

*Economic Growth and Tax Relief Reconciliation Act of 2001 & Small Business Jobs Act of 2010—How they Impact the Way We Advise Our Clients.*

Ladies and Gentlemen, it looks like certain provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) are set to sunset this years. Unless Congress acts, this means higher tax rates for both employers and workers in 2011. Kindly note the following:

**Higher Tax Brackets**—While EGTRRA provided for lower income tax rates, without a revision the 10% bracket would potentially disappear, and the lowest bracket would become 15%. This also means that the top four tax brackets could rise from 25%, 28%, 33% and 35% to 28%, 31%, 36% and 39.6%.

**Supplemental Wage Rate**--The supplemental wage rate (e.g., bonuses, commissions, severance pay) is set to increase from 25% to 28% on supplemental wages totaling \$1 million or less in the calendar year. For supplemental wage payments of over \$1 million, the rate will increase from 35% to 39.6%.

**Backup Withholding**-- Backup withholding is required on certain nonwage payments made to payees for whom an information return was filed which had a missing or incomplete taxpayer identification number. The current backup withholding rate of 28% will increase to 31% starting in 2011 unless this provision is extended by Congress.

**Employer-Provided Educational Assistance**—Presently employers are able to reimburse up to \$5,250 of an employee's non-job-related educational expenses tax-free. This is assuming that the reimbursement program meets the requirements set forth in Code Section 127. Neither this fringe benefit nor the education assistance exclusion for graduate level education will be available beginning in 2011.

**Advanced Earned Income Credit**--This credit allowed low-income employees to receive an advance payment of the earned income credit on their paychecks. Their withholding was lowered to account for the payment.

**Making Work Pay Credit**--Under the American Recovery and Reinvestment Act of 2009 (ARRA), the provision provided a refundable tax credit to individuals below a certain income tax level. This credit was received through a reduction in the amount withheld from the employee's paycheck.

These changes will affect both your clients that are employers and employees. Being mindful of the increase in tax rates, means that the amount of the employer's federal tax deposit ("FTD") will increase and the employee's take home pay will decrease. If your clients are on the edge of being able to keep up with their FTD requirements and otherwise, it is best to counsel them on how the change will impact both them and their employees and workers. For employees struggling to get by as it is, the decrease in take home pay will certainly impact employers.

Additionally, the *Small Business Jobs Act of 2010* was signed into law on September 27, 2010. It includes a numbers of tax provisions affecting both businesses and individuals. Some of these provisions are effective either retroactively, immediately from the date the bill was signed or beginning in 2011.

**Retroactively Effective**--These provisions will have more of a tax impact as they are retroactively effective starting at the beginning of 2010:

- Increased Code Sec. 179 and qualified real property expense deduction beginning in 2010 and 2011.

- 50% bonus depreciation and an additional \$8,000 luxury auto depreciation limit apply for qualified property placed in service in 2010.
- Cell phones are no longer “listed property” subject to strict substantiation rules for tax years beginning after 2009.
- Increased startup expense deduction applies for tax years beginning after 2009 and before 2011.
- Eligible small business credits that are determined in a taxpayer’s first tax year beginning in 2010 but are unused are eligible for 5-year carryback.
- Eligible small business credits determined in tax years beginning in 2010 can offset AMT liability and, to an increased extent, regular tax liability for credits determined in tax years beginning after 2009.
- Health insurance costs for a taxpayer and his family are deductible in computing 2010 self-employment tax.
- The Code Sec. 6707A penalty for failure to report a tax shelter transaction is completely restructured for penalties assessed after 2006.

**Immediately Effective**--These provisions are effective as of the September 27, 2010 enactment date:

- The 100% gain exclusion for qualified small business stock (QSBS) for regular tax and alternative minimum tax (AMT) purposes applies for QSBS acquired after September 27, 2010 and before January 1, 2011.
- The provision allowing retirement plan distributions to be rolled over to a designated Roth account applies for distributions made after Sept. 27, 2010.
- The new sourcing rule for guarantees applies for guarantees issued after Sept. 27, 2010.
- The elimination of the requirement for a pre-levy collection due process (CDP) hearing for certain Federal contractors applies for levies issued after Sept. 27, 2010.

**Prospective Changes**--These provisions are to apply after 2010:

- Temporary reduction in the S Corporation’s built-in gain period from 7 to 5 years.
- Partial annuitization of nonqualified annuities
- Code Sec. 457 governmental plans are permitted to include a qualified Roth contribution program.
- Information reporting requirement for rental income from realty and the increased information return penalty and failure to furnish payee statement penalty;
- The accelerated estimated tax for large corporations (assets of at least \$1 billion) applies to estimated tax otherwise due in July, August or September of 2015.

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Please remember to join us at our Fall CLE on *What To Do In the Event of An IRS Blitz* and our monthly meetings whereby members of our tax section speak to us about topics of interest. We meet the first Wednesday of every month with our next meeting to be held at 110 North Washington St., Ste. 406, Rockville, MD 20850, promptly at 5:30pm. Our topics for this year will cover: FBARs, estate tax, divorce tax, state taxes, choice of business entity, sales and use tax and bankruptcy. Please do let me know if you would like to speak!