

August 6, 2001

**“WHAT DOES THE NEW LAW MEAN TO ME RIGHT NOW?”
TAX BREAKS FOR INDIVIDUALS IN THE ECONOMIC GROWTH AND TAX RELIEF
RECONCILIATION ACT OF 2001**

As you probably know, Congress recently passed a major tax bill. Although many of its provisions won't go into effect for several years, most individuals will see at least some income tax benefits this year. These include a new 10% bracket, an across-the-board one-point cut on July 1st in each of the current tax brackets above the 15% bracket, modest relief from the alternative minimum tax (AMT) and a higher child credit. Here is a brief overview of these tax changes.

NEW 10% BRACKET

The Act carves a new 10% bracket out of part of the current 15% bracket. Specifically, the first \$6,000 of taxable income for singles and married taxpayers filing separately, \$10,000 for heads of household and \$12,000 for married persons filing joint returns will be taxed at 10%. Individuals will get the benefit from the new bracket for 2001 in the form of checks from the Federal government of up to \$300 for a single person or married individual filing separately, up to \$500 for a head of household such as a single parent and up to \$600 for a married couple. Individuals who are eligible to be claimed as dependents on another taxpayer's return (such as a dependent child) and nonresident aliens won't get a check.

IRS officials expect to start cutting checks (called “advance refund checks”) in August at a rate of about nine million a week, based on 2000 income tax returns. The Act instructs the Treasury to send the advance refund checks by October 1st, but people who filed late or got filing extensions may get their checks later. The payments will be made in numerical order based on the last two digits of the lead Social Security number on the tax return. Those eligible individuals who filed no tax return for 2000 or owed no tax will benefit from the 10% bracket when they file their 2001 tax return—they'll get a credit of up to \$300, \$500 or \$600, depending on filing status.

ONE-POINT ACROSS-THE-BOARD TAX-RATE CUT

As the first installment of the individual income tax rate cuts that will unfold over the next five years, the “old” income tax rates of 28%, 31%, 36% and 39.6% will each be reduced by one percentage point, effective July 1st of this year, resulting in blended tax rates, for all of 2001, of 27.5%, 30.5%, 35.5% and 39.1%, respectively. The 15% rate, however, will remain unchanged. In the near future, the Treasury Department will notify employers of new withholding schedules, which will be adjusted to reflect the initial one-percentage-point reduction in tax rates. The lower marginal rates should result in slightly bigger paychecks as the amount withheld for taxes is reduced.

MODEST AMT RELIEF

The Act provides only limited, temporary AMT relief for individuals. To find out if you owe AMT, you start with regular taxable income, modify it with various adjustments

and preferences (such as addbacks for property and state income taxes and dependency exemptions) and then subtract an exemption amount. The result is subject to an AMT tax rate of 26% or 28%. You pay the AMT only if it exceeds your regular tax bill. For 2001, the Act increases the AMT exemption amount by \$4,000 for married taxpayers filing joint returns, and by \$2,000 for other individuals. However, the AMT exemption amount phases out at higher levels of income and the boosted exemption will only remain in place through 2004. Many taxpayers, particularly those residing in states with high income and/or property taxes, will not receive the full benefit of the new tax cuts and instead will have to pay the AMT unless Congress enacts additional AMT relief. Thus, it is still necessary to plan how to avoid or at least reduce the AMT.

HIGHER CHILD CREDIT

Parents of dependent children younger than 17 may claim a tax credit per child, if parental income doesn't exceed certain dollar limits. (A tax credit reduces your tax bill dollar for dollar, as opposed to a deduction, which reduces the amount of your income subject to taxation.) Under the 2001 Act, the maximum credit per child increases from \$500 to \$600 for 2001, meaning eligible taxpayers will be able to claim the additional \$100 credit on their 2001 returns filed next year. In later years the credit gradually climbs until it reaches \$1,000 in 2010.

LOOKING DOWN THE ROAD

Much of the \$1.35 trillion tax cut in the 2001 Act will take longer to materialize. Many of the larger tax cuts in the Act don't kick in until 2002 or later. Some new tax breaks phase in over the next decade, while some current rules phase out over that period, creating tax-planning challenges for everyone. If you would like to discuss how the Act may affect your individual tax and financial planning situation, please do not hesitate to call.

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