



a Wolters Kluwer business

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Special Report

HIGHLIGHTS:

- ✓ *Extends Over 50 Tax Breaks*
- ✓ *Widespread Benefits*
- ✓ *\$31 Billion in Tax Relief/Increases*
- ✓ *Targets Offshore Accounts*
- ✓ *Closes Carried Interest Loophole*
- ✓ *Impacts Year-End Planning*

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House-Passed Extenders/Jobs Bills Await Senate Action in 2010

The House of Representatives approved a package of tax extenders on December 9, 2009, by a largely party-line vote of 241 to 181. The \$31 billion Tax Extenders Act of 2009 (H.R. 4213) extends more than 50 popular, but temporary, tax incentives through December 31, 2010. Two revenue raisers - a change in the taxation of carried interest and heightened information reporting and disclosure requirements for foreign bank and financial accounts - would pay for the one-year extensions.

The House also approved the Jobs for Main Street Act of 2010 (H.R. 2847) (the Jobs bill) on December 16, 2009, by a slim 217 to 212 margin. In addition to extending unemployment insurance benefits and COBRA premium assistance, the Jobs Act would increase eligibility for the refundable child tax credit, temporarily exempt tax refunds as income for eligibility in means-tested federal programs, and add a refundable credit for certain Qualified Zone Academy Bonds and Qualified School Construction Bonds. This bill would be paid for from existing TARP funds and, therefore, does not include revenue raising provisions as passed.

Impact *The Senate is not expected to voted on the extenders or jobs bills until January or February 2010. The Senate may make changes to both bills, which would then require final conference negotiations with the House. The tax benefits under the*

extenders and the jobs bills are expected to be made retroactive to January 1, 2010, if and when they are finally approved.

Comment In separate legislation, the FY 2010 Defense Appropriations Act (H.R. 3326), the House and Senate approved a temporary two-month extension of COBRA premium assistance and unemployment benefits. Eligibility for COBRA premium assistance was scheduled to expire after December 31, 2009. President Obama signed the FY 2010 Defense Appropriations Act on December 19, 2009.

Impact *Noticeably missing from both the extenders and the jobs bills are two temporary business provisions that expire after December 31, 2009: Code Section 179 small businesses expensing at the enhanced \$250,000 level and bonus depreciation for all businesses. President Obama recently announced that he wants these provisions extended as part of a jobs growth package.*

In a related development, the Senate did not take up the federal estate tax bill, also passed by the House earlier in December. The Permanent Estate Tax Relief for Families, Farmers and Small Businesses Bill of 2009 (H.R. 4154), was approved by the House on December 3, by a 225-200

vote. This delay technically triggers estate tax repeal and modified carry-over basis for estates of decedents dying in 2010. Expectations are that the estate tax will eventually be preserved by Congress, although not necessarily at a \$3.5 million exclusion level, and will be made retroactive to January 1, 2010, along with the repeal of carry-over basis.

INDIVIDUAL EXTENDERS

All of the individual tax breaks in the House bill made an appearance in the last round of extenders legislation: the itemized state and local sales tax deduction, the additional standard deduction for real property taxes, the deduction for qualified tuition/expenses, and the deduction for teacher classroom expenses. These provisions were extended by the Emergency Economic Stabilization Act of 2008 (EESA) for a two-year period, through December 31, 2009. The House bill extends these individual tax breaks for one year only, through December 31, 2010.

Impact *The House bill does not include an AMT “patch” for 2010, probably due to its cost. It will likely be addressed separately in early 2010, when it would be made retroactive. Unless renewed, the AMT exemption amounts will fall dramatically from their 2009 levels (from \$70,950 to \$45,000 for joint filers and from \$46,700 to \$33,750 for single individuals/heads of household).*

Comment The centerpiece of the American Recovery and Reinvestment Act of 2009 (2009 Recovery Act) --the Making Work Pay Credit (MWPC)-- does not expire until the end of 2010. President Obama has urged Congress to make the MWPC permanent but the current Congress won’t consider it because of the cost.

Deduction for State and Local Sales Taxes

The American Jobs Creation Act of 2004 allowed taxpayers an itemized deduction for either: (1) state and local income taxes or (2) state and local general sales taxes. The deduction for state and local sales taxes was temporary and was set to expire after December 31, 2005. Since 2005, Congress has routinely extended the deduction for state and local sales taxes. The House bill extends the deduction for state and local sales taxes through December 31, 2010.

Impact *This deduction option primarily benefits residents of states that do not impose an individual income tax. Jurisdictions without a statewide income tax include Alaska, Florida, Nevada, New Hampshire, South Dakota, Texas, Washington, and Wyoming. Taxpayers can calculate their deduction either by saving receipts or using the Optional State Sales Tax Tables provided by the IRS. A Texas resident with \$100,000 income and claiming two exemptions, for example, is entitled to a \$1,145 deduction under the 2009 tables.*

Comment The separate state and local sales tax deduction for new vehicles purchased after February 17, 2009, and before January 1, 2010, is not part of the House bill and is not expected to be extended in a final bill.

Additional Standard Deduction for State/Local Real Property Taxes

Non-itemizers can claim an additional standard deduction for qualified state and local real property taxes, up to \$500 (\$1,000 for joint filers). This special treatment is temporary and is set to sunset after December 31, 2009. The House bill extends the deduction through December 31, 2010.

