

# TAX RELIEF/JOB CREATION ACT OF 2010

December 16, 2010

Special Report

## HIGHLIGHTS

- Reduced Individual Tax Rates
- Reduced Capital Gains/Dividend Tax Rates
- \$1,000 Child Tax Credit
- AOTC And Other Education Incentives
- Two-Year AMT Patch
- Payroll Tax Cut
- 100 Percent Bonus Depreciation
- Business Extenders
- Energy Incentives
- Estate Tax Relief

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## Congress Passes Two-Year Extension Of Bush-Era Tax Cuts, Payroll Tax Relief, Estate Tax Compromise

Congress has approved, and President Obama is expected to quickly sign, a multi-billion dollar tax cut package, the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (2010 Tax Relief Act) (H.R. 4853). The new law follows through on the framework agreed to December 6 by President Obama and GOP leaders in Congress. The 2010 Tax Relief Act extends the Bush-era individual and capital gains/dividend tax cuts for all taxpayers for two years. The bill also provides for an AMT “patch,” a one-year payroll tax cut, 100 percent bonus depreciation through 2011 and 50 percent bonus depreciation for 2012, a top federal estate tax rate of 35 percent with a \$5 million exclusion, and more.

**IMPACT.** *The new law gives taxpayers some certainty in tax planning for the next two years, especially concerning the individual income tax rates, capital gains/dividend tax rates and the estate tax. However, the provisions are temporary and the new law punts the ultimate fate of the Bush-era tax cuts to 2012, a presidential election year.*

The framework unveiled on December 6 initially met with strong opposition on a number of fronts. The bi-partisan agreement eventually held together, however, as consensus grew that delay into next year was untenable. The Senate passed the 2010 Tax Relief Act on December 15 by an overwhelming 81 to 19 margin. The House followed with its approval on December 16 by a vote of 277 to 148 that now sends the bill to the White House.

**IMPACT.** *For most individuals, the most immediate impact of the new law will be the payroll tax cut and the extension of the reduced individual income tax rates. The IRS has cautioned Congress that it would need time to program its computer systems for late legislation. It is possible that taxpayers will not see the effects of the payroll tax cut until mid January 2011.*

## INDIVIDUALS

### Individual Tax Rates

Under the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), the individual income tax rates had been scheduled to revert from their current levels of 10, 15, 25, 28, 33, and 35 percent to 15, 28, 31, 36, and 39.6 percent after December 31, 2010. The 2010 Tax Relief Act extends all individual rates at 10, 15, 25, 28, 33 and 35 percent for two years, through December 31, 2012.

**IMPACT.** *EGTRRA made across the board rate reductions and the 2010 Tax Relief Act will keep all of them, albeit for only two years, at an estimated cost of over \$186 billion. President Obama has said he will make the sunset of the two highest brackets an issue in the 2012 presidential campaign. Also being readied for later debate by certain GOP leaders is the status of post-2012 health care taxes —higher-income individuals will also be faced with additional taxes after 2012 in the form of a 0.9 percent additional Medicare tax and a 3.8 percent Medicare contribution tax.*

**IMPACT.** Combined with the payroll tax cut (discussed below), the extension of the individual rate cuts will give many individuals a significant increase in immediate dollars available to them in 2011 over what would have resulted without a tax bill. For example, an individual earning \$50,000 in 2011 will see an approximate tax savings of \$1,890 in combined income tax and payroll tax rate reductions (\$890 and \$1,000, respectively) over what was scheduled under the EGTRRA sunset.

The income tax rate schedule used by estates and nongrantor trusts (15, 25, 28, 33 and 35 percent) also has been extended for two years. The 10 percent bracket established under EGTRRA for individuals has never applied to estates and trusts.

### Capital Gains/Dividends

Qualified capital gains and dividends currently are taxed at a maximum rate of 15 percent (zero percent for taxpayers in the 10 and 15 percent income tax brackets) for 2010. The 2010 Tax Relief Act continues

this treatment for two years, through December 31, 2012.

**IMPACT.** Without any action on Capitol Hill, the maximum rate on net capital gain had been scheduled to rise to 20 percent in 2011 (10 percent for taxpayers in the 15 percent bracket), under the sunset rule within the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA). Without the 2010 Tax Relief Act, the rate on qualified dividends also would have risen from 15 percent to the tax rates on regular income that threatened to reach as high as 39.6 percent.

**COMMENT.** The 2010 Tax Relief Act also extends the 100 percent exclusion of gain realized from qualified small business stock held for more than five years. See *Business Incentives/Small Business Stock*, below, for details.

Qualified dividends, which continue to be eligible for the reduced tax rates, are dividends received from a domestic corporation or a qualified foreign corporation, on which the underlying stock is held for at

least 61 days within a specified 121 day period. A qualified foreign corporation is eligible for U.S. treaty benefits or has stock that is readily tradable on an established U.S. securities market. The reduced tax rates do not apply to dividends received from an organization that is exempt from taxation under Code Sec. 501 or was a tax-exempt farmers' cooperative in either the tax year of the distribution or the preceding tax year, dividends received from a mutual savings bank that received a deduction under Code Sec. 591, or deductible dividends paid on employer securities.

