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The Emergency Economic Stabilization Act of 2008

-by Neil E. Harl*

After a narrow rejection by the U.S. House of Representatives on September 29, approval by a comfortable margin by the U.S. Senate on October 2 and passage by the House on October 3 in a turn around from the September 29 vote, the Emergency Economic Stabilization Act of 2008 became law with the President's signature on October 3, 2008.[1] The shift in the House occurred with sharply deteriorating stock markets globally which convinced a group of hold outs that passage was in the national interest. What had started out as a crisis in the U.S. housing sector several months earlier had escalated into a credit crisis with credit markets spiraling rapidly downward as liquidity evaporated and risky strategies long pursued world-wide became a threat to economies around the globe.[2]

In order to induce some House members to switch positions on the legislation, the bill was expanded in intense negotiations to include several additional provisions, some of which were tax-related. Thus, the initial estimate of a $700 billion cost became considerably more expensive with the final cost largely unknown. Depending upon how successful the Department of the Treasury is in selling the "bad" paper acquired in the bail-out and propping up banks and other financial institutions, which is related heavily to when investor confidence are restored, the net cost ultimately could be significantly under $700 billion. On the other hand, the cost could well exceed estimates if the steps taken do not restore confidence in the financial system.

Emergency economic stabilization

The legislation gives the United States Treasury $250 billion to expend immediately and requires the President to certify if an additional $100 billion is necessary. An additional $350 billion may be disbursed with Congressional approval. The Department of the Treasury is to report on the use of funds and the progress made in addressing the financial crisis. An oversight board and a special inspector general are to be created to watch over the moves of the Department of the Treasury.

Foreclosure mitigation efforts. The 2008 Act specifies that, to the extent that ". . . the Secretary [of the Treasury] acquires mortgages, mortgage-backed securities, and other assets secured by residential real estate. . . the Secretary shall implement a plan that seeks to maximize assistance for homeowners and use the authority of the Secretary to encourage the servicers of the underlying mortgages, considering net present value to the taxpayer, to take advantage [of programs], .. . to minimize foreclosures." Note that the legislation only "encourages" servicers to take advantage of programs to minimize foreclosures. **Act § 109(a).**

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The Secretary is to consent, where appropriate, to reasonable requests for loss mitigation measures such as term extensions, rate reductions or principal write-downs. Note: again the Secretary is not given strong encouragement to address the plight of home owners facing foreclosure. **Act § 109(c).**

Ordinary loss treatment for Fannie Mae and Freddie Mac stock. The 2008 Act grants ordinary income *and ordinary loss* treatment to preferred stock in the Federal National Mortgage Asssociation[3] and the Federal Home Loan Mortgage Corporation[4] that has been held by financial institutions. That is the case if the preferred stock was held on September 6, 2008 or the stock was sold on or after January 1, 2008 and before September 7, 2008. The effective date is for sales or exchanges occurring after December 31, 2007, in tax years ending after 2007. **Act, § 301, Div. A, Title III.**

Limit on compensation. The Act imposes a $500,000 limit on income tax deductions for compensation paid to the CEO or the chief financial officer and the top three employees of institutions participating in the bail-out. The provision applies to companies with more than $300 million of assets purchased by the Department of the Treasury. **Act § 302, Div. A, Title III, adding I.R.C. § 162(m)(5)**

Mortgage debt forgiveness. The Act extends the relief on discharge of indebtedness of cancelled debt on a qualified principal residence through December 31, 2012. The forgiveness of indebtedness is limited to the acquisition indebtedness with the amount boosted for purposes of this provision to $2,000,000 on a joint return, $1,000,000 for a separate return. The discharge amount may be applied to reduce the income tax basis of the principal residence (but not below zero). The provision applies to discharges of indebtedness occurring on or after January 1, 2010. **Act § 303, Div. A, Title III, amending I.R.C. § 108(a)(1)(E).**

Energy improvement

Renewable energy credit. The Act extends for one additional year (through 2009) the credit for wind and a two year extension (through 2010) for certain other facilities. **Act § 101(a), Div. B, amending I.R.C. § 45(d).**

Small wind energy property. The legislation provides for a credit of up to $4,000 for qualified wind energy property. **Act § 104, Div. B, Title I, Subtitle A, amending I.R.C. § 48(a).**

