


BEST TAX IDEAS

Compiled from speakers at the AICPA Tax Strategies for the High-Income Individual Conference


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Take advantage of what you can do right now

- Elections are approaching
- New President in 2009 and New Congress
- Don't know what will happen Post-election
- Take advantage of what is in the law now
 - Example – Recognizing capital gains now gets low capital gain rate of maximum 15% - maybe 0% if eligible

Small Business and Work Opportunity Tax Act of 2007

Enacted May 25, 2007

● Small Business Tax Relief Provisions

- Work opportunity tax credits extended through September 30, 2011
- Work opportunity credits and tip credits may offset AMT for years beginning after December 31, 2006



Take advantage of the Work Opportunity credit

- Must file within 21 days of hiring or credit is lost
- Employers should keep filing for jobs credit certification
- Allowed to offset AMT for years beginning after 12/31/06

Small Business and Work Opportunity Tax Act of 2007 con't

- Election available to married couple operating unincorporated business and filing joint return to elect not to file a partnership return beginning after December 31, 2006 (does not apply to state entities such as LLCs)

Small Business and Work Opportunity Tax Act of 2007 con't



● Revenue Provisions

- Unearned income of children under age 19 (under 24 if full-time student) subject to kiddie tax beginning in 2008
- Tax return preparer penalties expanded to all types of tax returns
- New penalty for filing erroneous refund claims for which there is no reasonable basis enacted



Use strategies to avoid the Kiddie Tax

- No return if child's income < \$850 (\$400 if self-employed)
- Child < 19/24 can receive \$1,700 of investment income in addition to compensation income before paying tax at parents' tax rate
- When child's investment income reaches \$1,700, consider investments that do not increase child's taxable income. Examples include:
 - Tax-exempt municipal bonds,
 - Growth stocks, mutual funds, and exchange-traded funds which pay no current dividends,
 - Real property which appreciates in value, and
 - Tax-deferred U.S. Savings bonds
- Consider splitting the child's income with a trust

Energy Independence and Security Act of 2007

Enacted December 19, 2007

Tax Provisions

- FUTA surcharge of .2% (for total of 6.2%) extended by one year through 12/31/08
- Large oil companies' geological and geophysical expenditures required to be amortized over seven years rather than five years effective for amounts paid or incurred after 12/19/07

Tax Increase Prevention Act of 2007

Enacted December 26, 2007-Major Provisions

- AMT "patch" for 2007-exemptions
 - \$44,350 for single and head of households,
 - \$66,250 for married filing jointly, and
 - \$33,125 for married filing separately
- Credits allowed to offset AMT for 2007
 - Dependent care credit,
 - HOPE and Lifetime Learning credits, and
 - District of Columbia first-time homebuyer's credit

Mortgage Forgiveness Debt Relief Act of 2008

Enacted December 20, 2007

- Foreclosure Relief
- Discharges of up to \$2 million of indebtedness secured by principal residence excluded from income beginning 1/1/07 and ending 12/31/09
- Deduction for mortgage insurance premiums extended through 12/31/10

Mortgage Forgiveness Debt Relief Act of 2008 con't.

- Period of time for which surviving spouse may use joint-filer's \$500,000 home sale gain exclusion extended to two years after spouse's date of death effective 1/1/08

Mortgage Forgiveness Debt Relief Act of 2008 con't.

- **Other Provisions**

- Failure to file penalty for partnerships increased to \$85 per partner per month, up to 12 months (\$85 was increased to \$86 for returns required to be filed for taxable years beginning in 2008)
- New failure to file penalty for S corporations enacted at \$85 per S corporation shareholder per month, up to 12 months

Economic Stimulus Act of 2008

Enacted February 13, 2008

- **Tax Credit for Middle-Low Income People**

- One-year tax “rebate” credit allowed with advance payments to be sent to those eligible

Economic Stimulus Act of 2008 con't.

- **Incentives for Businesses**

- Section 179 increased to \$250,000 for 2008; phase-out level increased to \$800,000
- 50% bonus depreciation allowed for certain property during 2008 including most types of new property and qualified leasehold improvements other than buildings
- 2008 bonus depreciation of up to \$8,000 allowed for luxury automobiles (thus 1st year depreciation \$10,960)



Be alert if you have fiscal year flow through entities

- \$250,000 limit is for years beginning in 2008
- \$250,000 limit for indiv.'s year beg. in 2008
- If an individual, generally calendar year, gets an allocation from a fiscal year flow through entity for years beg. in 2008 but ending in 2009, the individual will be limited based on to 2009 limit (\$125,000)
- Bottom line – fiscal year LLC or S Corp cannot really utilize the expanded \$250,000 if it has a majority partner or S/H who would receive the allocation

Heroes Earnings Assistance and Relief Act of 2008

Enacted June 17, 2008

- Military Pay and Retire. Savings Provisions
- Several military pay/retirement savings provisions made permanent
- 20% credit for differential wage payments up to \$20,000 for small employers

Heroes Earnings Assistance and Relief Act of 2008 con't.

