Out with the Old … In with the New

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Along with the arrival of 2010 comes various income tax law changes that are highlighted below.

Individual Taxpayers

- The unpopular alternative minimum tax (the "AMT Tax") still exists, but the exemption amount has been reduced. The AMT Tax exemption amount for 2009 was $46,700 for single filers, $70,950 for married taxpayers filing jointly or a qualifying widow or widower, and $35,475 for married taxpayers filing separately. For 2010, these exemption amounts have dropped to $33,750 for single filers, $45,000 for married taxpayers filing jointly or a qualifying widow or widower, and $22,500 for married taxpayers filing separately.
- Required minimum distributions had been waived for 2009 but are again required for 2010.
- The income limit on eligibility to convert a traditional IRA to a Roth IRA has been eliminated (see the related article in this newsletter for more detail).
- The phase-out of the personal exemption and of itemized deductions based on the taxpayer's adjusted gross income is eliminated in 2010.
- With the repeal of the Federal Estate Tax, the rules for increasing the cost basis of assets passing from a decedent have changed (see the related article in this newsletter for more detail).
- Any taxpayer who claimed the first-time homebuyer credit must begin to repay that credit if the taxpayer disposes of the taxpayer's residence before the end of the fifteen-year recapture period.
- The ability to claim either an itemized deduction or an increased standard deduction for state or local sales or excise taxes on the purchase of a new motor vehicle has expired.
- The tax deduction for qualified tuition and related expenses and the $250 tax deduction for education professionals for certain expenses have both expired.
- Taxpayers who are older than 70.5 years of age may no longer make a tax-free distribution from an IRA to a charity.

The reduced AMT Tax exemption amounts likely will have the greatest impact on taxpayers since the reduced exemption amounts greatly widen the net cast by the AMT Tax. Hopefully, Congress will pass another "patch" to increase the exemption amounts as it has done for the past few years. In general, tax deductions are popular and the expiration of the tax deductions outlined above and various other tax deductions that expired at the end of 2009 hopefully will be addressed by Congress as well. One significant benefit in 2010, though, is the elimination of the adjusted gross income phase-out of the personal exemption and itemized deductions. The elimination of the phase-out will benefit higher income taxpayers who in the past saw these benefits reduced or eliminated.

Business Taxpayers

- Employer-sponsored qualified retirement plans must now offer non-spouse beneficiaries the right to rollover an inherited plan account to an IRA. This option was permitted but not required in 2009.

- The deduction for domestic production activities increases for 2010. Taxpayers will be able to claim a deduction generally equal to 9% of the lesser of: (1) the taxpayer's "qualified production activities income" for the tax year or (2) taxable income without regard to this deduction for the tax year. In prior years the percentage limitation was 6%.
- The deduction for additional first-year 50% bonus depreciation for qualified property has expired (but note that certain aircraft and long-production-period property continues to be eligible if placed in service in 2010).
- The maximum amount that may be expensed under section 179 is reduced to $134,000 (down from $250,000 for tax years beginning in 2008 or 2009).
- Various accelerated depreciation rules have expired (for example, the five-year depreciation period for farm business equipment and the fifteen-year, straight-line cost recovery for qualified leasehold improvements and retail improvements).
- Various enhanced charitable deductions have expired, including the enhanced deduction for the contribution of food and book inventories and for the contribution of computer equipment for educational purposes.
- Pursuant to the Worker, Homeownership, and Business Assistance Act of 2009, most businesses may now carry back net operating losses for three, four, or five years.

As with individual taxpayers, business taxpayers favor tax deductions. Arguably, the behavior of business taxpayers is influenced by the availability of tax deductions. For example, a business taxpayer may purchase less equipment because of the expiration of the 50% bonus depreciation or the reduced section 179 deduction. Conversely, a domestic manufacturer may increase domestic production activities due to the increase of the domestic production activities deduction.

Many of the tax benefits that expired for both individuals and businesses on December 31, 2009 were extended as part of the "Tax Extenders Act" passed by the House of Representatives in December, 2009. This Act, however, did not pass the Senate. Predicting how Congress will act is difficult, but practitioners (and clients) hope that Congress will pass legislation to address the expiration of the many popular tax breaks that expired on December 31, 2009.

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