Residential Alternative Energy Credit. The 2008 Act extended the non-refundable credit through 2016 (which helps individual taxpayers pay for specific residential alternative energy equipment installed on or in connection with a dwelling unit) and expanded the credit to include expenditures for small wind energy property and qualified geothermal heat pump property placed in service in 2008 through 2016. The $2,000 maximum annual credit limit for qualified solar electric property expenditures is eliminated after 2008. The residential alternative energy credit may be offset against regular tax and alternative minimum tax liabilities in 2008. **Act § 106, Div. B, amending I.R.C. § 25D.**

Credits for biodiesel and renewable diesel. The Act extends the credit for biodiesel and renewable diesel for an additional year through 2009. **Act § 202, Div. B, Title II, amending 40A(g).**

Alternative fuel credit. The Act extended the alternative fuel credit for three months, through December 31, 2009. The alternative fuel mixture credit is extended by three months, also, through 2009. **Act § 204, Div. B, Title II, amending I.R.C. § 6426(d), (e).**

Plug-in Electric Drive Motor Vehicle Credit. The Act enacts a new credit for tax years beginning after December 31, 2008, for new qualified plug-in electric drive motor vehicles placed in service after 2008 through 2014. The maximum amount of the credit is $2,500 plus $417 for each kilowatt hour of traction battery capacity in excess of four kilowatt hours. The provision is effective for tax years beginning after 2008 and for eligible property purchased before 2015. The provision is subject to the "sunset" rules as included in the 2001 tax act (EGTRRA) **Act § 205, Div. B, Title II, amending I.R.C. § 30D.**

Energy-efficient deduction for commercial buildings. The 2008 Act extends the energy-efficient commercial buildings deduction through 2013. **Act § 303, Div. B, Title III,.amending I.R.C. § 179D(h)**

Energy-efficient improvements for new homes. The 2008 legislation extends the credit for energy-efficient improvement sto new homes through 2009. **Act § 304, Div. B, Title III, amending I.R.C. § 45L(g).**

Energy-efficient appliance credit. The Act modifies and extends the energy-efficient appliance credit through 2010.The modifications apply to appliances produced after December 31, 2007. **Act 305, Div. B, Title III, amending I.R.C. § 45M(b).**

Extension of FUTA surcharge. The legislation extends the 0.2 percent FUTA surcharge on wages paid after December 31, 2008 through calendar year 2009. The tax rate is 6.2 percent through 2009 and 6.0 percent for 2010 and thereafter. The changes apply to wages paid after December 31, 2008. **Act § 404, Div. B, Title IV, amending I.R.C § 3301.**

Tax provisions

Alternative minimum tax. The legislation includes an increased exemption amount for alternative minimum tax (AMT) for 2008. Under the new law, the exemption is $69,950 for those married and filing jointly, $46,200 for single taxpayers and $34,975 for married taxpayers filing separately. That represents an increase over the figures for 2007 filing -- $66,250 for those married filing jointly, $44,350 for single taxpayers and $33,125 for married taxpayers filing separately. **Act § 102, Div. C, Title I, amending I.R.C. § 55(d)(1).**

For the tax year 2008, an individual taxpayer's entire regular tax liability and the alternative minimum tax liability may be offset by the non-refundable personal tax credits. **Act § 101, Div. C, Title I, amending I.R.C. § 26(a)(2).**

Depreciation classification for new farm machinery and equipment. For property placed in service after December 31, 2008 and before January 1, 2010, the classification has been changed statutorily from seven-year property to five-year property for new farm machinery and equipment used in a farming business as defined in I.R.C. § 263A(e)(4) (other than grain bins, cotton ginning assets, fences and land improvements). The original use for the property must commence with the taxpayer. Used machinery and equipment, grain bins, cotton ginning assets and farm fences remain as seven year property. Land improvements remain as 15-year property with single purpose agricultural and horticultural property remaining as 10-year property. The ADS life remains at 10-years for new machinery and equipment. **Act § 505, Div. C, Title V, amending I.R.C. § 168(e)(3)(B).**

Charitable giving. The bill also includes a two-year extension (through 2009) of the provision allowing taxpayers aged 70 ½ or older to transfer as much as $100,000 per year directly from an IRA to a charitable organization without triggering income tax on the contribution as income in respect of decedent. The amount transferred under the provision is not included in the donor's adjusted gross income. That is important because higher AGI levels can lead to loss of part of the itemized deductions and personal exemption amounts. **Act § 205, Div. C, Title II, amending I.R.C. § 408(d)(8).**

