



Department of the Treasury
Internal Revenue Service

Publication 553

(Rev. June 2009)
Cat. No. 39297R

Highlights of 2008 Tax Changes



Get forms and other information
faster and easier by:

Internet www.irs.gov

Volume 1

Contents

Topic	Regular Page	Large Print Page
Introduction	1	5
Chapter		
1. Tax Changes for Individuals	2	9
2. Tax Changes for Businesses	17	67
3. IRAs and Other Retirement Plans	25	101
4. Estate and Gift Taxes	29	116
5. Excise Taxes	29	117
6. Foreign Issues	31	124
7. How To Get Tax Help	33	129
Index	36	139

This page intentionally left blank.

Introduction

This publication highlights major tax law changes that take effect in 2008, 2009, and later years, except those covered in Publication 4492-A, Information for Taxpayers Affected by the May 4, 2007, Kansas Storms and Tornadoes; and in Publication 4492-B, Information for Affected Taxpayers in the Midwestern Disaster Areas. The chapters are divided into sections based on when the changes take effect.

Tax relief for the Kansas disaster area.

Publication 4492-A explains the temporary tax relief provided by the Food, Conservation, and Energy Act of 2008 for taxpayers in Kiowa County, Kansas, and the surrounding areas who were affected by the storms and tornadoes that began on May 4, 2007.

Special tax relief provisions apply for:

- Casualty and theft losses,
- Net operating losses,
- Replacement period for nonrecognition of gain,
- IRAs and other retirement plans,
- Special depreciation allowance,
- Section 179 expense deduction,
- Demolition and clean-up costs, and
- Employee retention credit.

For more information, see Publication 4492-A.

Tax relief for the Midwestern disaster areas.

Publication 4492-B explains the major provisions of the Heartland Disaster Tax Relief Act of 2008 that were provided for taxpayers in Midwestern disaster areas. Midwestern disaster areas are those areas for which a major disaster was declared by the President during the period beginning on May 20, 2008, and ending on July 31, 2008, in the states of Arkansas, Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, and Wisconsin, as a result of severe storms, tornadoes, or flooding that occurred on the applicable disaster date.

Some of the special tax relief provisions are:

- Casualty and theft losses,
- Charitable giving incentives,
- Net operating losses,
- Replacement period for nonrecognition of gain,
- IRAs and other retirement plans,
- Education credits,
- Exclusion of certain cancellations of indebtedness,
- Demolition and clean-up costs, and
- Employee retention credit.

For more information, see Publication 4492-B.



The tax information for 2008 and later years is accurate as of June 30, 2009. Subsequent changes to the tax law may occur. For more information, go to www.irs.gov/formspubs.

Adjusting your withholding or estimated tax payments for 2009. If your tax for 2009 will be more or less than your 2008 tax, you may need to adjust your withholding or estimated tax payments accordingly. If your tax will decrease, you can get the benefit of lower taxes throughout the year. If you will owe more tax, you can avoid a penalty when you file your tax return.

See the following table for forms and publications that will help you adjust your withholding or estimated tax payments. See chapter 7 for information on ordering forms and publications.

To adjust your...	Get Form...	And Publication...
Withholding	W-4 , Employee's Withholding Allowance Certificate	919 , How Do I Adjust My Tax Withholding?
Estimated tax payments	1040-ES , Estimated Tax for Individuals	505 , Tax Withholding and Estimated Tax

Photographs of missing children. The Internal Revenue Service is a proud partner with the National Center for Missing and Exploited Children.

Photographs of missing children selected by the Center may appear in this publication on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling **1-800-THE-LOST (1-800-843-5678)** if you recognize a child.

Comments and suggestions. We welcome your comments about this publication and your suggestions for future editions.

You can write to us at the following address:

Internal Revenue Service
Business Forms and Publications Branch
SE:W:CAR:MP:T:B
1111 Constitution Ave. NW, IR-6526
Washington, DC 20224

We respond to many letters by telephone. Therefore, it would be helpful if you would include your daytime phone number, including the area code, in your correspondence.

You can email us at ["taxforms@irs.gov"](mailto:taxforms@irs.gov). (The asterisk must be included in the address.) Put "Publications Comment" on the subject line.

Although we cannot respond individually to each email, we do appreciate your feedback and will consider your comments as we revise our tax products.

1.

Tax Changes for Individuals

Note. Some of the changes listed in this section apply to both individuals and businesses.

2008 Changes

Recovery Rebate Credit

This credit is figured like last year's economic stimulus payment, except that your 2008 tax information is used to figure this credit. Your 2007 tax information was used to figure your economic stimulus payment. The maximum credit is \$600 (\$1,200 if married filing jointly) plus \$300 for each qualifying child.

You may be able to take this credit only if:

- You did not get an economic stimulus payment,
or

- Your economic stimulus payment was less than \$600 (\$1,200 if married filing jointly for 2007), plus \$300 for each qualifying child you had for 2008.

For more information, see the instructions for Form 1040, line 70; Form 1040A, line 42; or Form 1040EZ, line 9.

Federally Declared Disasters

New rules apply to losses of personal use property attributable to federally declared disasters declared in tax years beginning after 2007 and that occurred before 2010. A federally declared disaster is any disaster determined by the President of the United States to warrant assistance by the Federal Government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act. A disaster area is the area determined to warrant such assistance. The new rules discussed here do **not** apply to losses in the Midwestern disaster areas.

The new rules are as follows.

1. The net disaster loss (defined in (3) below) is not subject to the 10% of adjusted gross income (AGI) limit.

2. You can deduct a net disaster loss even if you do not itemize your deductions on Schedule A (Form 1040). You do this by completing Form 4684, Casualties and Thefts, and entering your net disaster loss on line 6 of the *Standard Deduction Worksheet-Line 40* in the Form 1040 Instructions.
3. Your net disaster loss is the excess of—
 - a. Your personal casualty losses attributable to a federally declared disaster and occurring in a disaster area, over
 - b. Your personal casualty gains.

For more information, see Form 4684.

Special Rules for Individuals Impacted by Hurricanes Katrina, Rita, and Wilma

If you claimed a casualty or theft loss deduction and in a later year you received more reimbursement than you expected, you generally do not recompute the tax for the year in which you claimed the deduction.

Instead, you must include the reimbursement in your income for the year in which it was received, but only to the extent the original deduction reduced your tax for the earlier year. **However**, an exception applies if you claimed a casualty or theft loss deduction for damage to or destruction of your main home caused by Hurricane Katrina, Rita, or Wilma, and in a later

year you received a hurricane relief grant. Under this exception, you can choose to file an amended income tax return (Form 1040X) for the tax year in which you claimed the deduction (and for any tax year to which such deduction was included in a net operating loss carryback or carryforward) and reduce (but not below zero) the amount of the deduction by the amount of the grant. If you choose to file an amended return reducing the prior deduction, any underpayment of tax resulting from the reduced deduction will not be subject to any penalty or interest as long as the additional tax is paid not later than 1 year after the filing of the amended return. If you make this choice, you must file Form 1040X by the later of:

- The due date for filing your tax return for the tax year in which you receive the grant (including extensions), or
- July 30, 2009.

For special filing procedures you must follow and more information, see Publication 547, *Casualties, Disasters, and Thefts*.

Alternative Minimum Tax (AMT)

The following changes to the AMT went into effect for 2008. For more information, see Form 6251, *Alternative Minimum Tax-Individuals*, and its instructions.

AMT exemption amount increased. The AMT exemption amount has increased to \$46,200 (\$69,950 if married filing jointly or qualifying widow(er); \$34,975 if married filing separately).

AMT exemption amount for a child. The AMT exemption amount is now limited for certain children under age 24. (Before 2008, the limit applied to children under 18.) The minimum exemption amount for a child has increased to \$6,400.

Tax-exempt interest on certain housing bonds exempt from AMT. Tax-exempt interest on the following bonds is not an item of tax preference and therefore is not subject to the AMT if the bonds were issued after July 30, 2008.

- An exempt facility bond for which 95% or more of the net proceeds are to be used to provide qualified residential rental projects.
- A qualified mortgage bond.
- A qualified veterans' mortgage bond.

