

2009 *U.S. Master Tax Guide*®



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2009 U.S. Master Tax Guide.®

CCH Editorial Staff Publication

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Preface

Income taxation in the United States, as we know it on Form 1040, has been around for more than 90 years. From the very beginning, CCH was there and is still setting the standard after all these years. CCH is proud to serve the tax professional community with this new edition of the *U.S. Master Tax Guide*®. The 92nd Edition of this industry standard explains the maze of tax rules, restrictions, and requirements and is designed to provide fast and reliable answers to tax questions affecting individuals and businesses. In all, 29 chapters contain comprehensive, timely, and precise explanation of the ever-changing federal income tax rules for individuals, businesses, and estates and trusts.

The 2009 Edition reflects the Emergency Economic Stabilization Act of 2008 (P.L. 110-343), the Housing Assistance Tax Act of 2008 (P.L. 110-289), the Food, Conservation, and Energy Act of 2008 (P.L. 110-246), the Heroes Earnings Assistance and Relief Tax Act of 2008 (P.L. 110-245), the Economic Stimulus Act of 2008 (P.L. 110-185) and other significant developments that took place throughout the year. The Emergency Economic Stabilization Act, signed by President Bush on October 3, 2008, includes financial markets rescue provisions and tax incentives for both individuals and businesses. The Housing Assistance Act, signed on July 30, 2008, by President Bush, includes \$15.1 billion in tax incentives that are primarily targeted at home ownership and providing affordable housing. The Food, Conservation, and Energy Act became law after the House and Senate both voted on June 18, 2008, to override President Bush's veto. The bill provides significant benefits to farmers, ranchers and timber producers. On June 17, 2008, President Bush signed the Heroes Act which provides tax breaks for members of the military and their families and clarifies the tax treatment of state and local benefits provided to volunteer firefighters and emergency medical responders. The Economic Stimulus Act, signed by President Bush on February 13, 2008, includes a recovery rebate credit for individuals, increased Code Sec. 179 expensing amounts and a 50 percent bonus depreciation deduction for qualifying property.

As this edition of the *Guide* goes to press, there are legislative proposals in Congress facing uncertain futures. Bills have been introduced that cover a number of tax areas, including the estate tax, energy legislation, and technical corrections to the Pension Protection Act of 2006. However, it is unclear whether any proposals will make it through Congress and reach the President's desk by the end of the year. In an effort to keep users of the *Guide* current on events taking place after we go to press, CCH has established a website at <http://tax.cchgroup.com/mtg> for any late-breaking 2008 year-end tax legislation or for other significant developments that might affect the *Guide's* coverage.

As in previous editions, major legislative provisions are highlighted at ¶ 1 and reflected throughout the *Guide*, while important nonlegislative tax developments are conveniently highlighted at ¶ 2 and concisely explained for quick reference and understanding.

In addition, the *Guide* comes complete with many time-saving features that help users quickly and easily determine how particular tax items and situations should be treated (see the following page for a listing and description of these "Key Features"). The *Guide* also contains a handy Quick Tax Facts card that can be detached for an at-a-glance reference to key tax figures and other often-referenced amounts.

Not only does the *U.S. Master Tax Guide*® assist in the preparation of 2008 tax returns, it also serves as a reference tool for more comprehensive tax research and tax planning via extensive footnotes and other references to the Internal Revenue Code, Income Tax Regulations, and CCH's STANDARD FEDERAL TAX REPORTS® and FEDERAL ESTATE AND GIFT TAX REPORTER.

For additional analysis of new and complex tax issues, and as a way to earn valuable continuing education credits, *Top Federal Tax Issues for 2009* is provided along with the *Guide*. This course provides helpful insights for the practitioner to keep abreast of the most significant new rules and changes by explaining the most important new provisions and developments in 2008 specifically applicable to 2009 and the IRS rules and regulations that go into effect in 2009. It also examines current audit and litigation issues that have developed over the past year to create a new environment for tax strategies initiated in 2009.

We also point you to other CCH resources that complement the *Guide* and support your tax season work. *1040 Express Answers* is designed to help you and your staff prepare 1040 tax returns quickly, easily and accurately with line-by-line guidance to common tax preparation questions. *1065 Express Answers* is the ideal quick-answer tool for busy practitioners who prepare partnership returns and the partners' Schedule K-1s. The compliance-oriented *1120S Express Answers* will help you in preparing S corporation tax returns with concise and reliable answers right at your fingertips. The *1041 Express Answers* provides practical, plain-English guidance for practitioners who prepare fiduciary income tax returns. See <http://tax.cchgroup.com/ExpressAnswers> for more details.