**PLANNING TIP.** While the extension of the maximum capital gains tax rate is receiving the most press attention, continuation of the zero percent rate will be equally as important to many taxpayers, from graduate students to retirees to those who live on their portfolio savings. To the extent that capital gains and dividends, when added to other taxable income, do not exceed the top of the 15 percent income tax bracket (\$34,500 for single individuals or \$69,000 for joint filers in 2011), those capital gains and dividends are effectively tax-free, subject to the zero percent rate. Gifts of appreciated securities to taxpayers in that rate bracket might also continue to be a worthwhile technique to maximize the value of such gifts.

**CAUTION.** Installment payments are subject to the tax rates for the year of the payment, not the year of the sale. Thus, the capital gains portion of payments made after 2012 may be subject to a higher 20-percent rate under sunset provisions, irrespective of whether the sales agreement was executed in a year, such as 2010, 2011 or 2012, in which the maximum capital gains rate was set at a lower rate.

The 2010 Tax Relief Act also extends the treatment of dividends received from a regulated investment company (RIC), real estate investment trust (REIT) and other qualified pass-through entities as qualified dividends for purposes of the reduced tax rates. Rules setting the accumulated earnings tax and

## CCH PROJECTED TAX RATES FOR 2011 UNDER THE 2010 TAX RELIEF BILL

### Single Individuals

If taxable income is:	The tax will be:
Not over \$8,500	10% of taxable income
Over \$8,500 but not over \$34,500	\$850.00 plus 15% of the excess over \$8,500
Over \$34,500 but not over \$83,600	\$4,750.00 plus 25% of the excess over \$34,500
Over \$83,600 but not over \$174,400	\$17,025.00 plus 28% of the excess over \$83,600
Over \$174,400 but not over \$379,150	\$42,449.00 plus 33% of the excess over \$174,400
Over \$379,150	\$110,016.50 plus 35% of the excess over \$379,150

### Married Couples Filing Jointly

If taxable income is:	The tax will be:
Not over \$17,000	10% of taxable income
Over \$17,000 but not over \$69,000	\$1,700.00 plus 15% of the excess over \$17,000
Over \$69,000 but not over \$139,350	\$9,500.00 plus 25% of the excess over \$69,000
Over \$139,350 but not over \$212,300	\$27,087.50 plus 28% of the excess over \$139,350
Over \$212,300 but not over \$379,150	\$47,513.50 plus 33% of the excess over \$212,300
Over \$379,150	\$102,574.00 plus 35% of the excess over \$379,150

personal holding company tax at the maximum 15 percent rate for qualified dividends are also extended.

**COMMENT.** *The current 28 and 25 percent capital gains rates for collectibles and recaptured 1250 gain, respectively, would continue unchanged.*

### Itemized Deduction Limitation

The “Pease” limitation (named after the member of Congress who sponsored the bill enacting it) reduces the total amount of a higher-income individual’s otherwise allowable deductions. Under EGTRRA, the Pease limitation is repealed for 2010 but was scheduled to return in full after 2010 at a projected level of income starting at \$169,550 (\$84,775 for married couples filing separately). The 2010 Tax Relief Act extends full repeal of the Pease limitation for two years, through December 31, 2012.

**COMMENT.** *The Pease limitation was gradually repealed starting in 2006 until fully repealed for 2010. Certain deductions (medical expenses, investment interest, casualty, theft, and wagering losses), however, have never been impacted by the Pease limitation.*

### Personal Exemption Phaseout

Before 2010, taxpayers with incomes over certain thresholds were subject to the personal exemption phaseout (PEP). The PEP reduced the total amount of exemptions that may be claimed by two percent for each \$2,500 or portion thereof (\$1,250 for married couples filing separate returns) by which the taxpayer’s adjusted gross income (AGI) exceeded the applicable threshold (projected for 2011 to start at \$169,550 for singles and \$254,350 for joint filers). Under EGTRRA, the PEP is repealed for 2010. The 2010 Tax Relief Act extends repeal of the PEP for two years, through December 31, 2012.

**COMMENT.** *The personal exemption amount for 2010 is \$3,650. CCH projects the inflation-adjusted personal ex-*

*emption amount for 2011 will rise to \$3,700. The IRS is expected to release the official personal exemption amount after H.R. 4853 is signed by the president.*

**IMPACT.** *The Joint Committee on Taxation estimates that higher-income taxpayers will save over \$20 billion from the combined itemized deduction and personal exemption provisions in the new law.*

“For most individuals, the most immediate impact of the new law will be the payroll tax cut and the extension of the reduced individual income tax rates.”

### Marriage Penalty Relief

EGTRRA provided relief from the so-called marriage penalty by increasing the basic standard deduction for a married couple filing a joint return to twice the amount for a single individual. EGTRRA also temporarily expanded the size of the 15 percent income tax rate bracket for married couples filing a joint return to twice that of single filers to help mitigate the marriage penalty. The 2010 Tax Relief Act extends EGTRRA’s marriage penalty relief for two years, through December 31, 2012.

**IMPACT.** *Under EGTRRA’s sunset rules, the 2011 standard deduction for married couples filing jointly was projected to be \$9,650. CCH projects that under the new law it will be \$11,600 for 2011 (compared to \$11,400 for 2010).*

**IMPACT.** *Under EGTRRA sunset rules, the 15 percent bracket in 2011 for joint filers was projected to end at \$57,650. The new law effectively raises it to \$69,000.*

### Child Tax Credit

The 2010 Tax Relief Act extends the \$1,000 child tax credit for two years, through December 31, 2012. Also extended for two years are enhancements to the credit made by EGTRRA, the 2009 Recovery Act and other bills. The 2010 Tax Relief Act also extends alternative minimum tax (AMT) benefits: the credit is allowed against the AMT and the refundable portion is not reduced by the AMT.