This treatment also applies to interest on any refunding bond if the bond being refunded (or, in the case of a series of refunded bonds, the original bond) is one of the bonds listed above issued after July 30, 2008.

Special depreciation allowance for qualified disaster assistance property allowed against AMT.

No AMT adjustment is required for depreciation of qualified disaster assistance property that is eligible for the special depreciation allowance.

Qualified disaster loss. The 90% limit on the alternative tax net operating loss deduction (ATNOLD) does not apply to the portion of an ATNOLD attributable to qualified disaster losses.

Increase in standard deduction for net disaster loss allowed for AMT. If you claimed the standard deduction for the regular tax and it includes a net disaster loss attributable to a federally declared disaster, that net disaster loss is also allowable as a deduction for the AMT.

Kansas disaster area. The following benefits for the Kansas disaster area apply to the AMT.

- No AMT adjustment is required for depreciation of qualified recovery assistance property that is eligible for the special depreciation allowance.
- The 90% limit on the ATNOLD does not apply to the portion of an ATNOLD attributable to qualified recovery assistance losses.

Midwestern disaster areas. The following benefits for the Midwestern disaster areas apply to the AMT.

- The exemption amount on Form 8914 that is allowable for the regular tax if you provided housing for a person displaced by the Midwestern severe storms, tornadoes, and flooding is also allowable for the AMT.
- The interest on qualified Midwestern disaster area bonds is not a tax preference item. Do not include it on Form 6251, line 12.
- The 90% limit on the ATNOLD does not apply to the portion of an ATNOLD attributable to qualified disaster recovery assistance losses.

Maximum Tax Rate on Qualified Dividends and Net Capital Gain Reduced

For tax years beginning after 2007, the 5% maximum tax rate on qualified dividends and net capital gain (the excess of net long-term capital gain over net short-term capital loss) is reduced to 0%. This reduction applies for both regular tax and AMT. The 15% maximum tax rate on qualified dividends and net capital gain has not changed.

Investment Income of Certain Children

Increase in age of children whose investment income is taxed at parent's rate. The rules regarding the age of a child whose investment income may be taxed at the parent's tax rate have changed for 2008. These rules continue to apply to a child under age 18

at the end of the year but, beginning in 2008, will also apply in certain cases to a child who either:

- Was age 18 at the end of 2008 and did not have earned income that was more than half of the child's support, or
- Was a full-time student over age 18 and under age 24 at the end of 2008 and did not have earned income that was more than half of the child's support.

A student is a child who during any part of 5 calendar months of the year was enrolled as a full-time student at a school, or took a full-time, on-farm training course given by a school or a state, county, or local government agency. A school includes a technical, trade, or mechanical school. It does not include an on-the-job training course, correspondence school, or school offering courses only through the Internet.

Form 8615 is used to figure the child's tax. These rules also apply to parents who elect on Form 8814 to report their child's income on the parents' return.

Increase in investment income amount. The amount of taxable investment income these children can have with-out it being subject to tax at the parent's rate has increased to \$1,800 for 2008.

Standard Mileage Rate

Business-related mileage. For 2008, the standard mileage rate for the cost of operating your car for business use is:

- 50½ cents per mile for the period January 1 through June 30, 2008, and
- 58½ cents per mile for the period July 1 through December 31, 2008.

Car expenses and use of the standard mileage rate are explained in chapter 4 of Publication 463, *Travel, Entertainment, Gift, and Car Expenses*.

Medical- and move-related mileage. For 2008, the standard mileage rate for the cost of operating your car for medical reasons or as part of a deductible move is:

- 19 cents per mile for the period January 1 through June 30, 2008, and
- 27 cents per mile for the period July 1 through December 31, 2008.

See *Transportation* under *What Medical Expenses Are Includable* in Publication 502, *Medical and Dental Expenses*, or *Travel by car* under *Deductible Moving Expenses* in Publication 521, *Moving Expenses*.

Charitable-related mileage. For 2008, the standard mileage rate for the cost of operating your car for charitable purposes remains 14 cents per mile.

Earned Income Credit (EIC) Amounts Increased

The following paragraphs explain the changes to the credit for 2008. For details, see Publication 596, Earned Income Credit (EIC).

Amount of credit increased. The maximum amount of the credit has increased. The most you can get for 2008 is:

- \$2,917 if you have one qualifying child,
- \$4,824 if you have more than one qualifying child, or
- \$438 if you do not have a qualifying child.

Earned income amount increased. The maximum amount of income you can earn and still get the credit has increased for 2008. You may be able to take the credit if:

- You have more than one qualifying child and you earn less than \$38,646 (\$41,646 if married filing jointly),
- You have one qualifying child and you earn less than \$33,995 (\$36,995 if married filing jointly), or

- You do not have a qualifying child and you earn less than \$12,880 (\$15,880 if married filing jointly).

The maximum amount of AGI you can have and still get the credit also has increased. You may be able to take the credit if your AGI is less than the amount in the above list that applies to you.

Investment income amount increased. The maximum amount of investment income you can have and still get the credit has increased to \$2,950 for 2008.

Standard Deduction Increased

The standard deduction for people who do not itemize their deductions on Schedule A (Form 1040) is, in most cases, higher for 2008 than it was for 2007. In addition to the annual increase due to inflation adjustments, your 2008 standard deduction is increased by:

- Any state or local real estate taxes you paid that would be deductible on Schedule A if you were itemizing deductions, up to \$500 (\$1,000 if married filing jointly), and
- Any net disaster loss from a federally declared disaster.

You can figure your 2008 standard deduction by using the 2008 Standard Deduction Worksheet in Publication 501, Exemptions, Standard Deduction, and Filing Information.

Personal Exemption Amount Increased

The amount you can deduct for each exemption has increased to \$3,500 for 2008.

You lose part of the benefit of your exemptions if your AGI is above a certain amount. The amount at which the phaseout begins depends on your filing status. For 2008, the phaseout begins at:

- \$119,975 for married persons filing separately,
- \$159,950 for single individuals,
- \$199,950 for heads of households, and
- \$239,950 for married persons filing jointly or qualifying widow(er)s.

Beginning in 2008, you can lose no more than $\frac{1}{3}$ of the dollar amount of your exemptions. In other words, each exemption cannot be reduced to less than \$2,333.

If your AGI is more than the amount shown for your filing status, use the *Deduction for Exemptions Worksheet* in the Form 1040 or Form 1040A instructions to figure the amount you can deduct for exemptions.

Exemption for individual displaced by Midwestern disaster. You may be able to claim a \$500 exemption if you provided housing to a person displaced by a Midwestern disaster. For more information, see Publication 4492-B.

Tuition and Fees Deduction

Beginning in 2008, the definition of qualified education expenses for the tuition and fees deduction for students attending an eligible educational institution in the Midwestern disaster areas in the states of Arkansas, Illinois, Indiana, Iowa, Missouri, Nebraska, and Wisconsin is expanded. See Table 3-2 near the end of chapter 3 in Publication 970, Tax Benefits for Education, for a list of counties. For more information about the tuition and fees deduction, see chapter 6 in Publication 970.

Income Limits Increased for Student Loan Interest Deduction

For 2008, the amount of the student loan interest deduction is phased out (gradually reduced) if your filing status is married filing jointly and your modified AGI is between \$115,000 and \$145,000. You cannot take the deduction if your modified AGI is \$145,000 or more.

For all other filing statuses, your student loan interest deduction is phased out if modified AGI is between \$55,000 and \$70,000. You cannot take a deduction if your modified AGI is \$70,000 or more. For more information, see chapter 4 in Publication 970.

First-Time Homebuyer Credit

If you are a first-time homebuyer, you may be able to claim a one-time tax credit equal to the lesser of:

- \$7,500 (\$8,000 if you purchased your home in 2009), but only half of that amount if married filing separately, or
- 10% of the purchase price of your home.

You may be able to claim the credit if:

- You purchased your main home in the United States after April 8, 2008, and before December 1, 2009, and
- You (and your spouse if married) did not own any other main home during the 3-year period ending on the date of purchase.

If you constructed your main home, you are treated as having purchased it on the date you first occupied it.

Who cannot claim the credit. You cannot claim the credit if any of the following apply.

