Breaking News: Congress Passes Stimulus Law

As the April 15th tax return due date approaches, you might want to make a contribution to a traditional IRA for the 2008 tax year. Not only will this boost your retirement savings, you may be able to deduct all or part of the contribution on your return. However, deductions are not available if your income exceeds a specified level and you (or your spouse if you're married) are considered to "actively participate" in an employer-sponsored retirement plan. There's usually little disagreement over the amount of income. But taxpayers and the IRS often differ over what constitutes "active participation" for this purpose. As one recent Tax Court case illustrates, the courts can interpret this term quite broadly.

Background: The maximum amount you can contribute to an IRA for the 2008 and 2009 tax years is $5,000. An extra catch-up contribution of $1,000 is permitted if you're age 50 or over, for a total maximum contribution of $6,000.

This limit can be split between a traditional IRA and a Roth IRA but the combined limit is $5,000/$6,000. The deadline for making contributions for the 2008 tax year is April 15, 2009.

The IRS adjusts the annual income level for IRA deductions each year. The chart at the bottom of this article has the contribution amounts and income limits for 2008 and 2009. The exact amounts depend on your modified adjusted gross income and whether you or your spouse actively participate in an employer-sponsored retirement plan. (Modified AGI is the amount reported on the bottom of page 1 of your Form 1040 with certain add-backs that may or may not apply in your situation.)

But remember that these income levels are only half of the equation. If you don't actively participate in an employer plan (and neither does your spouse, if you're

Obama Calls New Law "Major Milestone on Our Road to Recovery"

On February 17, 2009, President Obama signed into law the American Recovery and Reinvestment Act of 2009. The wide-ranging legislation adds some new breaks to the tax code and extends other deductions and credits that expired. For example, another one-year "AMT patch" was put into place for 2009 to prevent millions more individuals from paying the alternative minimum tax.

Here is a quick rundown of eight more highlights:

1. Loss carryback improved. Businesses with losses can generally carry back net operating losses (NOLs) back two taxable years. For 2008, businesses with gross receipts of less than $15 million can carry back NOLs five years, which can potentially result in a refund.

2. Enhanced business equipment tax breaks extended. For the 2008 tax year, businesses could deduct up to $250,000 for "Section 179" depreciation. That enhanced deduction expired at the end of last year and the Section 179 deduction dropped to $133,000. The new law brings back the $250,000 amount for 2009 and also also reinstates "bonus depreciation" for eligible business equipment.

3. New employer hiring incentive. The new law includes a tax credit equal to 40 percent of the first $6,000 of wages paid to employees who are unemployed veterans or "disconnected youth." The latter is defined as individuals between the ages of 16 and 25 who have not been regularly employed or attending school in the past six months.

4. Sales tax deduction for vehicle purchases. For taxpayers within certain income limits, there is a new deduction for state, local and excise taxes paid when buying a new car, light truck or other vehicle through 2009.

Continues on next page…

married), you can deduct the full amount of your IRA contribution, regardless of the amount of income you earn during the year.

When are you treated as an "active participant" under this rule? Generally, you can rely on the wording of the retirement plan's documents, but the exact definition can vary among plans.

For example, you may be considered an active participant in a profit-sharing plan for the year in which your employer deposits the company contribution to your account, even if the contribution is being made for a different year. There can also be other extenuating circumstances.

Tax Court example: A retired worker for the state of New Mexico went back to work in order to protect the level of pension plan benefits currently available to him. However, he did not qualify for any additional retirement plan benefits as a result of the re-employment.

Nevertheless, the Tax Court ruled that the worker should be treated as an active participant subject to the income limits for deductible IRA contributions

That year, he and his wife each contributed $4,500 to an IRA and took a $9,000 deduction on their tax return. The IRS disallowed the deduction because the taxpayer was deemed to be an active participant in a qualified retirement plan. (Starnes, TC Summary Opinion 2008-148)

If you don't qualify for deductions under the two-part test, you can still contribute to a traditional IRA on a nondeductible basis.

Alternatively, you may be able to contribute to a Roth IRA within the same annual contribution limits. (The income phase-out ranges for Roth start at much higher levels.)

Obama Calls New Law "Major Milestone on Our Road to Recovery" (continued)

5. The "American Opportunity" education tax credit - For 2009 and 2010, the bill would provides taxpayers within certain income limits with a credit of up to $2,500 of the cost of tuition and related expenses paid during the taxable year.

6. Homebuyer tax credit - Last year, a law was passed providing first-time homebuyers with a refundable tax credit that was equivalent to an interest-free loan equal to 10 percent of the cost of a home (up to $7,500). Any amount received generally must be repaid to the government over a period of years. Under the new law, the repayment obligation is eliminated and the maximum amount of the credit increases to $8,000. There are income limits to qualify.

7. The "Making Work Pay" tax credit - For 2009 and 2010, working individuals and families within certain income limits will receive a refundable tax credit of $400 or $800. For employees, this credit will be in the form of reduced withholding from their paychecks.

8. Help for unemployed individuals. The first $2,400 of unemployment benefits will be exempt from federal income tax for 2009.

These are only some of the provisions in the new law.

Roth IRA contributions are never deductible, but future qualified distributions are tax-free.

Here are some other Roth advantages:

At age 70 1/2, you must begin to take withdrawals from a traditional IRA or face steep penalties. But with a Roth IRA, you don't have to take withdrawals at any age, meaning the account can continue to grow tax free.

Contributions can be made as long as you have earned income, no matter how old you are.

A Roth IRA can be passed on to your heirs, who can take tax-free withdrawals for decades if certain steps are taken.

Please call us if we if you would like help assessing the best retirement saving approach for your situation.

	2008 IRA Deadlines and Limits	For 2009
Traditional IRA and Roth IRA contribution limits	You can contribute up to $5,000 until April 15, 2009 ($6,000 is you were age 50 on 12/31/08).	Contribution limits unchanged from 2008 ($5,000/$6,000)
Age limits	You must be under age 70 1/2 at the end of 12/31/08 to contribute to a traditional IRA. Roth contributions can be made at any age, if you meet other requirements.	You must be under age 70 1/2 at the end of 12/31/09 to contribute to a traditional IRA. Roth contributions can be made at any age, if you meet other requirements.
IRA Phase-Out Ranges	For 2008	For 2009
Traditional IRA when active in employer retirement plan	■ For married filing jointly between modified AGI of $85,000 and $105,000. ■ For single or head of household, $53,000 to $63,000.	■ For married filing jointly between modified AGI of $89,000 and $109,000. ■ For single or head of household, $55,000 to $65,000.
Traditional IRA if spouse participates in employer plan	Phase-out occurs between modified AGI of $159,000 and $169,000.	Phase-out occurs between modified AGI of $166,000 and $176,000.
Roth IRAs	■ For married filing jointly, between modified AGI $159,000 to $169,000. ■ For single or head of household, $101,000 to $116,000.	■ For married filing jointly, between modified AGI of $166,000 to $176,000. ■ For single or head of household, $105,000 to $120,000.