**IMPACT.** *The child credit continues to be phased out for taxpayers with adjusted gross income starting at \$110,000 for joint filers (\$75,000 for others). The qualifying child must be under age 17 at the close of the year and satisfy relationship, residency, support, citizenship, and dependent tests.*

**IMPACT.** *Under EGTRRA’s sunset rules, the child credit was scheduled to revert to \$500 per qualifying child.*

**COMMENT.** *To the extent the child tax credit exceeds an individual’s tax liability, the taxpayer may be eligible for a refundable credit (the additional child tax credit) equal to 15 percent of earned income in excess of a threshold dollar amount. Under EGTRRA, the threshold was \$10,000 indexed for inflation. The 2009 Recovery Act reduced the threshold to \$3,000 for 2009 and 2010. The 2010 Tax Relief Act extends the \$3,000 threshold for two years, through December 31, 2012. However, the 2010 Tax Relief Act does not provide for indexing for inflation of the \$3,000 threshold beyond 2010.*

### Earned Income Tax Credit

EGTRRA and subsequent legislation temporarily increased the beginning and end points of the earned income tax credit (EITC), increased the credit for three or more children and made other taxpayer friendly changes. Legislation also simplified the definition of earned income, eliminated the rule that reduced a taxpayer’s EITC by the amount of AMT liability, reformed the

relationship test, modified the tie-breaking rule, and gave the IRS additional math error authority. All these enhancements were subject to the general EGTRRA sunset of December 31, 2010. The 2010 Tax Relief Act extends the enhanced EITC for two years, through December 31, 2012.

**COMMENT.** *Increasing the beginning and end points of the EITC helps to ameliorate a marriage penalty within the EITC.*

**COMMENT.** *In August 2010, President Obama signed legislation (P.L. 111-226) abolishing the advance payment option for the EITC. EGTRRA's sunset does not revive the advance EITC.*

### Adoption Credit

Taxpayers who incur qualified adoption expenses may be eligible for the adoption credit or, in the case of employer-provided assistance, an exclusion from income. EGTRRA increased the dollar limitation for the adoption credit and the income exclusion for employer-paid or reimbursed adoption expenses to \$10,000 (indexed for inflation) (both for non-special needs adoptions and special needs adoptions). The Patient Protection and Affordable Care Act (PPACA) increased the credit and exclusion by another \$1,000 (adjusted for inflation) for 2010 and 2011. The PPACA also made the adoption credit refundable for 2010 and 2011. The 2010 Tax Relief Act extends the enhancements in EGTRRA to the credit and exclusion amount through December 31, 2012.

**IMPACT.** *Both the adoption credit and the exclusion amount phase out ratably for taxpayers with modified AGI between \$182,520 and \$222,250 (indexed for inflation after 2010).*

**COMMENT.** *The 2010 Tax Relief Act does not extend the enhancements to the adoption credit and exclusion made by the PPACA. Therefore, the credit is not refundable for 2011 and 2012 and the additional \$1,000 under the PPACA is not available after 2010.*

### Dependent Care Credit

A taxpayer who incurs expenses to care for a child under age 13 or for an incapacitated dependent or spouse to enable him or her to work or look for work can claim a dependent care credit. EGTRRA temporarily increased the maximum amount of eligible expenses for the dependent care credit from \$2,400 to \$3,000 (from \$4,800 to \$6,000 for more than one qualifying individual). EGTRRA also raised the maximum credit from 30 to 35 percent of qualifying expenses and provided for a reduction in the credit, but not below 20 percent, by one percentage point for each \$2,000, or fraction thereof, of AGI above a \$15,000 threshold amount. The 2010 Tax Relief Act extends the enhanced dependent care credit for two years, through December 31, 2012.

**IMPACT.** *The 35 percent rate under the 2010 Tax Relief Act therefore continues to be applied to a maximum \$3,000 of eligible expenses, \$6,000 for more than one eligible dependent (for a maximum \$1,050/\$2,100 credit). The 35-percent credit rate will also continue to be reduced, but not below 20 percent, by each percentage point of AGI above \$15,000.*

### Employer-Provided Child Care

Employers that provide child care facilities may be eligible for a tax credit. Under EGTRRA, employers have been eligible for a tax credit equal to 25 percent of qualified expenses for employee child care plus an amount equal to 10 percent of qualified expenses for child care resource and referral services. The credit is subject to a \$150,000 annual cap on qualified costs. The new law extends the credit for two years, through December 31, 2012.

**COMMENT.** *Qualified costs include, but are not limited to, costs paid to acquire, construct or rehabilitate a property to serve as a child care facility as well as costs of training and compensating employees of the child care facility.*

### Mortgage Insurance Premiums

Under current law, taxpayers may deduct certain premiums paid for qualified mortgage insurance during the tax year in connection with acquisition indebtedness on a qualified residence. The deduction is subject to phase-out based on a taxpayer's income. The 2010 Tax Relief Act extends the deduction for one year subject to some limitations.