Impact *While most homeowners itemize their deductions, the extension will provide a benefit to taxpayers that otherwise have insufficient itemized deductions, such as homeowners who have paid off (or are close to paying off) their mortgages and have little home mortgage interest expense. For 2009, this additional standard deduction is taken on a new Schedule L to Form 1040A or 1040, along with any additional standard deduction for new vehicle sales tax and a special disaster loss deduction.*

Comment The \$500 deduction does not lower the taxpayer’s adjusted gross income. The deduction is an addition to the standard deduction, which is \$5,700 for singles and \$11,400 for joint filers for 2009.

Higher Education Tuition Deduction

The higher education tuition deduction allows eligible taxpayers an above-the-line deduction for qualified higher education expenses. Qualified expenses may be paid for the taxpayer, his or her spouse or a dependent. The full \$4,000 deduction is available to single individuals with modified adjusted gross income (AGI) of \$65,000 or less and to joint filers with AGI of \$130,000 or less (adjusted for inflation). A reduced deduction of \$2,000 is available to single individuals with AGI of \$80,000 or less and to joint filers with AGI of \$160,000 or less (adjusted for inflation). The House bill extends the higher education tuition deduction through December 31, 2010.

Comment The 2009 Recovery Act expanded and renamed the Hope scholarship credit “the American Opportunity Tax Credit (AOTC).” Taxpayers may not claim the deduction for qualified tuition and related expenses and an AOTC

or Lifetime Learning Credit for the same student in the same year. The AOTC can reach as high as \$2,500 per year for four years of post-secondary education and generally is more favorable than the higher education tuition deduction for those who qualify. The AOTC does not sunset until the end of 2010.

Teacher's Classroom Expense Deduction

Professional educators, such as teachers, principals and guidance counselors, may deduct - above-the-line - qualified out-of-pocket classroom expenses. The maximum deduction reaches \$250 and includes the cost of supplies, equipment, books, and software used in the classroom. The House bill extends the deduction through December 31, 2010.

Comment Generally, educators must work at least 900 hours during the school year to qualify. The deduction, however, is limited to \$250 for the calendar year.

Comment Taxpayers who itemize may be able to deduct expenses that exceed the \$250 cap as an employment-related miscellaneous itemized deduction, subject to the two-percent floor.

BUSINESS EXTENDERS

The House bill extends an extensive list of traditional business tax breaks. Among the more significant tax breaks are the research tax credit, enhanced depreciation for qualified leasehold, restaurant, and retail property, and expensing of environmental remediation costs.

Impact *The Obama administration had proposed making some of the provisions permanent, most notably the research tax credit. House lawmakers, conscious of the federal budget deficit, elected not to make any of these*

tax breaks permanent until the budget numbers improve.

Research Credit

The EESA extended the Code Sec. 41 tax credit for qualified research and experimentation (R&E) expenditures to qualified expenditures incurred in tax years beginning before January 1, 2010. The EESA also increased the alternative simplified credit from 12 percent to 14 percent for tax years ending after 2008 and repealed the alternative incremental research tax credit for tax years ending after 2008. The House bill extends

“The \$31 billion Tax Extenders Act of 2009 extends more than 50 popular but temporary tax incentives through December 31, 2010”

the research credit as enhanced by the EESA to apply to qualified expenditures incurred in tax years beginning before January 1, 2011.

Impact *The research credit is one of the most costly extenders, with the one year extension estimated to reach \$6.96 billion. Most legislators agree that making the research credit permanent would be ideal to allow businesses to make long-term R&E plans; however, the revenue cost is prohibitive, in the current economy and under existing budget rules.*

Exceptions for Active Financing Income/ Look-Through Exceptions

U.S. shareholders of a controlled foreign corporation (CFC) generally are subject to tax on certain income earned by the CFC even if the income is not currently distributed. Congress has routinely

provided exceptions from Subpart F, including “active financing” exceptions for certain income derived in the active conduct of a banking, financial, insurance, or similar business. Congress has also provided for look-through exceptions for certain dividends, interest, rents, and royalties received by one CFC from a related CFC. The House bill extends the exceptions for active financing and the look-through exceptions through December 31, 2010.

Leasehold, Restaurant and Retail Property

The EESA extended the 15-year recovery period for qualified leasehold improvement property and qualified restaurant building and improvement property for property placed in service before January 1, 2010. It also provided a 15-year recovery period for qualified retail improvement property placed in service before January 1, 2010. The House bill extends the current 15-year recovery period for qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property for property placed in service before January 1, 2011.

Comment Technically, the 15-year recovery period is non-elective, but taxpayers can get around this restriction by electing MACRS alternative depreciation system (ADS) treatment. Without this provision, however, these properties would be depreciated using straight-line depreciation over 39 years.

Film and Television Production

In lieu of capitalizing the costs of certain film and production costs and recovering it through depreciation allowances, qualified taxpayers may elect to deduct the first \$15 million of qualified film and television production costs, for productions commencing prior to January 1, 2010, in the year the expense is incurred. The House bill extends the expensing provision to qualified film

and television productions commencing after December 31, 2009 and before January 1, 2011.

Comment

Generally, at least 75 percent of the total compensation expended for the production must be for services performed in the U.S. by actors and other production personnel.