1. Your modified AGI is \$95,000 or more (\$170,000 or more if married filing jointly).
2. You are, or were, eligible to claim the District of Columbia first-time homebuyer credit for any taxable year. See Form 8859. This rule does not apply for a home purchased in 2009.
3. Your home financing comes from tax-exempt mortgage revenue bonds. This rule does not apply for a home purchased in 2009.
4. You are a nonresident alien.
5. Your home is located outside the United States.
6. You sell the home, or it ceases to be your main home, before the end of 2008.
7. You acquired your home by gift or inheritance.
8. You acquired your home from a related person. A related person includes:
 - a. Your spouse, ancestors (parents, grandparents, etc.), or lineal descendants (children, grandchildren, etc.).
 - b. A corporation in which you directly or indirectly own more than 50% in value of the outstanding stock of the corporation.

- c. A partnership in which you directly or indirectly own more than 50% of the capital interest or profits interests.

Repayment of credit. The following information is a brief overview concerning the repayment of the first-time homebuyer credit.

Homes purchased in 2008. You generally must repay the credit over a 15-year period in 15 equal installments. The repayment period begins in 2010 and you must include the first installment as additional tax on your 2010 tax return.

If your home ceases to be your main home before the 15-year period is up, you must include all remaining annual installments as additional tax on the return for the tax year that happens. This includes situations where you sell the home, you convert it to business or rental property, or the home is destroyed, condemned, or disposed of under threat of condemnation.

Homes purchased in 2009. You must repay the credit only if the home ceases to be your main home within the 36-month period beginning on the purchase date. This includes situations where you sell the home, you convert it to business or rental property, or the home is destroyed, condemned, or disposed of under threat of condemnation. You repay the credit by including it as additional tax on the return for the year

the home ceases to be your main home. If the home continues to be your main home for at least 36 months beginning on the purchase date, you do not have to repay any of the credit.

More information. For exceptions to the repayment rule, more information about the credit, and how to claim the credit, see Form 5405, First-Time Homebuyer Credit.

Hope and Lifetime Learning Credits

Beginning in 2008, the following changes apply to the Hope and lifetime learning (education) credits. For more information, see chapters 2 and 3 in Publication 970.

Income limits for credit reduction increased. For 2008, the amount of your Hope or lifetime learning credit is phased out (gradually reduced) if your modified AGI is between \$48,000 and \$58,000 (\$96,000 and \$116,000 if you file a joint return). You cannot claim an education credit if your modified AGI is \$58,000 or more (\$116,000 or more if you file a joint return).

Hope credit. Beginning in 2008, the amount of the Hope credit (per eligible student) is the sum of:

1. 100% of the first \$1,200 (\$2,400 if a student in a Midwestern disaster area) of qualified education expenses you paid for the eligible student, and
2. 50% of the next \$1,200 (\$2,400 if a student in a Midwestern disaster area) of qualified education expenses you paid for that student.

The maximum amount of Hope credit you can claim in 2008 is \$1,800 (\$3,600 if a student in a Midwestern disaster area) per student.

Students in Midwestern disaster areas. The following rules apply only to students attending an eligible educational institution in the Midwestern disaster areas in the states of Arkansas, Illinois, Indiana, Iowa, Missouri, Nebraska, and Wisconsin. See Table 3-2 near the end of chapter 3 in Publication 970 for a list of counties.

- **Hope credit increased.** The Hope credit for students in Midwestern disaster areas is 100% of the first \$2,400 of qualified education expenses and 50% of the next \$2,400 of qualified education expenses for a maximum credit of \$3,600 per student. See chapter 2 of Publication 970 for more information.

- **Lifetime learning credit increased.** The lifetime learning credit rate for students in Midwestern disaster areas is 40% of qualified expenses paid, with a maximum credit of \$4,000 allowed on your return.

See chapter 3 of Publication 970 for more information.

- **Definition of qualified expenses expanded.** The definition of qualified education expenses for the education credits is expanded for students in Midwestern disaster areas. See chapters 2 and 3 of Publication 970 for more information.

Reduction in Earned Income Needed to Claim Additional Child Tax Credit

For 2008, the amount your earned income must exceed to claim the additional child tax credit is reduced to \$8,500.

Residential Energy Credits

Nonbusiness energy property credit expired. You can-not claim the nonbusiness energy property credit for property placed in service in 2008.

Residential energy efficient property credit expanded. You can now include costs for qualified small wind energy property and geothermal heat pump

property in figuring the residential energy efficient property credit.

Limits Increased for Itemized Deductions

If your AGI is above a certain amount, you may lose part of your itemized deductions. In 2008, this amount is increased to \$159,950 (\$79,975 if married filing separately). See the instructions for Schedule A (Form 1040), line 29, for more information on figuring the amount you can deduct.

Deduction for Credit or Debit Card Convenience Fees

If you pay your income tax (including estimated tax payments) by credit or debit card, you can deduct the convenience fee you are charged by the card processor to pay using your credit or debit card. The deduction is claimed for the year in which the fee was charged to your card as a miscellaneous itemized deduction on line 23 of Schedule A (Form 1040) (and is subject to the 2% of AGI floor).

Definition of "Qualified Military Benefit" Expanded

A "qualified military benefit" generally means any excludable allowance or other in-kind benefit (other than personal use of a vehicle) received by a member or former member of the uniformed services of the

United States or the dependent of such a member because of the member's status or service as a member of such services. The definition of qualified military benefit has been expanded to include payments by a state or a political subdivision thereof to a member or former member of the uniformed services of the United States or to a dependent of such a member if the payments are made only because of the member's service in a combat zone. See Publication 3, Armed Forces' Tax Guide, for more information about qualified military benefits.

Exclusion on Sale of Main Home

Surviving spouse. For sales after 2007, the maximum exclusion on the sale of a main home by an unmarried surviving spouse is \$500,000 if the sale occurs no later than 2 years after the date of the other spouse's death. However, this rule applies only if the requirements for joint filers relating to ownership and use were met immediately before the date of such death, and during the 2-year period ending on the date of such death, there was no sale or exchange of a main home by either spouse which qualified for the exclusion.

Employees and volunteers of the Peace Corps. If you or your spouse is an employee, enrolled volunteer, or volunteer leader of the Peace Corps, you may be able to exclude from income a gain from

selling your main home, even if you did not live in it for 2 years during the 5-year period ending on the date of sale. Generally, you can elect to have the 5-year test period for ownership and use suspended for up to 10 years during any period you or your spouse serve outside the United States (on qualified official extended duty if an employee). This provision applies to a sale of a main home in tax years beginning after 2007. Similar benefits already apply to members of the uniformed services or Foreign Service or employees of the intelligence community. For more information, see Publication 523, *Selling Your Home*.

Discharge of Qualified Principal Residence Indebtedness

The Emergency Economic Stabilization Act of 2008 extended the exclusion from gross income for the discharge of qualified principal residence indebtedness by an additional 3 years. The exclusion now applies to debt discharged after 2006 and before 2013. See Form 982, *Reduction of Tax Attributes Due to Discharge of Indebtedness* (and Section 1082 Basis Adjustment), and Publication 4681, *Canceled Debts, Foreclosures, Repossessions, and Abandonments* (for Individuals), for more information.

Like-Kind Exchanges

Beginning with exchanges completed after May 22, 2008, the exchange of stock in a mutual ditch, reservoir, or irrigation company may qualify for the nonrecognition of gain or loss under section 1031.

The nonrecognition of gain or loss on the exchange may apply if, at the time of the exchange:

1. The company is a section 501(c)(1 2)(A) organization (determined without regard to the percentage of in-come collected from members for the purpose of meeting losses and expenses), and
2. The shares of stock in the company have been recognized by the highest court in the state in which the company was organized or by an applicable statute of that state as constituting or representing real property or an interest in real property.

Health Savings Accounts (HSAs)

High deductible health plan (HDHP). For HSA purposes, the minimum annual deductible of an HDHP re-mains at \$1,100 (\$2,200 for family coverage) and the maximum annual deductible and other out-of-pocket expenses limit increased to \$5,600 (\$11,200 for family cover-age).

Limit on contributions. The maximum HSA contribution increases to \$2,900 (\$5,800 for family coverage). The maximum contribution for individuals age 55 or older increased to \$900.

