

The Economic Growth and Tax Relief

Reconciliation Act of 2001

Eagerness and anticipation over promises of tax cuts were put to rest when President Bush signed the new 1.35 trillion tax reduction law on June 7, 2001. With the new law came real results of tax rebates, lower tax brackets and elimination of the widely unpopular "marriage penalty" and inheritance or "death" tax. Most of the changes will be phased in over a ten year period, so the purpose of this article will be to highlight some of the more widespread, timely and applicable changes.

TAX RATE REDUCTION

The lowest personal income tax rate, now at 15%, will be 10% retroactive to July 1, 2001. A one-time tax rebate (which will range from \$300 for single non-dependent taxpayers to \$600 for married couples) will be issued to taxpayers who filed their 2000 form 1040. The current top tax rate of 39.6% will be capped at 35% by the year 2006, with internal brackets at 15%, 25%, 28% and 33%.

CHILD TAX CREDIT

The current \$500 maximum credit for dependent children under age 17 will eventually double to \$1,000 by the year 2010. Income level phase-outs will increase to allow more taxpayers to benefit from this change.

MARRIAGE PENALTY

The so-called penalty that married taxpayers pay as opposed to two single people living together will be eventually eliminated. The increase in the standard deduction by 2009 will be equal to twice the single amount, which will only benefit taxpayers who do not itemize deductions. Eventually the taxable income level at which the rate bracket changes will effectively mirror a double single bracket, thus eliminating the inequity.

401 (K) and IRA Changes

The new maximum IRA contribution is \$3,000 beginning in 2001 and increasing to \$5,000, per qualifying taxpayer, by 2008. A special catch-up feature will be added for taxpayers who are age 50 or older in the year 2002. Maximum 401 (k), 403 (b) and 457 plan contributions will increase from \$11,000 to \$15,000 by 2006.

EARNED INCOME CREDIT

Parity between married and single taxpayers is also addressed in this area. Income level phase-outs will increase by \$1,000 in 2002-2004, \$2,000 in 2005-2007 and \$3,000 after 2007.

ADOPTION CREDIT

Adoption expenses up to \$10,000 will be credited to persons with adjusted gross income less than \$150,000 (phased in after 2001).

DEPENDENT CARE TAX CREDIT

Maximum allowable related expenses increases from \$2,400 to \$3,000 for one child and \$4,800 to \$6,000 for two children after 2002.

EDUCATION IRAs AND COLLEGE TUITION DEDUCTION

Increases from \$500 per child to \$2,000, through age 17 with, proceeds treated as non-taxable and available for elementary and secondary education costs. College tuition will be deductible for both itemizers and standard deduction taxpayers as an above the line deduction. Up to \$3,000 is deductible for married taxpayers with adjusted gross income less than \$130,000. Student loan interest deduction will be available to taxpayers who were otherwise income level phased-out, when levels are increased to \$65,00 for single and \$130,000 for married.

ESTATE TAX PHASE-OUT

The estate tax applies to property owned by individuals at the time of death. The maximum rate of 60% in 2001 will be reduced to 50%, then to 45%, before the tax is temporarily repealed in 2010. The individual exemption will go immediately to \$1million then increases to \$3.5 million by 2009. The bad news is that there is no indication to the contrary that this favorable legislation won't sunset in 2010.

EMPLOYER-PROVIDED RETIREMENT PLANS

New relaxed provisions will increase the allowable contributions to defined contributions and other qualified plans (profit-sharing, pension, etc). Effective after 2001, employees may contribute the lesser of 100% of compensation or \$40,000 (was \$35,000 or 25% of compensation).

Other unpopular provisions of the current law such as itemized deductions and personal exemption phase-outs will be repealed beginning in 2006. The alternative minimum tax (AMT) exemption amounts will increase, beginning this year, by \$4,000 for married filers.

This new law, with 85 major provisions and 441 Internal Revenue code changes, is the most impacting tax reduction in 20 years. I am eagerly awaiting tax filing early next year when I will demonstrate real tax relief to virtually all of my clients, regardless of income level and family status. As always I welcome your questions and comments.

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