovery Act provides AMT relief for 2009 by (1) increasing the exemption amounts above last year's levels and (2) allowing nonrefundable credits to offset AMT as well as regular tax.

College tax breaks. The Recovery Act expands tax breaks for individuals seeking a college education. For 2009 and 2010, it gives taxpayers a new "American Opportunity" tax credit of up to \$2,500 of the cost of tuition and related expenses paid during the tax year. You receive a tax credit based on 100% of the first \$2,000 of tuition and related expenses (including books) paid during the tax year and 25% of the next \$2,000 of tuition and related expenses paid during the tax year. The credit is available for the first four years of post-secondary education in a degree or certificate program and 40% of the credit is refundable. The credit is phased out for taxpayers with modified AGI between \$80,000 and \$90,000 (\$160,000 and \$180,000 for joint filers).

Section 529 Education Plans are tax-advantaged savings plans that can be used to pay qualified education expenses, including tuition, room and board, mandatory fees and books. Under the Recovery

Act, for 2009 and 2010, qualified education expenses under these plans include computer technology and equipment, as well as Internet access and related services.

Tax break for the unemployed. Unemployment compensation benefits ordinarily are fully taxable. However, under the Recovery Act, an individual does not have to pay tax on up to \$2,400 in unemployment benefits received in 2009.

Limited subsidy for COBRA continuation coverage of unemployed workers. The Recovery Act provides a 65% subsidy for COBRA continuation premiums for up to 9 months for workers who have been involuntarily terminated, and for their families. This subsidy also applies to health care continuation coverage if required by states for small employers. To qualify for premium assistance, a worker must be involuntarily terminated between Sept. 1, 2008 and Dec. 31, 2009. Workers who were involuntarily terminated between Sept. 1, 2008 and Feb. 17, 2009 but failed to initially elect COBRA because it was unaffordable must be given an additional 60 days to elect COBRA and receive the subsidy. The subsidy is not taxable when received, but higher income recipients—those with modified adjusted gross income above \$125,000 (\$250,000 for joint filers)—will have to pay back part or all of it at tax return time.

Refundable child credit expanded. A taxpayer receives a \$1,000 tax credit for each qualifying child under the age of 17. Before the Recovery Act, this credit was refundable only to a limited extent. The Recovery Act makes the child credit refundable to a much greater extent for 2009 and 2010.

Bigger earned income tax credit (EITC). The Recovery Act makes various changes to the earned income tax credit for 2009 and 2010. These changes will result in a bigger EITC for some taxpayers. For example, in 2009, taxpayers with three or more qualifying children may claim a credit of 45% of earnings up to \$12,570, resulting in a maximum credit of \$5,656.50.

Increased transit and vanpool transportation fringe benefits. For months beginning on or after Mar. 1, 2009 and before Jan. 1, 2011 the Recovery Act increases the monthly exclusion for employer-provided transit and vanpool benefits from \$120 to \$230. This figure is adjusted for inflation each year and could go up in 2010.

Improved energy tax breaks. The Recovery Act includes a number of provisions that are designed to promote the creation and use of alternative forms of energy including these new or improved energy tax breaks for individuals:

The Recovery Act extends the tax credit for energy-efficient improvements to existing homes through 2010 and modifies it in various ways so that a larger credit is possible after 2008.

Under pre-Recovery Act law, individuals could claim a 30% tax credit for qualified solar water heating property (capped at \$2,000), qualified small wind energy property (capped at \$500 per kilowatt of capacity, up to \$4,000), and qualified geothermal heat pumps (capped at \$2,000). For tax years beginning after 2008, the Recovery Act removes these individual dollar caps. As a result, each of these types of improvements is eligible for an uncapped 30% credit.

The Recovery Act modifies and increases the existing new qualified plug-in electric drive vehicle credit.

For vehicles bought after Feb. 17, 2009 and before Jan. 1, 2012, the Recovery Act creates a new 10% nonrefundable personal credit for electric drive low-speed vehicles, motorcycles, and three-wheeled vehicles.

For property placed in service after Feb. 17, 2009 and before Jan. 1, 2012, the Recovery Act creates a new 10% credit, up to \$4,000, for the cost of converting any motor vehicle into a qualified plug-in electric drive motor vehicle.

While not all of these changes to tax law will directly affect you, we are continuing to monitor the many changes we anticipate will occur with the new presidential administration. If you have any questions about these changes, please do not hesitate to call me. Also, if you need a referral to a qualified tax preparer, we will be happy to provide you with a name and contact information for one of the CPAs we frequently work with who have served our clients well.

Best regards,

A handwritten signature in black ink that reads "Ryan". The signature is fluid and cursive, with a prominent initial "R".

Ryan Veldhuizen
Financial Planning Associate

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Vice President