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General Business Update

2007 Year-End Tax Relief

In holding true to their promises, Congress passed and President Bush signed year-end tax relief legislation. Some of this legislation is important to the 2007 tax filing season, beginning in January, while others will have ramifications in the years to come. Below is an outline of the major provisions of two Acts.

Alternative Minimum Tax Relief

On December 26, 2007, President Bush signed into law the Tax Increase Prevention Act of 2007 (the "Act"), legislation that alleviates an immediate alternative minimum tax ("AMT") hit on millions of middle-class taxpayers. To do this, the Act increases the AMT exemption amount for 2007 to: (1) $66,250 for a married individual filing a joint return, or a surviving spouse; (2) $44,350 for an unmarried individual who is not a surviving spouse; and (3) $33,125 to married individuals filing separate returns. Without the AMT patch, the 2007 exemption amounts would have been $45,000 for joint filers, $33,750 for single filers, and $22,500 to separate return filers. Given the lateness of the enactment, the IRS has stated that early return filers will see a delay in getting their refunds.

In conjunction with the AMT relief above, the Act amends the tax code by extending to taxable years beginning in 2007 the limitation on the non-refundable personal credits that may be used to offset a taxpayer's AMT liability. These credits include the dependent care credit, the Hope and Lifetime Learning credits, and the D.C. First-Time Homebuyer's credit.

The AMT patch passed Congress without any offsets to pay for the revenue loss. This is what primarily delayed the legislation until late December. Congress has vowed to pay for this break during the next Congressional session.

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Discharge of Indebtedness Income Relief

On December 20th, 2007, President Bush signed into law the Mortgage Forgiveness Debt Relief Act of 2007 (the "Act"). The primary focus of the bill is to relieve taxpayers of the prior requirement that amounts discharged from indebtedness must be included in gross income.

The Act excludes from gross income any discharge of indebtedness income by reason of discharge of qualified principal residence indebtedness. Qualified principal residence indebtedness is similar to the definition used to determine whether you can deduct mortgage interest. However, this provision caps the debt that can be relieved income-free at $2,000,000 (or $1,000,000 in the case of married individuals filing separate returns). The provision only applies to a taxpayer's principal residence and not a second or vacation home. Under the provisions of the Act, taxpayers must reduce their basis in their principal residence (but not below zero) to the extent that amounts are excluded from income as a result of the discharge. This keeps open the possibility of taxation on any future appreciation of the property. However, the general exclusion rule (up to $500,000 for married couples filing jointly) may alleviate any and all taxes due on the sale.

These rules have retroactive effect as they apply to discharges occurring on or after January 1, 2007. However, the provision is not applicable for discharges on or after January 1, 2010.

The Act provides two additional relief provisions for homeowners. First, it extends the deduction for private mortgage insurance, which was set to expire December 31, 2007, to amounts paid or accrued on or before December 31, 2010. Second, effective for sales beginning in 2008, the Act extends the time a widow/widower has to sell the principal residence and be eligible for the $500,000 exclusion available to joint filers, rather than the $250,000 exclusion generally applicable for unmarried individuals. To qualify, the sale must occur not later than two years after the date of death of the spouse and both the widow/widower and the deceased spouse must have met the requirements of the exclusion provision immediately before the date of death. Prior to this provision, the sale had to occur in the year of death so that the widow/widower was eligible to file a joint return and claim the $500,000 exclusion.

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Please contact Glenn Booker at our office so we can discuss how the new tax changes affect your situation.