Health Flexible Spending Arrangements (FSAs)

A special rule allows amounts in a health FSA to be distributed to reservists ordered or called to active duty. This rule applies to distributions after June 17, 2008, if the plan has been amended to allow these distributions. A qualified reservist distribution is allowed if:

1. The individual was, by reason of being a member of a reserve component, ordered or called to active duty for a period in excess of 179 days or for an indefinite period, and
2. The distribution is made during the period beginning on the date of such order or call and ending on the last date that reimbursements could be made for the plan year which includes the date of such order or call.

For more information, see Publication 969, Health Savings Accounts and Other Tax-Favored Health Plans.

Adoption Benefits Increased

For 2008, the maximum adoption credit has increased to \$11,650. Also, the maximum exclusion from income for benefits under your employer's adoption assistance program has increased to \$11,650. These amounts are phased out if your modified AGI is between \$174,730 and \$214,730. You cannot claim the credit or exclusion if your modified AGI is \$214,730 or more. See Form 8839, Qualified Adoption Expenses, and its instructions for more information.

Income Limits Increased for Reduction of Education Savings Bond Exclusion

For 2008, the amount of your interest exclusion is phased out (gradually reduced) if your filing status is married filing jointly or qualifying widow(er) and your modified AGI is between \$100,650 and \$130,650. You cannot take the deduction if your modified AGI is \$130,650 or more.

For all other filing statuses, your interest exclusion is phased out if your modified AGI is between \$67,100 and \$82,100. You cannot take a deduction if your modified AGI is \$82,100 or more. For more information, see chapter 9 in Publication 970.

Increase in Deductible Limit for Long-Term Care Premiums

For 2008, the maximum amount of qualified long-term care premiums you can include as medical expenses has increased. You can include qualified long-term care premiums, up to the amounts shown below, as medical expenses on Schedule A (Form 1040).

- Age 40 or under - \$310.
- Age 41 to 50 - \$580.
- Age 51 to 60 - \$1,150.
- Age 61 to 70 - \$3,080.
- Age 71 or over - \$3,850. **Note.** The limit is for each person.

Increase in Limit on Long-Term Care and Accelerated Death Benefits Exclusion

The limit on the exclusion for payments made on *a per diem* or other periodic basis under a long-term care insurance contract increases for 2008 to \$270 per day. The limit applies to the total of these payments and any accelerated death benefits made on *a per diem* or other periodic basis under a life insurance contract because the insured is chronically ill.

Under this limit, the excludable amount for any period is figured by subtracting any reimbursement received (through insurance or otherwise) for the cost of qualified long-term care services during the period from the larger of the following amounts.

- The cost of qualified long-term care services during the period.
- The dollar amount for the period (\$270 per day for any period in 2008).

See section C of Form 8853, Archer MSAs and Long-Term Care Insurance Contracts, and its instructions for more information.

Archer Medical Savings Accounts (MSAs)

Expiration of Archer MSAs. After 2007, you cannot be treated as an eligible individual for Archer MSA purposes unless:

- You were an active participant for any taxable year ending before 2008, or
- You became an active participant for a tax year ending after 2007 by reason of coverage under a high deductible health plan of an Archer MSA participating employer.

Limits increased. For Archer MSA purposes, the minimum annual deductible of a high deductible health plan increased to \$1,950 (\$3,850 for family coverage). The maximum annual deductible of a high deductible health plan increased to \$2,900 (\$5,800 for family coverage). The maximum out-of-pocket expenses limit increased to \$3,850 (\$7,050 for family coverage).

Credit for Prior Year Minimum Tax

The following changes to the credit for prior year minimum tax went into effect for 2008. For more information, see Form 8801, Credit for Prior Year Minimum Tax-Individuals, Estates, and Trusts, and its instructions.

Decrease in credit for abatement of alternative mini-mum tax (AMT) related to incentive stock options (ISOs). If you owed AMT for 2007 or any prior year due to the AMT adjustment for the exercise of ISOs (Form 6251, line 13, for 2007), the amount of any such tax that you still owed as of October 3, 2008, has been abated. This means that your debt has been forgiven and you no longer owe this tax. However, you must reduce the amount of your credit for prior year minimum tax.

Increase in credit for interest and penalties related to ISO adjustments. If you paid interest and penalties on AMT for 2007 or any prior year due to the AMT adjustment for the exercise of ISOs, the amount of your prior year minimum tax that is eligible for the credit is increased for the first 2 years beginning after 2007 by 50% of the total of any such interest and penalties you paid before October 3, 2008.

Refundable credit for prior year minimum tax. The calculation of the tentative refundable credit (Form 8801, Part IV) has been revised to reflect changes made by the Tax Extenders and Alternative Minimum Tax Relief Act of 2008.

Foreign Earned Income Tax Worksheet revised. The *Foreign Earned Income Tax Worksheet* on page 2 of the Instructions for Form 8801 has been revised to reflect changes made by the Tax Technical Corrections Act of 2007.

Exclusion of Income for Volunteer Firefighters and Emergency Medical Responders

For tax years beginning after 2007 and before 2011, gross income does not include:

- Rebates or reductions of property or income taxes provided by a state or local government for providing services as a member of a qualified

emergency response organization (defined below). Any such re-bate or reduction reduces the amount of the income tax deduction for such taxes.

- Qualified payments made by a state or local government for providing services as a member of a qualified emergency response organization. The exclusion is limited to \$30 multiplied by the number of months the member performs such services. A charitable deduction for expenses paid by the member in connection with performing such services must be reduced by any payment excluded from income.

A qualified volunteer emergency response organization is any volunteer organization organized and operated to provide firefighting or emergency medical services for persons in a state or local jurisdiction and required by written agreement with that state or local jurisdiction to furnish such services.

Exclusion from wages. You can exclude any qualified state or local tax benefit and any qualified reimbursement payment from the employee's wages. The excluded wages are not subject to federal income tax withholding, social security and Medicare taxes, and federal unemployment tax.

Social Security and Medicare Taxes

The maximum amount of wages subject to the social security tax for 2008 is \$102,000. There is no limit on the amount of wages subject to the Medicare tax.

Wage Threshold for Household Employees

The social security and Medicare wage threshold for household employees is \$1,600 for 2008. This means that if you pay a household employee cash wages of less than \$1,600 in 2008, you do not have to report and pay social security and Medicare taxes on that employee's 2008 wages. For more information, see *Social security and Medicare wages* in Publication 926, Household Employer's Tax Guide.

Special Limitation Period for Retroactively Excluding Military Retirement Pay

If you retire from the armed services based on years of service and are later given a retroactive service-connected disability rating by the VA, your retirement pay for the retroactive period is excluded from income up to the amount of VA disability benefits you would have been entitled to receive. You can claim a refund of any tax paid on the excludable amount (subject to the statute of limitations) by filing an amended return on Form 1040X for each previous year during the retroactive period.

Generally, under the statute of limitations a claim for credit or refund must be filed within 3 years from the time a return was filed or 2 years from the time the tax was paid, whichever period expires later. However, if you receive a retroactive service-connected disability rating determination, the statute of limitations is extended for 1 year beginning on the date of the determination. The extension applies to claims for credit or refund filed after June 17, 2008, and does not apply to any tax year that began more than 5 years before the date of the determination.

Example. You retired in 2003 and receive a pension based on your years of service. On August 6, 2008, you receive a determination of service-connected disability retroactive to 2003. Generally, you could claim a refund for the taxes paid on your pension for 2005, 2006, and 2007. However, under the special limitation period, you can also file a claim for 2004 as long as you file the claim by August 5, 2009. You cannot file a claim for 2003 because that tax year began on January 1, 2003, which is more than 5 years before date of the determination.

Transition rules. If you received a retroactive service-connected disability rating determination after 2000 and before June 18, 2008, you have until June 17, 2009, to file your claims. You cannot make any claims for tax years that began before 2001.