State and local taxes. The 2008 law revives a provision allowing taxpayers who itemize their deductions to deduct their state and local sales taxes, rather than state and local income taxes, but not both. The amended provision is effective for 2008 and 2009. Taxpayers have a choice in how they calculate the deduction. They can claim the actual amount of sales tax paid, assuming that good records are kept, or taxpayers can deduct the amount shown on IRS tables – plus taxes paid on certain items such as an automobile. **Act § 201, Div. C, Title II, amending I.R.C. § 164(b)(5).**

Deduction for tuition and fees. The new legislation extended, through 2009, a provision allowing a deduction for higher-education tuition and fees which has been available up to a $4,000 maximum deduction, depending upon the level of income. This deduction can be claimed whether or not the taxpayer itemizes their deduction – it is an "above-the-line" deduction. **Act § 202, Div. C, Title II, amending I.R.C. § 222(e).**

Child tax credit. The Act reduced the refundable threshold of the child tax credit from $12,050 to $8,500, effective for tax years beginning after December 31, 2007. **Act § 501, Div. C, Title V, Subtitle A, amending I.R.C. § 24(d)(4).**

Preparer standard. The standard for preparers for most undisclosed positions is reduced by the Act to substantial authority. The amendment conforms the standard to the taxpayer standard under I.R.C. § 6662. The preparer standard for disclosed positions as to whether the preparer has a "reasonable basis" except for listed transactions and reportable transactions with significant avoidance or evasion purposes was not amended – the tax preparer must have a reasonable belief that the position would more likely than not be sustained on the merits. The provision is effective retroactively to May 25, 2007 except for positions described in I.R.C. § 6694(a)(2)(C) for which the effective date is October 3, 2008. **Act § 506, Div. C, Title V, Subtitle A, amending I.R.C. § 6694(a).**

Temporary (one-year) increase in casualty losses from non-business property. The $100 floor for non-business casualty losses was raised for 2009 to $500 with the floor reverting to $100 after 2009. **Act §§ 706(c), Div. C, Title VII, Subtitle B, amending I.R.C. § 165(h)(1).**

Expenditures incurred by elementary and secondary school teachers. The deduction of up to $250 for designated expenditures in connection with calculation of adjusted gross income which are incurred by elementary and secondary teachers was extended through 2009. **Act § 203, Div. C, Title II, amending I.R.C. § 62(a)(2)(D).**

Additional standard deduction for real property taxes. The 2008 Act extended through 2009 the additional standard deduction for real property taxes for taxpayers who do not itemize. The provision applies to taxable years beginning after December 31, 2007. **Act § 204, Div. C, Title II, amending I.R.C. § 63(c)(1)(C).**

Basis adjustment for S corporations making charitable contributions. The Act extended the provisions providing for an income tax basis adjustment for S corporations making charitable contributions. The provision is effective for contributions made in taxable years beginning after December 31, 2007. **Act § 307, Div. C, Title III, amending I.R.C. § 1367(a)(2).**

The enhanced charitable deduction. The legislation extended the enhanced charitable deduction for food inventory through 2009. The Act eliminates, temporarily, the percentage limitation for contributions made by certain farmers and ranchers after December 31, 2007 through December 31, 2008. The deduction is limited to twice the taxpayer's basis in the food inventory (which is often zero for farmers and ranchers). The provision is effective for contributions after 2007. **Act § 323, Div. C, Title III, amending I.R.C. § 170(e)(3)(C).**

Environmentally contaminated sites. The 2008 Act extends the provision allowing the expensing of costs stemming from cleaning up environmentally contaminated sites, through 2009. The provision is effective for expenditures paid or incurred after December 31, 2007. **Act § 318, Div. C, Title III, amending I.R.C. § 198(h).**

ENDNOTES

[1] Pub. L. 110-343, 110th Cong., 2d Sess. 2008).

[2] See generally Harl, "Will the Bail-out Halt Financial Panic?" *AgLender* Vol. 12, Issue 11, pp. 8-9, Nov., 2008; Elbert, "ISU's Harl: Finances Worse Than We Thought," *Des Moines Sunday Register*, September 28, 2008.

[3] 12 U.S.C. § 1716 *et seq*.

[4] 12 U.S.C. § 1451 *et seq*.