

## New Tax Statutes

Towards the end of 2004, two new tax laws were passed and signed into law that will impact most individual taxpayers. The first, The Working Families Tax Relief Act of 2004 (WFTRA), was signed into law on October 4, 2004 and the second, the American Jobs Creation Act of 2004 (AJCA), was signed into law on October 22, 2004. These new tax statutes have substantial additional implications to corporations and partnerships; however, this article will only address the major implications to individual taxpayers.

### Working Families Tax Relief Act of 2004

The general purpose of this statute is to extend some of the tax benefits of The Economic Growth and Tax Relief Reconciliation Act of 2001 (“2001 Tax Act”) that were set to expire. WFTRA extends the increased childcare credit of \$1,000 through 2009; however, the credit continues to be scheduled to decrease to \$500 for years after 2009.

WFTRA also provides for continued relief from the so-called “marriage penalty.” A bit of background here may be helpful. One would think that the tax rates for a married couple would apply at income levels equal to twice that of a single individual. Stated differently, a married couple with \$200,000 of taxable income should pay the same amount of tax as two single taxpayers, each with \$100,000 of taxable income. However, in actuality, the married couple would pay more than the two single people would cumulatively pay. This was referred to as the “marriage penalty.”

The 2001 Tax Act had a number of provisions to lessen the impact of the marriage penalty. One such provision was to increase the standard deduction for married taxpayers to equal twice that of single taxpayers. This provision was scheduled to begin to phase out after 2004; however, WFTRA now extends the provision through 2010. Similarly, the 2001 Tax Act increased the application of the 15% bracket for married taxpayers to twice that of single taxpayers but, that was scheduled to be phased out for tax years 2005 – 2010. The 2004 statute eliminates the phaseout through 2010.

In addition to extending some of the provisions of the 2001 Tax Act, WFTRA also establishes a uniform definition of a qualifying child. This uniform rule applies to determine if a child qualifies as a dependent, for the child tax credit, for the earned income credit, for the dependent care credit and to determine if one qualifies for the head of household filing status.

The uniform three part test considers the residency of the child, the relationship between the child and the taxpayer and the age of the child. To satisfy the residency part of the test, the child must have the same residence as the taxpayer for more than half of the tax year. To satisfy the relationship portion of the uniform rule, the child must be the son, daughter, stepson, stepdaughter, brother, sister, stepbrother, stepsister or any descendent of any such individual. Additionally, certain adopted and foster children may also qualify. Finally, the age test requires that the child be under the age of 19 or under the age of 24 and a fulltime student.

WFTRA provides specific complicated rules in the case where a child supports him/herself, a child is not a citizen and/or resident of the US or a child has divorced or separated parents. In accordance with WFTRA, even more confusing and complicated rules apply in cases where a child qualifies as a child of more than one person or the new uniform test is not met but the present dependency exemption is met. Thus, although WFTRA attempts to unify the tests applicable to children, there are so many exceptions to the rule that we are left with a new set of rules no less complicated than the previous ones.

WFTRA also extends a number of obscure tax provisions, including, but not limited to, the welfare to work credit, the deduction for expenses of school teachers, and the electric car credit. Overall, WFTRA attempts to help working families and, in some cases, does so, but the help is not likely to be felt by most taxpayers as most of the changes merely continue tax benefits that would otherwise cease either in 2004 or later.

#### American Jobs Creation Act of 2004

This statute has limited application to individual taxpayers; however, there are a few provisions that will impact a substantial number of such taxpayers. The first is that this statute increases the carryforward of the foreign tax credit from 5 to 10 years, but decreases the carryback of the same from 2 years to 1 year.

Small businesses will benefit from several provisions of the AJCA. First, the bonus depreciation rules that were set to expire in 2004 have been extended through 2005. Next, the increase in the amount of the small business expense election of \$100,000 has been extended through 2007. "S" corporations are now permitted to have 100 shareholders, an increase from the prior limit of 75. Finally, new businesses can benefit from the new provisions that permit the amortization of new business expenses over a 15 year period, previously it was a sixty month period; however, the new business can elect to deduct up to \$5,000 of start up expenses and up to \$5,000 of organizational expenses in its first year.

The 2004 tax statutes provide some benefit, but I think that the names, "The Working Families Tax Relief Act" and "The American Jobs Creation Act" overstate the benefit, to most Americans. The new rules do little more than further complicate the landscape; therefore, as always I recommend that you consult with a Certified Public Accountant or Tax Attorney before attempting to apply any of the new rules yourself.

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