
2001-2004 Bush Administration Tax Legislation as of January 1, 2005

Congress, along with President Bush, have provided 4 major and some minor pieces of tax legislation during each of the four years of the Bush administration. The 2001 bill, followed by the 2002 bill, contained what has been quoted as the "most retroactive, temporary and phase in/phase out, various effective dates bill" that has ever graced our nation's tax legislation. In 2003 and then finally in 2004, the President has been able to turn all of that around and has just about made most of the 2001 law permanent (2001 contained the majority of the tax bill changes). All of these tax cuts collectively will cost over 1.5 trillion dollars.

Individual Income Tax Rates

There are all new rates approved under the 2001 bill and formalized in the 2004 bill. The top rate is now 35%, while there is a new low rate of 10%, down from 15% previously. Since the 10% rate applies to all taxpayers irrespective of their marginal tax bracket, every single filer paying taxes at a marginal rate above the 10% bracket will receive at least a \$50 savings and joint filers over \$100. However, with all the changes, especially if you can benefit from the child tax credits for children under the age of 17 or the education credits, your savings could possibly bring tax cuts of over \$500-\$2,000 for single filers and possibly higher for joint filers.

Sales Tax

The main new "reinvention" (prior to 1986, this was a part of our tax code, along with non-mortgage or consumer interest) is the sales tax deduction. You are allowed all of your sales tax because our income tax in Texas is nonexistent. (this is an either/or type deduction - state sales tax or state income tax but not both). To make things much easier than saving receipts, there are tables available plus car and boat sales tax are additional to what is allowed by the amounts in the tables.

Deduction for Educational Supplies

Also now permanent is the Deduction for Educational Supplies. Previously, an educator who wanted to deduct educational supplies purchased by the educator for use in the classroom was limited to everything over 2% of their AGI (adjusted gross income). However, after 2001, educators (including aides) may deduct up to \$250 for books, supplies and most athletic equipment they provide.

This is accomplished "above the line," which means they are deductible in addition to the standard or itemized deductions and are therefore not subject to the 2% of AGI limitation. The form takes the remainder to itemized deductions and a two-educator family may deduct double.

Marriage Penalty Relief

Standard Deduction - 2003 law immediately doubled the standard deduction for married couples to twice the amount for single taxpayers. This relief was supposed to be temporary but 2004 made this permanent.

This increase will further influence the decision by joint filers in determining if they should itemize deductions or take the standard

Some Key Points

Programs with "Sunset" Provisions under the 2001 Law which are now Permanent:

- ⇒ Marriage Penalty Relief
- ⇒ Child Tax Credit
- ⇒ Alternative Minimum Tax Relief
- ⇒ Immediate Write Off of \$250 in Educational Supplies

deduction allowed in that tax year.

15% Tax Bracket - The 15% tax bracket is also expanded for joint filers to twice the width of the same bracket for single filers.

Retirement Savings and Pension Reform

There were no changes to the provisions under the 2001 bill. Taxpayers might want **to invest in or “increase” their 403(b) or 401(k)**. By doing this, taxpayers will “double up” on “tax relief” - using other rate cuts to create deductions that they would not have had otherwise.

Contribution Limits - The amounts which can be deposited in tax-advantaged retirement savings plans was raised, including 401(k) and the traditional IRA and will continue to increase progressively, through 2008, at which time it levels off. The 403(b) for educators was also raised and continues to increase progressively through 2006, at which time it levels off.

Catch Up Contributions - Taxpayers age 50 and older can contribute an extra amount to retirement plans, provided their base-line AGI limits are met for regular contributions.

Plan Contribution Limit Increases - 403(b)			
Year	Basic Limit	Additional Limits	
		For Age 50 & over	For 15+ Yrs. of Service with Same Employer
2002	\$11,000	\$1,000	For 403(b) only - Eligible employees may still contribute up to \$3,000 extra above these new amounts
2003	\$12,000	\$2,000	
2004	\$13,000	\$3,000	
2005	\$14,000	\$4,000	
2006 & forward	\$15,000	\$5,000	

Roth & Traditional IRA Contribution Limit Increases			
Year	Basic Limit	Year	Additional Limits
			for Age 50 & over
2002-2004	\$3,000	2002-2005	\$ 500
2005-2007	\$4,000	2006 & forward	\$1,000
2008 & forward	\$5,000		

Pension Portability - Eligible rollover distributions can be moved interchangeably to and from 403(b), 401(k), 457 and IRA plans, including an IRA that was accomplished through annual contributions. This portability extends to spousal beneficiaries who are no longer limited to placing death benefits in an IRA.