Income Averaging for Farmers and Fishermen

Exxon Valdez litigation. If you received qualified settlement income made up of interest and punitive damages in connection with the civil action *In re Exxon Valdez*, No. 89-095-CV (HRH) (Consolidated) (D. Alaska), you may treat this settlement payment as income from a fishing business for the purpose of income averaging. You are eligible to make this election only if you are a plaintiff in the civil action or you were a beneficiary of the estate of your spouse or a close relative who was such a plaintiff from whom you acquired the right to receive qualified settlement income. See the Instructions for Schedule J (Form 1040).

New rules for averaging farming and fishing income. The four items discussed below are effective for tax years beginning after July 22, 2008. However, you may apply any of these provisions to tax years beginning after 2003 and before July 23, 2008, if those provisions are consistently applied in each tax year. For more information, see Treasury Decision 9417, 2008-37 I.R.B. 693, available at www.irs.gov/irb/2008-37_IRB/ar07.html.

Farming and fishing business. If you operate both a farming and fishing business, you combine the income, gains, deductions, and losses from both

businesses to figure the amount of income eligible for income averaging.

Lessors of fishing boats. You are treated as being in a fishing business if you lease a boat and your lease payments are based on a share of the catch (or a share of the proceeds from the sale of the catch) from the lessee's use of the boat, but only if this manner of payment is determined under a written lease agreement entered into before the lessee begins significant fishing activities resulting in the catch.

Crewmembers on fishing boats. Crew members on a commercial fishing vessel are engaged in the fishing business for purposes of income averaging if their compensation is based on a share of the boat's catch or a share of the proceeds from the sale of the catch. The compensation of such a crew member is treated as income from a fishing business, whether or not he or she is treated as an employee for employment tax purposes.

Merchant Marine Capital Construction Fund (CCF) deposits. If you reduced your taxable income on Form 1040, line 43, or Form 1040NR, line 40, by any amount deposited into a CCF account, take into account the CCF reduction in figuring taxable income for income averaging purposes. Also, the CCF reduction is generally treated as a deduction attributable to your fishing business in figuring elected farm income. However, if any taxable income (without

regard to the carryback of any net operating or net capital loss) from the operation of agreement vessels in the fisheries of the United States or in the foreign or domestic commerce of the United States is not attributable to your fishing business, that amount does not reduce elected farm income.

Failure To File Income Tax Return Penalty Increased

If you do not file your return by the due date (including extensions) you may have to pay a failure-to-file penalty. For income tax returns required to be filed after 2008, the failure-to-file penalty for returns filed more than 60 days after the due date (including extensions) is increased. In this situation, the minimum penalty is the smaller of \$135 or 100% of the unpaid tax.

2009 Changes

Economic Recovery Payment

Any economic recovery payment you receive during 2009 is not taxable. These \$250 payments are being made to most people who:

- Receive social security benefits, supplemental security income (SSI), railroad retirement benefits, or veterans disability compensation or pension benefits, and

- Live in a U.S. state, the District of Columbia, Puerto Rico, Guam, the U.S. Virgin Islands, American Samoa, or the Northern Mariana Islands.

If you are married and you and your spouse both meet these requirements, each of you may get a \$250 payment.

If you are entitled to a payment, you will get it automatically. You do not need to apply for it.

Making Work Pay and Government Retiree Credits

Two new credits you may be able to take for 2009 are the:

- Making work pay credit, and
- Government retiree credit.

Making work pay credit. You may be able to take this credit if you have earned income from work. Even if your federal income tax withholding is reduced during 2009 because of the credit, you must claim the credit on your return to benefit from it.

You cannot take the credit if:

- Your modified AGI is \$95,000 (\$190,000 if married filing jointly) or more,

- You are a nonresident alien, or
- You can be claimed as a dependent on someone else's return.

The credit is 6.2% of your earned income but cannot be more than \$400 (\$800 if married filing jointly). The credit will be reduced if:

- You receive a \$250 economic recovery payment (described earlier) during 2009,
- Your modified AGI is more than \$75,000 (\$150,000 if married filing jointly), or
- You take the government retiree credit discussed next.

Government retiree credit. You can take this credit if you receive a pension or annuity payment in 2009 for service performed for the U.S. Government or any U.S. state or local government (or any instrumentality of one or more of these) and the service was not covered by social security. The credit is \$250 (\$500 if married filing jointly and both you and your spouse receive a qualifying pension or annuity). However, you cannot take the credit if you receive a \$250 economic recovery payment during 2009. If you file a joint return, both you and your spouse receive a qualifying pension or annuity, and both of you receive an economic recovery payment, no government retiree credit is allowed; if only one of you receives an economic recovery payment, the credit is \$250.

Social security number. To take either credit, you must include your social security number (if filing a joint return, the number of either you or your spouse) on your return. A social security number does not include an identification number issued by the IRS.

Schedule M. Generally, you will use new Schedule M (Form 1040A or 1040) to figure both the making work pay credit and the government retiree credit. Both credits are refundable, which means they are treated like payments you made and may give you a refund even if you had no tax withheld from your pay or your pension. If you are filing Form 1040EZ, you can take the making work pay credit on that form and do not have to file Schedule M.

More information. If you want to figure now the amount you can expect from these credits, see Worksheet 2-9 in Publication 505.

Hope Credit Expanded

For tax years 2009 and 2010, the following changes have been made to the Hope credit. The modified credit is also referred to as the American opportunity tax credit.

- The maximum amount of the Hope credit increases to \$2,500 per student. The credit is phased out (gradually reduced) if your modified AGI is between \$80,000 and \$90,000 (\$160,000

and \$180,000 if you file a joint return).

Exception. For 2009, if you claim a Hope credit for a student who attended a school in a Midwestern disaster area, you can choose to figure the amount of the credit using the previous rules. However, you must use the previous rules in figuring the credit for all students for which you claim the credit.

- The Hope credit can now be claimed for the first four years of post-secondary education. Previously the credit could be claimed for only the first two years of post-secondary education.
- Generally, 40% of the Hope credit is now a refundable credit, which means that you can receive up to \$1,000 even if you owe no taxes. However, none of the credit is refundable if the taxpayer claiming the credit is a child (a) who is under age 18 (or a student who is at least age 18 and under age 24 and whose earned income does not exceed one-half of his or her own support), (b) who has at least one living parent, and (c) who does not file a joint return.
- The term "qualified tuition and related expenses" has been expanded to include expenditures for "course materials." For this purpose, the term "course materials" means books, supplies, and equipment needed for a course of study whether or not the materials are purchased from the

educational institution as a condition of enrollment or attendance.

For more information, see chapter 2 of Publication 970.

Unemployment Compensation

For any tax year beginning in 2009, each recipient of unemployment compensation can exclude from gross income up to \$2,400 of the amount he or she received during the year.

Alternative Minimum Tax (AMT)

The following changes to the AMT went into effect for 2009.

AMT exemption amount increased. The AMT exemption amount has increased to \$46,700 (\$70,950 if married filing jointly or qualifying widow(er); \$35,475 if married filing separately).

AMT exemption amount for a child increased. The AMT exemption amount for a child whose unearned income is taxed at the parent's tax rate has increased to \$6,700.

Qualified motor vehicle tax allowed against AMT. If you claim the standard deduction for the regular tax and it includes any state or local sales or excise tax on the purchase of a qualified motor vehicle, that tax is also allowed as a deduction for the AMT.

Tax-exempt interest on specified private activity bonds issued in 2009 or 2010 exempt from AMT.

Tax-exempt interest on specified private activity bonds issued in 2009 or 2010 is not an item of tax preference and therefore is not subject to the AMT. A refunding bond is treated as issued on the date of the issuance of the refunded bond (or, in the case of a series of refundings, the original bond). However, tax-exempt interest on a specified private activity bond issued in 2009 or 2010 to currently refund a private activity bond issued after 2003 and before 2009 is not an item of tax preference.

Qualified Transportation Fringe Benefits

Beginning January 1, 2009, the monthly exclusion for commuter highway vehicle transportation and transit passes increased to \$120 and the monthly exclusion for qualified parking increased to \$230. Beginning March 1, 2009, the monthly exclusion for commuter highway vehicle transportation and transit passes increased to \$230.

