

Dear Client:

2009 has been a year of change for our economy and tax laws. Year-end tax planning has become more urgent in 2009 because of several significant tax law changes, including those that have taken place to stimulate the economy and those that will pay for the recovery.

Year-end planning is well worth considering to strategically lower your tax bill. Managing what income you recognize or defer can also pay dividends as you balance your tax rates between 2009 and 2010, and beyond, with tax reform on the horizon.

On November 6, 2009, President Obama signed the *Worker, Homeownership, and Business Assistance Act of 2009*, which extended the first-time homebuyer credit, creating a new tax credit for non first-time buyers and expanding the five-year net operating loss (NOL) carry back through 2010.

The first-time homebuyer credit, originally set to expire in November 2009, has been extended for purchases through April 30, 2010. Many homebuyers who are not first-timers may now be eligible for a tax credit up to \$6,500, while first-time homebuyers qualify for a maximum \$8,000 credit. Effective for purchases after November 6, 2009, individuals who are “long-time residents of the same principal residence” may be eligible for a modified credit of \$6,500 if they have owned and used the same residence as their principal residence for any five consecutive year period during the previous eight-year period ending with the date on which the new residence is purchased.

The new law also expanded the election to carry back net operating losses (NOL) to all U.S. businesses up to five years but with a 50 percent income limit on NOL offsets in the fifth year. Any remaining NOL can fully offset taxable income in the remaining four carry back years.

Many of the other tax breaks in recent stimulus tax bills will expire at the end of 2009. At this point, there is no guarantee that Congress will extend any of them for 2010:

- **For individuals**, these expiring tax breaks include the itemized state and local sales tax deduction, the \$4,000 higher education tuition deduction, and the additional standard deduction for real property taxes
- **For businesses**, bonus depreciation and enhanced “section 179 expensing,” both designed to

temporarily encourage businesses to make capital investments, will most likely expire at the end of 2009

Accelerating qualifying expenses into 2009 and taking advantage of the incentives above may make a significant difference in your overall tax bill, rather than incurring them early in 2010.

What is on the horizon for 2010 and beyond is also critical for effective year-end tax planning this year.

- In 2010, the opportunity to convert any IRA into a Roth IRA without the long-time \$100,000 income restriction has many individuals already saving. Some individuals may be better off, however, converting Roth IRAs before the end of 2009 because the value of their accounts and the consequential income that must be recognized on conversion are at historic lows.
- Effective for 2011, the Obama administration has proposed to increase the income and capital gains tax rates on single individuals with incomes of more than \$200,000 and married couples with incomes exceeding \$250,000. For these taxpayers, including unincorporated small businesses with owners that recognize income on their individual returns, following the traditional year-end planning maxim of deferring income into next year may not work well this year. Deferring too much income into 2010 could result in overloading income next year, especially if you are looking to accelerate income into 2010 to escape the expected higher rates in 2011.

As this challenging year draws to a close, matching losses with gains is not necessarily a simple task in the tax law. Different rules apply to different losses. Losses can be ordinary losses, passive losses, at-risk losses, capital losses, hobby losses, casualty losses, gambling losses, or Code Sec. 1231 losses. Knowing the differences and acting before year-end to match them correctly can bring significant tax savings.

Planning for deductions and credits at year-end can also be complex but can be equally as rewarding. Timing and qualification rules create traps and opportunities:

continued

Year-End Planning

- Pre-paying certain expenses, such as real estate taxes or mortgage interest, do not necessarily translate into a larger deduction this year.
- Paying a spring college tuition bill in late December instead of early January, however, can impact whether you maximize the benefit of the new American Opportunity Tax Credit for both 2009 and 2010.
- Year-end charitable giving generally has always been a smart way to reduce current year taxes, but strict timing rules and revised substantiation requirements for property donations cannot be overlooked.
- Homeowners should also take advantage of the new residential energy property credit, which has a unique set of rules on qualifying expenses and deadlines for installations.

Another important point to consider is planning your estate. It's an important part of ensuring the financial security of your loved ones. Annual gifting is a common tool used in estate planning. While large gifts are subject to gift taxation, you can give away up to \$13,000 in 2009 per recipient per year free of gift tax. These gifts also do not reduce the amount that you can pass free of gift tax (\$1 million lifetime exclusion, adjusted for inflation each year; \$2 million if gifts are "split" with a spouse).

Another potentially valuable technique may be to make a charitable contribution from your IRA. Individuals age 70 1/2 and older may distribute up to \$100,000 from their IRAs tax-free to charitable organizations during the 2009 tax year. Qualified charitable distributions must be made directly by the IRA trustee to eligible organizations, and they are not deductible as a charitable contribution nor are they included in income.

Another way to further the financial security of others without incurring gift tax is by payment of medical and educational expenses. You can pay an unlimited amount for these expenses tax free as long as the payments are made directly to the medical service provider or educational institution. The person you benefit does not need to qualify as a dependent for tax purposes. Any medical expenses, however, must not be reimbursed by insurance, to either you or to the beneficiary.

Especially during 2009, TravisWolff considers a year-end tax checkup an essential service for our clients. If you would like more information on any of the planning strategies described in this letter, or if you would like to explore how year-end tax planning can be customized to your individual circumstances, please give us a call.

Contact

For more information or to discuss year-end planning, please contact your TravisWolff partner or manager.



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