### American Opportunity Tax Credit

The 2009 Recovery Act enhanced and renamed the Hope education credit as the American Opportunity Tax Credit (AOTC) for 2009 and 2010. The 2010 Tax Relief Act extends the AOTC for two years, through December 31, 2012. Also extended are income limitations (the AOTC begins to phase out for single individuals with modified AGI of \$80,000 (\$160,000 for married couples filing jointly) and completely phases out for single individuals with modified AGI of \$90,000 (\$180,000 for married couples filing jointly).

**IMPACT.** *Qualified taxpayers with higher education expenses will continue to benefit from an AOTC that is 40 percent refundable. However, the AOTC is not refundable if the taxpayer claiming the credit is a child who has at least one living parent, does not file a joint return, and meets other criteria.*

**COMMENT.** *The AOTC can be claimed for all four years of postsecondary education. The old HOPE credit was limited to the first two years of post-secondary education.*

### Educational Assistance Exclusion

EGTRRA allows employees to exclude up to \$5,250 in employer-provided education assistance annually from income and employment taxes. Employers may deduct up to \$5,250 annually for qualified education expenses paid on behalf of an employee. This treatment was scheduled to expire after 2010. The 2010 Tax Relief Act extends these provisions for two years, through December 31, 2012.

**IMPACT.** *Prior to EGTRRA, graduate school tuition assistance did not qualify for the exclusion. EGTRRA allows graduate school tuition to qualify and the 2010 Tax Relief Act extends this benefit for two years.*

### Student Loan Interest Deduction

EGTRRA eliminated a 60-month rule for the \$2,500 above-the-line student loan interest deduction and expanded the modified AGI range for phase-out. This treatment was scheduled to expire after December 31, 2010. The 2010 Tax Relief Act extends the enhancements for two years, through December 31, 2012.

### Coverdell Education Savings Accounts

EGTRRA increased the maximum contribution amount to a Coverdell Education Savings Account (ESA) from \$500 to \$2,000 and, among other things, made elementary and secondary school expenses, in addition to post-secondary school expenses, qualified expenses. These enhancements were scheduled to sunset after 2010. The 2010 Tax Relief Act extends them for two years, through December 31, 2012.

### Scholarships

Under EGTRRA, the National Health Service Corps Scholarship Program and the Armed Forces Scholarship Program are qualified scholarships for exclusion from income purposes. Because of EGTRRA's sunset rules, these scholarships were scheduled to be included in a recipient's income after 2010. The 2010 Tax Relief Act extends the income exclusion for these scholarships for two years, through December 31, 2012.

### Individual Tax Extenders

The 2010 Tax Relief Act extends a number of temporary individual tax incentives which had expired at the end of 2009. These incentives, known as extenders, are extended for two years (2010 and 2011).

The individual incentives are:

- State and local sales tax deduction
- Higher education tuition deduction
- Teacher's classroom expense deduction
- Charitable contribution of IRA proceeds
- Charitable contributions of appreciated property for conservation purpose

**COMMENT.** *The amount of qualified tuition and related expenses for the higher education tuition deduction must be reduced for certain items. These include any exclusion from gross income for a Coverdell ESA and income from savings bonds used to pay higher education tuition and fees. Other limits also apply relating to the HOPE and Lifetime Learning credits.*

**COMMENT.** *The 2010 Tax Relief Act does not extend the additional standard deduction for real property taxes, which expired at the end of 2009.*

### ALTERNATIVE MINIMUM TAX

The 2010 Tax Relief Act provides an AMT "patch" intended to prevent the AMT from encroaching on middle income taxpayers by providing higher exemption amounts and other targeted relief for 2010 and 2011. Without this patch, which had expired at the end of 2009, an estimated 21 million additional households would be subject to the AMT.

The 2010 Tax Relief Act increases the exemption amounts for 2010 to \$47,450 for individual taxpayers, \$72,450 for married taxpayers filing jointly and surviving spouses, and \$36,225 for married couples filing separately.

**IMPACT.** *Without the AMT patch, the exemption amounts for 2010 and again for 2011 would have dropped to \$33,750 for unmarried individuals filing a single return, \$45,000 for married couples filing a joint return and surviving spouses, and \$22,500 for married individuals filing a separate return. The exemption amounts under the 2009 patch were \$46,700 for unmarried individuals filing a single return, \$70,950 for married couples filing a joint return and surviving spouses, and \$35,475 for married couples filing a separate return.*

**COMMENT.** *The President's Deficit Commission recommended on December 1, 2010 what some experts are calling a "super AMT" for all taxpayers that would replace the current income tax and AMT structure entirely. A "super AMT" would be similar to the current AMT in denying certain tax preference items... but more so, with many more deductions and credits disallowed in computing taxable income. For example, the mortgage interest deduction might be severely or completely eliminated. In exchange, tax rates would be significantly lower than they now exist. President Obama has endorsed a serious discussion of tax reform starting next year. Momentum for a broader solution to annual AMT "patches" may gradually start to build.*

### PAYROLL TAX CUT

The 2010 Tax Relief Act reduces the employee-share of the OASDI portion of Social Security taxes from 6.2 percent to 4.2 percent for wages earned in calendar year 2011 up to the taxable wage base of \$106,800.

### AMT PATCH

**Exemption amounts for 2010 and 2011 with/and without a patch:**

	2010	2011
Single individuals/not surviving spouse:	\$47,450/\$33,750	\$48,450/\$33,750
Married couples filing jointly/surviving spouse:	\$72,450/\$45,000	\$74,450/\$45,000
Married couples filing separately:	\$36,225/\$22,500	\$37,225/\$22,500

Self-employed individuals would pay 10.4 percent on self-employment income up to the threshold.

