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tax bulletin

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# Extension of the Bush Tax Cuts

On December 6th, President Obama announced a tentative deal with congressional Republicans to extend the 2001 and 2003 tax cuts (the "Bush Tax Cuts"). On December 9th, legislation was introduced titled Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010, with the goal of providing the following relief for American Taxpayers:

- extend the Bush Tax Cuts for 2011 and 2012 for all taxpayers;
- reduce the employee share of Social Security ("FICA") taxes from 6.2% to 4.2% for 2011;
- allow for 100% expensing for bonus depreciation investments through 2011;
- provide an estate, gift and generation-skipping transfer tax rate of 35% and exemption amount of $5 million for 2 years;
- extend the alternative minimum tax ("AMT") relief (the "AMT Patch") for two years;
- extend various expiring tax provisions; and
- extend unemployment benefits for 13 months.

The final details are subject to negotiation and may change as the proposed legislation makes its way through the House and the Senate. At this point, the proposed legislation does not include significant revenue raising offset provisions.

### Tax Cuts

The proposed legislation extends the Bush Tax Cuts, which are set to expire at the end of 2010, for all taxpayers, including individuals with incomes above $200,000 ($250,000 for married couples). Under the proposed legislation, the extension would encompass:

- keeping the current tax rates at all income levels;
- repealing the phase-outs of personal exemptions and itemized deductions;
- keeping the top capital gain and dividend rate at 15%;
- maintaining marriage penalty relief; and
- continuing the $1,000 child tax credit.

### Payroll Tax Holiday

The proposed legislation reduces the employee share of FICA taxes from 6.2% to 4.2% for 2011. It would not affect the employer share of FICA taxes. This provision is meant to replace the Making Work Pay Credit that was in effect for 2009 and 2010. Unlike the Making Work Pay Credit, however, there is no phase-out for high income taxpayers. Thus, to a taxpayer with wages at or above the $106,800 cap, this reduction will be worth $2,136. To provide parity, a similar reduction in self-employment ("SECA") taxes will be provided for self-employed individuals.

### Expensing

The proposed legislation would provide for full expensing of investments that currently qualify for bonus depreciation and are placed in service through the end of 2011. This will allow businesses to expense the full cost of equipment and other qualifying property placed in service in 2011. Additionally, bonus depreciation at the current level (i.e., 50% expensing followed by regular depreciation) will be available for such investments in 2012.

### AMT Patch

The proposed legislation also includes a two-year AMT patch. The patch would prevent the AMT exemption from dropping in 2010, thus causing the AMT to apply to many taxpayers who would otherwise be exempt.

### Other Provisions

The proposed legislation also extends numerous other expiring tax provisions that have benefited both individuals and businesses, such as the tax cuts enacted by the stimulus bill of 2009 and many of the tax provisions commonly referred to as "extenders." These provisions include things such as:

- American Opportunity Credit;
- earned income tax credit enhancements;
- child credit enhancements;
- research credit; and
- itemized deduction for state and local sales taxes.

### Estate, Gift and Generation-Skipping Transfer Tax Relief

The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) phased out the estate and generation-skipping transfer taxes such that we currently have a full repeal of those taxes for 2010 only. The gift tax rate for 2010 is 35% with a $1 million exemption amount. The estate tax is scheduled to return on January 1, 2011 with only a $1 million lifetime gift, estate and generation-skipping transfer tax exemption amount and a 55% tax rate. In 2009 there was a $1 million lifetime exemption and a $3.5 million estate and generation-skipping transfer tax exemption amount. The proposed legislation introduced on December 9th increases the estate, gift and generation-skipping transfer tax exemption amount while providing additional relief as well. The proposed legislation provides for the following:

- increases the estate, gift and generation-skipping transfer tax exemption to $5 million per person and $10 million per couple, indexing these amounts for inflation beginning in 2012;
- sets the top tax rate at 35% for the estate, gift and generation-skipping transfer taxes for an additional two years, through December 31, 2012;
- provides for the option of electing to choose between no estate tax and modified carryover basis or an estate tax and stepped up basis for estates arising on or after January 1, 2010 and before January 1, 2011; and
- sets a $5 million generation-skipping transfer tax exemption and zero percent rate for the 2010 year.

### Portability of Spouse's Unused Exemption Amounts

Under current law, couples have to do complicated estate planning to claim their entire exemption (which was $7 million for a married couple in 2009). The proposed legislation provides:

- the executor of a deceased spouse's estate has an ability to transfer any unused exemption to the surviving spouse; and
- the proposal would be effective for estates of decedents dying after December 31, 2010.

### Reunification of Gift and Estate Tax Exemption Amounts

Prior to the EGTRRA, the estate and gift taxes were unified, creating a single graduated rate schedule for both the estate tax and the lifetime gift tax. In the past, that single exemption could be used for gifts and/or bequests at death. The EGTRRA decoupled these systems and left taxpayers with a $1 million lifetime gift tax exemption and in 2009 a $3.5 million estate tax exemption reduced by amounts given away during lifetime. The proposed legislation would reunify the estate and gift taxes such that each person would have one exemption for gift and estate taxes of $5 million, as well as a $5 million exemption from generation-skipping transfer taxes, and as described above, married couples would have a total of $10 million. The proposed legislation would be effective for gifts made after December 31, 2010.

The proposed legislation is scheduled for a key vote today, December 13th. Stay tuned, as the final days of this Congress are sure to be interesting. It has always been our practice at Venable to provide clients with flexible estate planning documents designed to accommodate changes in tax laws and family circumstances. However, in light of this proposed legislation that provides taxpayers with options and elections that need to be made at various times in 2011, you may wish to contact us in the new year to ensure your estate plan continues to meet your goals.

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