O'MALLEY NEWS & VIEWS

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Accounting and tax preparation for today

Financial planning for tomorrow

a publication by

O'MALLEY & O'MALLEY, LLP ■ Certified Public Accountants
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IN THIS ISSUE...

In addition to Chuck's "Washington Watch", this issue also provides information about new tax laws affecting the preparation of your 2009 tax return and includes the current tax rates, exemption amounts, and other figures subject to annual adjustment, in an easy-to-read **Tax Reference Guide**, see pages 4 and 5. Page 6 has some thoughts on the economy and Roth IRA conversions.

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Please call us if you would like to receive an extra copy of "News & Views" or if you would like to have a copy sent to another family member or friend.

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CLIENTS, FRIENDS & FELLOW PROFESSIONALS – *A SPECIAL THANKS!*

Our continued success would not be possible without your support and recommendations. ***We are actively looking for new clients - businesses, trusts and/or individuals.*** Your continued confidence and referrals are appreciated. Thank you for giving us the opportunity to serve you and your friends.

Washington Watch ■

by Charles K. O'Malley, CPA, CFP®

As I watched Congress during the first year of this historic presidency, I began to realize that in spite of all the post-election rhetoric, this was not going to be a bipartisan Congress. Yes, three Republican Senators, Collins, Snowe and Specter (now a Democrat) voted for the Stimulus Act and one House Republican voted for healthcare reform, but the Congressional leadership of both parties is so polarized that debate, negotiation and compromise does not exist.

The Congressional Democrats outnumber the Republicans, but between the Democrats from conservative GOP states worrying about being re-elected and the GOP voting in unison, numeric control is almost meaningless. The Healthcare Reform Bill is an example of this. There appears to be general agreement that meaningful healthcare reform is needed, but the House version passed by only five votes and the Senate needed lots of wheeling and dealing to squeak through a Christmas Eve passage without any GOP votes. The two different versions went to the House/Senate Conference Committee to finalize in 2010. However, the recent GOP victory in Massachusetts will change the voting power in the Senate, which requires sixty affirmative votes to close the debate and call for an up or down vote. We will keep you updated.

Lots of legislation was postponed to 2010.

Approximately fifty tax issues (bills) were not decided during 2009. While none of these affect the preparation of your 2009 tax return, they could affect your tax planning for 2010 and future years, because many of the 2001 George W. Bush tax cuts are scheduled to expire at the end of 2010.

(continued on page 9)

WHAT'S NEW AT O'MALLEY & O'MALLEY, LLP

We have a new logo and a significantly updated website, see page 8 for more information. Karen's Champion Ramblin' Red Luxury Tax, (a Gypsy granddaughter from Mariette's breeding) is back on the dog show circuit and winning breeds and sporting group placements. David's son Ryan is having a hot hockey season on a winning team in the Empire League that was topped off with his hat trick at Fitchburg, MA. Jackie graduated from The College of New Jersey in December with a BS in Accounting and acquired her own condo in October, qualifying for the New Homeowner's Tax Credit. Our four-legged office greeter Champion Ramblin' Red Chernobog "Charles" had a successful year in the Veteran's show ring with several wins, topped off with a first place in a Veteran's sporting group.

. Tax Tips From

IMPORTANT DUE DATES

March 15 - Corporate Tax Returns (two & a half months after their year end)

April 15 - Individual, Partnership & LLC Returns

Estate and Trust returns (three and a half months after their year end)

First Individual Estimate Payment

A six-month filing extension is generally available for individual and corporation income tax returns, but partnership, LLC, estate and trust returns that supply K-1 reports to participants can only get a five-month extension, now making the final extended due date September 15th. Taxes, however, must be paid by the original due date in order to avoid penalties and interest.

Make sure your Social Security number is properly entered on all of your tax returns and any checks for tax payments.

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Estimated Tax Payments

For 2010, individuals and corporations must pay at least 90% of the current year's tax, or 100% of the prior year's tax. If your Adjusted Gross Income (AGI) is over $150,000, you must pay 110%, some limited exceptions apply.

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Individual Tax Rates

There are six graduated tax rate brackets applied to taxable income after subtracting deductions and exemptions, see page 4.

Tax withholding on bonuses, commissions and miscellaneous income is required at a flat rate of 25%. Most pension distributions require a 20% withholding, and if done before reaching age 59 1/2 are subject to a 10% penalty, some limited exceptions apply.

