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2009 – ANOTHER GOOD YEAR FOR CAPITAL EXPENDITURES

The tax law has long been used to stimulate the economy, and 2009 is no exception. The Economic Stimulus Act of 2008 made significant changes in the business capital expenditure expensing and depreciation rules for 2008, and the American Recovery and Reinvestment Act of 2009 extended these stimulus rules through December 31, 2009.

Expensing Rules. Prior to the 2008 law, an expense deduction was available for business taxpayers who elected to treat the cost of certain qualifying new or used property (Section 179 property) as a current expense rather than as a depreciable capital expenditure. The annual limitation, however, was significantly increased for 2008, and that increase was extended to December 31, 2009 by the 2009 law change. The annual limit is \$250,000. The larger phase-out of the deduction from 2008 was also carried over into 2009 by the new law. Under the new law, the 179 expense deduction limit is \$250,000 for business taxpayers placing qualified property costing \$800,000 or less in service during 2009. Businesses acquiring and placing in service between \$800,000 and \$1,050,000 of such property can deduct a reduced amount under Section 179. The deduction is completely phased out if such property costing over \$1,050,000 is placed in service during 2009.

The election to expense is available whether or not the small business taxpayer has net trade or business income. The current deduction, however, is disallowed if the taxpayer does not have net trade or business income for the year in which the property is placed in service, but the deduction will be available for use in future years. For the individual taxpayer, W-2 wages are considered trade or business income for this purpose.

The new law does not change the rules for the type of property that is eligible for expensing.

Generally, the property must be tangible personal property (e.g., equipment, furnishings, livestock, etc.) that is used in the taxpayer's business and for which a depreciation deduction would normally be allowed. **Both new and used property are eligible.** The property must be used more than 50 percent for the business and must be placed in service by year end. There are also special rules for vehicles. The expense deduction is generally not available for a business vehicle with a Gross Vehicle Weight (GVW) of 6,000 lbs. or less. The expense deduction is generally available to business vehicles with a GVW over 6,000 lbs. (e.g., most trucks, vans, etc.), but the deduction is limited to \$25,000 for an SUV with a GVW over 6,000 lbs.

Additional Depreciation Rules. The new law also extends the 50-percent bonus first-year depreciation for qualified property. Qualified property generally includes all new (**used property is not eligible**) tangible personal property that is depreciable over 20 years or less, such as equipment, fences, land improvements, farm buildings, billboards, livestock, and qualified leasehold improvements. Qualified new property must be acquired during 2009 (or pursuant to a written binding contract in 2009) and, generally, must be placed in service in 2009. However, property with typically longer production periods (e.g., a barn, land improvements) can be placed in service in 2010.

To illustrate the interrelation of bonus depreciation and the increased expensing election, assume a business acquires new equipment with a five-year life costing \$510,000 during 2009. The total deduction available for 2009 is \$406,000 (\$250,000 Section 179 expense, \$130,000 50 percent first-year bonus, and \$26,000 regular depreciation), or almost 80 percent of the original cost in the year of acquisition. We will be happy to discuss how these deductions might apply to your situation.

2009 YEAR-END TAX PLANNING

The opportunity for most significant tax planning for 2009 has probably passed. However, you still have time to change your 2009 federal income tax liability. If you review your 2009 tax situation now, you might still be able to take advantage of some tax-planning opportunities to lower your total tax for the next two years.

The usual general plan involves accelerating deductions into 2009 and, where possible, deferring income into 2010. If you decide that your tax rate for 2010 will likely not be higher and if you expect to itemize your deductions on your 2009 return, you might consider paying deductible expenses before the end of the year to lower your 2009 taxes.

Deductible Interest. Consider making your January 2010 mortgage payment in late December 2009, so that the interest will be deductible on your 2009 return.

Medical and Miscellaneous Expenses. To be deductible, medical expenses must exceed 7.5 percent of adjusted gross income and miscellaneous expenses must exceed 2 percent of adjusted gross income. Bunching, if possible, two years of your unreimbursed medical or miscellaneous expenses (such as certain job-related expenses and investment expenses) into one year might allow you to exceed the deduction floors and obtain a deduction for at least part of these expenses. Thinking longer term, should you have a Health Savings Account?

Charitable Contributions. If you are planning to make a charitable donation in early 2010, consider a 2009 year-end donation instead. If you hold highly appreciated stock or other investment, you might want to make a donation of the investment (rather than of cash) to your charity. By doing so, you will get a deduction for the full value of the investment without recognizing the gain. Also, contributions charged on your credit card in 2009 count as 2009 deductions, even if you don't receive or pay the credit card bill until 2010.

Taxes. If you pay quarterly estimated state income taxes, you might consider paying your last 2009 estimate before December 31 so that it will be deductible on your 2009 tax return. You might also want to include any projected state balance due for

2009 (generally payable in 2010) in the estimated tax payment paid in 2009. Doing so will allow you to deduct the payment in 2009 rather than in 2010. If you are an employee, you might want to increase the amount withheld from your remaining 2009 paychecks to cover any projected balance due.

If, however, high income in 2009 causes your itemized deductions to be limited, if you expect to be in a much higher tax bracket in 2010, or if you are subject to the alternative minimum tax for 2009, accelerating these deductions into 2009 might not be your best course of action. We will be glad to help you with this analysis.

Rapid Depreciation on Equipment. If you are considering the acquisition of depreciable business equipment, you might want to read the preceding article concerning capital expenditures

Long-Term Deferrals

Retirement Savings. Maximize your 2009 contributions to any tax-deferred retirement savings plan in which you participate, such as a 401(k) plan, a 403(b) plan, or a 457(b) plan.

Part-time businesses, self-employed business owners, etc. Self-employed business owners (including those with part-time or sideline businesses) who do not have a tax-deferred retirement plan should consider adopting one before year end. With 401(k) plans, a self-employed person can defer the income taxation on the first \$16,500 (\$22,000 in some cases) of self-employment earnings and approximately 20 percent of earnings above \$16,500. For those sideline businesses without employees, this can be done without any staff coverage cost. Other options include Simplified Employed Pension plans (SEPs) and SIMPLE plans, both of which are often very cost effective.

Can we Help? Please remember that the above comments and suggestions are general strategies only. They might or might not be appropriate for you, especially considering the new administration's stated plan to raise the ordinary income tax, capital gains tax, and payroll tax. As always, please let us know if we can help with your planning.