Finally, for *Master Guide* type treatment of state tax topics, please refer to CCH's *State Tax Guidebooks* (14 states available—CA, CT, FL, IL, MD, MA, MI, NJ, NY, NC, OH, PA, TX and VA) and CCH's *State Tax Handbook* covering all 50 states and the District of Columbia.

Key Features

In addition to 29 chapters of concise tax law explanations, the *U.S. Master Tax Guide*® provides a wealth of information in the pages that lead up to Chapter 1. Some of these time-saving tools and collections of information are described below, listed by paragraph location:

OVERVIEW (§ 1-5): The Overview division contains informative features available to facilitate research and dealing with clients. Included are:

- “New Legislation,” a highlight of provisions from this year’s enacted tax legislation.
- “What to Watch on 2008 Returns,” a listing of important nonlegislative tax developments, including key inflation-adjusted amounts.
- “Where to File,” a listing of income tax return mailing addresses.
- “Government Agency and Tax/Accounting Directories,” a feature comprised of addresses and telephone numbers for numerous federal agencies and tax and accounting organizations.
- “Due Dates in 2009,” a tax calendar showing filing dates for 2008 tax returns and tax payments throughout 2008.

TAX RATES (§ 11-53): This section contains the 2008 and 2009 tax rate schedules for individuals and estates and trusts, the Tax Computation worksheet, the 2008 tax tables for individuals, the corporate tax rate schedule and related rates, and the estate and gift tax rate schedule, as well as a listing of excise and other taxes.

CHECKLISTS (§ 55-59): A collection of checklists designed to provide tax return preparers with quick answers (and references) to common questions regarding the inclusion of items in income, the deductibility of certain expenses, and the treatment of various medical expenses.

COMPUTATION OF TAXABLE INCOME (§ 61-64): Provides a summary overview of how taxable income is computed for an individual, a corporation, a partnership, and an estate or trust. References are provided to detailed explanations within the *Guide*.

SPECIAL TAX TABLES (§ 83-88C): This is a collection of often-used interest rates and percentages including:

- applicable federal rates (AFRs)
- adjusted applicable federal rates
- federal long-term tax-exempt rates
- low-income housing credit percentages
- earned income credit amounts

Also presented are the average itemized deductions for 2006 (the latest year of available figures), broken down by AGI ranges, as well as the AGI thresholds for a number of tax items subject to phaseout restrictions in 2008 and outlines of state conformity with bonus depreciation and the domestic production activities (manufacturer’s) deduction.

ADDITIONAL FORMATS: To provide flexibility for users, the *Guide* is available in a loose-leaf edition with quarterly updates, a hardbound edition, and a CD-ROM edition that may be purchased with or without the softbound print edition. The *Guide* is also part of CCH’s Federal Tax Guide Library, an electronic tax research library available on the Internet or monthly CDs that combines the quick-reference ease and reliability of the *Guide* with current primary sources including the Internal Revenue Code, Income Tax Regulations, cases, IRS rulings and more.

USER COMMUNITY: CCH has established a website at <http://tax.cchgroup.com/mtg> for users of the *Guide* to visit periodically in order to stay current with significant post-publication developments.

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Filing 2008 Returns

OVERVIEW

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¶ 1 New Legislation

2008 Legislation. *Economic rescue bill.* On October 3, 2008, President Bush signed a historic financial markets rescue bill that includes over 100 tax provisions and \$150 billion in separate tax breaks. The Emergency Economic Stabilization Act of 2008 (P.L. 110-343) cleared the Senate on October 1 by a 74-25 vote, followed by a 263-171 vote in the House on October 3. The measure includes tax incentives for both individuals and businesses, as well as \$44 billion in revenue offsets.

The following provisions are included in the Emergency Economic Stabilization Act:

(1) The alternative minimum tax (AMT) exemption amount for individuals is increased for tax years beginning in 2008, to \$69,950 for married individuals filing a joint return and surviving spouses; \$46,200 for unmarried individuals; and \$34,975 for married individuals filing separate returns (see ¶ 1405).

(2) For tax years beginning in 2008, the nonrefundable personal tax credits are allowed to the full extent of the taxpayer's regular tax and AMT liability (see ¶ 1415).

(3) Homeowners may claim an additional standard deduction for real property taxes, up to \$500 (\$1,000 for joint returns) for any tax year beginning in 2008 or 2009 (see ¶ 1002).

(4) The election to deduct state and local general sales taxes in lieu of state and local income taxes is extended to apply to tax years beginning before January 1, 2010 (see ¶ 1021).