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Alternative Minimum Tax

Another temporary fix for 2009 will allow millions of taxpayers to avoid this costly tax trap. The exempt income amounts were increased $70,950 for joint filers (2008 was $69,950) and $46,700 for single filers (2008 was $46,200). Without the temporary fix, the limits would have been $45,000 for joint filers and $33,750 for single filers. This temporary fix may allow those who escaped AMT last year to avoid it in 2009, but if AMT got you in 2008, then it will probably get you in 2009. As of now, pending Congressional action, 2010 will return to exempt limits of $45,000 and $33,750.

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IRS Substantiation Test

The regulations have increased the potential for tax preparation penalties in cases where the Internal Revenue deems the preparer aided the taxpayer in avoiding taxes.

Your O'Malley & O'Malley, LLP tax advisers (all State licensed CPA's and PA's) maintain a high ethical standard, stay up-to-date by attending Continuing Professional Education courses and through the years have performed their tax preparation services in accordance with Internal Revenue regulations.

This year, we will again be asking clients to sign a tax return preparation engagement letter. Please discuss it with your tax adviser; we want you to be comfortable with it before you sign your tax return.

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Page 1 Deductions from Total Income To Determine AGI

They're all allowed again, even teacher's expenses ($250 limit per taxpayer – any excess deducted on Schedule A) and tuition and fees per Form 8917. Other Page 1 deductions include certain reservists and National Guard expenses, moving expenses, alimony paid, certain student loan interest, a variety of retirement plans and health plans and other limited items. These deductions were extended through 2009.

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Itemized Deductions

Your standard vs. itemized deductions should always be compared. You may deduct the greater figure.

Millions of taxpayers miss this valuable deduction every year. You get to make this choice each year. Thus, by doubling up on deductions (pay ahead on real estate taxes, charitable contributions, etc.) in one year, you can increase your itemized deductions for that year and then use the standard deduction the following year.

Don't itemize? - Don't miss these add-on deductions:

- You may increase your allowed standard deduction for part of the real estate tax you paid on your home. You may add the lower of what you paid or $500 if single or $1,000 if married/joint to your standard deduction amount.

- Sales and excise tax paid on a vehicle cost of up to $49,500. See Washington Watch for details. You may add this amount to your standard deduction amount, or if you itemize look at the schedule A tax section.

- If you live in a federally declared disaster area, complete Form 4684 and add the amount on Line 18a to your allowed standard deduction.

Read and follow the Page 2 instructions to get all of these additions to your standard deduction. To claim these additional deductions on the standard 1040 Form, on Page 2, check box 40b and place the combined total on line 40a.

The following items are deductible as itemized deductions on your federal income tax return:

- Medical expenses paid by you, including dental costs, eyeglasses, health insurance, (long-term care insurance premiums are considered medical expenses, but there is a limit to the yearly deduction, $3,180 for 2009 and $3,290 for 2010 for individuals between 61 and 70; and $3,980 for 2009 and $4,110 for 2010 for those over 70), which exceeds 7.5% of your AGI. New Jersey will also allow medical expenses after a 2% of income reduction. If you are self-employed, 100% of your health insurance premium, including long-term care insurance, subject to age limits, is deductible on page 1 as an AGI adjustment.

- All state and local income taxes or sales tax, whichever is higher (check out *Washington Watch* for new vehicle sales and excise tax deducion), plus real estate, unemployment and personal property (intangible) taxes.
- Mortgage interest for personal and one vacation residence, usually yachts, mobile homes and travel trailers qualify, subject to some limitations. Interest expense on home equity loans up to $100,000 regardless of how the loan proceeds were used, plus points and investment interest, subject to some restrictions. For 2007 through 2010, mortgage insurance premiums on new principal residence mortgages (FHA, VA, etc.) are deductible.
- Charitable contributions, including non-cash gifts - proof is now required for all cash contributions of any amount, estimated amounts are not allowed. A substantiation letter is required for each individual gift that exceeds $250. Non-cash contributions over $250 require receipts; over $500 require receipts plus additional information; and over $5,000 requires an appraisal. Donations of artwork, stock or other appreciated property can be deducted at the current fair market value with some limitations. **Note:** Deductions for donations of vehicles, boats, motor homes, etc. have been substantially restricted. Check with us before making this type of donation.
- Unreimbursed business and work-related expenses, professional/union dues, costs incurred searching for employment, investment advisory fees, tax preparation fees, etc., are deductible subject to the 2% of AGI limitation.

2009 is supposed to be the last year for the itemized deduction phase-out reduction. It is 1% of the excess AGI for joint filers above $166,800 and single filers above $83,400.

