



WEALTH PRESERVATION AND TAX PLANNING ALERT

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Emergency Economic Stabilization Act of 2008

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The Emergency Economic Stabilization Act of 2008 (“Act”) was passed by Congress and signed into law by President Bush last month and contains numerous tax provisions which affect individuals and businesses. Some of the relevant provisions are described below.

Individual Tax Provisions

Mutual Funds. The new law extends 3 rules primarily affecting nonresidents who are not U.S. citizens. The first concerns “interest-related” dividends from mutual funds. The second is a “look-through” rule for determining the taxability of mutual fund assets for estate tax purposes. The third concerns the treatment of mutual funds for purposes of the Foreign Investment in Real Property Tax Act (“FIRPTA”).

Qualified Stock Options. Many employees have paid alternative minimum tax (“AMT”) as a result of exercising incentive stock options (“ISOs”), then later suffered losses on selling the stock after its value had declined sharply. This scenario is often called the “phantom income” problem because tax is paid on gains that never materialize. The new law addresses this problem in two ways. First, it liberalizes a rule, which originally took effect in 2007, designed

to allow taxpayers to recover some of the benefit of previously unused AMT credits over a 5-year period. The new law provides additional relief by eliminating a phase-out provision in the original rule and reducing the recovery period to 2 years. Second, the new law forgives any tax, including interest and penalties, outstanding on October 3, 2008 (date of enactment), if attributable to the minimum tax adjustment for ISOs. For taxpayers who have already paid any interest and penalties which would have been abated under this new rule, such interest and penalties can be used—half in 2008 and half in 2009—to increase the “AMT refundable credit amount” and the minimum tax credit.

AMT Patch. The Act includes an AMT patch which raises the AMT exemption amounts to \$69,950 for married couples filing jointly and surviving spouses, \$46,200 for single individuals and head of households, and \$34,975 for married couples filing separately. In addition, the Act allows taxpayers to take nonrefundable personal credits to reduce their AMT liability. These provisions are particularly important to “middle-class” taxpayers who often get caught in the AMT trap that was originally designed to tax higher income individuals. Another AMT change may benefit

energy-conscious taxpayers. Beginning in 2008, the credit for “energy efficient residential property” can be used to offset the AMT.

Extension of Debt Cancellation Income Exclusion for Qualified Principal Residence. The Act extends the exclusion from gross income applicable to qualified principal residence indebtedness under last year’s Mortgage Forgiveness Debt Relief Act for an additional 3 years through 2012.

Charitable Distributions from IRAs. The Act extends the ability of individuals age 70 ½ or older to make tax-free distributions of up to \$100,000 from their IRAs to charitable organizations through December 31, 2009 without any charitable deduction.

Deduction for Sales Taxes and Qualified Tuition Expenses. The election to deduct state and local general sales taxes in lieu of state and local income taxes has been extended by the Act for an additional 2 years through December 31, 2009. This provision has particular relevance to Florida taxpayers since there is no state income tax in Florida. The Act also extends the deduction for qualified tuition and related expenses for an additional 2 years through December 31, 2009.

Business and Investment Tax Provisions

Depreciation. The Act extends the ability to use 15-year cost recovery (depreciation) for qualifying restaurant improvements and leasehold improvements for property placed in service in 2008 and 2009. The Act also creates a new category of 15-year cost recovery property for “qualified retail improvement property.”

Research Tax Credit and New Markets Tax Credit. The Act also extends the research tax credit to amounts paid or incurred in 2008 and 2009 and the new markets tax credit through 2009.

Energy-Related Provisions: Credits

Nonbusiness Energy Property Credit Extended and Expanded. The non-business energy property credit expired after 2007. The Act extended it for 2009 only - it does not retroactively apply the credit to 2008. Thus, you should delay purchase of qualifying energy-saving property until 2009 in order to qualify for this credit. In addition, the list of eligible property is expanded to include expenditures made after 2008 for stoves that burn biomass fuel to heat homes and residential water heaters, as well as expenditures for water heaters with a thermal efficiency of at least 90%. Certain asphalt roofs also qualify as nonbusiness energy property.