Beginning January 1, 2009, you may be reimbursed for reasonable expenses of qualified bicycle commuting. Reasonable expenses include the purchase of a bicycle and bicycle improvements, repair, and storage. The exclusion for a calendar year is \$20 multiplied by the number of qualified bicycle commuting months during that year. A qualified

bicycle commuting month is any month you use the bicycle regularly for a substantial portion of the travel between your residence and place of employment and you do not receive any of the other qualified transportation fringe benefits. You are not entitled to this exclusion if the reimbursement for bicycle commuting is made under a compensation reduction agreement.

Definition of Qualifying Child Revised

For 2009, the following changes have been made to the definition of a qualifying child.

- To be your qualifying child, the child must be younger than you.
- A child cannot be your qualifying child if he or she files a joint return, unless the return was filed only as a claim for refund.
- If the parents of a child can claim the child as a qualifying child but no parent so claims the child, no one else can claim the child as a qualifying child unless that person's AGI is higher than the highest AGI of any parent of the child.
- Your child is a qualifying child for purposes of the child tax credit only if you can and do claim an exemption for him or her.

Increase in Investment Income Amount of Certain Children

The amount of taxable investment income a child can have without it being subject to tax at the parent's rate has increased to \$1,900 for 2009.

Standard Mileage Rate

Business-related mileage. For 2009, the standard mileage rate for the cost of operating your car for business use is 55 cents per mile.

Car expenses and use of the standard mileage rate are explained in chapter 4 of Publication 463.

Medical- and move-related mileage. For 2009, the standard mileage rate for the cost of operating your car for medical reasons or as part of a deductible move is 24 cents per mile. See *Transportation* under *What Medical Expenses Are Includable* in Publication 502 or *Travel by car* under *Deductible Moving Expenses* in Publication 521.

Charitable-related mileage. For 2009, the standard mileage rate for the cost of operating your car for charitable purposes remains 14 cents per mile.

Earned Income Credit (EIC) Amounts Increased

The following paragraphs explain the changes to the credit for 2009.

Amount of credit increased. The maximum amount of the credit has increased. The most you can get for 2009 is:

- \$3,043 if you have one qualifying child,
- \$5,028 if you have two qualifying children,
- \$5,657 if you have three or more qualifying children, or
- \$457 if you do not have a qualifying child.

Earned income amount increased. The maximum amount of income you can earn and still get the credit has increased for 2009. You may be able to take the credit if:

- You have three or more qualifying children and you earn less than \$43,279 (\$48,279 if married filing jointly),
- You have two qualifying children and you earn less than \$40,295 (\$45,295 if married filing jointly),
- You have one qualifying child and you earn less than \$35,463 (\$40,463 if married filing jointly), or
- You do not have a qualifying child and you earn less than \$13,440 (\$18,440 if married filing jointly).

The maximum amount of AGI you can have and still get the credit also has increased. You may be able to take the credit if your AGI is less than the amount in the above list that applies to you.

Investment income amount increased. The maximum amount of investment income you can have and still get the credit has increased to \$3,100 for 2009.

Advance payment of the credit. If you get advance payments of the credit from your employer with your pay, the total advance payments you get during 2009 can be as much as \$1,826.

Standard Deduction Increased

The standard deduction for people who do not itemize their deductions on Schedule A (Form 1040) is, in most cases, higher for 2009 than it was for 2008. In addition to the annual increase due to inflation adjustments and the increase allowed for the deduction for certain real estate taxes and a net disaster loss, your 2009 standard deduction is increased by any state or local sales tax imposed on the purchase of a qualified motor vehicle in 2009 after February 16. For details, see *Deduction for Sales and Excise Taxes Imposed on Purchase of New Motor Vehicles*, next. To figure your 2009 standard deduction now, see Worksheet 2-3 in Publication 505.

Deduction for Sales and Excise Taxes Imposed on Purchase of New Motor Vehicles

In 2009, you can deduct the state or local sales and excise taxes imposed on the purchase of a qualified motor vehicle after February 16, 2009, and before 2010. A qualified motor vehicle includes a passenger automobile, light truck, or motorcycle, the original use of which begins with that purchaser and that has a gross vehicle weight rating of 8,500 pounds or less. A qualified motor vehicle also includes a motor home, the original use of which begins with that purchaser. The amount of tax you are able to deduct is limited to the tax that is imposed on the first \$49,500 of the purchase price of the vehicle. The deduction is phased out over a \$10,000 range that begins when modified AGI is more than \$125,000 (\$250,000 if married filing a joint return). No deduction is allowed when modified AGI is equal to or more than \$135,000 (\$260,000 if married filing a joint return). The new deduction can be used to increase the amount of your standard deduction or you can take it as an itemized deduction (if you are not electing to take the state and local general sales tax deduction).

Increase in Personal Casualty and Theft Loss Limit

Generally, a personal casualty or theft loss must exceed \$500 to be allowed for 2009. This is in addition to the 10% of AGI limit that generally applies to the net loss.

Personal Exemption Amount Increased

The amount you can deduct for each exemption has increased to \$3,650 for 2009.

You lose part of the benefit of your exemptions if your AGI is above a certain amount. The amount at which the phaseout begins depends on your filing status. For 2009, the phaseout begins at:

- \$125,100 for married persons filing separately,
- \$166,800 for single individuals,
- \$208,500 for heads of households, and
- \$250,200 for married persons filing jointly or qualifying widow(er)s.

For 2009, each exemption cannot be reduced to less than \$2,433.

See Publication 505 for more information on figuring the amount you can deduct.

New Rules for Children of Divorced or Separated Parents

Revocation of release of claim to an exemption.

For tax years beginning after July 2, 2008 (the 2009 calendar year for most taxpayers), new rules apply to allow the custodial parent to revoke a release of claim to exemption that was previously released to the noncustodial parent on Form 8332, Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent, or similar form. The revocation is effective no earlier than the tax year beginning in the calendar year following the calendar year in which the custodial parent provides, or makes reasonable efforts to provide, the noncustodial parent with written notice of the revocation. Therefore, if the custodial parent provides notice of revocation to the noncustodial parent in 2009, the earliest tax year the revocation can be effective is the tax year beginning in 2010. You can use Part III of Form 8332 for this purpose. You must attach a copy of the revocation to your return for each tax year you claim the child as a dependent as a result of the revocation.

Post-1984 decree or agreement. If the divorce decree or separation agreement went into effect after 1984 and before 2009, the noncustodial parent can still attach certain pages from the decree or agreement instead of Form 8332. For any decree or

agreement executed after 2008, Form 8332 or similar form must be used.

Income Limits Increased for Student Loan Interest Deduction

For 2009, the amount of the student loan interest deduction is phased out (gradually reduced) if your filing status is married filing jointly and your modified AGI is between \$120,000 and \$150,000. You cannot take the deduction if your modified AGI is \$150,000 or more.

For all other filing statuses, your student loan interest deduction is phased out if your modified AGI is between \$60,000 and \$75,000. You cannot take a deduction if your modified AGI is \$75,000 or more. For more information, see chapter 4 in Publication 970.

Income Limits for Lifetime Learning Credit Increased

For 2009, the amount of your lifetime learning credit is phased out (gradually reduced) if your modified AGI is between \$50,000 and \$60,000 (\$100,000 and \$120,000 if you file a joint return). You cannot claim a lifetime learning credit if your modified AGI is \$60,000 or more (\$120,000 or more if you file a joint return). For more information, see chapter 3 in Publication 970.

Expanded Definition of Qualified Expenses for Qualified Tuition Programs

The definition of qualified higher education expenses for tax-free distributions from a qualified tuition program is expanded to include amounts paid in 2009 or 2010 for the purchase of computer software, any computer or related peripheral equipment, fiber optic cable related to computer use, and Internet access (including related services) that are to be used by the beneficiary and the beneficiary's family during any of the years the beneficiary is enrolled at an eligible educational institution.

For more information, including restrictions on qualifying software, see chapter 8 of Publication 970.

Reduction in Earned Income Needed to Claim Additional Child Tax Credit

For 2009, the amount your earned income must exceed to claim the additional child tax credit is reduced to \$3,000.

Residential Energy Credits

Nonbusiness energy property credit. This credit, which expired after 2007, has been reinstated. You may be able to claim a nonbusiness energy property credit of 30% of the cost of certain energy-efficient property or improvements you placed in service in

2009. This property can include high-efficiency heat pumps, air conditioners, and water heaters. It also may include energy-efficient windows, doors, insulation materials, and certain roofs. The credit has been expanded to include certain asphalt roofs and stoves that burn biomass fuel.

