

**WHO HAS THE TABLES?** Each December EDD mails new withholding tables to all Employer Return filers. The newest tables were NOT mailed to everyone! In fairness, most employers either use in-house software or a commercial payroll service. Most adopted the new tables in May, some were in June, others in July – a few are still not using the new tables!

**IN NOVEMBER** tables will change again – a 10% increase in withholding!

**DEPENDENT EXEMPTION CREDITS IGNORED!** Back in 1998 California began offering different credits for the dependent exemption – the value has been about *triple* the value of a personal exemption. Worksheets for the Form DE-4 (California's equivalent to the Federal Form W-4) have suggested since 1998 that workers claim

- One allowance for self
- One allowance for spouse
- Three allowances for each dependent child.

Thus, California's withholding tables don't really reflect *dependents*, simply *allowances*!

**HAVE YOU SPOKEN WITH CLIENTS RECENTLY?** This change will have a dramatic impact on many low-to-moderate income families. If they don't hear about it until February or March they will be upset, but are not likely to *blame you*. We urge you to consider finding a way to contact these clients before tax season.

### **BACK TO OUR EXAMPLE**

ASSUMING BOTH COUPLES' EMPLOYERS use the new tables, how much of our "shortfall" is erased?

AT FIRST GLANCE you might think we must look at the difference in base tax – after all, the tables are designed to correct for this.

MUCH MORE COMPLEX. We only gave "gross income". More is needed:

- Do both spouses work? Are there multiple jobs?
- Did employers use BOTH revised tables (May & November)?
- How much unearned income is present?
- If there are multiple jobs, are DE-4s similar?

NOT A SIMPLE PROBLEM at all. This will be a real nightmare!

**RESIDENTIAL ENERGY EFFICIENT  
PROPERTY CREDIT****RESIDENTIAL ENERGY EFFICIENT PROPERTY CREDIT****OVERVIEW.**

It is covered by IRC §25(D).

This is a Federal only non-refundable credit.

It is permanently available to offset AMT.

Any excess can be carried over to another tax year.

It applies to the purchase of residential energy efficient property for the taxpayer's residence located in the U.S.

It is available for the principal residence as well as for second or vacation homes (fuel cell property requires principal residence only) but not for residential rental property.

Originally available 2006 through 2008, it is extended through 2016.

This law is effective for tax years beginning before 2017 only.

*Energy Policy Act of 2005, Tax Relief & Health Care Act of 2006 and Emergency Economic Stabilization Act of 2008.*

**COMPARISON TABLE**

**RESIDENTIAL ENERGY EFFICIENT PROPERTY CREDIT COMPARISON.** We will compare the 2008 and 2009 laws on the next page.

## 1) CIVIL ISSUES

**LOCAL LAW** will demand certain steps be taken. In most cases, these will be handled by a hospital and/or a mortuary. These involve handling of remains, autopsy (if required), recording of death and issuance of death certificates. Other steps may be involved, depending upon location and circumstances.

**IDENTIFICATION OF ASSETS & LIABILITIES** is a key concern in closing the “financial” life of the decedent.

**ASSETS** are anything at all “owned” by the decedent. Personal belongings, real estate, businesses, financial accounts – everything. A key step is locating and identifying these. At what point is it agreed all these have been properly identified? Once again, local law can vary here.

**LIABILITIES** cover anything decedent may have left unpaid. Mortgages and large debts are obvious. However, each locale has rules in place to provide public assurance that all bills are settled – doctor bills, credit card balances, utility bills, everything.

**CONTROL OF ASSETS** depends upon the steps decedent took prior to death.

**NO WILL (INTESTATE).** Generally assets are frozen. Control passes to the Court. Generally a probate is required. This takes up to a year, and can cost anywhere from a few hundred dollars to many thousands of dollars.

**SIMPLE WILL.** Once the will is located, recorded, and reviewed, an Executor is identified. The executor, under supervision of a Court, will do most of the “legwork” to handle the tasks associated with identifying assets, dealing with estate and income taxes, and transferring the assets to the beneficiaries.

**LIVING TRUST.** The trust, which was “revocable” while decedent was alive and in total control, now becomes “irrevocable”. It is now a legal “person”, controlled by the Successor Trustee. As a true legal “person” the trust needs an ID Number (something like a social security number). Its income and expenses are reported by the Trustee, who has become a “fiduciary” with the responsibility of carrying out the terms of the trust as well as the dictates of civil and tax laws.

**ARE YOU RESPONSIBLE** for one or more of these areas? If so, please pay careful attention to all instructions.

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**LENDER MAY STILL BE DECIDING** whether or not to attempt enforcing his rights. In California, under the proper circumstances, lender could have as long as four years to decide whether or not to pursue any shortfall – the 1099-C could come three years later!!

**IRS INSTRUCTIONS** to lenders (not well-followed by lenders!!) suggest Forms 1099-A and 1099-C are both used only in cases where the events happen in different years. In practice, lenders cannot be counted upon to follow IRS instructions.

