New Federal Tax Legislation

Philip E. Harris
Department of Agricultural and Applied Economics
University of Wisconsin-Madison
Its Not My Job Award

In this day and age of ever increasing departmentalization, it becomes necessary to recognize those departments that have become good at separating responsibilities.
Pension Protection Act of 2006 (PPA) pp. 1-12

- Repeal of sunset provisions
- Charitable contributions
- Life insurance contracts
- Pension plans
Retirement plan provisions

Saver’s credit

I.R.C. §529 plan provisions

Regulatory authority to combat abuses
I.R.C. §529 plans p. 4

- Qualified higher education costs
  - Prepaid tuition credits
  - Tax-advantaged savings accounts
- Donor retains control of assets
- Treated as completed gift
- No federal income tax deduction
Ineligible for education exclusion

- Annual exclusion does apply
- 5-year election allows spread
- Gift-splitting comes first
- Check box on Sch. A (Form 709)
- Excess is current year gift
Example 1 pp. 4-5

Contribution $90,000
5-year election (60,000)
Excess 30,000
1/5 of election 12,000
Current gift $42,000
Exclusion (12,000)
Taxable gift $30,000
Future year reporting  p. 5

- Include on Form 709 if otherwise required to file it
- Include remainder in gross estate if contributor dies before last year of 5-year carryover period
Distributions  p. 5

- Used for qualifying expense:
  No income tax

- Used for ineligible expense:
  Earnings portion is taxable, 10% penalty may apply

- Death is exception to penalty
Example 3 p. 6

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td>Basis</td>
<td>$12,000</td>
</tr>
<tr>
<td>Earnings</td>
<td>2,800</td>
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<tr>
<td>Distribution</td>
<td>$14,800</td>
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<tr>
<td>Eligible expense</td>
<td>7,400 (50%)</td>
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<tr>
<td>Taxable amount</td>
<td>$1,400 (50% of $2,800)</td>
</tr>
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</table>
Revocation is taxable event

- Rules for rollovers
  - Complete within 60 days
  - Only once in 12 months

- Change of beneficiary
  - Member of the family
  - No gift tax if new beneficiary is in the same or higher generation
Cash contributions  p. 7

- Effective for tax years beginning after August 17, 2006
- Receipt or bank record required for all cash contributions
- Example 5: kettle contributions
- Example 6: church contributions
Clothing, household items

- Good used condition or better
- Regulations authorized to deny deduction for old socks, underwear
- Deduction allowed for single item in fair or poor condition if > $500 deduction and qualified appraisal
- Effective August 18, 2006
Recapture of Deduction

- FMV deduction because charity planned use for exempt purpose
- Valued at more than $5,000
- Charity sells it within 3 years
- Recapture of excess deduction (FMV – basis) as ordinary income
- Effective September 2, 2006
Valuation misstatement p. 9

Effective August 17, 2006

Income tax

▪ Substantial: 150% or more of actual value
▪ Gross: 200% or more of actual value

▪ Estate and gift tax
▪ Substantial: 65% or less of value
▪ Gross: 40% or less of value

▪ No reasonable cause if gross inaccuracy
Qualified appraiser  p. 9

- Recognized credentials or meet minimum training requirements
- Regularly make appraisals for compensation
- Not prohibited from practicing before the IRS
IRA donation  p. 10

- Taxpayer at least age 70½
- Direct transfer to charity from IRA
- Counts as required minimum distribution
- No income inclusion, no deduction
- $100,000 limit per year
- Income distributed before any basis
- Effective for transfers in 2006, 2007
- Non-spouse beneficiary may request direct transfer to IRA of distributions made after 2006
IRA provisions p. 11

- Direct deposit of refund to IRA

Form 8888
Beginning in 2010:

- Payments under long-term care rider are not taxable (basis is reduced)
- Tax-free exchange allowed for LTC contract
Murphy’s Lesser Known Laws

A fine is a tax for doing wrong.
A tax is a fine for doing well.
TIPRA pp. 13-23

- Tax Increase Prevention and Reconciliation Act of 2005
- Enacted in 2006
- Carryover from 2005 budget measures
Exemption amount increased for 2006 only

- $62,550 for MFJ or QW
- $42,500 for Single or HOH
- $31,275 for MFS

Exemption phaseout unchanged
Most nonrefundable personal credits may offset AMT for 2006

Exception: vehicle credits
### Example 7 p. 14

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
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<tr>
<td>2006 taxable income</td>
<td>$125,000</td>
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<tr>
<td>Regular tax before credits</td>
<td>24,404</td>
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<tr>
<td>Child tax credit</td>
<td>- 6,000</td>
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<tr>
<td>Alternative vehicle credit</td>
<td>- 1,700</td>
</tr>
<tr>
<td>Tax w/out AMT</td>
<td>$ 16,704</td>
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</table>
Example 7 p. 14