Limitation. The total amount of credit you can claim in 2009 and 2010 is limited to \$1,500.

Residential energy efficient property credit.

Beginning in 2009, there is no limitation on the credit amount for qualified solar electric property costs, qualified solar water heating property costs, qualified small wind energy property costs, and qualified geothermal heat pump property costs. The limitation on the credit amount for qualified fuel cell property costs remains the same.

Limits Increased for Itemized Deductions

If your AGI is above a certain amount, you may lose part of your itemized deductions. In 2009, this amount is increased to \$166,800 (\$83,400 if married filing separately).

See Publication 505 for more information on figuring the amount you can deduct.

Sale of Main Home

Gain from the sale or exchange of the main home is no longer excludable from income if allocable to periods of nonqualified use.

Generally, nonqualified use means any period after 2008 where neither you nor your spouse (or your former spouse) used the property as a main home (with certain exceptions).

A period of nonqualified use does not include:

1. Any portion of the 5-year period ending on the date of the sale or exchange that is after the last date you (or your spouse) use the property as a main home;
2. Any period (not to exceed an aggregate period of 10 years) during which you or your spouse is serving on qualified official extended duty:
 - a. As a member of the uniformed services,
 - b. As a member of the Foreign Service of the United States, or
 - c. As an employee of the intelligence community; and
3. Any other period of temporary absence (not to exceed an aggregate period of 2 years) due to change of employment, health conditions, or such other unforeseen circumstances as may be specified by the IRS.

To figure the portion of the gain that is allocated to the period of nonqualified use, multiply the gain by the following fraction:

$$\frac{\text{Total nonqualified use during period of ownership after 2008}}{\text{Total period of ownership}}$$

Health Savings Accounts (HSAs)

High Deductible Health Plan (HDHP). For HSA purposes, the minimum annual deductible of an HDHP increases to \$1,150 (\$2,300 for family coverage) and the maximum annual deductible and other out-of-pocket expenses limit increases to \$5,800 (\$11,600 for family coverage).

Limit on contributions. The maximum HSA contribution increases to \$3,000 (\$5,950 for family coverage). The maximum contribution for individuals age 55 or older increases to \$1,000.

Adoption Benefits Increased

For 2009, the maximum adoption credit has increased to \$12,150. Also, the maximum exclusion from income for benefits under your employer's adoption assistance program has increased to \$12,150. These amounts are phased out if your modified AGI is between \$182,180 and \$222,180. You cannot claim the credit or exclusion if your modified AGI is \$222,180 or more.

Income Limits Increased for Reduction of Education Savings Bond Exclusion

For 2009, the amount of your interest exclusion is phased out (gradually reduced) if your filing status is married filing jointly or qualifying widow(er) and your modified AGI is between \$104,900 and \$134,900. You cannot take the exclusion if your modified AGI is \$134,900 or more.

For all other filing statuses, your interest exclusion is phased out if your modified AGI is between \$69,950 and \$84,950. You cannot take the exclusion if your modified AGI is \$84,950 or more. For more information, see chapter 10 in Publication 970.

Increase in Deductible Limit for Long-Term Care Premiums

For 2009, the maximum amount of qualified long-term care premiums you can include as medical expenses has increased. You can include qualified long-term care premiums, up to the amounts shown below, as medical expenses on Schedule A (Form 1040).

- Age 40 or under - \$320.
- Age 41 to 50 - \$600.
- Age 51 to 60 - \$1,190.
- Age 61 to 70 - \$3,180.
- Age 71 or over - \$3,980.

Note. The limit is for each person.

Increase in Limit on Long-Term Care and Accelerated Death Benefits Exclusion

The limit on the exclusion for payments made on *a per diem* or other periodic basis under a long-term care insurance contract increases for 2009 to \$280 per day. The limit applies to the total of these payments and any accelerated death benefits made on *a per diem* or other periodic basis under a life insurance contract because the insured is chronically ill.

Under this limit, the excludable amount for any period is figured by subtracting any reimbursement received (through insurance or otherwise) for the cost of qualified long-term care services during the period from the larger of the following amounts.

- The cost of qualified long-term care services during the period.
- The dollar amount for the period (\$280 per day for any period in 2009).

See section C of Form 8853 and its instructions for more information.

Archer Medical Savings Accounts (MSAs) Limits Increased

For Archer MSA purposes for 2009, the minimum annual deductible of a high deductible health plan increases to \$2,000 (\$4,000 for family coverage). The maximum annual deductible of a high deductible health plan increases to \$3,000 (\$6,050 for family coverage). The maximum out-of-pocket expenses limit increases to \$4,000 (\$7,350 for family coverage).

Decreased Estimated Tax Payments for Qualified Individuals With Small Businesses

For 2009, qualified individuals with small businesses may be eligible to make smaller estimated tax payments. If you qualify, your required annual payment for 2009 is the smaller of 90% of the tax shown on your 2008 tax return or 90% of the tax shown on your 2009 tax return. You must check box F in Part II on Form 2210 or box C on Form 2210-F to certify that you qualify.

You are a qualified individual if:

- More than 50% of your gross income was from a business that had an average of fewer than 500 employees in 2008, and
- Your AGI in 2008 was less than \$500,000 (\$250,000 if you are filing married filing separately for 2009).

Social Security and Medicare Taxes

The maximum amount of wages subject to the social security tax for 2009 is \$106,800. There is no limit on the amount of wages subject to the Medicare tax.

Wage Threshold for Household Employees

The social security and Medicare wage threshold for household employees is \$1,700 for 2009. This means that if you pay a household employee cash wages of less than \$1,700 in 2009, you do not have to report and pay social security and Medicare taxes on that employee's 2009 wages. For more information, see *Social security and Medicare wages* in Publication 926.

Health Coverage Tax Credit

Increase in the amount of the health coverage tax credit (HCTC). For coverage months beginning after April 2009 and before 2011, the credit increases to 80%.

Payment for monthly premiums paid prior to commencement of advance payments. For coverage months beginning after 2008 and before 2011, newly-enrolled monthly participants will be able to receive a retroactive credit on their HCTC account for qualified health insurance payments they paid while enrolling in the monthly HCTC program.

Note. Although these payments will not begin until August 2009, the credits will apply to any coverage month beginning after 2008.

TAA recipients not enrolled in training programs eligible for credit. For coverage months beginning after February 2009 and before 2011, training and waiver requirements have changed for TAA recipients, making it easier for them to be eligible for the HCTC. Certain individuals who are receiving unemployment compensation (whether or not they meet TAA training requirements) and certain individuals who have a break from training, are now eligible for the HCTC.

Other changes. Effective as of February 17, 2009, qualified health insurance is expanded to include coverage under an employee benefit plan funded by a voluntary employees' beneficiary association.

Individuals receiving COBRA premium assistance are not eligible for the credit for any month that assistance is provided.

2.

Tax Changes for Businesses

2008 Changes

Depreciation and Section 170 Deduction

Increased section 179 limits. The maximum section 179 deduction you can elect for qualified section 179 property you placed in service in tax years that begin in 2008 has increased to \$250,000 (\$285,000 for qualified enterprise zone property and qualified renewal community property). This limit is reduced by the amount by which the cost of section 179 property placed in service in the tax year exceeds \$800,000. For qualified section 179 Gulf Opportunity (GO) Zone property, qualified section 179 recovery assistance property, and qualified section 179 disaster assistance property, the maximum deduction is higher than the deduction for most other section 179 property. See chapter 2 of Publication 946, How to Depreciate Properly.

Depreciation limits on business vehicles. The total depreciation deduction (including the section 179 deduction) you can take for a passenger automobile (that is not a truck or a van) you use in your business and first placed in service in 2008 is \$2,960 (\$10,960 for automobiles for which the special depreciation

allowances applies). The maximum deduction you can take for a truck or a van you use in your business and first placed in service in 2008 is \$3,160 (\$11,160 for trucks or vans for which the special depreciation allowance applies). See chapter 5 of Publication 946.