- Other Provisions
- 5-year ownership & use period for excluding gain on sale of home suspended while homeowner serves in Peace Corps outside US
- Persons who relinquish their US citizenship subject to new expatriation rules and generally treated as if they sold all property on the day before expatriation– generally limited to individuals with net worth of at least \$2 million

Heartland, Habitat, Harvest, and Horticulture Act of 2008

Enacted May 22, 2008 by override of veto

- **Farm Income and Losses**
- Deductible farm losses limited to > \$300,000 (\$150,000 for MFS) or total net farm income for previous 5 years if receiving Commodity Credit Corporation loans or agricultural program pymts
- CRP payments exempt from SE tax and Social Security benefit calculations for retired or disabled taxpayers

Heartland, Habitat, Harvest, and Horticulture Act of 2008 con't.

- Racehorse MACRS recovery period shortened to 3 years for race horses placed in service during 2009 through 2013
- **Timber Provisions**
- Capital gains rate for C corporations with qualified timber gains temporarily reduced to 15%

Heartland, Habitat, Harvest, and Horticulture Act of 2008 con't

- **Other Provisions**
- 2007 Greensburg, Kansas disaster area allowed special tax relief
- Special rules for charitable contrib. of qualified conservation property allowing charitable contrib. deductions of up to 100% of contribution base for contributions of qualified conservation property extended for two years through 2009

Housing and Economic Recovery Act of 2008

Enacted July 30, 2008

- **Single Family Housing**

- 1st-time home buyer tax credit (better called an interest-free loan) of 10% of purchase price up to \$7,500 for lower-income individuals which generally must be repaid over 15 years starting two years after year in which residence is purchased effective for homes purchased on or after April 9, 2008 and before July 1, 2009

Housing and Economic Recovery Act of 2008 con't.

- 2008 Real property tax deduction allowed for non-itemizers up to \$500 (\$1,000 if Joint)
- Residence used for rental or second home after 2008 not fully eligible for home-sale exclusion based on ratio of time after 2008 when home was used for other than principal residence to total time seller owned home



Act quickly to convert 2nd home into main home

- Housing and Economic Recovery Act restricts tax break
 - For homes converted after 2008, some of the gain will be ineligible for the home-sale exclusion
 - Portion of profit taxed is ratio
 - Time after 2008 home was used as non-personal (second home or rental) - to
 - Total time seller owned the house

Housing and Economic Recovery Act of 2008 con't.

- **Other Provisions**

- Corporations allowed to forego 50% bonus depr. - use accumulated AMT and R&D credits (treated as refundable) limited to 20% of difference between depr. allowed if bonus and depr. allowed if no bonus
- Tax-free bonds used for low-income housing and mortgages for veterans/low-income people exempt from AMT for bonds issued after 7/30/08



Always review repairs vs. capitalized expenses (Connors #1; Page 4-4)

- Look at economic useful life of the total property (not depreciable life)
- Dollar amount is not the controlling factor
- New Proposed Regs. came out in March
 - Was building already in service
 - Conditions were not present when purchased
 - Did not substantially alter the building
 - Did not materially increase value



Take full advantage of §199 (Turnbull #1; Page 4-23)

- Covers more than taxpayers who manufacture tangible personal property
- QUESTION - Is my taxpayer producing something?
- Tier 1 issue for audit
 - It will get questioned if you are audited



Know about Rev. Rul. 2008-22 that allows grantor power to substitute assets in a trust and not trigger inclusion in the estate (Gallo-not listed)

- Unnecessary ruling-but focuses our attention on grantor trusts
- Substitution power is not a power under §2036 that would trigger inclusion in the estate



Rev. Rul. 2008-22 con't.

- Requirements
 - Power of substitution must be exercised in a non-fiduciary capacity (Grantor should not be trustee)
 - Trustee must have fiduciary obligation to make sure substitution is of equivalent value (don't have provision waiving liability of trustee in regards to transactions with grantor)
 - Substitution power cannot be used to shift benefits among beneficiaries (Trustee needs fiduciary duty to the beneficiaries)



Review beneficiary designations often (Finn #1; page 4-6)

- Insurance policies
- Qualified plans
- IRAs
- Coordinate with entire estate distribution plan to provide maximum estate and income tax deferral



Do cost segregation studies and deduct catch-up depreciation (Connors #2; Page 4-4)

- Hot area for many businesses
- Cost segregation-might be able to segregate up to 25% of real estate projects into 15-, 7-, or 5-year assets



Do cost segregation studies and deduct catch-up depreciation (Connors #2; Page 4-4) CONTINUED

- If items previously were misclassified (useful life), catch-up missed depreciation
- Use Form 3115 Application for Change in Accounting Method
 - Negative 481 adjustment all in one year
- No IRS user fee



Exporters consider establishing IC-DISC (Turnbull #3; Page 4-23)

- Look for clients doing exports owned primarily by individuals (P/S or S Corp)
- Dividends paid by IC-DISC may qualify for 15% rate
 - Allows individual taxpayers to convert income taxed at otherwise higher rate for ordinary income to the 15% rate



Exporters consider establishing IC-DISC (Turnbull #3; Page 4-23) con't.

