

2010 Tax Relief Enacted

December 2010

The Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (2010 TRA) was enacted on December 17, 2010. The legislation postpones certain sunset provisions under The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) relating to federal individual income-tax rates (commonly referred to as the Bush-era tax cuts). The Act contains numerous business-related provisions, such as incentives for businesses to invest in machinery and equipment, as well as several other tax breaks for individuals.

Much of the new law simply retains favorable tax rules that applied in prior years. It includes a temporary extension of favorable dividend and long-term capital gains rates, as well as estate-tax relief. The Act also provides a two-year AMT “patch,” and a two percentage point reduction in employee paid payroll taxes (and self employment tax) for 2011. Following is a summary of the Act’s key provisions.

Individual Taxpayers Provisions

- The 2010 TRA retains the more favorable 2010 individual marginal tax rates for 2011 and 2012: 10%, 15%, 25%, 28%, 33%, and 35%. The 2011 rates were scheduled to be 15%, 28%, 31%, 36%, and 39.6%.
- Marriage penalty relief is extended through 2012.
- Favorable tax rates (15% for most taxpayers, 0% for those in the 10% or 15% tax brackets) on net capital gains are extended through 2012.
- Qualified dividends continue to be subject to the same maximum rates as net capital gains through 2012.
- The Act extends the 100% capital gain exclusion for qualified small business stock (QSBS) through 2011.

- For 2011 only, employees will pay a 4.2% (instead of 6.2%) Social Security Tax on wages up to \$106,800. Similarly, the new law reduces the tax rate for the Social Security portion of self employment tax on self employment net earnings up to \$106,800.
- The Act delays the sunset provisions relating to the limitation on itemized deductions and personal exemptions for certain higher income taxpayers for two years, through 2012.
- The maximum available credits for both the Child Tax Credit and Dependent Care Credit are extended through December 31, 2012.
- The American Opportunity Tax Credit (formerly the Hope Credit) is extended for 2011 and 2012.
- The maximum per beneficiary contribution limitation of \$2,000 for Coverdell Education Savings Accounts (ESAs) is extended through 2012.
- The above-the-line qualified tuition deduction is retroactively reinstated and extended for 2010 and 2011.
- The \$2,500-a-year limitation for deducting higher education student loan interest (including higher income phase out limits) is extended through 2012.
- The 2010 TRA retroactively applies (to 2010 and extends through 2011) an “AMT patch,” raising the exemption amounts before an individual is subject to AMT.
- The favorable changes made by prior law to the adoption credit, which is available to individuals who adopt an eligible child, are extended through 2012.

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- The Act retroactively extends the election for taxpayers to claim an itemized deduction for state and local general sales tax, instead of a deduction for state and local income taxes, through 2011.
- Certain energy credits are extended for non-business energy property placed in service by December 31, 2011, although credit rates, dollar, and lifetime limits revert to prior, less favorable levels.
- The Act retroactively reinstates and extends the deduction available to K-12 teachers (and certain other educators) for eligible out-of-pocket expenses for supplies and equipment for 2010, and through 2011.
- The tax-free treatment (up to \$100,000 a year) of IRA charitable distributions by persons age 70½ or older is retroactively reinstated and extended for 2010 and 2011.
- The Act retroactively extends for 2010 and 2011 the rules permitting a C corporation to claim an enhanced deduction for contributions of computers and book inventories to public schools.
- Under the Act, employers may continue to provide employees up to \$5,250 of educational assistance free of federal income tax through 2012.
- The Act also contains provisions relating to enhanced income tax free benefits from an employer's adoption-assistance program.

Estate-, Gift-, and GST-Tax Provisions

For 2010, 2011, and 2012, the 2010 TRA provides a more favorable tax rate and exemption amount than those previously scheduled to go into effect for 2011 and beyond.

- The Act reduces the impact of estate and gift taxes in 2011 and 2012 by increasing the exemption amount to \$5 million (subject to a potential inflation adjustment in 2012) and reducing the top gift- and estate-tax rate to 35%.
- Due to the \$5 million exemption, the estate- and gift-tax rate in 2011 and 2012 is effectively a flat 35%.
- The Act also subjects the estates of individuals who died in 2010 to estate tax (with a \$5 million exemption amount and a 35% rate) unless the estate's executor elects to have certain "carryover basis" rules apply.
- The new law allows a deceased spouse's executor to elect to transfer any unused estate-tax exemption to the surviving spouse. This provision is effective for 2011 and 2012.
- The Act reinstated the GST tax, effective for 2010, and set the exemption to equal the \$5 million estate- and gift-tax exemption amount for 2010, 2011, and 2012 (subject to inflation adjustment in 2012). Note that the applicable GST-tax rate for 2010 is 0%, effectively keeping the repeal of the GST tax in place. In 2011 and later, the GST-tax rate returns to the highest federal estate-tax rate.

Call the professionals at Doeren Mayhew today to help determine how the new law affects you.

Provisions Affecting Business Taxpayers

The 2010 TRA includes several tax incentives aimed at spurring business investment in machinery, equipment, and other assets.

- The new law generally allows businesses to deduct 100% of the cost of qualified property acquired and placed in service after September 8, 2010, and before January 1, 2012 (conditions apply). Note that the new law does not place a dollar limit on the amount of qualified property eligible for the 100% write-off.
- The new law allows businesses to make an election to write off 50% of the cost of qualified property placed in service during 2012 (and 2013 for certain longer lived and transportation property).
- The new law sets the dollar limitation on property eligible for the Section 179 expensing election at \$125,000, as indexed for inflation, for the 2012 tax year. The \$125,000 limit will be reduced dollar for dollar as the cost of Section 179-eligible property placed in service during the 2012 tax year exceeds \$500,000, as indexed for inflation.
- Various business credits have been extended by the Act, including the research credit, Work-opportunity credit, differential wage credit, and the credit for employer provided child care.
- The penalty tax rate applicable to accumulated earnings will be 15% (not 20%) for tax years beginning before 2013.