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Phase Out of Exemption Deduction

The annual deduction for personal exemptions can be reduced (possibly to $2,433 per exemption) for higher income taxpayers. This complicated calculation to restrict the deduction benefit of exemptions is supposed to end with 2009 tax returns, but is currently scheduled to be reinstated in 2011. This and the itemized deduction phase-out above were part of the 2001 tax cuts. The yearly phase-out of AGI amounts are listed on the tax reference guide.

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Child Credits

Single parents with AGI under $75,000 and married/joint families with AGI under $110,000 may receive a credit of up to $1,000 for each dependent child under age seventeen. Currently, this credit is applicable through 2010. The credit will be reduced $50 for each $1,000 of additional income. If you qualify for this credit, it is in addition to the childcare and/or earned income credits and under certain conditions may be refundable.

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Children

Dependent children under 19, or dependent students under 24, cannot claim themselves as exemptions on their tax returns. Dependent children may not be required to file a tax return if their investment income is below $950 for 2009 and 2010 and/or their earned wages are below $5,700. However, a tax return is required to receive a refund of withheld income tax. Children under 18 with investment income over $1,900 for 2009 and 2010 are taxed at their parents' tax rate (Kiddie Tax) and must file Form 8814. Beginning January 1, 2008, the tax rules changed for children and dependent students under 24 years old; they are now subject to the Kiddie Tax rules.

Tax exempt or tax-deferred bonds may be a solution for these young taxpayers.

Saving for Education

Section 529 Plans continue to improve. They offer tax free earnings, allow single contributions of up to $13,000 in 2009 and 2010 annually, plus a special one time $65,000 for 2009 or 2010 five years at once. If a joint gift, double contribution limits. They do not have phase-out limitations and offer lots of flexibility. More information is available at **www.collegesavings.com** and **www.collegesavings.org**.

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Tax Exempt Interest Income

To maximize your after-tax income, you must first know your tax bracket. The higher your tax bracket, the greater the benefit from tax-exempt investments, see our Equivalent Percent of Interest Income table on page 4. Income yield will be affected if bonds are purchased above or below face value. Generally, bonds must be invested in your resident state to be tax-free on your state return.

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Investments

Currently through 2010, qualifying dividends (generally domestic corporations held for more than 60 days) will be taxed at 0% if your regular tax rate does not exceed 15%, or at 15% maximum if your regular tax rate exceeds 15%.

Long term capital gains for qualified sales through 2010 will be taxed at 0% if your regular tax rate does not exceed 15%, or at 15% maximum, if your regular tax rate exceeds 15%. This is the current tax law but it could change before the end of 2010.

All investments should be reviewed periodically for risk, balance and diversification. Bank account balances, including internet banks, are FDIC insured up to $250,000 through December 31, 2013, any excess is not insured. On January 1, 2014 the limit is scheduled to be reduced to $100,000. Certain retirement accounts will continue to be insured for $250,000 beyond December 31, 2013. Treasury bills and US Bonds are an excellent alternative to traditional bank instruments. Although not insured, they are backed by the US Government and tax free on the state return. Watch your investments closely and beware of schemes and con-artists. As many investors have found, if the return sounds too high, there may be a problem; don't get caught in a Ponzi scheme. You will sleep better at night if your money is invested in nice, big, public mutual funds or bona-fide listed companies through reputable brokers with SIPC insurance. Their fraud coverage is $500,000 per person, per account.

. Tax Tips From Your Tax Advisors .

Individual Tax Rates For 2009

(AGI less itemized or standard deductions and allowed exemptions)

Tax Rate	Single Income	Married/Joint Income
10%	Up to $8,350	Up to $16,700
15%	$8,350 to $33,950	$16,700 to $67,900
25%	$33,950 to $82,250	$67,900 to $137,050
28%	$82,250 to $171,550	$137,050 to $208,850
33%	$171,550 to $372,950	$208,850 to $372,950
35%	Over $372,950	Over $372,950

Individual Tax Rates For 2010*

(AGI less itemized or standard deductions and allowed exemptions)

Tax Rate	Single Income	Married/Joint Income
10%	Up to $8,375	Up to $16,750
15%	$8,375 to $34,000	$16,750 to $68,000
25%	$34,000 to $82,400	$68,000 to $137,300
28%	$82,400 to $171,850	$137,300 to $209,250
33%	$171,850 to $373,650	$209,250 to $373,650
35%	Over $373,650	Over $373,650