Environmental Remediation

Taxpayers may elect to treat certain environmental remediation expenditures as deductible in the year paid or incurred. The EESA extended expensing of brown-fields remediation costs to expenses incurred before January 1, 2010. The House bill extends expensing of brown-fields remediation costs to expenses incurred before January 1, 2011.

Differential Wage Payments to Military Personnel

The Heroes Earnings Assistance and Relief Tax Act of 2008 (2008 HEART Act) provided eligible small businesses (those with fewer than 50 employees) with a tax credit reaching 20 percent of differential wages up to \$20,000 paid to qualified employees who are called to active military duty. Currently, this credit ends on December 31, 2009. The House bill extends the military differential wage credit to qualified payments made after December 31, 2009, and before January 1, 2011.

Impact

The employer's deduction for compensation paid is reduced by the amount of the employer's differential wage credit.

Regulated Investment Companies

The EESA extended several temporary provisions applicable to regulated investment companies (mutual funds) through December 31, 2009. These include provisions with respect to interest-related dividends and short-term capital gains dividends of mutual funds; the treatment of stock in a mutual fund for purposes of

determining estates of nonresidents who are not U.S. citizens; and the treatment of a mutual fund investing in real estate as a qualified investment entity with respect to dispositions of investments in U.S. real property. The House bill extends these provisions through December 31, 2010. With respect to estates of nonresidents who are not U.S. citizens the extension applies to estates of decedents dying after December 31, 2009.

More Business Extenders

The House bill also extends through December 31, 2010 the following business-related extenders:

- Suspension of the percentage depletion limitation for oil and gas from marginal wells;
- Five-year write-off of farm machinery/equipment;
- Mine rescue training credit and bonus depreciation allowance;
- Indian employment credit;
- Accelerated depreciation for business property on an Indian reservation;
- Railroad track maintenance credit;
- Motorsports entertainment complex accelerated recovery;
- Code Sec. 199 domestic production activities deduction for qualified activities in Puerto Rico;
- Temporary increase in limit on cover over of run excise taxes to Puerto Rico and the U.S. Virgin Islands; and
- American Samoa Economic Development Credit.

CHARITABLE EXTENDERS

Tax-Free Distributions from IRAs for Charitable Purposes

Under current law, taxpayers age 70 1/2 and older may make a direct tax-free charitable contribution from an individual retirement account (IRA) to a charity on or before December 31, 2009. The contribution may not exceed \$100,000 per individual in the applicable tax year. The House bill extends tax-free distributions from IRAs for charitable contributions through December 31, 2010.

Impact

The extension, if passed, provides taxpayers with a valuable tax planning tool for one more year. However, the tax-free treatment is offset by the lack of a deduction (no charitable deduction is allowed with respect to any amount excluded from income). This potential downside may be offset by the fact that the exclusion reduces the taxpayer's AGI, lowering the floor for deducting medical expenses and miscellaneous deductions.

Comment

The provision applies to traditional IRAs and Roth IRAs.

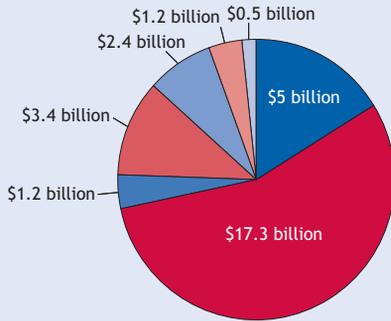
Contributions of Capital Gain Real Property for Conservation Purposes

The Pension Protection Act of 2006 (PPA) and subsequent legislation encouraged taxpayers to donate capital gain real property to qualified charities for conservation purposes. Among other things, the PPA increased the donor's contribution cap on deductions for qualified conservation contributions from 30 percent to 50 percent, and increased the cap to qualified ranchers and farmers to 100 percent. The PPA and subsequent laws also increased the number of years that qualified conservation contributions in excess of the 50 percent and 100 percent caps may be carried forward from five to 15 years. These provisions will sunset after December 31, 2009, under current law. The House bill extends them through December 31, 2010.

Charitable Deduction for Food Inventory

The EESA extended the enhanced deduction for charitable donations of food inventory by non-corporate taxpayers engaged in a trade or business for contributions made through December 31, 2009. The House bill extends the deduction through December 31, 2010.

COST OF EXTENDERS



Individuals	.....	\$5 billion
Businesses	.....	\$17.3 billion
Charitable	.....	\$1.2 billion
Communities	.....	\$3.4 billion
Disaster Relief	.....	\$2.4 billion
Energy	.....	\$1.2 billion
Miscellaneous	.....	\$0.5 billion

Comment The EESA also temporarily suspended the 10-percent limitation applicable to qualified donations of food inventory made by qualified farmers and ranchers on or after October 3, 2008, but before January 1, 2009. The House bill does not renew this provision.

Corporate Contributions of Book Inventory

A corporation, other than an S corporation, may take a special deduction for qualified book contributions. For purposes of this deduction, a qualified book contribution is a charitable contribution of books to a public school providing elementary or secondary education with a regular faculty and a regularly enrolled student body. The EESA extended the qualified book charitable contribution deduction through December 31, 2009. The House bill extends the deduction through December 31, 2010.