These limits are reduced if the business use of the vehicle is less than 100%.

Special depreciation allowance for qualified property. You may be able to take an additional first year special depreciation allowance for qualified recovery assistance property, certain qualified property acquired after 2007, qualified reuse and recycling property, qualified cellulosic biofuel plant property, and qualified disaster assistance property placed in service during the tax year. The allowance is an additional deduction of 50% of the property's

Qualified recovery assistance property. A special depreciation allowance is available for qualified recovery assistance property you acquired after May 4, 2007, and placed in service in the Kansas disaster area.

Certain qualified property acquired after 2007. A special depreciation allowance is available for certain qualified property acquired after 2007 and placed in service before 2010 (before 2011 for certain property with a long production period and certain aircraft).

Qualified reuse and recycling property. A special depreciation allowance is available for qualified reuse and recycling property acquired after August 31, 2008.

Qualified cellulosic biofuel plant property. A special depreciation allowance is available for qualified cellulosic biofuel plant property placed in service after October 3, 2008, and before 2013.

Qualified disaster assistance property. A special depreciation allowance is available for qualified disaster assistance property placed in service in federally declared disaster areas in which the disaster occurred after 2007.

Disqualified Corporate Interest Expense Disallowed Under Section 163(j) and Related Information

For tax years beginning after 2007, corporations will use Form 8926, Disqualified Corporate Interest Expense Disallowed Under Section 163(a) and Related Information, to figure the amount of any corporate interest expense deduction disallowed by section 163(j). A corporation's interest expense may be disallowed if it paid or accrued disqualified interest during the tax year.

Disqualified interest is:

- Interest paid or accrued (directly or indirectly) to a related person not subject to U.S. income tax on the interest,
- Interest paid or accrued on indebtedness held by an unrelated person if there is a disqualified guarantee of the indebtedness and the interest is not subject to a U.S. gross basis income tax (a tax figured on the gross amount of an item of income without reduction for any allowed deduction), or
- Interest paid or accrued (directly or indirectly) to a taxable real estate investment trust (as defined in section 856(1)) by a subsidiary of the trust.

Also, any disqualified interest disallowed as a deduction by section 163a) in a tax year is carried forward and treated as disqualified interest paid or accrued in the next tax year.

However, if at least one of the following statements is true, disqualified interest paid or accrued in the current tax year will not be disallowed by section 163a).

- The corporation's debt to equity ratio at the end of the tax year does not exceed 1.5 to 1.
- The corporation does not have any excess interest expense for the tax year.

For more information, see the Instructions for Form 8926.

Business Start-up and Organizational Costs

A separate election statement is no longer required to elect to deduct up to \$5,000 of business start-up and organizational costs paid or incurred after September 8, 2008. This amount is reduced (but not below zero) by the amount by which your costs exceed \$50,000. Any costs not deducted must be amortized ratably over a 180-month period.

You can also apply the same treatment to business start-up costs and organizational costs paid or incurred after October 22, 2004, and before September 9, 2008, provided the period of limitations on assessment of tax has not expired for the year of the election. For more information, see chapter 8 of Publication 535, Business Expenses.

Meal Expenses When Subject to "Hours of Service" Limits

In general, you can deduct only 50% of your business-related meal expenses. However, for 2008 and later years, you can deduct 80% of meal expenses while traveling away from your tax home for business purposes if the meals take place during or incident to any period subject to the Department of Transportation's "hours of service" limits. Business

meal expenses are covered in chapter 1 of Publication 463. Reimbursements for employee meal expenses are covered in chapter 11 of Publication 535.

Self-Employment Tax

Maximum amount subject to tax. The maximum amount of net earnings subject to the social security part of the self-employment tax for tax years beginning in 2008 is \$102,000. All net earnings of at least \$400 are subject to the Medicare part of the tax.

Conservation Reserve Program (CRP) payments. CRP payments you receive after 2007 are excluded from net earnings from self-employment when figuring your self-employment tax if you are receiving social security benefits for retirement or disability. Qualifying individuals will deduct CRP payments on line 1b of the 2008 Schedule SE (Form 1040).

Optional methods to figure net earnings. For tax years beginning in 2008, the dollar thresholds for using the optional methods to figure net earnings from self-employment have increased. You may use the farm optional method to figure your net earnings from farm self-employment if your gross farm income was \$6,300 or less or your net farm profits were less than \$4,548. The nonfarm optional method may be used to figure your net earnings from nonfarm self-employment if your net non-farm profits were less

than \$4,548 and also less than 72.189% of your gross nonfarm income.

In 2008, the maximum social security coverage under the optional methods has increased to four credits, the equivalent of \$4,200 of net earnings from self-employment. In future years, the thresholds will be indexed to maintain that level of coverage.

Election to Accelerate Certain Credits in Lieu of the Special Depreciation Allowance

Generally, corporations and a certain automotive partner-ship can elect to accelerate pre-2006 unused research credits or minimum tax credits in lieu of claiming the special depreciation allowance for certain eligible qualified property acquired after March 31, 2008, and placed in service before January 1, 2010 (before January 1, 2011, for long production period property and noncommercial aircraft). For more information, see chapter 3 of Publication 946. Also, see Form 3800, General Business Credit; Form 8827, Credit for Prior Year Minimum Tax-Corporations; and related instructions.

Alcohol and Cellulosic Biofuel Fuels Credit

For credits claimed on returns filed after May 14, 2008, you cannot claim the alcohol and cellulosic biofuel fuels credit for alcohol produced outside the United States for use as a fuel outside the United

States. For this purpose, the term "United States" includes any U.S. possession.

For more information, see Form 6478, Alcohol and Cellulosic Biofuel Fuels Credit.

Biodiesel and Renewable Diesel Fuels Credit

The following changes apply to the biodiesel and renewable diesel fuels credit.

- For credits claimed on returns filed after May 14, 2008, biodiesel and renewable diesel do not include fuel produced outside the United States for use as a fuel outside the United States. For this purpose, the term "United States" includes any U.S. possession.
- For fuel produced, and sold or used, after October 3, 2008, renewable diesel does not include any fuel derived from co-processing biomass with feedstock that is not biomass.

For more information, see Form 8864, Biodiesel and Renewable Diesel Fuels Credit.

Low-Income Housing Credit

The low-income housing credit attributable to buildings placed in service after 2007 is allowed against both the regular tax and the AMT. For more information about this credit, see Form 8586, Low-Income Housing Credit.

Agricultural Chemicals Security Credit

The Food, Conservation, and Energy Act of 2008 added the agricultural chemicals security credit as part of the general business credit. Use Form 8931, Agricultural Chemicals Security Credit, to claim the credit for qualified agricultural chemicals security costs. Only qualified agricultural chemicals security costs paid or incurred after May 22, 2008, and before 2013 can be used to figure the credit. The credit is only available to eligible agricultural businesses. The credit is 30% of the qualified agricultural chemicals security costs paid or incurred during the tax year.

Facility limit. The amount of the credit for any facility for a tax year cannot be more than \$100,000 minus the total of the credits figured for the facility for the 5 prior tax years.

Annual limit. The amount of the credit figured for any tax year cannot be more than \$2 million.

Eligible agricultural business. An eligible agricultural business is any person in either of the following trades or businesses.

- Selling agricultural products, including specified agricultural chemicals, at retail to farmers and ranchers.
- Manufacturing, formulating, distributing, or aerially applying specified agricultural chemicals.

Specified agricultural chemical. A specified agricultural chemical is either of the following.

1. Fertilizer commonly used in agricultural operations that is listed under any of the following.
 - a. Section 302(a)(2) of the Emergency Planning and Community Right-to-Know Act of 1986.
 - b. Section 101 of part 172 of title 49, Code of Federal Regulations.
 - c. Part 126, 127, or 154 of title 33, Code of Federal Regulations.
2. Any pesticide (as defined in section 2(u) of the Federal Insecticide, Fungicide, and Rodenticide Act), including all active and inert ingredients, that is customarily used on crops grown for food, feed, or fiber.

Qualified agricultural chemicals security costs.

Qualified agricultural chemicals security costs are any of the following costs paid or incurred by an eligible agricultural business during the tax year to protect specified agricultural chemicals.

- Employee security training and background checks.