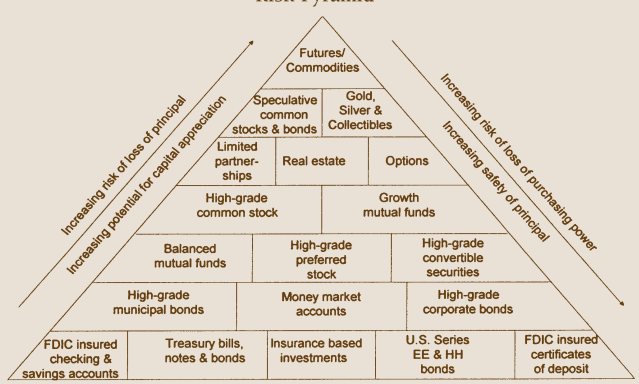
*Effective as of January 2010 - subject to change if Congress passes and the President signs new tax rates into law. Speculation is 33% could become 36% and 35% could become 39.6% at some future unknown date. These were the tax rates in 2000.

Equivalent Percent of Interest Income

Tax Free	15%	25%	28%	33%	35%
3.0%	3.53%	4.00%	4.17%	4.48%	4.62%
4.0%	4.71%	5.33%	5.56%	5.97%	6.15%
5.0%	5.88%	6.67%	6.94%	7.46%	7.69%
6.0%	7.06%	8.00%	8.33%	8.96%	9.20%
7.0%	8.24%	9.33%	9.72%	10.44%	10.77%

As the tax rates decline the equivalent interest income percent declines.

Risk Pyramid



Annual Tax Reference Guide

	2008	2009	2010
Personal Exemptions	3,500	3,650	3,650
AGI Phase-out starts at			
Single	159,950	166,800	None
Married/Joint	239,950	250,200	None
Standard Deductions			
Single	5,450	5,700	5,700
Married/Joint	10,900	11,400	11,400
AGI Limit for 3% reduction			
Single	159,950	166,800	None
Married/Joint	159,950	166,800	None
Alternative Minimum Tax			
Exempt Income			
Single	46,200	46,700	33,750 *
Married/Joint	69,950	70,950	45,000 *
Tax Rates			
AMT Income up to $175,000	26%	26%	26%
AMT Income over $175,000	28%	28%	28%
Social Security			
Taxable Wage Limits	102,000	106,800	106,800
Employee			
Tax Rate	6.2%	6.2%	6.2%
Maximum Tax	6,324	6,622	6,622
Self-employed			
Tax Rate	12.4%	12.4%	12.4%
Maximum Tax	12,648	13,243	13,243
Medicare Tax			
Taxable Wage Limits	No Limits	No Limits	No Limits
Tax Rate			
Employee	1.45%	1.45%	1.45%
Self-employed	2.9%	2.9%	2.9%
Earnings Limits if Collecting			
Prior to full retirement age	13,560	14,160	14,160
Full retirement age	36,120	37,680	37,680
Beyond full retirement age	No Limit	No Limit	No Limit
Benefits are taxable at up to 50% if total income exceeds:			
Single	25,000	25,000	25,000
Married/Joint	32,000	32,000	32,000
Benefits are taxable at up to 85% if total income exceeds:			
Single	34,000	34,000	34,000
Married/Joint	44,000	44,000	44,000
Maximum Contributions to Retirement Plans			
IRA's - Traditional and Roth	5,000	5,000	5,000
IRA's - Non-working spouse	5,000	5,000	5,000
Age 50 + additional contribution	1,000	1,000	1,000
401K, 403B, 457, and SARSEP	15,500	16,500	16,500
Age 50 + additional contribution	5,000	5,500	5,500
Simple IRA plans	10,500	11,500	11,500
Age 50 + additional contribution	2,500	2,500	2,500
Defined contribution plans (profit sharing, Keogh & money purchase)			
Maximum compensation	230,000	245,000	245,000
Maximum contribution	25% up to 46,000	25% up to 49,000	25% up to 49,000
Health Savings Accounts			
Contribution, plan deduction not to exceed:			
Single	2,900	3,000	3,050
Married/Joint	5,850	5,950	6,150
Age 55+ additional contribution	900	1,000	1,000
Federal estate tax exemption	2,000,000	3,500,000	*
Federal gift tax exemption			
Annual per person	12,000	13,000	13,000
Lifetime exclusion (for estate planning)	1,000,000	1,000,000	1,000,000