- **Set up C corp and make DISC election**
 - Watch for states that allow DISC rules
- **Pay a commission from exporting company to DISC & distribute a dividend– greater of**
 - 4% of qualified foreign export receipts, or
 - 50% of combined taxable income



Use of transactions with ILITs (Gallo-unlisted)

- **Don't overlook combining grantor trusts with insurance trusts**
- **Sales of residence to ILIT and residence gets rented back**
 - Can use a QPRT
 - If ILIT is grantor trust, ILIT owns interest in family residence



Use of transactions with ILITs (Gallo-unlisted) con't.

- Grantor pays reasonable rent for use of residence
- Rent is not taxable income since payment is to grantor
- Rent payment is not a gift since it is for full and adequate consideration
- Thus, a non-gift funding mechanism for payment of future life insurance premiums



Roth IRAs are the best asset to inherit (Jones #1; Page 4-8)

- **Great generation skipping candidate**
 - Provides beneficiary with tax-free rate of return over the entire life expectancy of beneficiary
 - e.g. 25 year old Beneficiary can stretch out distributions for 58 years
- **2006 began Roth 401(k)s for high income taxpayers**



When discussing the ROTH IRA conversions for 2010, remember that the tax rates are scheduled to increase in 2011

- **The 2010 conversions can either be included in income in 2010 or spread over the following 2 years**
 - Thus, will need to evaluate the impact of spreading the income over two years with the expected higher tax rates versus including the income all in 2010



If high income taxpayer has no IRAs

- **Consider making nondeductible IRA contributions that can be rolled into ROTH IRAs in 2010**
 - Tax upon conversion would probably be minimal due to short time-span
 - As long as full amount of all IRAs are converted in 2010, it avoids potential loss of records regarding nondeductible basis



Educate clients and their children on IRA benefits (Jones #2 & #4; Page 4-8)

- Traditional IRAs-income tax deferral is as powerful after death as it was during lifetime
 - Given a sufficient # of years to stretch out RMDs in the inheritor’s hands, traditional IRA can out-earn income tax that would be paid without stretch out, even for high income inheritors
- Help inheritors understand economic power of taking only RMD annually



Use passive activity “Grouping Rules” to avoid recharacterization on self-rentals (Connors #8; Page 4-5)

- If T/P owns building and rents it to another flow-thru entity the T/P owns, you can group the 2 activities
 - Allows loss on rental building to be deducted against operating business in the other entity
 - Must own same proportion of each entity (rental entity and the operating entity)



Review accounting methods for opportunities (Turnbull #5; Page 4-23)

- Cash method of accounting
 - C corp converts to S Corp
- Defer income from advance payments
- Prepaid expenses
- Obsolete inventory
- Cost segregation study



When was the last time you had an efficiency study of your life insurance? (Slavutin #1; Page 4-21)

- Many don't pay attention to life insurance policy after the purchase
 - Make sure it is still good and appropriate for the needs of the client
 - Are there better policies for the client
 - Trustees of ILITs should do the same



Make annual exclusion gifts to children and grandchildren (Christerson #4; Page 4-3)

- Remind clients how much they can get out of their estates, tax-free
- Currently \$12,000 per year (\$24,000 if spouse agrees to split the gift)



Move to a low-tax or no-tax state before receiving a large gain or making a large retirement plan withdrawal (Kreider #3; Page 4-13)

- Must be a bona fide move
- Establish residence as far in advance of the transaction as possible
- Register to vote, Change driver's license
- Establish financial connections and social connections
- Etc.



Avoid alimony recapture rules (Linton #4; Page 4-14)

- If spousal support over \$15,000 per year is paid during first three years, make sure it doesn't decrease by more than \$15,000 in any of those three years



Corporate AMT (Walloch #6; Page 4-24)

- If C Corp. is paying AMT, it may be in error
 - Less than 15,000 C Corps. Out of over 2 million are subject to AMT
 - Primarily because of small business gross receipts exemption




For self-employed person with no employees, consider solo 401(k) (Welch #5; Page 4-25)

- Max 401(k) contribution for 2008 is \$15,500
 - Add \$5,000 if age 50+
- Profit sharing contribution on top of that (max 25% of net earnings from self-employment)
- Example, someone age 50+ with \$70,000 of Sch C earnings can contribute \$33,511 into solo 401(k) – almost 50% of the Sch C amt!
 - The 401(k) portion can be a ROTH 401(k)

Solo 401(k) Plan


Earnings	70,000
Less contrib	(13,011)
Less 1/2 SE tax	(4,946)
Net earnings	52,043
Plan %	x 25%
Contribution	13,011
401(k)	15,000
Total contrib	28,011
50+ add 401(k)	5,000
Total contrib	33,011



Please, Mr. Chairman (Tune of Please Mr. Postman)

Please, Mr. Chairman, look and see
(Oh yeah)
If there's a tax break in your mark for me
Please, please Mr. Chairman ...
Why's it taking such a long time
(Oh yeah)
For me to get that goodie of mine

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Wall Street Journal-Tom Herman's column



Questions?????

THANK YOU!

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