

# Timely Tax Tips

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Over the last several weeks Congress delivered taxpayer tricks and treats in new legislation; The Working Families Tax Relief Act, and American Jobs Creation Act of 2004. How will they affect you, your business and your family?

## Individual Tax Provisions

### Treats:

**Marriage Penalty Relief** - 15% rate bracket and standard deduction for joint filers' remains double of that available for single filers through 2010.

**Expansion of the Ten Percent Rate Bracket**

**Child Tax Credit** - extension of current \$1,000 tax credit per child through 2010, subject to income limitations.

**Educator Expenses** - extension of above the line deduction of \$250 for qualifying classroom expenses made by full time primary and secondary education teachers and other school personnel.

**State and Local Tax Deduction versus State Sales Tax Deduction** - taxpayers may choose, for years 2004 and 2005, to deduct state sales taxes in lieu of state and local taxes. This may be accomplished using tables created by the Secretary of the Treasury based on average consumption

rates, or by compiling receipts for actual sales taxes paid. This new deduction is likely to be most beneficial for residents of states without an income tax.

**Clean Fuel Vehicle Deduction** - extended through 2005 with phase-out to begin in 2006.

**Alternative Minimum Tax** - Increased exemption amount has been extended through 2005.

Credits allowed for AMT as well as regular tax:  
Child and Dependent Care Credit  
Hope and Lifetime Learning Credits

### Tricks:

**Recognition of Gain on the Sale of a Principle Residence if Acquired in a Like-Kind Exchange within Five Years of the Sale Date** - effective for sales of personal residences after October 21, 2004. This provision effectively extends the holding period of rental property which was received in a Section 1031 exchange and converted to personal residence to avoid payment of tax on the gain on sale. The two year holding period still applies to residence acquired in traditional manner.

**Limitation on Charitable Contributions**  
*Motor Vehicles, Boats and Airplanes* - deductions for donations of these items would depend on the use by the charity. If the property is used by the charity, the property's value, as determined by the

charity, is deductible. If the donee organization sells the item, the largest deduction available would be the gross proceeds resulting from the sale of the item. This law applies to items with a claimed value over \$500, donated post December 31, 2004; steep penalties apply. Documentation from the charity required.

**Non-Cash Charitable Contributions** - all contributions over \$5,000 must have a qualified appraisal whether gifted by an individual or any entity, including C Corporations.

**Patents and Other Intellectual Property** - limited to lesser of basis or appraised fair market value of the property in the year gifted. Additional amounts will be deductible in subsequent taxable years based on income derived from the donated property by the charity.

## Business Tax Provisions

### Treat:

**Extension of Section 179 Expensing Allowance** - \$100,000 of property placed in service through year 2007 may be deducted with income and other current limitations applying.

### Trick:

The maximum Section 179 deduction for SUV's is \$25,000 for property placed in service after October 21, 2004.

### Treat:

**Certain Leasehold Improvements and Restaurant Property** - placed in service prior to January 1, 2006 qualify for 15 year depreciable life. This is effective October 22, 2004.

### Treat:

**Start-Up and Organizational Expenses Deduction** - Up to \$5,000 each in year the trade or business begins, if not in excess of \$50,000 in total, respectively. Effective October 22, 2004.

### Trick:

**Bonus Depreciation Allowance Not Extended** - Fixed assets must be placed in service by December 31, 2004 to qualify for additional 50% bonus depreciation.

### Trick:

**Repeal of Foreign Sales Corporation/ Extraterritorial Income Exclusion** - Effective after 2004, this bill provides transitional relief in 2005 and 2006. If your company has foreign sales transactions, there may be significant planning opportunities during this transition period.

### Treat:

**Deduction from income for United States Production Activities** - This deduction is phased in from 2005 - 2009. The deduction is initially 3% and increases over this time frame to 9% of qualified production activities income. This deduction is allowable for domestic production activities of all entities and is also allowed for purposes of AMT. It has the effect of reducing the effective tax rate from one to three percent.

### Treats - Credits:

**Research Credit** - business credit for certain qualified research expenses are extended through 2005.

**Foreign Tax Credits** - Unused credits may be carried back one year and forward ten years, beginning October 22, 2004. Bill also repeals the 90% limitation on the utilization of the AMT foreign tax credit effective after December 31, 2004.

**Other Business Credits** - Work Opportunity and Welfare to Work Credits extended through 2005.

### Trick:

**Nonqualified Deferred Compensation Plan Rules Tightened** - The changes affect deferral elections, distribution restrictions, accelerated payment restrictions and taxability of certain transfers of property. They apply to deferrals made after December 31, 2004. Most plans need to make changes in their agreements and operations.

### Treat:

**Stock Options** - Effective October 22, 2004, the exercise of qualified stock options will not be subject to FICA and FUTA taxes.

### Trick:

**New Penalties and Extension on Statute of Limitations on Unreported Listed Transactions** - The Bill implements new penalties and an infinite statute of limitations on unreported reportable or listed (tax shelter) transactions.

### Treat:

**Suspension of Interest and Penalties** - The IRS must notify the taxpayer of any adjustments to his return within 18 months after tax return filing, or suspend interest and penalties from this date forward.

This is a brief overview of some of the provisions most likely to affect the majority of taxpayers. However, the law is broad, with numerous provisions, which are being reviewed in detail to determine their full impact. Please feel free to send me any questions you have about these or any other tax issues and how they may affect your tax situation.

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