Credit for Residential Energy Efficient Property Extended and Expanded. The Act extends through 2016 the credit for “residential energy efficient property,” which was scheduled to expire at the end

of 2008. Also, beginning in 2008, taxpayers can use the credit against the alternative minimum tax. Moreover, the Act retroactively adds two new types of qualifying property, and, beginning after 2008, removes the credit limit for “qualified solar electric property.”

Previously, the credit was based on expenditures for 3 defined types of qualifying property: (i) qualified solar electric property, (ii) qualified solar water heating property and (iii) qualified fuel cell property. The Act adds 2 more categories: (i) qualified small wind energy property and (ii) qualified geothermal heat pump property. The credit for each type of property is 30% of qualifying expenditures, subject to a dollar limit for each. These limits are as follows:

- \$2,000 for qualified solar electric property expenditures in 2008, the limit is removed after 2008.
- \$2,000 for qualified solar water heating property expenditures.
- \$2,000 for qualified geothermal heat pump property expenditures.
- \$500 for each half kilowatt of capacity (not to exceed \$4,000) for qualified small wind energy property expenditures.
- \$500 for each half kilowatt of capacity for qualified fuel cell property expenditures.

Alternative Fuel Vehicle Refueling Property Credit. The Act extends the credit for 1 year through 2010 and designates electricity as an eligible clean-burning fuel, effective for property placed in service after October 3, 2008, in tax years ending after that date.

New Credit for New Plug-in Electric Cars and Trucks. The credit for plug-in electric cars and trucks applies to taxable years after 2008 and equals \$2,500 plus \$417 for each kilowatt hour of traction battery capacity in excess of four kilowatt hours. This credit cannot exceed the following amounts:

- \$7,500 for vehicles with a gross vehicle weight rating of 10,000 pounds or less;
- \$10,000 for vehicles with a gross vehicle weight rating between 10,001 and 14,000 pounds.
- \$12,500 for vehicles with a gross vehicle weight rating between 14,001 and 26,000 pounds.
- \$15,000 for vehicles with a gross vehicle weight rating of more than 26,000 pounds.

The credit for plug-in electric cars and trucks may also offset AMT. A reduced credit is provided for during certain phase-out periods.

Credit for Biodiesel and Renewable Diesel. The Act extends this credit through 2009 and increases the credit rate from \$.50 to \$1.00. The increased rate applies to fuel produced, and sold or used after 2008.

Energy Efficient Appliance Credit Extension and Modification. The credit has been extended for appliances manufactured through 2010. In addition, the Act set credit amounts for the following appliances: dishwashers \$45 to \$75; clothes washers \$75, \$125, \$150, \$250; and refrigerators \$50, \$75, \$100, and \$200, depending on the manufacture date and level of efficiency. The \$75,000 overall limit on the energy efficient appliance credit is increased by resetting the limitation so as to disregard

credits for tax years beginning before 2008.

Long-Term Extension of the Energy Credit. The Act extends the 10% credit for microturbine property and the 30% investment tax credit for solar energy property and qualified fuel cell property through 2016. It also increases the \$500 per half kilowatt of capacity cap for qualified fuel cells to \$1,500 per half kilowatt of capacity.

Also, combined heat and power system property as well as geothermal heat pump systems are now eligible for this credit. Small wind energy property that uses a qualifying small wind turbine to generate electricity also qualifies as energy property, but with a \$4,000 maximum credit limit. Finally, the energy credit may offset AMT beginning in the first year after the October 3, 2008 enactment date.

Energy-Related Provisions: Deductions

Depreciation Deduction for Recycling Property. The Act allows an additional 50% depreciation deduction for any machinery and equipment, including software, used exclusively to collect, distribute, or recycle certain recyclable materials. The deduction is allowed against AMT.

Energy Efficient Commercial Buildings Deduction. This deduction, scheduled to expire in 2008, has been extended through 2013.

Tax Return Preparers

The Act amends Code Section 6694 by replacing the “more likely than not” standard for undisclosed, non-abusive positions with a “substantial authority” standard. The Act

retains the “more likely than not” standard for tax shelters and reportable transactions.

Summary

The foregoing items are just some of the many tax provisions affecting individuals and businesses which were added by the Act. The Act contains provisions above and beyond those summarized above.

If you have any questions regarding any of these changes, please contact any member of our Wealth Preservation and Tax Planning Group. ■

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