2006 taxable income $125,000
Exemption deductions 26,400
Taxes 7,900
AMTI $159,300
Exemption -60,225
Minimum tax base $99,075
Example 7 p. 14

Minimum tax base $99,075
Minimum tax rate x 26%
Tentative minimum tax $25,760
Regular tax - 24,404
AMT $ 1,356
Regular tax +24,404
Total tax $25,760
<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
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<tr>
<td>Total tax</td>
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<td>Child tax credit</td>
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<td>Tax after credits</td>
<td>$19,760</td>
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<tr>
<td>Year</td>
<td>Tax after Credits</td>
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<tr>
<td>----------------</td>
<td>-------------------</td>
</tr>
<tr>
<td>2006</td>
<td>tax after credits</td>
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<tr>
<td>2005</td>
<td>tax after credits</td>
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<tr>
<td>2007</td>
<td>tax after credits</td>
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</table>
Capital gains rates pp. 15-16

- Tax years 2009 and 2010
- 0% and 15% tax rates will apply to individuals’ capital gains and qualifying dividends
- Example 8: keep income low in 2008 – 2010 to use 0% bracket
Musical works pp. 16-17

- Compositions or copyrights
- Disposition by creator or taxpayer who has substituted basis
- Treated as capital asset for sale or exchange (not contribution)
- Example 9: Cee Cee sells copyrights
- Expires after 2010 tax year
Kiddie tax pp. 17-18

- Tax on unearned income of minor
- $1,700 threshold for 2006
- Age limit increased to 18 years
- Exception for married child filing joint return
- Exception for qualified disability trusts
- Example 10: teenager’s income
Deposit (loan) with qualifying continuing care facility
Age limit reduced to 62
Dollar cap removed
Progressive disability rule changed
Nursing home may qualify
Example 11: $250,000 “life occupancy fee”
Roth conversions pp. 20-21

- Effective in 2010 and later years
- No income limit for conversion of traditional IRA to Roth
- For 2010 conversions, half reportable in 2011, half in 2012
Example 12   pp. 20-21

- $10,000 in traditional IRA
- Converted to Roth IRA in 2010
- $2,000 distributed in 2010
  - $2,000 taxed in 2010
  - $5,000 taxed in 2011
  - $3,000 taxed in 2012
I.R.C. §179 pp. 21-22

- Expanded deduction extended to 2008 and 2009 tax years
- $100,000 limit adjusted for inflation
- Off-the-shelf computer software
- Example 13: purchases $250,000 per year
Tax-exempt interest  p. 22

- Effective in 2006
- State/local bond interest must be reported on Form 1099-INT
- Affects taxation of SSA benefits
- Example 14: $1,500 tax exempt interest
Reduction of Itemized Deduction pp. 23-24

Under prior law, the itemized deduction was reduced by the lesser of:

2. 3% of adjusted gross income that exceeds $150,500 ($75,250)

4. 80% of the itemized deductions
Reduction is phased out:

2. Reduced to 2/3 for 2006 and 2007
3. Reduced to 1/3 for 2008 and 2009
4. Reduced to zero in 2010
5. Back to 10% in 2011
Phase-out of Exemption Deduction pp. 24-25

- Under prior law, exemption deduction was phased out over a range of adjusted gross income.
- New law phases out the reduction at the same rate that itemized deduction reduction is phased out.
Importing:

- Not deductible if illegal to import
- It’s illegal.
Making a residence more energy efficient
Installing solar or fuel-cell energy
Purchasing clean renewable energy bonds
Reducing heat gain/loss
- Insulation
- Energy efficient windows
- Skylights
- Doors
- Metal roof
Factors for Energy Credit

- Calculated at 10% of cost
- Lifetime limit $500
- Only for 2006-07 expenditures
- No carry over of credit
- Claim on Form 5695
Limitations on energy credit

Subject to 10% credit for the cost of building envelope

- Insulation
- Exterior windows ($200 max)
- Exterior doors
- Metal roof
Subject to property costs limited by dollar amounts and maximum credit of $500

- Energy-efficient building $300
- Qualified heating system $150
- Advanced circulating fan $50
BUT!! One more limitation from Form 1040

- Enter line 46 your tax liability
- Enter your total credit lines
  47. Foreign tax credit
  48. Child & dependent care exp
  49. Elderly or disabled credit
  50. Education Credits
  51. Retirement Savings Credit

Subtract if zero or less NO energy credit
Questions?