

TAX RELIEF/JOB CREATION ACT OF 2010

December 15, 2010

Special Report

HIGHLIGHTS

- Reduced Individual Tax Rates
- Reduced Capital Gains/Dividend Tax Rates
- Estate Tax Relief
- \$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

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Senate Approves Two-Year Extension Of Bush-Era Tax Cuts, Payroll Tax Relief And Estate Tax Compromise

In a highly-anticipated vote, the Senate on December 15, 2010, approved by a 81 to 19 margin, H.R. 4853, the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010. H.R. 4853, as amended by the Senate, follows through on the framework agreed to on December 6 by President Obama and GOP leaders in Congress. The Senate bill extends the Bush-era individual and capital gains/dividend tax cuts for all taxpayers for two years. The bill also provides for a one-year payroll tax cut, 100 percent bonus depreciation through 2011 and 50 percent bonus depreciation for 2012, extenders relief, an AMT “patch,” a top federal estate tax rate of 35 percent with a \$5 million exclusion, and more.

Passage by the Senate is certain to put great pressure on reluctant Democrats in the House to support the bill. Although the margin may be closer in the House, and may possibly include a change to the estate tax compromise that the Senate may then need to approve, a final bill is anticipated before Congress adjourns for the year.

IMPACT. *The Senate bill gives taxpayers some certainty in tax planning for the next two years. Based on revenue costs estimated by the Joint Committee on Taxation, it also will inject over \$850 billion into the economy. However, the plan also punts the ultimate fate of the Bush-era tax cuts to 2012, a presidential election year.*

COMMENT. *On December 9, the Democratic caucus voted not to support the White House-brokered bill, apparently over dissatisfaction about the estate tax*

provisions. The caucus vote, however, may slow the bill's progress but is not expected to derail the bill. A White House spokesperson said after the caucus' vote that the administration remains confident the package will pass the House.

INDIVIDUALS

Individual Tax Rates

Under the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), the individual income tax rates are scheduled to revert from 10, 15, 25, 28, 33, and 35 percent to 15, 28, 31, 36, and 39.6 percent after December 31, 2010. The Senate bill extends the 10-percent rate and the other reduced individual income tax rates for two years, through December 31, 2012, for all taxpayers.

IMPACT. *EGTRRA made across the board rate reductions and the Senate bill keeps 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 face 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 a \$1,890 tax savings in combined income tax and payroll tax rate reductions over what was scheduled under the EGTRRA sunset.

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 Senate bill continues this treatment for two years, through December 31, 2012.

IMPACT. Without any action on Capitol Hill, the maximum rate on net capital gain is scheduled to rise to 20 percent in 2011 (10 percent for taxpayers in the 15 percent bracket). Of equal if not greater concern to the equities markets and many corporations, the rate on all dividends would rise from 15 percent to the tax rates on regular income that threaten to reach as high as 39.6 percent.

IMPACT. Only qualified dividends are eligible for the reduced tax rates. Generally, these are dividends received from a domestic corporation or a qualified corporation, on which the underlying stock is held for at least 61 days within a specified 121 day period.

“The Senate bill gives taxpayers some certainty in tax planning for the next two years. Based on unofficial revenue costs, it also will inject \$800 billion into the economy. “

COMMENT. Also extended for two years are special rules for treating the percentage of excluded gain as a tax preference item subject to the alternative minimum tax (AMT). Previous legislation, now extended, treated seven percent (rather than

42 percent) of the excluded gain as a tax preference item subject to the AMT.

The Senate bill also provides for treating 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. Also extended are rules for collapsible corporations, the accumulated earnings tax and personal holding companies.

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. The Pease limitation is repealed for 2010 but is scheduled to return in full after 2010 under EGTRRA’s sunset rules at a projected level of income starting at \$169,550 (\$84,775 for married couples filing separately). The Senate bill extends 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.

CCH PROJECTED TAX RATES FOR 2011 UNDER SENATE BILL

Single Individuals

If taxable income is:	The tax would 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 would 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 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, \$254,350 for joint filers). Under EGTRRA, the PEP is repealed for 2010. The Senate bill extends repeal of the PEP for two years, through December 31, 2012.

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 Senate bill.*

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. The Senate bill extends EGTRRA's marriage penalty relief for two years, through December 31, 2012.

IMPACT. *Under the EGTRRA sunset, the 2011 standard deduction for married couples filing jointly is projected to be \$9,650. The Senate bill raises it to \$11,600.*

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 Senate bill extends this treatment through December 31, 2012.

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

Child Tax Credit

The Senate bill 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 in EGTRRA, the 2009 Recovery Act and other bills. Under the EGTRRA sunset, the child credit would revert to \$500 per qualifying child.

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 17 at the close of the year and satisfy relationship, residency, support, citizenship and dependent tests.*

COMMENT. *The 2009 Recovery Act, among other things, increased the refundable portion of the child tax credit for 2009 and 2010. The Senate bill continues this treatment for 2011 and 2012.*

Earned Income 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. The Senate bill extends the enhanced EITC for two years, through December 31, 2012.