Contributions of Computer Technology/Equipment

For contributions of property, a corporation's charitable deduction is generally limited to the corporation's basis in the property up to 10 percent of the corporation's taxable income. However, contributions of computer technology

and equipment for educational purposes qualify for preferred treatment: a deduction equal to the corporate donor's basis in the donated property plus one-half of the ordinary income that would have been realized if the property had been sold. That deduction will sunset after December 31, 2009. The House bill extends the deduction through December 31, 2010.

Impact *The deduction cannot exceed the twice the corporation's basis in the property. Most businesses are allowed to fully depreciate software over 36 months and hardware over five years.*

Basis Adjustment to Stock of S Corps Making Charitable Contributions

The PPA provided that an S corporation shareholder's basis in the stock of an S corporation making a charitable contribution is reduced by the shareholder's pro rata share of the adjusted basis of the contributed property. The EESA extended this provision to tax years beginning before January 1, 2010. The House bill extends this provision to tax years beginning before January 1, 2011.

Impact *The provision generally preserves the intended benefit of the fair market value deduction for the contributed appreciated property without causing the shareholders to recognize gain or a reduced loss attributable to the appreciation upon a subsequent sale of the stock.*

More Charitable Extenders

Additional charitable extenders in the House bill are:

- Modification of tax treatment of certain payments to controlling exempt organizations; and
- Exclusion of gain or loss on sale or exchange of certain brownfields sites from unrelated business taxable income.

NATIONAL DISASTER RELIEF EXTENDERS

For the first time, Congress provided national disaster relief in the EESA. The provisions are temporary and will expire at the end of 2009. The House bill generally extends national disaster relief for one year, through December 31, 2010.

Impact *Often overlooked in reviews of the current extenders package are the generous but temporary nationwide disaster relief provisions first enacted in 2008. The House bill extends nationwide disaster relief, including enhanced casualty loss deductions and incentives for businesses to rebuild after a natural disaster, through December 31, 2010.*

Net Disaster Loss Extension

Uncompensated 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). Additionally, a temporary additional standard deduction is available for taxpayers affected by a federally declared disaster. However, as a partial tradeoff for these benefits, the EESA raised the per casualty floor for any qualified personal casualty loss from \$100 to \$500. The House bill extends the provisions for one year, through December 31, 2010.

Impact *As somewhat of a "hidden" tax increase, the House bill extends into 2010 the \$500 floor for personal casualty loss deduction. This floor applies whether the deduction is subject to the special disaster relief treatment or not. For example, a homeowner replacing part of a roof because of wind damage in a storm that was not declared a federal disaster would be required to deduct \$500 from the cost of repairs, rather*

than \$100, before also applying the 10 percent AGI floor.

Comment A federally declared disaster is a disaster occurring in an area that is later determined by the President to warrant assistance by the federal government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act. Under current law, a taxpayer may elect to deduct a casualty loss on his or her return for the immediately preceding tax year to accelerate the benefit.

Business Expensing of Qualified Disaster Expenses

The House bill extends the expensing election provided to any trade or business to clean up or repair property from damage caused on account of a federally declared disaster under circumstances in which the expenses would otherwise be required to be capitalized. The provision would apply to amounts paid or incurred in connection with a federally declared disaster occurring after December 31, 2009 and before January 1, 2011.

Impact *A qualified disaster expense under Code Sec. 198A is any expense that can otherwise be capitalized and that is paid or incurred in connection with a trade or business or with business-related property that is (1) for the removal of debris, (2) demolition of structures on real property, (3) the repair of business-related property damaged, or (4) the abatement of hazardous substances released as a result of a federally-declared disaster.*

NOL Carryback

The House bill extends for one-year the special five-year carryback for net operating losses (NOLs) allowed for qualified disaster losses. The carryback applies to qualified disaster losses incurred in connection with federally-declared disasters occurring after December 31, 2009, and before January 1, 2011.

Impact *This NOL tax break, which is elective, can work in tandem with the 2009 Worker Act signed into law on November 6, 2009. The 2009 Worker Act allows a five year carryback of all NOLs from either 2008 or 2009 (one year only, at the election of the taxpayer). Carryback to the fifth year under that provision, however, is limited to 50 percent of taxable income for that year. There is no 50-percent limit under the House extends bill for that fifth carryback year to the extent the NOL is attributable to a qualified disaster loss.*

Special Depreciation for Qualified Disaster Property

The House bill extends the additional 50-percent bonus depreciation deduction on property that rehabilitates or replaces qualified business property on account of a federally declared disaster. The provision applies to property placed in service in a disaster area with respect to a federally-declared disaster occurring before January 1, 2011, and is effective for disasters occurring after December 31, 2009. The deduction is allowed for both regular and alternative minimum tax (AMT) purposes.

Expanded Code Sec. 179 Expensing

In lieu of taking bonus depreciation, qualified taxpayers can alternatively elect to expense the cost of qualifying property (Code Sec. 179 expensing). Qualified disaster assistance property is eligible for increased dollar limits on expensing.

Impact *Under current law, for tax years beginning in 2010, the maximum amount a business can normally expense under Code Sec. 179 is \$125,000 of the cost of qualifying property placed in service for the tax year. The \$125,000 amount is reduced (not below zero) by the amount by which the cost of qualifying property placed in ser-*

vice during the tax year exceeds \$500,000. If Congress decides to extend regular Code Sec. 179 expensing at its current 2009 levels of \$250,000/\$800,000, the special qualified disaster limits would be raised proportionately to \$350,000/\$1.4 million.