**3) NON-RECOURSE LOAN.** Sometimes the loan itself is non-recourse. In a few cases, lender's *actions* can convert a recourse loan into a non-recourse loan.

**DEBT CANCELLATION IS IMPOSSIBLE** with non-recourse loans. Lender must always agree his only recourse was to the property itself – no further remedy exists.

**WHOOOPS! SELL PRICE IS LOAN BALANCE.** If the evidence indicates the loan is a non-recourse instrument, we must treat the property as never worth less than the outstanding loan balance. Client's reported "sale price" will be the loan balance, even though the actual transaction involved a much lower price! It's the law. (*IRC §7701(g)*)

**TIER 1 – ARE YOU A REPRO?** Let's look closely at the first three tests.

1. **REAL ESTATE TRADE OR BUSINESS.** Is defined as real property “development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business.” (IRC 469(c)(7)(C)).
2. **50% RULE.** More than 50% of the personal services taxpayer performs in ALL trades or businesses during the year must be in real estate trade or businesses in which T/P materially participates. **SERVICES OF AN EMPLOYEE WILL NOT QUALIFY** unless the employee has more than a 5% ownership interest in the employer.
3. **750-HOUR RULE.** Taxpayer must spend more than 750 hours of service in the real property trades or businesses in which T/P materially participates.

**MATERIAL PARTICIPATION (MP).** This term appears repeatedly above – we'd best review it. The 7 basic tests from Regulations 1.469-5T:

- 1) **500 HOURS** or more are spent on the activity during the tax year.
- 2) **SUBSTANTIALLY ALL PARTICIPATION.** T/P is a MP if substantially all of the work done in connection with the activity for the year is done by T/P.
- 3) **100 HOURS & NO-ONE DOES MORE.** T/P is a MP if T/P spends more than 100 hours on the activity for the year, and no other person spends more time on the activity.
- 4) **SIGNIFICANT PARTICIPATION.** “Significant Participation” (SP) is defined as spending more than 100 hours on an activity, but not meeting the MP test. This test allows T/P to qualify as MP if the **AGGREGATE** of time spent in all SP activities exceeds 500 hours.
- 5) **5 OUT OF 10 YEARS.** T/P is a MP if T/P was a MP in the activity for any 5 years out of the most recent 10 tax years.
- 6) **PERSONAL SERVICE - ANY 3 YEARS!** If the activity involves supplying personal services T/P is a MP if T/P was a MP in any 3 years in the past!!
- 7) **FACTS AND CIRCUMSTANCES.** A useless test, as no clear definitions are given.

**SPECIAL NOTE FOR SPOUSES.** Spouses on a joint return may combine their hours in any given activity. (Although the tasks must be those a manager of a business would normally become involved in. Time spent on “investment” pursuits does not count as time spent on the “activity”).

**CONSIDER THESE OCCUPATIONS:**

- **SCHOOL TEACHERS**
- **POLICE OFFICERS & FIREMEN**
- **MANY LIBRARIANS**
- **STATE & FEDERAL EMPLOYEES**
- **AND MANY MORE!**

**CAN'T BEAT THE 2% FLOOR?** For such clients we often ignore their “business expenses” as too small an amount to surpass the floor.

**COULD SOME BE CONTRIBUTIONS?** Possibly. Apply the “freely given with no expectation of return” test.

**EXAMPLE: TEACHERS (THEY'RE EASY!!)**

Sally teaches in a public school (or Church-owned school), and has expenses, but barely passes the 2% floor. Let's look at which expenses offer an “expectation of return for Sally. In fact, let's divide the expenses by who benefits:

	<u>Sally's Benefit</u>	<u>Students' Benefit</u>
Union Dues	\$600	
Classroom Supplies		\$188
Professional Society Dues	\$125	
Mileage for class field trips		750 miles*
Periodicals used in classroom	\$85**	\$85**
Student treats (cookies, etc)		\$110***
Processing of classroom photos		\$46

\* charitable miles are only 14 ¢ (vs. 55¢ for business)

\*\* Perhaps 50-50 is reasonable. Some periodicals have personal use, others are bought to be cut up by the kids!

\*\*\* Meals/entertainment is 100% for a charity, not 50%

**MOVE SOME OR ALL OF COLUMN TWO TO CHARITY??** Many practitioners are hesitant. Ask yourself again – were these monies “freely given, with no expectation of return”?

**AMT ALSO!** Some folks have so many miscellaneous deductions they pay an AMT. Consider moving some of these to Charity!

**CIVILIAN EMPLOYEES – NO!!** This works only if employer is a “charity”.

**RECORD REQUIREMENT.** Remember – amounts over \$250 at one time DEMAND a receipt from the agency. For any other amounts, a log and proof of payment are sufficient.

**THINK ABOUT IT!!**

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