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*A CPA Firm Servicing the Needs of Small Businesses*

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Dear Clients and Friends,

As we approach the end of 2009, it seems evident that taxes will soon go higher. In the past decade tax legislation has provided lower tax rates and many targeted tax deductions and credits. Most of these provisions will expire at the end of 2010. That fact and the current search for revenue to fund health care reform will lead inevitably to higher taxes. The only questions are when, at what income levels, and by how much?

This Letter is being sent to remind you that right now is the ideal time to identify actions you can take before year-end to cut your 2009 taxes. It's also the right time to review your overall tax strategy in light of the coming tax changes. Use this as a check list to identify the issues that may apply to you. Please call if you have questions or if you would like to get together to discuss your tax-cutting options.

- **Retirement plans for your business** – Starting a small business retirement savings plan can be easier than you think. In addition, a retirement plan has significant tax advantages. Employer contributions are deductible from the employer's income, employee contributions are not taxed until distributed to the employee and investments in the program grow tax-deferred. Further, the tax law offers a small incentive of a \$500 per year tax credit for the first three years of a new SEP, SIMPLE or other retirement plan to cover the initial setup expenses.
  
- **Depreciation** – The American Recovery and Reinvestment Act of 2009 (ARRA) extended the expensing and depreciation incentives contained in the Economic Stimulus Act of 2008, but only through Dec. 31, 2009.
  - **Section 179** – Congress extended the \$250,000 expensing election limit to qualifying property purchased and placed in service during 2009. As a result, many businesses will receive an immediate tax write-off for the cost of most new and used tangible personal property. Unless Congress acts to further extend the higher limit, it will drop to \$134,000 in 2010.
  - **Bonus depreciation** – Property that does not qualify for an immediate tax write-off under the expensing election may qualify for an increased first-year depreciation deduction under bonus depreciation rules. This deduction is equal to 50 percent of the cost of qualifying property purchased and placed in service by Dec. 31, 2009.

To qualify for bonus depreciation, the property must be new. Used property does not qualify.

- **Buildings and other structures** – Buildings and other real estate generally do not qualify for bonus depreciation or the expensing election.

- **Losses from pass-through entities** – Economic pressures are causing many historically profitable businesses to experience operating losses. If you are an owner of a pass-through business entity operating as a partnership, LLC, S corporation or trust, and the business incurs a loss in 2009, you need to plan ahead to be sure you can take advantage of that loss on your personal tax return.

If your business activity is “passive” – generally a rental real estate activity or a business in which you do not materially participate – you may not be able to deduct the loss unless you also experience passive income. Even if you are actively involved in the business, your loss may not be deductible if you do not have “basis.” These rules are complicated, and you should consult with your tax professional. But if you can take steps prior to the end of the tax year to invest more in the business or otherwise increase your basis, you may be able to deduct the loss on your return.

- **Five-year carry-back for net operating losses** – Corporations and owners of pass-through entities that experience a net operating loss may be entitled to an extended five-year carry-back period. Even if you took advantage of the extended carry-back period in 2008, under the new law, you may be again eligible for an extended carry-back of a 2009 loss. And the rules have been expanded to allow more businesses and their owners to qualify.


If you are expecting a net operating loss for 2009 and could benefit from the extended carry-back period, you may want to take steps to try to maximize the amount of the loss by, to the extent possible, deferring income and accelerating deductions. You may also want to plan to complete your 2009 tax return early to accelerate the filing of your carry-back claim so that you can get your tax refund as soon as possible.

- **Gift tax** – The annual gift tax exclusion for 2009 was increased to \$13,000 per person and will remain at the level for 2010. If you are married, you can gift up to \$26,000 per donee by using the gift-splitting rules, without any federal gift tax ramifications. Gifting is a good way to reduce your taxable estate and may be important in a good estate plan. For example, if you and your spouse have two children, with gift-splitting you can give each child \$26,000 in late December and another \$26,000 in early January. If your children are married and/or you have grandchildren, the opportunity increases accordingly.

Future legislation may address some of the provisions that are set to expire at the end of 2010, but the final result is always a mystery until a bill is passed. For example, some proposals to pay for healthcare changes include a new income tax bracket approaching 45 percent for the highest income earners.

Although we have covered a number of topics in this letter, we undoubtedly did not address every issue relating to your specific situation. Please contact us to review your year end tax strategies. For more information on our firm and the services we provide, please visit our website at [www.wittscpa.com](http://www.wittscpa.com).

Sincerely,

  
Peter Witts, CPA