*Pending 2010 Congressional action

Annual Tax Reference Guide

	2008	2009	2010
Education Deductions/Credits			
Teachers Expense Deduction (deduct excess on Sch. A)	250	250	*
Student Loan Interest Deduction			
Single			
Income below $60,000 (2009)	2,500	2,500	*
Income above $75,000 (2009)	None	None	None
Married/Joint			
Income below $120,000 (2009)	2,500	2,500	*
Income above $150,000 (2009)	None	None	None
American Opportunity Tax Credit	None	2,500	2,500
Hope Credit – First two years			
Single			
Income below $50,000 (2009 and 2010)	1,800	1,800	1,800
Income above $60,000 (2009 and 2010)	None	None	None
Married/Joint			
Income below $100,000 (2009 and 2010)	1,800	1,800	1,800
Income above $120,000 (2009 and 2010)	None	None	None
Lifetime Credit at 20%			
Single			
Income below $50,000 (2009 and 2010)	2,000	2,000	2,000
Income above $60,000 (2009 and 2010)	None	None	None
Married/Joint			
Income below $100,000 (2009 and 2010)	2,000	2,000	2,000
Income above $120,000 (2009 and 2010)	None	None	None
Tuition and Fee Deduction			
Single			
Income under $65,000	4,000	4,000	*
Income above $80,000	2,000	2,000	*
Married/Joint			
Income under $130,000	4,000	4,000	*
Income above $160,000	2,000	2,000	*
Per diem allowance (effective from 10/1 to 9/30)			
High cost average			
Meals	58	58	65
Lodging	179	198	193
Low cost average			
Meals	45	45	52
Lodging	107	113	111
Standard Mileage Rates			
Business use (Rate change 7/1/08)	$0.505 $0.585	$0.55	$0.50
Non business use			
Charitable activities	$0.14	$0.14	$0.14
Medical (Rate change 7/1/08)	$0.19 $0.27	$0.24	$0.165
Moving (Rate change 7/1/08)	$0.19 $0.27	$0.24	$0.165
Tolls and Parking (for above usage)	Actual Cost	Actual Cost	Actual Cost
Vehicle Depreciation (Under 6,000 pounds gross weight)			
Automobiles			
First year	2,960	2,960	N/A
Second year	4,800	4,800	N/A
Third year	2,850	2,850	N/A
Future years	1,775	1,775	N/A
Vans and light trucks			
First year	3,160	3,060	N/A
Second year	5,100	4,900	N/A
Third year	3,050	2,950	N/A
Future years	1,875	1,775	N/A
Depreciation – Sec 179			
First year write off	250,000	250,000	134,000
Total equipment purchases must be under:	800,000	800,000	530,000
Trucks and SUV's – Must be new (Between 6,000 and 14,000 LBS GVW)	25,000	25,000	25,000

N/A: Not available at publication date.

Don't use the mutual fund's name as an investment guide.

Find out how the fund is invested.

Does their mix meet your risk tolerance and diversification requirements?

The Risk Pyramid (see Page 4) may help you determine your investing comfort level. Mariette and Chuck are both CERTIFIED FINANCIAL PLANNER™ professionals, but they are not investment advisors (stock pickers) and do not sell any products. Our services are limited to analyzing and planning.

Social Security and Medicare

Nearly everybody agrees that a fix is needed but fixing it is a very political issue with many opposing ideas. The Obama administration, at some point in time, may try to fix Social Security. We will continue to watch for political recommendations to fix Social Security and report them to you. The Tax Reference Guide on Page 4 contains a list of Social Security data. If you need more information, contact Social Security at 1-800-772-1213 or on the Internet at **www.socialsecurity.gov**.

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Divorce

A complex area made more difficult by complicated tax laws. A divorce property settlement agreement may be one of the most important documents you will ever sign. Before you sign it, have your tax consultant review the agreement and explain the tax consequences.

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Retirement Options

The AGI upper phase-out limits for deductible IRA's, by an active participant in an employer-sponsored plan, have been increased to $65,000 single and $109,000 married/joint for 2009; $66,000 single and $109,000 married/joint for 2010, when both spouses are active participants.

A working spouse, who is not an active participant in an employer sponsored plan, may now make a tax deductible contribution if their joint AGI is less than $176,000 (2009); $177,000 (2010), even though the other spouse is an active participant.

Roth IRA contribution (not deductible) phase-out limits are: single $120,000 (2009 and 2010), and married/joint $176,000 (2009); $177,000 (2010).

A taxable conversion to a Roth IRA from a traditional IRA is allowed during 2009 if your AGI (excluding the conversion money) is less than $100,000. In 2010 the AGI limitation is eliminated. See below for some thoughts on the economy and Roth IRA conversions.

