

October 13, 2008

**ALERT: Bailout bill delivers tax benefits:
many tax incentives renewed or expanded**

The newly signed Emergency Economic Stabilization Act of 2008 includes nearly 300 changes to the tax code and \$150 billion in tax incentives. Many changes simply extend existing incentives. The following listed items are a summary of a few of the more important changes affecting Kansas businesses and individuals.

Research and development tax credits extended

The research and development tax credit, which had expired at the end of December 2007, was reinstated for 2008 and 2009, and the alternative, simplified method of calculating eligible R&D expenses was raised from 12% to 14%. The alternative incremental research credit was repealed.

R&D tax credits, which may be earned in addition to the deductions taken for eligible R&D expenses, may be available to businesses which design or develop new products or processes, have an engineering department, or develop software. A simplified calculation for R&D tax credit calculation was introduced in 2006: the credit was 12% of qualified research expenses that exceed 50% of the average qualified research expenses for the three preceding tax years. This simplified method increased the number of businesses the R&D tax credit could benefit.

Accelerated depreciation of retail, restaurant and leasehold improvements

Qualifying restaurant and leasehold improvements may now be depreciated over a 15-year period, rather than a 39-year period, through Dec. 31, 2009. Retailers who own their own buildings may use the 15-year period for certain improvements to retail space as well as leaseholders.

Even businesses which aren't retailers or restaurants but which have made major leasehold improvements should discuss their renovations with their AGH tax professional. The renovations may be appropriate for a cost-segregation study, in which personal property currently being depreciated over a 39-year period as part of a major renovation or building project is reclassified as personal property with a shorter tax life of 5, 7 or 15 years. The accelerated depreciation increases cash flow.

New Markets Tax Credit extension

This credit, which encourages investment in or loans to small businesses in economically distressed areas, has now been extended through Dec. 31, 2009. The current credit crunch could make this provision even more meaningful.

Alternative Minimum Tax patch

The new law, valid only for 2008, raises the AMT exemption amounts slightly from 2007, and provides another year of tax relief for many middle-class individual taxpayers. As well, the law eliminates any AMT tax liability outstanding as of Oct. 3 for taxpayers who incurred the liability

by exercising incentive stock options (ISOs) before 2008. Any interest or penalties on the unpaid tax liability also disappears.

Midwestern Disaster Area earns more tax relief

In addition to the bonus depreciation tax relief outlined in an earlier tax alert, the bailout bill provides tax relief for presidentially declared disaster areas, including many in Kansas. Incentives include increased expensing for demolition, environmental remediation and clean-up costs, education, housing tax benefits, and a higher standard mileage rate for charitable use of vehicles.

Net operating losses attributable to severe storms, tornadoes or flooding on or after May 20, 2008, and before August 1, 2008, in the presidentially declared disaster areas of the Midwest, are eligible for a five-year carryback period. This provision applies for losses paid or incurred after the applicable disaster date, and before January 1, 2011. *(Note that disaster area losses in 24 Kansas counties already have a five-year carryback rule covering losses that arise after May 5, 2007 and before January 1, 2010 under legislation passed earlier this year.)*

Special rules for the use of retirement funds.

Tax favored withdrawals. Many victims of the Midwestern storms are able to access retirement funds without triggering the standard early withdrawal penalties. In addition, income attributable to a "qualified Disaster Recovery Assistance distribution" may be included in income ratably over three years, and may be recontributed to an eligible retirement plan within three years without being included in the distributee's income. These include distributions made on or after the applicable disaster date, and before January 1, 2010, to an individual whose principal place of abode on the applicable disaster date, is in the Midwestern disaster area and who has sustained an economic loss due to the relevant storms. Such distributions are limited to \$100,000 and are subject to the income tax withholding rules applicable to distributions other than eligible rollover distributions. Thus, the 20-percent mandatory withholding does not apply.

Recontributions of withdrawals for home purchases. A "qualified storm damage distribution" from certain retirement plans may be recontributed to such plans in certain circumstances when it is received after the date which is six months before the applicable disaster date, and before the date which is the day after the applicable disaster date, where the distribution was to be used to purchase or construct a principal residence in the Midwestern disaster area. The recontribution of the distribution may be made without tax or penalty if it is recontributed between the applicable disaster date, and March 3, 2009.

Loans from qualified plans to individuals sustaining an economic loss. Under the Act there is an exception to the income inclusion rule for loans from a qualified employer plan if the loan is to an individual whose principal place of abode on the applicable disaster date, is located in the Midwestern disaster area and who has sustained an economic loss due to the relevant storms. The exception only applies to the extent that the loan meets certain tests.

If you did not receive the earlier bonus depreciation tax alert for Kansas disaster-stricken counties, please contact your AGH tax professional to request another copy.

Brokers' Statement to Arrive Later Beginning this Filing Season

The Act extends the date by which brokers must furnish information forms to customers from January 31, to February 15 starting in 2009 for 2008 statements.

For financial institutions only

Aside from the large national banking institutions affected by the bailout plan's authorization for government purchases of troubled assets, community banks and other qualified financial institutions gain some assistance. Any community bank which held preferred stock in Fannie Mae and Freddie Mac on Sept. 6, 2008 or held preferred stock which was sold or exchanged on or after Jan. 1, 2008 but before Sept. 7, 2008 may treat those losses as ordinary losses. This provision is not available to individuals.

Not included in the bailout act, but also pertinent to financial institutions: New IRS guidance on changes in bank ownership states that any deduction related to losses on loans or bad debt properly allowed after a bank ownership change will not be treated as a built-in loss or deduction attributed to periods before the change date.

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