TAX NEWS LETTER 2008
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January 12, 2009

The tax filing season is here! Please note that I do anticipate the 2009 tax laws to change significantly from those items listed below.

The following is a listing of significant changes for the 2008 including 2009 where applicable.

New federal tax law changes:

- **Real Estate Tax "Standard" Deduction –** For taxpayers that do not itemize their deductions (on Schedule A), a separate additional real estate tax deduction is allowed up to $1,000 for joint returns and $500 for single taxpayers. Taxes include amounts paid for your residence or investment property but not for those used in a business.

- **First-Time Homebuyers Credit** – Credit applies to a primary home purchases during the period April 9, 2008 through June 30, 2009. Credit is 10% of the purchase price up to a maximum amount of $7,500. First time home-buyers are those individuals not owning a home in the three years prior to the purchase date. Credit must be "paid back" to the IRS over a 15 year period.

- **Recovery Rebate Credit** – The economic stimulus check most taxpayers received this past summer was based on your 2007tax returns. However, the credit was will be applied to the 2008 year. Therefore, any individual who received a "less than maximum" credit will be entitled to an additional refund on the 2008 returns.

- **Energy Tax Credits** – Prior to 2008 a federal tax credit was allowed for the purchase and installation of storm doors, windows, energy efficient furnaces, insulation, heat pumps central air conditioners and water heaters. This provision was terminated for 2008 but will be resumed beginning in 2009.

- **Bonus depreciation for business taxpayers** – Business taxpayers are allowed a tax deduction of up to 50% of the basis of property purchased after March 31, 2008 and before January 1, 2009.

- **Required minimum pension distributions (RMD)** – For those affected over age 70, the RMD distribution is waivered for the 2007 year.

On-going federal tax provisions:

- **Charitable donations** - Beginning January 1, 2007, all cash charitable donations must be supported by a written document to be deductible. Written documents include a check written, receipt or letter of acknowledgement. **For amounts greater than $250 (new)** to anyone group, an acknowledgement must have been received from the charity to be deductible.

- **State sales taxes** continue to be deductible as "itemized deduction" if larger than any state income taxes deducted.

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On-going federal tax provisions (*Continued*):

- **School teachers** - Out-of-pocket expenses paid are deductible - limit $250

- **Qualified college tuition payments -** deduction paid for a post-secondary college education limited to$4,000. The Hope and Life-time learning's credits remain the same.

- **Mortgage insurance premiums** - Mortgage insurance contract premiums paid in 2007 (or pre-paid in 2006 for 2007) are deductible as an itemized deduction on Schedule A (1040). Home mortgage insurance contracts include those on a first or second home and include those from Dept. of Veteran Affairs, Federal Housing Administration, Rural Housing Service and other private qualified contacts. Deductible amounts may appear in box 4 of IRS Form 1098 sent to you.

Federal Facts and Rates:

- **IRA deductions** - The allowed contribution for 2008 and 2009 will be $5,000 per person ($6,000 if age 50).

- **Mileage deduction standard rates** –

  - Business: $0.505 cents per mile from January 1 through June 30, 2008
  - Business: $0.585 cents per mile from July 1 through December 31, 2008
  - Business: $0.55 cents per mile beginning January 1, 2009

  - Medical care and moving: $0.19 per mile from January 1 through June 30, 2008
  - Medical care and moving: $0.27 per mile from July 1 through December 31, 2009
  - Medical care and moving: $0.24 per mile beginning January 1, 2009

  - Charitable remains the same at 14 cents per mile

- **Standard deduction** -2008 filing joint deduction is $10,900 ($11,400 in 2009), $8,000 head of household ($8,350 in 2009) and $5,450 ($5,700 in 2009)) for single or filing separate.

- **Personal exemption** - 2008 exemption deduction will be $3,500; $3,650 in 2009.

- **Gift Tax exemption** limited to $13,000 in 2009.