(5) The deduction for qualified tuition and related expenses is extended for two years, through December 31, 2009 (see ¶ 1082).

(6) The deduction for eligible educator expenses, allowing eligible educators an above-the-line deduction of up to \$250 for educational expenses, has been extended to apply to tax years beginning in 2008 and 2009 (see ¶ 1084).

(7) For the 2008 tax year, if the total amount of a taxpayer's allowable child tax credit exceeds the taxpayer's total tax liability (regular and alternative minimum), the taxpayer is eligible for a refundable child credit equal to 15 percent of the taxpayer's earned income in excess of \$8,500, up to the per child credit amount (see ¶ 1302).

(8) For 2009, the definition of a "qualifying child" is modified with respect to age and joint returns, the tiebreaker rules are clarified, and the child tax credit is tied to the child's dependency exemption (see ¶ 137A).

(9) The 15-year MACRS recovery period for qualified leasehold improvement property is extended to apply to property placed in service in 2008 and 2009 (see ¶ 1240).

(10) A credit is available for tax years beginning after December 31, 2008, for new qualified plug-in electric drive motor vehicles. The amount of the credit is

\$2,500, plus \$417 for each kilowatt hour of traction battery capacity in excess of four kilowatt hours (see ¶ 1318).

(11) Personal casualty losses attributable to a federally declared disaster occurring in 2008 and 2009 are deductible without regard to whether the losses exceed 10 percent of a taxpayer's adjusted gross income (AGI) (see ¶ 1124).

Housing assistance. Reacting to the continued slump in housing sales, rising unemployment numbers and weakness in the credit markets, Congress passed the Housing and Economic Recovery Act of 2008 (P.L. 110-289). The legislation's tax title, the Housing Assistance Tax Act of 2008, includes \$15.1 billion in tax incentives that are fully offset by far-reaching revenue raisers. The House passed the measure on July 23, 2008, by a vote of 272 to 152. After a procedural delay, the Senate followed suit and passed the legislation on July 26, 2008, by a vote of 72 to 13. President Bush signed the bill on July 30, 2008, retracting a previous veto threat.

The following highlights some of the provisions in the Housing Assistance Act:

(1) A first-time homebuyer who purchases a principal residence after April 8, 2008, and before July 1, 2009, can qualify for a credit of up to \$7,500. The credit is recaptured ratably over 15 years, with no interest charge (see ¶ 1310B).

(2) Homeowners may claim an additional standard deduction for real property taxes, up to \$500 (\$1,000 for joint returns), for any tax year beginning in 2008 (see ¶ 1002).

(3) Gain from sale of a principal residence allocable to periods the property is not used as the principal residence by a taxpayer, the taxpayer's spouse or the taxpayer's former spouse is not excluded from the taxpayer's income (see ¶ 1705).

(4) The state housing credit volume cap for the low-income housing credit is temporarily increased for calendar years 2008 and 2009 (see ¶ 1334).

(5) A corporation may elect to claim a credit for a portion of its unused alternative minimum tax and research credits that are attributable to tax years beginning before January 1, 2006, instead of taking the 50 percent bonus depreciation deduction on any eligible qualified property (see ¶ 1237).

(6) The increased estimated tax payment required to be made by certain large corporations (a corporation with at least \$1 billion in assets) in July, August, or September of 2012, has been repealed. However, the estimated tax payment required to be made in July, August, September of 2013 has been increased to 117.75 percent of the amount otherwise due (see ¶ 227).

Military tax relief. On June 17, 2008, following passage by Congress on May 22, 2008, President Bush signed the Heroes Earnings Assistance and Relief Tax Act of 2008 (P.L. 110-245). The bill provides tax breaks for members of the military (active and reserve) and their families and clarifies the tax treatment of state and local benefits provided to volunteer firefighters and emergency medical responders. As revenue offsets, the bill changes the tax treatment of certain government contractors and individuals who expatriate as well as raises the failure to file penalty and extends the mental health parity excise tax.

The Heroes Act includes the following:

(1) Members of a military family, their spouses and qualifying children are not required to have a social security number to claim the refundable tax credit for eligible individuals for the 2008 tax year (the recovery rebate credit) if the credits are claimed on a joint return (see ¶ 126).

(2) The availability of the election to treat combat zone compensation that is otherwise excluded from gross income under Code Sec. 112 as earned income for purposes of the earned income credit is made permanent (see ¶ 1375).

(3) An eligible small business employer can claim a temporary tax credit for up to 20 percent of the military differential wage payments it makes to qualified workers during the tax year. The military differential credit does not apply to any payments made after December 31, 2009 (see ¶ 1323).