Qualified Mortgage Bonds

The House bill extends the relaxation of certain mortgage revenue bond requirements following a federally-declared disaster for one year, through 2010. Qualified mortgage bonds generally cannot be used to finance a mortgage for a homebuyer who had an ownership interest in a principal residence in the three years preceding the execution of the mortgage. The election to waive certain mortgage revenue bond rules includes the election by certain taxpayers to waive this first-time homebuyer credit rule for residences located in federally-declared disaster areas.

The House bill also extends the treatment of residences located in federally-declared disaster areas as "targeted area residences" for purposes of income and purchase price limits that otherwise apply to certain qualified mortgage bonds. The extension would be effective for bonds issued after December 31, 2009.

ENERGY EXTENDERS

Credits for Biodiesel and Renewable Diesel Fuel

The biodiesel mixture tax credit is \$1.00 for each gallon of biodiesel used to produce a mixture of biodiesel and diesel fuel that is sold or used by the taxpayer. The credit is taken when the fuel is sold or used. The mixture need only have 0.1 percent of diesel fuel. The credit is refundable. The biodiesel mixture excise tax credit is also \$1.00 per gallon.

Comment Taxpayers cannot claim both the income tax credit and the excise tax credit for the same fuel.

The biodiesel credit is \$1.00 per gallon for 100 percent biodiesel fuel that is used in the taxpayer's business or sold at retail. The agri-biodiesel credit is 10-cents per gallon for up to 15 million gallons of agri-biodiesel produced by small producers (who produce no more than 60 million gallons of agri-biodiesel per year).

Comment Biodiesel is derived from plant or animal matter. Agri-biodiesel is derived solely from virgin plant oils and animal fats.

The credit for renewable diesel fuel is \$1.00 per gallon. Renewable diesel fuel is liquid fuel from biomass used in diesel engines or for aviation. Kerosene used for aviation is also treated as renewable diesel fuel.

The House bill extends these credits through December 31, 2010.

Alternative Motor Vehicle Credit for Heavy Hybrids

The tax code provides an alternative motor vehicle credit for hybrid vehicles that use gasoline and electricity. The credit can depend on the vehicle's weight class, technology, fuel economy, and incremental cost of the technology. Separate credits are available for (1) automobiles and light trucks, and (2) medium and heavy trucks weighing more than 8,500 pounds. The House bill extends the credit for medium and heavy trucks through December 31, 2010.

Comment The credit for automobiles and light trucks is already effective through 2010.

Credits for Natural Gas and Liquefied Petroleum Gas Used as Transportation Fuel

The House bill extends the alternative fuel production credit and payment provisions for compressed and liquefied natural gas and liquefied petroleum gas through December 31, 2010.

Impact *The credits are taken against excise tax liability; any excess is refundable.*

Comment The bill would not extend the credit for liquefied petroleum gas used in forklifts. The credit for liquefied hydrogen already applies through September 30, 2014.

Sales of Electric Transmission Property

Vertically integrated electric utilities can defer gain up to eight years when they sell electric transmission property to certain independent transmission companies and then reinvest the proceeds in certain natural gas or electricity production (reinvestment property). The House bill would extend the deferral provision to sales before January 1, 2011.

Comment Reinvestment property must be located in the United States.

COMMUNITY ASSISTANCE PROVISIONS

Empowerment Zone Tax Incentives

The Community Renewal Act of 2000 extended a number of targeted tax incentives for empowerment zones, including an employer's wage credit for eligible employees, increased Code Sec. 179 expensing, a partial exclusion of capital gains on certain small business stock, expanded tax-exempt financing, and more. Under current law, the empowerment zone tax incentives will sunset after December 31, 2009. The House bill extends the empowerment zone tax incentives through December 31, 2010, with a companion change that further extends through December 31, 2015 (from a previous sunset date of December 31, 2014) for the period for which gain from the sale or exchange of qualified business stock held for more than five years is deferred.

Comment An existing Work Opportunity Tax Credit (WOTC), not set to expire until August 31, 2011, also provides incentives to hire certain individuals who live in an empowerment zone or renewal community.

Renewal Community Tax Incentives

The Community Renewal Tax Relief Act of 2000 provided targeted tax incentives for renewal communities, including an employer's wage credit for eligible employees, additional Code Sec. 179 expensing, a commercial revitalization deduction, a zero percent capital gains rate for the sale of a qualified community asset held for more than five years, and more. The House bill extends the renewal community tax incentives through December 31, 2010, with a further extension through December 31, 2015, for the period for which qualified capital gain from the sale or exchange of a qualified community asset held for more than five years is excluded from gross income.

Comment Only "qualifying assets" are eligible for the special zero percent gains rate. These include a partnership interest in a community renewal business, qualified community stock, and qualified community property.

District of Columbia Tax Incentives

Under current law, certain census tracts in the District of Columbia are designated as enterprise zones. Targeted tax incentives for enterprise zones in the District of Columbia include an employer's wage credit for eligible employees, additional Code Sec. 179 expensing, expanded tax-exempt financing, and a zero percent capital gains rate on the sale of certain assets held for more than five years. The House bill extends these incentives through December 31, 2010 and extends the zero percent tax on capital gains from the sale of qualified D.C. zone assets held for more than

five years. The qualifying capital gain must be attributable to periods before December 31, 2015.