Maine tax return information -

As many of you know, Maine taxable income is based on the federal adjusted gross income. To this amount certain adjustments are made to arrive at taxable income. Items the state does not allow includes (but is not limited to) the following: state income tax deduction (from any state),

<u>Maine tax return information *(Continued)*-</u>

qualified tuition deduction, 50% bonus depreciation, non-Maine Municipal interest earned and taxable social security benefits. Items of deduction allowed include: $6,000 pension deduction for non-IRA and pre-mature pension distributions, US government interest and Maine municipal bond interest. Other items include:

- **Standard deduction -** $8,900 for joint filers ($9,500 in 2009), $5,350 for single ($5,700 in 2009), $8,000 head of household ($8,350 in 2009) and $4,450 for separate returns ($4,750 in 2009)
- **Personal exemption / dependent deduction** remains the same at $2,850
- **Section 529 plan** - deduct up to $250 for contributions to a beneficiary's account used for educational purposes
- **Educational opportunity credit** - loan payments made for a Maine resident post -graduate student who with an associates or bachelor's degree and stays in Maine to work after college
- **Domicile "Safe Harbor" rules adopted -** For ""snow birds" living in Maine that want to charge residency to a different state (like Florida)

<u>Steve's Tax Corner:</u>

<u>Topic 1: Business use of Auto:</u>

Many of us use our personal cars as an employee or for business purposes. Use of the vehicle can provide significant tax deductions. However, taking the deduction is complicated and requires significant record keeping procedures. Failure to not keep adequate records will result in the denial of these deductions.

Tax law requires that adequate records be **<u>written.</u>** Records should include: (1) mileage driven or amount of the expenses paid, (2) time and place of use, (3) business purpose and (4) business relationship. Items (3) and (4) are related and self-explanatory. However, items (1) and (2) would ordinarily require **<u>keeping an account book or log</u>**. Other documents such as timesheets or expense reports are also allowed. As a starting point, I would suggest recording the beginning and ending odometer readings as of January 1st each year.

Most employees are reimbursed from their employer for miles traveled using the "mileage" method under an "IRS Accountable Plan". The individual is reimbursed at a standard IRS defined rate (see above for "Federal facts and rates") for miles traveled. The employer is entitled to a tax deduction and the employee is considered to have been fully reimbursed for the expense. The mileage rate includes: gasoline, insurance, vehicle depreciation, tires and other repairs. It does not include: tolls, excise taxes, registration fees and loan interest. Corporations are not allowed to use the mileage method for Company owed vehicles; only individuals are allowed this method.

Topic 1: Business use of Auto (Continued):

The employee is entitled to a tax deduction on Schedule A (Form 1040) as an itemized deduction limited to 2% of the taxpayer's income for employer reimbursement amounts **less** than the standard IRS rate allowed; taxable income if more.

The "actual' method is available to both self-employed individuals and employees and is the only method allowed to business entities (corporations, LLCs and partnerships) for Company owned vehicles. The "actual" deduction is based on the expenses (see items covered by the mileage method) paid prorated for the business miles divided by the total miles the auto was used. Depreciation is deducted at a slower rate. The tax deduction is the greater of the actual or mileage methods.

Topic 2: Paying your federal and state income taxes:

Ugh, paying taxes! Actually, the method you use will help to help to reduce any unwanted interest and penalty charges.

There are only two methods to pay federal and state income taxes: the "withholding method" and via estimated tax payments. Simply, the "withholding method" requires the employer or other agent to "withhold" income taxes at the point of payment. At a later time, the agent remits the tax to the federal or state government. The estimated tax payment method requires you and for corporations to make four, quarterly tax payments due: April 15th, June 15th, September 15th and January 15 (of the following year).

By far and away the best method to pay your taxes is via the "withholding method". This method will not only reduce or eliminate any most interest and penalty charges but will also reduce the amount you owe at year end more effectively. Out of pocket, out of mind is what I say!

Alternatively, making quarterly estimated tax payments (federal and state) is difficult to remember and often can result in significant over and underpayments at year end. In addition, the most effective payment is the April 15th one while the least effective payment is the one due January 15th of the following year. Paying most of your taxes in the fourth quarter is almost totally ineffective while making the April payment is made during a period when little information is known for that year.

I hope this information has been helpful. I look forward to hearing from you again this year!

Sincerely,

Stephen B. Smith, CPA