**IMPACT.** *The new payroll tax holiday is estimated to inject over \$110 billion into the economy in 2011. Unlike the Making Work Pay credit, which will expire as scheduled after 2010, the two percent OASDI reduction is available to all wage earners, with no phase out limit irrespective of income level. Thus, individuals earning at or above the OASDI cap of \$106,800 will receive a \$2,136 tax benefit in 2011.*

**EXAMPLE.** *Jason earns \$50,000 a year and pays OASDI on his earnings. Under the 2010 Tax Relief Act, Jason's employee-share of OASDI tax is reduced from 6.2 percent to 4.2 percent for 2011. Instead of paying \$3,100 in OASDI tax for 2011, Jason would pay \$2,100 in OASDI tax, resulting in a tax savings of \$1,000.*

**IMPACT.** *The employer's share of OASDI remains at 6.2 percent. For 2010, certain employers may be eligible for payroll tax forgiveness under the Hiring Incentives to Restore Employment (HIRE) Act. However, payroll tax forgiveness for employers under the HIRE Act ends after December 31, 2010 and is not extended under the 2010 Tax Relief Act.*

**IMPACT.** *Individuals who do not pay into Social Security, for example, some public employees, will not benefit from the payroll tax cut. These individuals did benefit from the Making Work Pay credit.*

**COMMENT.** *The 2010 Tax Relief Act makes no changes to the Medicare (HI) portion of Social Security taxes, which is 2.9 percent.*

**PLANNING NOTE.** *Self-employed individuals under the 2010 Tax Relief Act would calculate the deduction for employment taxes without regard to the temporary rate reduction (that is, one-half of 15.3 percent of self-employment*

*income). However, the 2010 Tax Relief Act provides an enhanced percentage representing the employer portion of the deduction.*

## BUSINESS INCENTIVES

### 100 Percent Bonus Depreciation

The 2010 Tax Relief Act boosts 50-percent bonus depreciation to 100-percent for qualified investments made after September 8, 2010 and before January 1, 2012. The 2010 Tax Relief Act also makes 50-percent bonus depreciation available for qualified property placed in service after December 31, 2011 and before January 1, 2013. Certain long-lived property and transportation property is eligible for 100-percent expensing if placed in service before January 1, 2013.

“The 2010 Tax Relief Act reduces the employee-share of the OASDI portion of Social Security taxes from 6.2 percent to 4.2 percent for wages earned in calendar year 2011 up to the taxable wage base of \$106,800.”

**IMPACT.** *This provision is one of the most expansive for businesses. Unlike Code Sec. 179 expensing, it is not limited to use by smaller businesses or capped at a certain dollar level.*

**COMMENT.** *The 2010 Small Business Jobs Act extended 50-percent bonus depreciation for one year (qualified property placed in service during 2010; 2011 for certain long-lived property and transportation property).*

**COMMENT.** *The 2010 Small Business Jobs Act also increased the Code Sec. 179 dollar and investment limits to \$500,000 and \$2 million respectively, for tax years beginning in 2010 and 2011. The new law provides for Code Sec. 179 expensing at a level of \$125,000 for 2012 (see below). Bonus depreciation is not limited by the size of a taxpayer's investments in qualified property and it can generate net operating losses. Bonus depreciation, however, applies only to new property and is not exempt from certain uniform capitalization rules as is small business expensing.*

**Refundable credits in lieu of bonus depreciation.** Under the 2009 Recovery Act, a corporation otherwise eligible for additional first year depreciation may elect to claim additional research or minimum tax credits in lieu of claiming depreciation for qualified property placed in service after March 31, 2008 and before December 31, 2008. The 2010 Tax Relief Act generally extends similar treatment for two years, through December 31, 2012.

### Code Sec. 179 Expensing

Congress has repeatedly increased the dollar and investment limits under Code Sec. 179 to encourage business spending. The 2010 Small Business Jobs Act increased the Code Sec. 179 dollar and investment limits to \$500,000 and \$2 million, respectively, for tax years beginning in 2010 and 2011. The 2010 Tax Relief Act provides for a \$125,000 dollar limit (indexed for inflation) and a \$500,000 investment limit (indexed for inflation) for tax years beginning in 2012 (and sunsetting after December 31, 2012). The 2010 Tax Relief Act also extends the treatment of off-the-shelf computer software as qualifying property if placed in service before 2013.

**IMPACT.** *The \$500,000/\$2 million thresholds for tax years beginning in 2010 and 2011 were scheduled to revert to \$25,000/\$200,000, respectively, for tax years beginning in 2012 (both amounts not indexed for inflation)*

**COMMENT.** *Qualified real property does not share in the expensing benefits allowed under the 2010 Tax Relief Act. Under the 2010 Small Business Jobs Act, a taxpayer can elect up to \$250,000 of the \$500,000 Code Sec. 179 deduction limit (subject to the investment limit) for qualified real property (qualified leasehold improvement property, qualified restaurant property and qualified retail improvement property) for any tax year beginning in 2010 or 2011. The 2010 Tax Relief Act does not extend this treatment.*

### Research Tax Credit

The Code Sec. 41 research tax credit expired at the end of 2009. The 2010 Tax Relief Act renews the credit for two years, through December 31, 2011 and is effective for amounts paid or incurred after December 31, 2009.