(4) The rules allowing for penalty-free distributions from retirement plans for individuals ordered or called to active duty on or after December 31, 2007 for more than 179 days are now permanent (see ¶ 2157).

(5) For purposes of the exclusion of gain from the sale of a principal residence, an individual can elect to suspend the running of the five-year ownership and use testing period during any period that the individual or the individual's spouse is serving outside the United States as part of the Peace Corps (see ¶ 1705).

(6) A mark-to-market tax is imposed on the net unrealized gain in the property of certain individuals who expatriate (see ¶ 2412).

(7) The minimum penalty for failure to file a tax return within 60 days of the due date (with extensions) is increased to the lesser of \$135 or 100 percent of the net amount of tax due (see ¶ 2801).

Farm bill. With the House and the Senate both voting on June 18, 2008 to override President Bush's veto, the Food, Conservation, and Energy Act of 2008 (P.L. 110-246) became law for the second time. The House voted 317-109 to override the veto and the Senate followed with an 80-14 vote to override. P.L. 110-246 repeals previously passed farm legislation, HR 2419, also titled the Food, Conservation, and Energy Act of 2008, then re-enacts the provisions of HR 2419 plus approximately 34 pages of trade provisions inadvertently omitted from the enrolled version of HR 2419. The Farm bill provides significant benefits to farmers, ranchers and timber producers, while raising revenue from certain groups of farmers, ethanol producers and large corporations.

The following are some of the provisions of the Farm bill:

(1) For most taxpayers who receive Commodity Credit Corporation loans or agricultural program payments, deductible farm losses are limited to the greater of \$300,000 or total net farm income for the previous five years (see ¶ 767).

(2) Payment thresholds increased and indexed for farm and nonfarm optional methods of computing net earnings from self-employment (see ¶ 2676).

(3) The loan limits for agricultural bonds has been increased from \$250,000 to \$450,000, indexed for inflation and the dollar limitation in the definition of substantial farmland has been eliminated (see ¶ 729).

(4) An alternative maximum tax rate of 15 percent will apply to the qualified timber gain of a C corporation for a tax year (see ¶ 1772).

(5) A nonrefundable income tax credit of up to \$1.01 per gallon for the production of cellulosic biofuel has been added as a component of the alcohol fuels income tax credit (see ¶ 1329A).

(6) The credit amount for the alcohol mixture credit and the alcohol credit for the use or sale of ethanol as fuel in 2009 and 2010 is reduced from 51 cents per gallon to 45 cents per gallon for ethanol with a proof of greater than 190 (the blender amount) and from 37.78 cents per gallon to 33.33 cents per gallon for ethanol with a proof of at least 150 but less than 190 (the low-proof blender amount) (see ¶ 1326).

(7) Special rules for contributions of real property for conservation purposes extended through December 31, 2009 (see ¶ 1063).

(8) The estimated income tax payment required to be made by certain large corporations in July, August, or September of 2012, has been increased to 125 percent of the amount otherwise due (see ¶ 1063).

(9) Many of the tax benefits extended to the victims of the Katrina, Wilma and Rita hurricanes are modified and available for victims of the tornadoes and storms that hit the Greensburg, Kansas area in May 2007 (see ¶ 897; ¶ 1134; ¶ 1141).

Economic Stimulus package. President Bush signed the Economic Stimulus Act of 2008 (P.L. 110-185) on February 13, 2008, which includes a recovery rebate credit,

business incentives and relief to assist the depressed real estate sector. The Stimulus bill includes the following provisions:

(1) A refundable rebate is available for individuals in 2008, and the rebate amount is equal to the greater of: the taxpayer's net income tax liability (not to exceed \$600, or \$1,200 for joint filers) or \$300 (\$600 for joint filers) if the individual has either: (a) at least \$3,000 of earned income, Social Security benefits or certain veterans' benefits (including survivors of disabled veterans), or (b) net income tax liability of at least \$1 and gross income greater than the sum of the applicable basic standard deduction amount and one personal exemption (two if a joint return) (see ¶ 126).

(2) The Code Sec. 179 expensing amounts are increased for 2008. The dollar limit is increased to \$250,000 and the investment limit is increased to \$800,000 (see ¶ 1208).

(3) The 50 percent first-year bonus depreciation deduction is available for qualifying property acquired after December 31, 2007 and placed in service before January 1, 2009. Qualifying property must be (a) eligible for the modified accelerated cost recovery system (MACRS) with a depreciation period of 20 years or less; (b) water utility property; (c) computer software (off-the-shelf); or (d) qualified leasehold property (see ¶ 1237).