Comment The House bill also extends the District of Columbia first-time homebuyer credit. The District of Columbia first-time homebuyer credit is available to all qualified residents of the District regardless of census tract designation.

New York Liberty Zone

After 9-11, Congress designated parts of Manhattan as a “Liberty Zone,” eligible for targeted tax incentives to encourage remediation and reconstruction. The House bill extends for one year the additional 30 percent depreciation deduction for qualified property placed in service in the Liberty Zone on or before December 31, 2010. The House bill also extends the deadline for issuing tax-exempt private activity bonds to finance the construction and repair of infrastructure in the Liberty Zone through December 31, 2010.

Gulf Opportunity Zone

Under current law, targeted but temporary tax incentives help businesses and homeowners recover from the 2005 hurricanes along the Gulf Coast. Among the Gulf Coast incentives extended by the House bill are the Hurricane Katrina WOTC through August 27, 2010 and increased rehabilitation tax credits for qualified expenses incurred before January 1, 2011.

New Markets Tax Credit

The New Markets Tax Credit (NMTC) program provides taxpayers with a credit against federal income taxes for making equity investments in investment vehicles known as Community Development Entities (CDEs). The House bill extends the NMTC program through December 31, 2010. The maximum amount of equity investment (and resulting deduction) remains at \$5 billion.

Comment The bill also extends the carryover period for unused NMTC for one year to 2015.

Impact *The Administration has been heavily promoting the NMTC as a win-win for investors and the community. Recently, it has also emphasized that the credit has been very effective at generating jobs and providing capital to businesses.*

COBRA PREMIUM ASSISTANCE

The American Recovery and Reinvestment Act of 2009 (2009 Recovery Act) provided a nine month subsidy to help individuals involuntarily terminated from employment to continue their health insurance coverage under COBRA continuation coverage. Under the 2009 Recovery Act, involuntary termination from employment must occur between September 1, 2008, and December 31, 2009 and the individual must be eligible for COBRA coverage at any time during that period.

The 2010 defense bill extends eligibility for COBRA premium assistance to an individual (and family members who are qualified beneficiaries) who is involuntarily terminated from employment through February 28, 2010. The 2010 defense bill also extends the maximum duration of COBRA premium assistance to 15 months and provides an election to pay premiums retroactively and maintain COBRA coverage.

Comment Separate legislation, the Jobs for Main Street Bill of 2010 (H.R. 2847), would extend COBRA premium assistance through June 30, 2010 and make other enhancements. The House approved the Jobs for Main Street Bill on December 17 but the Senate failed to take it up before its holiday recess.

Comment The 2009 Recovery Act COBRA subsidy requirements apply to all plans subject to the COBRA requirements, including self-insured plans.

Involuntary termination. The IRS described what constitutes “involuntary termination from employment” in Notice 2009-27. An involuntary termination, the IRS explained, is a severance from employment due to the employer’s unilateral authority to terminate the employment. Involuntary termination can also occur, among other things, when an employer declines to renew an employee’s contract, tells an employee “resign or be fired or reduces the employee’s hours to zero.

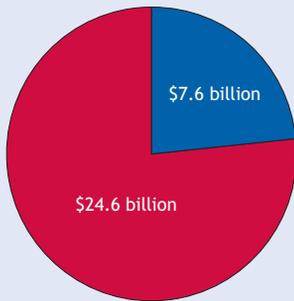
Employer payroll credit. An assistance-eligible individual receives the subsidy in the form of reduced COBRA premiums. Qualified individuals only have to pay 35 percent of the premium to receive COBRA coverage. Employers are reimbursed for the remaining 65 percent through a credit on Form 941, Employer’s Quarterly Federal Tax Return. The IRS revised Form 941 to reflect COBRA premium assistance.

Caution *When the COBRA credit exceeds payroll tax liabilities the IRS will issue a refund. If the employer has unpaid payroll tax liabilities, the IRS will offset the overpayment against the balance due before refunding any balance. Employers will be notified of any offset.*

Comment COBRA premium assistance applies until the earliest of (1) the first date the assistance eligible individual becomes eligible for other group health plan coverage (with certain exceptions) or Medicare, (2) the date that is nine months after the first day of the first month for which the premium reduction provisions apply to the individual, or (3) the date the individual ceases to be eligible for COBRA continuation coverage.

Income limitations. COBRA premium assistance is excluded from gross income. However, the subsidy phases out for higher income individuals. Individu-

REVENUE RAISERS



Foreign Account
Tax Compliance \$7.6 billion
Carried Interest
Income Reform \$24.6 billion

Notes: Corporate Estimated Tax: \$0 net from \$13.7 in 2013 offset by -\$13.7 billion in 2014. Joint Committee on Taxation estimates overall revenue gain of \$1.12 billion from House bill.

als with modified adjusted gross income (AGI) between \$125,000 and \$145,000 (\$250,000 and \$290,000 married couples filing jointly) must repay a portion of the subsidy. If a taxpayer's modified AGI exceeds \$145,000 (\$290,000 for married couples filing jointly) the full amount of the subsidy will be repaid as an additional tax.