**COMMENT.** *Earlier in 2010, President Obama urged Congress to make the credit permanent (the credit has been regularly extended since its creation in 1981). The 2010 Tax Relief Act reflects a temporary two-year extension of the credit that alone carries a \$13 billion tax cost. Consideration of an expensive, permanent extension is left to another Congress.*

**COMMENT.** *Under current law, taxpayers must choose between calculating their Code Sec. 41 credit under a formula that provides a 20 percent credit rate for investments over a certain base or a formula that provides a 14 percent credit in excess of a base amount. President Obama urged Congress to increase the 14 percent credit to 17 percent. The 2010 Tax Relief Act leaves the 14 percent amount unchanged.*

### Small Business Stock

The 2010 Small Business Jobs Act enhanced the exclusion of gain from qualified small business stock to non-corporate taxpayers. For stock acquired after September 27, 2010 and before January 1,

2011, and held for at least five years, the 2010 Small Business Jobs Act provided an exclusion of 100 percent. The 2010 Tax Relief Act extends the 100 percent exclusion for one more year, for stock acquired before January 1, 2012.

**IMPACT.** *With the 100-percent exclusion, none of the gain on qualifying sales or exchanges of small business stock is subject to federal income tax. In addition, the excluded gain is not treated as a tax preference item for AMT purposes, so none of the gain will be subject to AMT. Investors, however, must be patient to realize this benefit because they must hold the qualified shares for at least five years (or rollover proceeds to other qualified shares).*

“The 2010 Tax Relief Act boosts 50-percent bonus depreciation to 100-percent for qualified investments made after September 8, 2010 and before January 1, 2012.”

Certain baseline requirements for the exclusion continue to apply:

- To qualify as small business stock, the stock must be issued by a C corporation that invests 80 percent of its assets in the active conduct of a trade or business and that has assets of \$50 million or less when the stock is issued
- Qualified stock must be held for more than five years (rollovers into other qualified stock are allowed).
- The amount taken into account under the exclusion is limited to the greater of \$10 million or ten times the taxpayer's basis in the stock.
- Any taxpayer, other than a C corporation, can take advantage of the exclusion.

### Transit Benefits

The 2009 Recovery Act provided for parity among employer-provided transit benefits (at \$230 adjusted for inflation) for March 2009 through the end of 2010. These benefits may be realized as a tax-free fringe benefit offered by employers or as pre-tax benefit when paid for by the employee. The 2010 Tax Relief Act extends parity among transit benefits for one year, through December 31, 2011.

**IMPACT.** *Affected benefits are employer-provided transit and vanpool benefits and the exclusion for employer-provided parking benefits. CCH projects the inflation-adjusted ceiling on this benefit will remain at \$230 for 2011. Without the extension, the ceiling for transit passes and vanpool benefits would drop to a projected \$120.*

### Work Opportunity Tax Credit

The Work Opportunity Tax Credit (WOTC) is intended to encourage employers to hire individuals from targeted groups. The WOTC is equal to 40 percent of up to \$6,000 of the targeted employee's qualified first-year wages, subject to certain requirements and limitations. The WOTC was scheduled to expire after August 31, 2011. The 2010 Tax Relief Act extends the WOTC for individuals who begin employment after August 31, 2011 and before January 1, 2012, but with some modifications.

**IMPACT.** *The 2009 Recovery Act added two new targeted groups, unemployed veterans and disconnected youth, who begin work for an employer in 2009 or 2010. The 2010 Tax Relief Act does not extend these two targeted groups beyond 2010.*

### Business Tax Extenders

The 2010 Tax Relief Act extends a number of business tax extenders, which had expired at the end of 2009. These business tax extenders are generally extended for two years: 2010 and 2011 (in some cases calendar years, in other

cases tax years beginning after December 31, 2009 and before January 1, 2012 and in other cases for property placed in service on or before December 31, 2011). The business tax incentives extended by the 2010 Tax Relief Act are:

- Indian employment credit and accelerated depreciation for business property on an Indian reservation
- New Markets Tax Credit with modifications
- Railroad track maintenance credit
- Mine rescue training credit and election to expense advance mine safety equipment
- Differential wage credit
- 15-year recovery period for qualified leasehold improvements, restaurant building and improvements, and retail improvements
- Seven year motor sports entertainment costs recovery
- Film and television production costs
- Brownfields remediation
- Code Sec. 199 deduction for Puerto Rico
- Payments to controlling exempt organizations
- Tax treatment of certain dividends of RICs and certain investments of RICs
- Active financing exception/look-through treatment for CFCs
- Five-year write-off of farm machinery/equipment
- Tax incentives for empowerment zones
- Tax incentives for investment in the District of Columbia
- Cover over of rum excise taxes to Puerto Rico and USVI
- American Samoa economic development credit

**COMMENT.** *The 2010 Tax Relief Act extends the first-time homebuyer credit for purchases of a qualified residence in the*

*District of Columbia but does not extend the national first-time homebuyer credit, which generally has expired except for qualified military personnel.*

## ENERGY INCENTIVES

The 2010 Tax Relief Act temporarily extends for one or two years a number of energy tax incentives, primarily targeted to businesses. One popular energy incentive for individuals, the Code Sec. 25C residential energy property credit, is extended but with some limitations.