A Quick Guide to Retirement Planning:

- **Day dream a little**, fantasize for a few minutes about what you want in retirement. How much will it cost? What will you need?
- **Give yourself a tax break**, look at the Annual Tax Reference Guide and pick and choose which plan can help you best. Don't miss out on employer matching contributions.
- **Don't lift a finger**, set up automatic deductions from your paycheck or bank account to fund your chosen plan(s).
- **Don't waste time picking an investment**, choose a proven, reliable mutual fund. There are now many targeted retirement age funds available.
- **DON'T TINKER**, frequent adjustments, trying to out-guess the market can be costly. Pick a good fund and check it every three months, but **be patient.**

Check all of your IRA and employer sponsored retirement plans for a designated beneficiary, including secondary beneficiary. Generally, it should be a person and not your estate or a trust.

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Our thoughts on the economy

It's been eleven months since the Dow hit its low of 6,547.05 on March 9, 2009. By December 31, 2009 the Dow had reached 10,428.05, still substantially below the all time high of 14,164.53, set on October 9, 2007. The investment world appears to be slowly and steadily regaining its prior lost earnings. There are lingering signs of caution, but some investors are optimistic and believe that there are still some buys in the stock market of undervalued companies. Unemployment is still around 10% and there is speculation that some jobs may be gone forever. The housing market is still weak but the First Time Homebuyer Tax Credit has helped, and mortgage interest is low but qualifying for a mortgage is challenging. The Cash for Clunkers help for the automobile industry was very successful, but temporary, and is now over. Because 70% of the U.S. gross domestic product is consumer spending, future growth may be dependent on jobs. The politicians are aware of the economy and the lack of jobs, so expect additional efforts to stimulate job growth. If history repeats itself, because this is a midterm election year (all of the House and one third of the Senate), the economy may slowly expand and job growth may follow.

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Roth IRA Conversions

One of the most frequently asked questions now is, should I convert my traditional (tax deferred) IRA to a Roth IRA? This is not an easy answer. There are a lot of facts that must be considered. Why is it now so popular? 2010 is the first year that the adjusted gross income limitations have been removed. Anybody, no matter how high their income, can now convert to a Roth IRA.

What are the Roth IRA advantages?

Roth IRA's have some very unique advantages. After they have been in existence for five years, nothing is taxable, not even the earnings. You can continue to contribute to them after you are 70 ½, traditional IRA's don't allow contributions after 70 ½. Minimum distributions are not required, just let the Roth continue to grow tax free now and forever. While they will be included in your total estate, they are not considered taxable income to your beneficiaries, unlike traditional IRA's. Conversions are not right for everyone, they may be more advantageous for younger taxpayers because of their expected lifespan, but there are reasons for older taxpayers to consider a Roth conversion. **You can do a partial conversion.** Talk to your tax adviser first and don't do it without calculating the amount of tax that will be due on the conversion.

At your option, you may pay the tax based on your 2010 taxable income or split the taxable IRA income in half, reporting half on 2011 and half on 2012. Doing it now and paying the tax later may sound good, but what will the tax rates be in 2011 and 2012? Will you be in a higher or lower tax bracket? Will Congress pass new tax laws that effectively raise the tax cost of a Roth conversion that elects to pay the tax based on 2011 and 2012 taxable income? There is also the time value of money benefit when you delay a tax payment one or two years. So place your bet and take your chances. However there are several reasons to make this bet. These include the prospects of not paying any additional tax in the future, avoiding required minimum distributions, the ability to make contributions after 70 ½, and possibly the benefit of your age.

There is another reason to encourage the conversion choice. What do you think your investments will be worth when you reach 70 ½? The December 31, 2009 Dow was 10,428.05, 26.4% lower than the October 6, 2007 all time high of 14,164.53. Most investors believe some day the market will be higher. Just during 2009 it increased 18.9% from the December 31, 2008 value of 8,776.39 and 59.3% from the March 9, 2009 low of 6,547.05. This could be the best reason for doing a Roth conversion now. Pay tax on maybe 74%+/- of what it might be worth in the future. So in reality, **if you do a Roth conversion you are making two bets**. One is your investment value will substantially increase in the future and the other is taxes will not increase before 2013 but will increase after 2012 and be more costly at retirement time. You can also hedge your bets prior to filing your 2010 tax return (can be extended to October 15, 2011) by recharacterization. This allows you to void your conversion prior to filing your tax return. Confused? Ask your O'Malley & O'Malley, LLP tax adviser to do some projections for you to consider before doing a Roth IRA conversion.

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Health Savings Accounts

Basically, HSA's are a type of medical IRA account linked to a "high deductible" health insurance policy. Many employers are now offering this type of plan as a part of their benefit program. They are also available for self-employed people. To have an HSA you must maintain a health insurance policy that qualifies. The policies are fairly simple to find, appear to be "major medical" type plans and do not cover the day-to-day doctor visits, etc. until you exceed your annual deductible.