Comment A higher income individual can elect to waive COBRA premium assistance

REVENUE RAISERS

Under the House "pay-go" rules, the cost of every tax benefit must be paid for by provisions that raise revenue in an equal total amount. As generous as the Tax Extenders Act of 2009 is to taxpayers, the House bill also collects through tax increases in an equal amount.

Impact *The one "budget trick" performed to lessen the impact of the revenue raisers, however, is that taxpayers get to spend the \$31 billion for the one-year*

extenders upfront during the required 10-year revenue scoring period, while the \$31 billion collected from enhanced foreign account tax compliance, foreign account disclosure reporting and a change in the taxation of carried interest would be spread out fairly evenly over the 2010-2019 period.

Foreign Account Tax Compliance

The IRS and Congress have targeted offshore accounts as a source of substantial tax evasion. Title 5 of the Tax Extenders Act is based on the Foreign Account Tax Compliance Act introduced earlier this year by several members of Congress and on proposals in the president's 2010 budget.

The House bill imposes withholding taxes on foreign banks and other foreign financial institutions that fail to comply with new reporting requirements for foreign accounts owned by U.S. individuals or U.S.-owned foreign entities. A withholding agent who makes a payment would be required to withhold 30 percent on any "withholdable" payment made to a foreign financial institution that violates the reporting rules.

Impact *The House bill provides significant new tools for the IRS to find and prosecute U.S. taxpayers that hide assets overseas. The law would apply to payments made after December 31, 2012, and is estimated to raise \$7.67 billion over 10 years. The law would not require withholding on a payment made under an obligation that is outstanding two years after enactment.*

Comment Withholding would not be required if the foreign institution agrees to: identify its U.S. accounts; report certain information on the account; deduct 30 percent of "pass-thru" payments; and either obtain a waiver to any foreign secrecy laws or close the account if a waiver cannot be obtained.

For each U.S. account, the foreign financial institution would be required to report: the name, address, taxpayer identification number (TIN) of each account holder that is a specified U.S. person and, in the case of any account holder which is a U.S. owned foreign entity, the name, address and TIN of each substantial U.S.-owner of the entity; the account number; the account balance or value; and the gross receipts and gross withdrawals or payments from the account.

Comment A "withholdable payment" is defined broadly to include any payment of income from a U.S. source, including interest, dividends, compensation, and other fixed or determinable annual or periodic gains. A foreign account includes stock and debt in a foreign financial institution. Reporting would also be imposed on hedge funds and private equity funds. A substantial U.S. owner would be defined as the holder of an interest greater than 10 percent in a corporation, partnership or trust

Impact *The House bill provides an exception from reporting with respect to holders of accounts in which the aggregate value of all accounts held in whole or in part by the holder and maintained by the same financial institution does not exceed \$50,000. Withholding would not apply to accounts held by a publicly-traded corporation, tax-exempt organization, retirement plan, government entity, mutual fund, or real estate investment trust.*

Reporting by Individuals of Foreign Assets

The House bill requires individuals to report on their returns an interest in a "specified foreign financial asset" if the taxpayer's holdings exceed \$50,000. In addition to foreign bank accounts, these assets include stock and securities issued

by foreign persons, financial instruments and contracts issued by a foreign person, and any interest in a foreign entity.

Individuals who fail to disclose are subject to a minimum penalty of \$10,000. The penalty increases in increments to a maximum penalty of \$50,000 if the individual does not make the requisite disclosure report after the IRS notifies the individual of a failure to report. The House bill provides a reasonable cause exception to the penalty. A 40-percent penalty would apply to any understatement of tax from an undisclosed asset. The House bill provides a new six-year statute of limitations for understatements attributable to foreign financial assets.

Comment The amendments made by the House bill would apply to returns filed after the date of enactment of the bill and returns filed on or before the date of enactment if the period specified in Code Sec. 6501 for assessment of such taxes has not expired.

Comment The fact that a foreign jurisdiction would impose a civil or criminal penalty for disclosing the information is not reasonable cause under the House bill.

Comment The House bill also increases reporting by a foreign trust with a U.S. beneficiary or a U.S. grantor under the grantor trust rules. Penalties would be enhanced for failure to report concerning a foreign trust.

Carried Interest

The House bill requires that investment fund managers be taxed at ordinary income rates on income from a partnership interest received for services provided to the partnership. Under current law, this income is taxed at capital gains rates.

Under the House bill, amounts paid on this “carried interest” would be ordinary income to the extent the income does not reflect a reasonable return on invested capital. The House bill imposes a 40-per-

cent penalty on underpayments from violations. The ordinary income would be subject to self-employment tax.

The House bill applies to partners providing investment, management, or financial services regarding securities, real estate, interests in partnerships, or commodities. Securities include stock, debt, derivatives, a hedge on securities, and other financial instruments. Ordinary income treatment would also apply to certain dispositions of partnership interests that would ordinarily be capital gain.

Impact *The House bill generally applies to tax years ending after December 31, 2009. Ordinary income treatment would be prorated for a partnership's first fiscal year ending after December 31, 2009.*

Comment Some members of Congress have questioned the fairness of this provision and have raised objections that it may adversely impact oil and gas partnerships and other entities that are not the target of the reformed carried interest rules. This provision may be the deal breaker that will hold up Senate consideration of the House bill until early 2010. Under one scenario, the immediate effective date of this revenue raiser would be postponed to give partnerships time to adjust to the new regime.