### Business Energy Incentives

Business energy incentives extended by the 2010 Tax Relief Act are:

- Credits for biodiesel and renewable diesel fuel (two years)
- Credit for refined coal facilities (two years with modifications)
- New energy efficient home credit for qualified builders and manufacturers (homes purchased before January 1, 2012)
- Excise tax credits and outlay payments for alternative fuel and alternative fuel mixtures (two years)
- Sales of electric transmission property (sales before January 1, 2012)
- Percentage depletion for oil and gas from marginal wells (two years)
- Grants for certain energy property in lieu of tax credits (variable)
- Tax credits and outlay payments for ethanol and duties on imported ethanol (one year with modifications)
- Energy efficient appliance credit (one year with modifications)

**COMMENT.** *Authority to provide grants in lieu of tax credits for certain energy property is extended for one year, through December 31, 2011. Generally, qualified property must be placed in service in calendar years 2009, 2010 or 2011 or construction of qualified property must begin in that period and be completed before 2013 for wind energy property (or 2014 or 2017 for other qualified property). An application for a grant must be made before October 11, 2011.*

### Individuals

The Code Sec. 25C credit is designed to reward individuals who make energy efficiency improvements to their residences with a tax benefit. Under current law, the credit amount is 30 percent of the sum of expenditures for qualified energy efficiency improvements and property, such as furnaces, water heaters, insulation materials, exterior windows and doors, and other items, for 2009 and 2010 property. The credit under current law is limited to a lifetime maximum credit of \$1,500 for 2009 and 2010 property. The 2010 Tax Relief Act extends the Code Sec. 25C credit through 2011. However, the new law returns the credit to its pre-2009 Recovery Act parameters.

**IMPACT.** *The 2009 Recovery Act tripled what was a \$500 credit to a \$1,500 credit. The 2009 Recovery Act also provided that previous 10 percent credits and \$50, \$100 and \$150 sub-capped items would be eligible for the full 30 percent credit up to \$1,500. The 2010 Tax Relief Act does not renew these enhancements in the 2009 Recovery Act for 2011.*

**COMMENT.** *The Code Sec. 25C credit remains nonrefundable under the 2010 Tax Relief Act.*

## DISASTER INCENTIVES

The 2010 Tax Relief Act extends a number of targeted disaster relief measures for one or two years. They are:

- Tax-exempt bond financing for the New York City Liberty Zone (9-11 relief) (two years)

EXTENSION EFFECTIVE DATES FOR EXPIRING & EXPIRED PROVISIONS			
	2010	2011	2012
Individual Tax Rates		01/01/11 – 12/31/12	
Individual Extenders	01/01/10 – 12/31/11		
AMT Relief	01/01/10 – 12/31/11		
100% Bonus Depreciation		9/9/10 – 12/31/11	

- Increased rehabilitation credit for historic structures in the Gulf Opportunity Zone (GO Zone)(two years)
- Placed-in service deadline for low income housing tax credits for GO Zone (one year)
- Tax-exempt bond financing for GO Zone (one year)
- Bonus depreciation for certain GO Zone property (generally one year)

**BONDS**

The 2010 Tax Relief Act temporarily extends several bond programs. These include tax exempt private activity bonds for qualified education facilities and qualified zone academy bonds.

**COMMENT.** *Notably absent from the list of bonds extended by the 2010 Tax Relief Act are Build America Bonds. Under the 2009 Recovery Act, Build America Bonds must be issued by state and local governments before January 1, 2011.*

**CHARITABLE INCENTIVES**

In addition to extending tax-free distributions from IRAs for charitable purposes and special rules for contributions of capital gain real property for conservation purposes, the 2010 Tax Relief Act also extends through 2011:

- Charitable deduction for contributions of food inventory
- Charitable deduction for contributions by C corporations of books to public schools
- Charitable deduction for corporate contributions of computer equipment for educational purposes
- Basis adjustment to stock of S corporations making charitable contributions of property

**FEDERAL ESTATE TAX**

EGTRRA gradually reduced over a period of years and then abolished the federal estate tax for decedents dying in 2010. The pre-EGTRRA estate tax (with a maximum tax rate of 55 percent and a \$1 million ex-

clusion) was scheduled to be revived after 2010. Additional EGTRRA changes affected the gift tax and the generation-skipping transfer (GST) tax.

**Estate Tax Compromise**

The 2010 Tax Relief Act revives the estate tax for decedents dying after December 31, 2009, but at a significantly higher level than had been scheduled after 2010 under EGTRRA. The maximum estate tax rate is 35 percent with an exclusion amount of \$5 million. This new estate tax regime, however, is itself temporary and is scheduled to sunset on December 31, 2012.

**IMPACT.** *The applicable exclusion amount is adjusted for inflation for any decedent dying in 2012. The new rate and exclusion represent a significant reduction from the 45 percent rate and \$3.5 million exclusion applicable for 2009, which many House Democrats wanted to continue before the compromise bill was approved.*

Together with the revival of the estate tax, the 2010 Tax Relief Act eliminates the modified carryover basis rules and replaces them with the stepped up basis rules that had applied until 2010. Property with a stepped-up basis receives a basis equal to the property’s fair market value on the date

of the decedent’s death (or on an alternate valuation date). Under a modified carryover basis that EGTRRA had put into place for 2010, the executor may increase the basis of estate property only by a total of \$1.3 million, with other estate property taking a carryover basis equal to the lesser of the decedent’s basis or the fair market value of the property on the decedent’s death.