The HSA portion of the plan is a savings vehicle where tax deductible funds can be accumulated, much like an IRA account, for the payment of day-to-day medical costs. Naturally, there are limitations on how much can be deposited into these accounts, see our Tax Reference Guide. The account must be created under a written trust agreement with a bank or insurance company and the funds accumulate income tax deferred, much like an IRA. Distributions used to pay qualified medical expenses will not be includible in gross income, but it should be noted that qualified medical expenses do not include paying health insurance premiums, except in very limited circumstances.

For more information or details on HSA's contact your tax advisor.

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House Sale and Mortgage Debt Forgiveness

The sale of your principal personal residence at a gain of up to $250,000 single or $500,000 married/joint (if you have lived there for two years out of the last five years, there are some limited exceptions) usually will not be taxed. This rule applies only to your principal personal residence and does not include vacation, rental, or business properties.

An exception to the tax rules on debt forgiveness allows foreclosures and mortgage renegotiations (workouts), only on a principal personal residence, between January 1, 2007 and December 31, 2012 of up to $2 million to escape taxation.

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Real Estate Loss Deductions

Real estate investments are normally capital assets, subject to the capital gain and loss rules. However, real estate rental losses are subject to the passive loss rules and are not always deductible. Suspended losses are carried forward until there is a profit or the property is sold. Taxpayers who are actively working in real estate (at least 750 hours per year) may be eligible to deduct their rental losses.

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Domestic Workers Tax

The so-called "Nanny Tax" covers all domestic workers (over age 18), including baby-sitters and requires annual reporting of payroll taxes. The wage threshold is $1,700 for 2009 and 2010, per employee. Employers of domestic household workers must provide a W-2 by January 31 and file a Schedule "H" (Household Employment Taxes) as part of their personal tax returns. Domestic employers may also be subject to federal and state unemployment taxes, which may require quarterly state filings and workman's compensation insurance. Check your homeowner's insurance to see if you have coverage for domestic workers.

Home Offices

If you use part of your home for business, you may be able to claim a deduction for office in home expenses, such as utilities, insurance, maintenance and depreciation. To qualify for this deduction, you must use the area of your home regularly and exclusively as your principal place of business, or a place of business where you meet or deal with clients, patients, or customers in the normal course of business, or if you use a space in your home exclusively and regularly for administrative and management activities of your trade or business and you do not have another permanent location where you can conduct these activities. Employees must also prove that they used their home office for the convenience of their employer.

Because the definition of "principal place of business" has been expanded more individuals are able to qualify for the home office deductions.

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Business Expenses

The key to this area is accountability. Reimbursement plans must meet the IRS deductibility requirements. An employee/taxpayer must be required to report and justify any reimbursed expense, including the business purpose and mileage information. If reimbursement is based strictly on these figures, then there isn't any tax impact. However a non-accountable plan (documentation isn't provided) - such as a car or travel allowance - will result in taxable income to the employee/taxpayer, will subject the employer to payroll taxes and is includible in the W-2 as income.

Per Diem allowances (see our Tax Reference Guide) can be paid to employees if they own less than 10% of the company, in lieu of exact expense reporting. Travel and other cost of living expenses for a temporary job assignment, which is for less than one year, are deductible.

Employees who deduct unreimbursed business expenses as part of their itemized deductions (Schedule A, Miscellaneous Deductions) are subject to the 2% AGI limitation.

Meals and entertainment, including sporting events, are only 50% deductible. Working through lunch and overtime meals for employees, trade association dues and similar items are 100% deductible. Social and golf club dues, political contributions (PAC) and lobbyist travel are not deductible.

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Our New Logo

This new logo first appeared on your 2008 "blue book" client's tax return copy, but it's official debut was with our new, recently completed, firm brochure. As the second "O" in the logo indicates, O'Malley & O'Malley, LLP is putting more emphasis on planning. We have always encouraged our clients to plan for the future, but now we are attempting to make you more aware of how much assistance O'Malley & O'Malley, LLP can be in helping you create, implement, monitor and adjust your plans.

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Our Website

Thanks to Jackie's inquisitive mind and constantly expanding computer skills, **www.omalleycpa.com** has been significantly updated and now has a completely new look. After an extensive search for the best way to update our aging website, we decided to do it ourselves. The website now contains:

- More information about our services
- Several thoughts on planning for the future
- A quick guide to retirement planning
- Expanded personnel biographies
- Directions to our office
- The Annual Tax Reference Guide
- Current tax rates
- Equivalent percent of tax free interest income
- The Risk Pyramid
- A full page of pertinent website links

And now that we know how to do it, you have our promise to keep improving its contents.