Corporate Estimated Tax Payments

In a budget maneuver already used several times to squeeze fairly significant “five-year” revenue out of a relatively non-controversial tax collection technique, the House bill temporarily increases the required corporate estimated tax payments factor for certain large corporations. The latest iteration adds \$13.7 billion to the federal coffers in 2014 by requiring corporations with assets of at least \$1 billion to accelerate estimated tax payments due in July,

August, and September 2014 by a factor of 26.5 percentage points.

Comment Congress approved the Andean Trade Preference Extension Act of 2009 before recessing in December. The trade act increases a recent adjustment in estimated tax payments made by large corporations. Under the trade act, the required payment of estimated tax otherwise due in July, August or September 2014 by large corporations under the Corporate Estimated Tax Shift Act is increased by 1.5 percent.

JOBS LEGISLATION

Before recessing for the holidays, the House passed the Jobs for Main Street Bill of 2010 (H.R. 2847). Along with extending COBRA premium assistance through June 30, 2010, the Jobs for Main Street Bill would enhance eligibility for the refundable portion of the child tax credit by removing the \$3,000 floor for 2010 and provide a single standard for excluding federal income tax refunds from income for purposes of determining eligibility for certain federal programs in 2010. The Jobs for Main Street Bill would also enhance Qualified School Construction Bonds and Qualified Zone Academy Bonds by providing a direct payment option.

COBRA premium assistance. Under the House bill, the maximum duration of COBRA premium assistance would be extended from nine to 15 months. Eligibility for COBRA premium assistance would be extended to involuntarily terminations from employment occurring on or before June 30, 2010.

Comment The House bill clarifies that individuals involuntarily terminated from employment after December 31, 2009, and before the date of enactment of the new law will not lose their eligibility for COBRA premium assistance. The House bill also clarifies that a reduction in hours may be treated as a qualifying event for COBRA

premium assistance.

Comment The House bill requires employers to notify assistance eligible individuals of the extension and expansion of COBRA premium assistance.

Involuntary termination. The House bill clarifies that employer's must maintain supporting documentation of an employee's involuntary termination from employment, including the employer's attestation of the covered employee's involuntary termination.

Child tax credit. Under current law, individuals with dependent children under age 17 at the close of the calendar year get a \$1,000 per child credit through 2010. The 2009 Recovery Act increased the refundable tax credit to 15 percent of earned income in excess of \$3,000 effective for 2009 and 2010. The House bill would repeal the earned income threshold of \$3,000 for determining the refundable portion of the child tax credit for tax years beginning after December 31, 2009, and before January 1, 2011.

Impact *Repeal of the \$3,000 threshold will make all lower-income families eligible for the child tax credit.*

Comment The Obama administration has proposed making the \$3,000 threshold permanent for tax years beginning after December 31, 2010.

Refunds. The House bill clarifies that individual income tax refunds shall not be taken into account as income, and shall not be taken into account as resources, for the month of receipt and the following 11 months, when determining an individual's eligibility for benefits or assistance under any federal program or under any state or local program financed in whole or in part with federal funds. This provision would apply to amounts received after December 31, 2009 and before January 1, 2011.

Bonds. The 2009 Recovery Act created a new category of tax credit bonds, qualified school construction bonds, authorized for issue in 2009 and 2010, with a national volume cap of \$11 billion per year. The bond proceeds must be used to fund the construction, rehabilitation, or repair of a public school, or for the purchase of land on which a funded school will be built. The 2009 Recovery Act also extended the authority of state and local governments to issue qualified zone academy bonds and authorized \$1.4 billion of issuing authority to state and local governments in 2009 and 2010.

The House bill provides a direct payment option for qualified school construction bonds and qualified zone academy bonds. Another 2009 Recovery Act provision, Build America Bonds, includes a direct payment option.

Comment Under the 2009 Recovery Act, there are two types of Build American Bonds. The first

type of Build America Bonds provides a subsidy to investors, which equals 35 percent of the interest payable by the issuer. Under the second type, a direct federal subsidy is paid to state and local governments in an amount equal to 35 percent of the interest. The second type is known as a direct payment Build America Bond.

TECHNICAL CORRECTIONS

House Democrats also introduced a package of technical corrections to recent tax acts. The Tax Technical Corrections Bill of 2009 (H.R. 4169) would make technical corrections to the American Recovery and Reinvestment Act of 2009, the Emergency Economic Stabilization Act of 2008, the Heroes Earnings Assistance and Relief Tax Act of 2008, the Economic Stimulus Act of 2008 (P.L. 110-185), and the Tax Technical Corrections Act of 2007.

Comment Among the technical corrections are clarifications to the 2009 Recovery Act's provision that temporarily shortened from 10 to seven years the holding period for assets subject to the built in gains tax imposed after a C corporation elects to become an S corporation. The technical corrections clarify that Congress intended seven calendar years and not seven taxable years.



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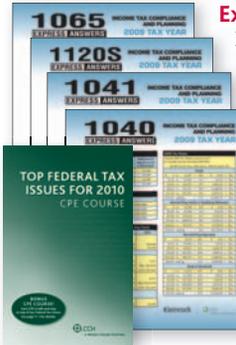
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