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

Adoption Credit

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). The Patient Protection and Affordable Care Act increased the credit and exclusion by another \$1,000 (adjusted for inflation) for 2010 and 2011. The PPACA also made the adoption credit refundable. The Senate bill extends the enhancements in EGTRRA to the credit and exclusion amount through December 31, 2012.

Dependent Care Credit

Taxpayer who incurs expenses to care for child under age 13 or for incapacitated dependent or spouse 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 Senate bill extends the enhanced dependent care credit for two years, through December 31, 2012.

IMPACT. *The 35 percent rate under the Senate bill 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. Therefore, the credit continues to top out at \$600/\$1,200 for any qualifying taxpayer with an AGI over \$43,000.*

Employer-Provided Child Care

Under EGTRRA, employers may qualify for a tax credit if they make available child care to employees before 2011. The credit reaches \$150,000 for qualified costs. The Senate bill extends the credit for two years, through December 31, 2012.

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 Senate bill 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 adjusted gross income (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.*

COMMENT. *The AOTC delivers a maximum credit of \$2,500 in qualified higher education expenses for qualified individuals (100 percent of the first \$2,000 and 25 percent of the next \$2,500).*

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

Educational Assistance Exclusion

EGTRRA allows employee 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 is scheduled to expire after 2010. The Senate bill 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 Senate bill 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 is scheduled to expire after December 31, 2010. The Senate bill 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 are scheduled to sunset after 2010. The Senate bill 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 will be included in a recipient's income after 2010. The Senate bill extends the income exclusion for these scholarships for two years, through December 31, 2012.

Individual Tax Extenders

The Senate bill extends a number of temporary individual tax incentives which had expired at the end of 2009. These incentives, known as extenders, would be extended for two years, through December 31, 2011. The individual incentives extended by the Senate bill 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 Senate bill does not extend the additional standard deduction for real property taxes, which expired at the end of 2009.*

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

ALTERNATIVE MINIMUM TAX

The Senate bill 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 its reach. The Senate bill increases the exemption amounts for 2010 to \$47,450 for individual taxpayers, and to \$72,450 for married taxpayers filing jointly. For 2011, the amounts would be increased to \$48,450 for individuals and \$74,450 for married taxpayers filing jointly.

IMPACT. *Without a patch for 2010, the exemption amounts for 2010 and again for 2011 will plummet 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 Senate bill also allows the nonrefundable personal credits to the full amount of an individual's regular tax or AMT.*

PAYROLL TAX CUT

The Senate bill reduces the employee-share of OASDI (Social Security tax) from 6.2 percent to 4.2 percent for wages earned in calendar year 2011 up to \$106,800. 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 \$120 billion into the economy in 2011. Unlike the Mak-*

ing 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 Senate bill, 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 Senate bill.

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 Senate bill makes no changes to the Medicare (HI) portion of Social Security taxes.

PLANNING NOTE. Self-employed individuals under the Senate bill 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).

BUSINESS INCENTIVES

100 Percent Bonus Depreciation

The Senate bill boosts 50-percent bonus depreciation to 100 percent for qualified

investments made on or after September 9, 2010 and on or before December 31, 2011. The Senate bill also would make 50 percent bonus depreciation available for qualified property placed in service after December 31, 2011 and on or before December 31, 2012. Certain long-lived property and transportation property is eligible for 100 percent expensing if placed in service before January 1, 2013.

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.

"The Senate bill reduces the employee-share of OASDI from 6.2 percent to 4.2 percent for wages earned in calendar year 2011 up to \$106,800. "

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 Senate bill extends Code Sec. 179 expensing at an enhanced 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. The Senate bill allows taxpayers to monetize accumulated AMT credits in lieu of taking bonus depreciation. This treatment would apply for tax years 2011 and 2012.

COMMENT. The 2009 Recovery Act and earlier legislation provided similar treatment.

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 \$2,000,000, respectively, for tax years beginning in 2010 and 2011. The Senate bill 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.

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

Research Tax Credit

The Code Sec. 41 research tax credit expired at the end of 2009. The Senate bill extends the research tax credit, retroactively, for two years, through December 31, 2011.

COMMENT. Earlier in 2010, President Obama urged Congress to make the credit permanent. The Senate bill 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.

Small Business Capital Gains

The 2010 Small Business Jobs Act enhanced the exclusion of gain from qualified small

business stock to non-corporate taxpayers. The qualified stock must be acquired at original issue and held for more than five years. For stock acquired after September 27, 2010 and before January 1, 2011, the exclusion is 100 percent. The Senate bill extends the 100 percent exclusion for qualified small business stock acquired before January 1, 2012 and held for more than five years.

COMMENT. *The 2009 Recovery Act provides for a 75 percent exclusion for qualified small business stock acquired after February 17, 2009 and before September 27, 2010 and held for more than five years.*

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. The Senate bill extends parity among transit benefits through the end of 2011.