For information on further legislative developments in 2008, visit the *U.S. Master Tax Guide's* website at <http://tax.cchgroup.com/mtg>.

A Decade of Change. A decade of tax cuts began with the Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L. 107-16), which reflected congressional compromises on tax rate reduction, estate tax repeal, marriage penalty relief, education incentives, child tax credit increase, pension reform, and alternative minimum tax relief. However, to meet budgetary constraints, provisions are phased in and out over the next 10 years, with an anticipated sunset in 2011 that would reinstate the Code as it was prior to this enactment.

Subsequent legislation accelerated some of EGTRRA's changes. The following table outlines some of the changes taking place over the next few years, subject to future legislative efforts.

	2008	2009	2010	2011
Tax rate brackets				
Top bracket	35%	35%	35%	39.6%
Fifth bracket	33%	33%	33%	36%
Fourth bracket	28%	28%	28%	31%
Third bracket	25%	25%	25%	28%
Second bracket	15%	15%	15%	15%
Initial bracket	10%	10%	10%	n/a
Child tax credit	\$1,000	\$1,000	\$1,000	\$500
IRA contributions	\$4,000	\$5,000	\$5,000*	\$5,000*
IRA catch-ups	\$1,000	\$1,000	\$1,000	\$1,000
SIMPLE contributions	\$10,000*	\$10,000*	\$10,000*	\$10,000*
Elective deferrals	\$15,000*	\$15,000*	\$15,000*	\$15,000*
Elective catch-ups				
—SIMPLES	\$2,500*	\$2,500*	\$2,500*	\$2,500*
—401(k), 403(b), 457 plans	\$5,000*	\$5,000*	\$5,000*	\$5,000*
AMT exemption				
—single	\$44,350	\$33,750	\$33,750	\$33,750
—married filing jointly	\$66,250	\$45,000	\$45,000	\$45,000
Estate tax				
—top rate	45%	45%	0%	55%
—exemption amount	\$2 million	\$3.5 million	\$0	\$675,000
Gift tax				
—exemption amount	\$1 million	\$1 million	\$1 million	\$1 million

* subject to inflation adjustments

¶ 2 What to Watch on 2008 Returns

The *Guide* reflects all of the important administrative and judicial developments of 2008 . . . final regulations, major court decisions, and important rulings of the Internal Revenue Service. Legislative highlights are at ¶ 1. Below are additional highlights of the changes in 2008 with the greatest impact on individuals and businesses.

Individuals

Income levels at which individuals must file income tax returns have increased for 2008	¶ 109
Basic standard deduction amounts have increased for 2008	¶ 126
The deduction for each personal exemption has increased to \$3,500 for 2008	¶ 133
Inflation-adjusted income amounts that trigger the reduction of allowable itemized deductions and personal exemptions for high-income taxpayers have increased for 2008	¶ 88A, ¶ 133, ¶ 1014
"Kiddie" tax amount is \$1,800 for 2008	¶ 706
The standard mileage rate for all business use of a car is 50.5 cents per mile for 1/01/08 - 6/30/08 and 58.5 cents per mile for 7/01/08 - 12/31/08	¶ 947
Per diem rates under the high-low method of substantiating travel expenses are at \$237 for high-cost localities and \$152 for low-cost localities for travel on or after 10/01/07; per diem rates under the high-low method of substantiating travel expenses are at \$256 for high-cost localities and \$158 for low-cost localities for travel on or after 10/01/08	¶ 954A
Student loan interest, up to \$2,500 in 2008, may be deducted "above-the-line" by qualifying taxpayers.	¶ 1082
The transportation fringe benefit exclusion amount in 2008 for employer-provided transit passes or vehicles is \$115 per month and \$220 per month for employer-provided parking	¶ 863

Depreciation, Amortization and Depletion

The maximum Code Sec. 179 deduction for 2008 is \$250,000	¶ 1208
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Tax Credits

For 2008, the maximum earned income credit for eligible taxpayers with no qualifying children is \$438, with one qualifying child is \$2,917, and with two or more qualifying children is \$4,824	¶ 87, ¶ 1375
The child tax credit is \$1,000 for 2008	¶ 1302
The education tax credits (Hope and Lifetime Learning) are \$1,800 and \$2,000, respectively, for 2008	¶ 1303

Withholding

The 2008 OASDI wage base for FICA and self-employment tax purposes is \$102,000	¶ 47, ¶ 49, ¶ 2648, ¶ 2670
The 2008 wage threshold for "Nanny Tax" reporting is \$1,600	¶ 2650