

# How the 2010 Tax Act impacts you

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On 17 December 2010, President Obama signed into law The Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (the "2010 Tax Act"). The following is a primer on the changes made to the federal income, gift, estate and generation-skipping tax:

## FEDERAL INCOME TAX

### Income Taxes:

The Bush-era tax brackets of 10%, 15%, 25%, 28%, 33% and 35% are extended through 2012 (avoiding a return to pre-2001 levels). The personal exemption phase out and limit on itemized deductions for higher-income tax payers will also not apply for two years. Both served as "back-door tax increases" for many affluent taxpayers.

### Capital Gains Tax:

The 0% capital gains tax rate remains in effect for taxpayers in the 10% and 25% income tax bracket. All other taxpayers, those in the 28%, 33% and 35% income tax bracket, will pay a 15% tax on long-term capital gains.

### Extended Tax Credits & Incentives:

The \$1,000 per child credit, dependent care credit, adoption tax credit and assistance program, employer credit for child care, earned income tax credit, Coverdell education savings accounts, employer-provided educational assistance, expanded student loan interest deductions, \$250 classroom supplies deduction for teachers, state and local sales tax

deduction and the American Opportunity Tax Credit (an expansion of the HOPE tax credit) are all extended through 2012. These changes should be noted as they modify the guidance provided in my January 2011 tax return article.

### Alternative Minimum Tax (AMT):

The 2010 AMT exemption amounts are adjusted to \$72,450 for couples and \$47,450 for single persons. In 2011, the AMT exemption amounts will increase to \$48,450 and \$74,450 respectively. This change should also be noted as it modifies the guidance provided in my January 2011 tax return article.

### Charitable Giving:

The law resurrects an expired tax provision to provide taxpayer's, age 70 and older, with the ability to contribute up to \$100,000 from an individual retirement account ("IRA") directly to a qualifying charitable organization without recognizing the distribution as taxable income. The tax benefit is extended through 2011 and provides taxpayers, who desire to make a 2010 charitable donation from their IRA, until 31 January 2011 to make the donation and have it count for 2010.

The IRA distributed funds may serve as the taxpayers' required minimum distribution. To qualify, the charitable gift must pass directly from the IRA sponsor to the charitable organization. An added benefit of utilization of the provision will allow the taxpayer to avoid an increase in Medicare premiums and an increase

in Social Security taxes. However, the taxpayer is not entitled to a corresponding charitable deduction for the distribution.

## FEDERAL ESTATE AND GIFT TAXES

### Federal Estate Tax:

For 2011 and 2012, the federal estate tax exemption will be \$5 million, with a top estate-tax rate of 35%, reinstatement of the "step-up in basis" and marital deduction portability. The law provides estate administrators (personal representatives and executors) of 2010 estates to elect whether to use the 2010 rules or new 2011 rules. This allows estate beneficiaries to select between (1) having no estate tax, but a step-up in basis of only \$1.3 million for an heir and \$3 million for a surviving spouse; or (2) an estate tax exemption of \$5 million, 35% estate tax rate on amounts above the exemption, and a full step-up in basis.

The law additionally allows the estates of decedents dying after 31 December 2010 to transfer any unused estate tax exemption amount to a surviving spouse. This eliminates the need for spouses to insure an equalization of estates prior to the first spouse's death.

### Federal Gift Tax Exemption:

The federal gift tax exemption is increased to \$5 million per individual. Gifts in excess of the exemption amount will be taxed at the rate of 35%. The annual exclusion remains at \$13,000 in 2011 and will be indexed for inflation in 2012.

### **Federal Generation-Skipping Tax Exemption:**

The federal generation-skipping tax exemption is increased to \$5 million per individual. Generation-skipping gifts in excess of the exemption amount will be taxed at the rate of 35%.

## **EXTENDED MILITARY BENEFITS**

### **Employer Wage Credit for Activated Military Reservists:**

The law extends through 31 December 2011 for eligible small business employers, a credit equal to twenty (20%) percent of the amount of differential wage payments made to a mobilized Reservist.

### **Work Opportunity Tax Credit:**

The law extends through 31 December 2011 the current tax credit, equal to forty (40%) percent of the first \$6,000 of wages paid by a business, for the hiring of a new employee in one of nine targeted groups. The targeted groups include family members receiving benefits under the Temporary Assistance to Needy Families (TANF) program, qualified veterans, designated community residents, etc. ↴