Check out our updated website
www.omalleycpa.com
It's loaded with information and
other pertinent website links.

This newsletter is designed to provide general information about the subject matter. It does not constitute professional advice. As required by United States Treasury Regulations, you should be aware that this communication is not intended to be used, and it cannot be used, for the purpose of avoiding penalties under the United States federal tax laws. If you would like to discuss a particular item of interest please call our office!

Washington Watch

Continued from page 1

One of these postponed tax issues is re-writing the estate tax laws. The 2001 tax cuts eliminated all estate taxes for only 2010 and re-instituted the more restrictive 2001 tax laws for 2011 and future years. Congress had promised to fix this for 2010 and future years but failed to get it done during 2009. The plan now is to re-write the estate tax laws during 2010 and make it retroactive to January 1, 2010. This delay in timely passing tax legislation could possibly cause a big tax issue for some 2010 estates that happen prior to the re-write and possibly cause a tax court challenge. While this delay will not affect most taxpayers, it is an example of what can happen when Congress fails to act in a timely manner.

**Once there is a new estate tax law,
you should review your will and estate plan.**

Congress did manage to pass some new tax relief items:

- The First Time Homebuyer Credit of up to $8,000, for the purchase of a primary personal residence, originally scheduled to expire on November 30, 2009, was extended to April 30, 2010 and can include settlements through June 30, 2010 if a binding contract is signed by April 30, 2010. It also now includes a credit of up to $6,500 for existing homeowners if they have lived in their primary residence for at least five consecutive years of the last eight year period ending on the date of the new home purchase, with the same 2010 expiration date, subject to adjusted gross income limitations.

- In addition to the now expired Cash for Clunkers trade-in bonus, anyone who purchased a new motor vehicle (gross vehicle weight up to 8,500 pounds) between February 16, 2009 and December 31, 2009 can deduct the sales and excise tax paid on a vehicle cost of up to $49,500 (no limit on the number of vehicles purchased), even if they do not itemize their deductions, but the deduction is subject to adjusted gross income limitations.

- For 2009 and 2010, there is a new college education credit (American Opportunity Tax Credit – AOTC) allowing up to $2,500 a year for all four years (up to 40% is refundable) for qualified tuition and related expenses including books, supplies, equipment, etc. subject to adjusted gross income limitations

- For 2009 and 2010 there is a new energy credit of 30% up to $1,500 for certain high-efficiency heating and air-conditioning systems, hot water heaters plus windows, doors and insulation and a second 30% credit for solar, geothermal and wind turbine systems and there may be more credits next year.

- $2,400 of unemployment compensation benefits are not taxable in 2009, and this could be extended to 2010.

- There is another temporary patch to the alternative minimum tax for 2009 only. See page 2 for the details.

The government websites generally allow e-mails to senators and representatives, but your e-mail may be limited by zip code to only those who actually represent you. To share your views with other senators and representatives you need to either mail them a letter or send it to their specific fax number. We have compiled a list of the available fax numbers. The opening paragraph of my current letter to Senators and Representatives now states, *"You may not represent me and I may not be able to vote for you, but your votes do affect my life."*

The polls generally give Congress a lower favorable rating and a higher unfavorable rating. In my opinion, many of the members of Congress "*…Do not play well with members of the other party…*" In 1979, Peter Allen and Carole Bayer Sager wrote a song that Frank Sinatra made popular. Some of the words of the song could possibly apply to this Congress:

You and me, we wanted it all...
You and me, we reached for the sky, the limit was high.
Never giving in, certain we could win that prize…
But look what we've become, isn't it a cryin' shame.
That we almost made it, But we wanted it all.

Very few of us can have it all.

Life is not perfect and no piece of legislation is 100% perfect for all Americans. President Lincoln told us that, *"You can satisfy some of the people all of the time, all of the people some of the time. But never all of the people all of the time."* It's time for this Congress to debate, negotiate, compromise and accomplish something in a bipartisan manner.

A failed administration hurts all of us.

**It's the American Dream that they are holding hostage,
and if they wait too long,
it could become the Impossible Dream.**

We have to get involved. There are three lobbyist for each member of Congress, and based on the TV ads, an unlimited amount of money. We need to tell Congress how we want them to vote. To get the name(s), address, phone and fax numbers of the senators or representatives you want to contact, go to the web site: www.senate.gov - OR - www.house.gov and also check your state's website for local issues.

Remember to vote on November 2, 2010!