IMPACT. *Affected benefits are employer-provided transit and vanpool benefits and the exclusion for employer-provided parking benefits.*

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. The WOTC is scheduled to expire after August 31, 2011. The Senate bill extends the WOTC through December 31, 2011 and is effective for employees hired after the date of enactment.

COMMENT. *The 2009 Recovery Act added two new target groups: unemployed veterans and disconnected youth,*

Business Tax Extenders

The Senate bill extends a number of business tax extenders, which had expired at the

end of 2009. These business tax extenders are extended for two years: 2010 and 2011. The business tax incentives extended by the Senate bill are:

- Indian employment credit and accelerated depreciation for business property on an Indian reservation
- New Markets Tax Credit
- 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
- Renewal community investments
- Cover over of rum excise taxes to Puerto Rico and USVI
- American Samoa economic development credit

ENERGY INCENTIVES

The Senate bill extends a number of energy tax incentives, primarily targeted to businesses, scheduled to expire after 2010. One popular energy incentive for individuals, the Code Sec. 25C residential energy property credit would be extended but with some limitations.

Business Energy Incentives

Business energy incentives extended by the Senate bill are:

- Credits for biodiesel and renewable diesel fuel
- Credit for refined coal facilities
- New energy efficient home credit
- Excise tax credits and outlay payments for alternative fuel and alternative fuel mixtures
- Sales of electric transmission property
- Percentage depletion for oil and gas from marginal wells
- Grants for certain energy property in lieu of tax credits
- Tax credits and outlay payments for ethanol and tariff on imported ethanol
- Energy efficient appliance credit

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 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 Senate bill extends the Code Sec. 25C credit through 2011. However, the Senate bill 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. These enhancements under the Senate bill would not be renewed for 2011.*

DISASTER INCENTIVES

The Senate bill extends a number of targeted disaster relief measures. They are:

- Tax incentives for the New York City Liberty Zone (9-11 relief)
- Increased rehabilitation credit for historic structures in the Gulf Opportunity Zone (GO Zone)

- Low income housing tax credits for GO Zone
- Tax-exempt bonds for GO Zone
- Temporary depreciation allowance for GO Zone

COMMENT. *The Senate bill does not extend national disaster relief, which provides enhanced casualty loss rules, expensing and other relief for victims of designated disasters. National disaster relief expired at the end of 2009.*

BONDS

The Senate bill extends several bond programs through 2012. 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 Senate bill 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 Senate bill 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.

FEDERAL ESTATE TAX

EGTRRA gradually reduced and then abolished the federal estate tax for decedents dy-

ing in 2010. The pre-EGTRRA estate tax (with a maximum tax rate of 55 percent and a \$1 million exclusion) is scheduled to be revived after 2010. Additional EGTRRA changes affected the gift tax and the generation-skipping transfer tax.

Estate Tax Compromise

The Senate bill imposes a maximum estate tax rate of 35 percent and an applicable exclusion amount of \$5 million (\$10 million for married couples) for decedents dying on or after January 1, 2011 and on or before December 31, 2012.

IMPACT. *The applicable exclusion amount is adjusted for inflation for any decedent dying after 2011 (in 2012). The new rate and exclusion represent a significant reduction from the 45 percent rate and \$3.5 million exclusion applicable for 2009.*

Stepped-Up Basis

For 2010, EGTRRA repeals the stepped-up basis rules and replaces them with a modified carryover basis regime. The Senate bill revives the traditional stepped-up basis regime for all assets included in the gross estate for decedents dying on or after January 1, 2011 and on or before December 31, 2012.

IMPACT. *Under the stepped-up basis rules, the income tax basis of property acquired from a decedent at death generally is stepped up (or stepped down) to its value as of the date of the decedent's death (or the estate tax alternate valuation date, if elected).*

Option for 2010

The Senate bill gives estates of decedents dying after December 31, 2009 and before January 1, 2011 the opportunity to elect to apply the carryover basis rules under EGTRRA with no estate tax, or the revived estate tax and stepped-up basis rules under the bill.

Portability

The Senate bill provides for “portability.” 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.

Filings

The Senate bill 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

Under EGTRRA, the gift tax is retained despite repeal of estate and GST taxes after December 31, 2009. For gifts made after December 31, 2009, the 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. The Senate bill provides for a top tax rate of 35 percent and a \$5 million exclusion for two years, through December 31, 2012.

COMMENT. *The Senate bill reunifies the gift and estate taxes, which were decoupled under EGTRRA. Reunification would apply to gifts made after December 31, 2010.*

GST

Under EGTRRA, the GST tax does not apply to generation skipping transfers made after December 31, 2009 and before January 1, 2011. The Senate bill provides for a zero percent GST rate for 2010 and a \$5 million exemption. The Senate bill revives the GST tax for 2011 and 2012 at the maximum estate tax rates and exclusion.



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