**Option for 2010**

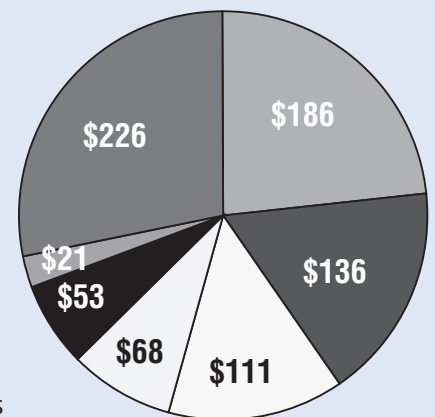
The 2010 Tax Relief Act gives estates of decedents dying after December 31, 2009 and before January 1, 2011, the option to elect not to come under the revived estate tax. The new law gives those estates the option to elect to apply (1) the estate tax based on the new 35 percent top rate and \$5 million exemption, with stepped-up basis or (2) no estate tax and modified carryover basis rules under EGTRRA. Any election would be revocable only with the consent of the IRS.

**EXAMPLE.** *Caleb, who is unmarried, died on September 30, 2010. Caleb’s estate is valued at \$15 million. Caleb’s estate can elect not to have the revived estate tax apply (with a maximum estate tax rate of 35 percent and a \$5 million exclusion). If Caleb’s estate makes this election, the estate would not be subject to the estate tax, and the carryover basis rules under EGTRRA would apply.*

**2010 TAX RELIEF ACT REVENUE COST**

Individual Tax Cuts .....	\$ 186 billion
AMT Relief.....	\$ 136 billion
Payroll Tax Deduction.....	\$ 111 billion
Estate/Gift Tax Relief .....	\$ 68 billion
Capital Gains/ Dividend Cuts .....	\$ 53 billion
Bonus Depreciation/179 Expensing .....	\$ 21 billion
Other .....	\$ 226 billion

\*\$801 Billion total cost of tax provisions  
 \*\*(\$857 Billion total cost of law includes \$56 Billion for Unemployment Insurance Extension)



**COMMENT.** *The 2010 Tax Relief Act instructs the IRS to determine the time and manner for making the election.*

### Portability

The 2010 Tax Relief Act provides for “portability” between spouses of the maximum exclusion. Generally, portability would allow a surviving spouse to elect to take advantage of the unused portion of the estate tax exclusion of his or her predeceased spouse, thereby providing the surviving spouse with a larger exclusion amount. A deceased spousal exclusion amount would be available to the surviving spouse only if an election is made on a timely filed estate tax return. Portability would be available after December 31, 2010.

**IMPACT.** *With the election and careful estate planning, married couples can effectively shield up to \$10 million from estate tax by providing that each spouse maximize his or her \$5 million exemption under the 2010 Tax Relief Act.*

**EXAMPLE.** *David dies in 2011, having made taxable transfers of \$3 million and having no taxable estate. An election is made on David's estate tax return to permit David's wife Alicia to use David's unused exclusion amount. At the time of David's death, Alicia had made no taxable gifts. Alicia's exclusion amount would be her \$5 million exclusion plus \$2 million of David's unused exclusion for a total exclusion amount of \$7 million.*

**COMMENT.** *If the surviving spouse is predeceased by more than one spouse, the exclusion amount available for use by the surviving spouse would be limited to the lesser of \$5 million or the unused exclusion of the last deceased spouse. The 2010 Tax Relief Act continues the rule that prevents a surviving spouse from using the GST tax exemption of a predeceased spouse.*

### State death tax credit/deduction

EGTRRA repealed the state death tax credit for decedents dying after 2004 and replaced the credit with a deduction. Under EGTRRA's sunset provisions, the credit, as it existed before 2002, is revived for decedents dying after 2010. The 2010 Tax Relief Act extends the deduction through 2012.

**COMMENT.** *The 2010 Tax Relief Act also extends EGTRRA's provisions affecting conservation easements, small and family-owned businesses and the installment payment of estate tax for closely-held businesses for purposes of the estate tax.*

### Filings

The 2010 Tax Relief Act gives estates of decedents dying after December 31, 2009 and before the date of enactment extended time (generally nine months) to perform certain acts. These include the filing of any return and the making of any payment.

### Gift Taxes

For gifts made in 2010, the 2010 Tax Relief Act provides that gift tax is computed using a rate schedule having a top tax rate of 35 percent and a maximum applicable exclusion amount of \$1 million. For gifts made after 2010, the gift tax is reunified with the estate tax with a top gift tax rate of 35 percent and a maximum applicable exclusion amount of \$5 million.

**COMMENT.** *EGTRRA decoupled the gift and estate taxes. The 2010 Tax Relief Act reunifies the gift and estate taxes for gifts made after December 31, 2010.*

**COMMENT.** *Donors of lifetime gifts continue to be able to apply an annual gift tax exclusion before having to use part of their now unified exclusion. For 2010 and 2011, that inflation-adjusted annual exclusion amount is \$13,000 (married couples may continue to “split” their gift and may make combined gifts of \$26,000 to each donee).*

### GST Tax

The 2010 Tax Relief Act provides a \$5 million exemption for 2010 (equal to the exclusion for estate tax purposes) with a GST tax rate of zero percent for 2010. For transfers made after 2010, the GST tax rate would be equal to the highest estate and gift tax rate in effect for the year (35 percent for 2011 and 2012). The 2010 Tax Relief Act also extends certain technical provisions under EGTRRA affecting the GST tax.

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