Participant Protection - Numerous measures were enacted that increase protection for plan participants in SEP, simple 401(k) and traditional 401(k), including shortening of vesting schedules, permitting workers to become vested sooner, which allows eligibility for employer-matching contributions in 3 rather than 5 years.

Contribution Tax Credit - Lower income taxpayers are entitled to a tax credit, instead of a deduction, for contributions to retirement savings.

Child Tax Credit

Under the original 2001 bill, the Child Tax Credit for children under the age 17 of \$1,000 was scheduled to expire but is now permanent.

Education Tax Cuts

College Tuition Deduction - In 2001, an “above the line” deduction for qualified higher education expenses was created. The amount of deduction varies, depending on gross income. This deduction cannot be taken in the same year as a HOPE or Lifetime Learning Credit for the same student (both credits were introduced under 1997 tax law).

Education Savings Account - Previously called an “Education IRA,” these savings accounts are free from Federal taxation if used to pay for qualified educational expenses. The previous contribution limit of \$500 is now \$2,000 and taxpayers in higher tax brackets may take advantage of this tax break (previously limited to taxpayers in lower brackets). Contributions counted toward any tax year will be permitted through April 15 of the following year.

Funds may be used for "qualified" elementary and secondary education expenses, as well as expenses for higher education. Some "qualified" expenses include tutoring, computer equipment, room and board, uniforms and costs of "extended day" programs.

Enhanced Student Loan Interest Deduction - This portion of the law removes the annual limit on the amount of the deduction and raises the income threshold. In addition, the 60 month limit was removed. Voluntary payments, such as "interest only" payments made while the loan is in forbearance, are also eligible for deduction.

Qualified Tuition Plans (529 Plans) - The restriction that allowed only "state sponsored plans for in-state attendance" (i.e. Texas Tomorrow Fund) was removed. Private institutions of post-secondary learning and mutual fund and financial companies are now sponsoring qualified tuition plans. In addition, it is now possible to make contributions to an education IRA and qualified "state sponsored" tuition plans in the same tax year. Distributions from both state sponsored and other 529 plans are presently excludable. These programs allow flexibility and large annual contributions. **Contact our office for more details at 800.950.1829.**

Employer-Provided Education Assistance - The employer-assisted educational assistance exclusion (up to \$5,000 annually) became permanent, with coverage extended to undergraduate courses.

Alternative Minimum Tax (AMT)

Despite predictions that the Alternative Minimum Tax (AMT) will eventually capture millions of middle-income taxpayers, Congress has resisted a complete overhaul of the tax law. Congress "tweaked" the AMT in 2001 and did so again in 2003, still falling short of reforming the AMT. It does raise the exemption for AMT. The single filer moves from \$35,750 to \$40,250 AMT tax exemption and joint filers move from \$49,000 to \$58,000. This was temporary for tax years 2003 and 2004 only but the 2004 law makes it permanent. The AMT does not apply to most readers of this summary.

Reduced Tax Rates for Capital Gains and Dividends

Capital Gains

Under the new law, the maximum net capital gains tax rate immediately falls 5% (from 20% to 15%). The current 10% capital gains rate for lower-income taxpayers falls to 5%. These new rates are effective for sales and exchanges (and payments received) on or after May 6, 2003 through December 31, 2007 (with the 15% rate continuing in 2008 as well). The lower rates apply for both regular tax and AMT purposes. There are special rules related to property held for more than five years.

Dividends

For most taxpayers, dividend income received by an individual shareholder from a domestic or qualified foreign corporation will be taxed at the maximum rate of 15% for most taxpayers. Lower income individuals will pay tax on dividends at a new rate of 5%.

This special tax treatment is temporary and is set to terminate on December 31, 2008. The 5% rate terminates on December 31, 2007, when it falls to 0% in tax year 2008. The old 2003 rates return in 2009.

In addition to the complexity created by the various effective and sunset dates for dividend relief, the determination of exactly what is a qualifying dividend for purposes of the lower rates has already created reams of regulations, rules and commentary for both distributing corporations and shareholders. For more detailed information on this or any of these provisions, please **consult my CPA office at 800.950.1829.**

Dividends paid into a tax-free fund, such as a 403(b), IRA or 401(k), are not eligible for the reduced tax rate. They remain pre-tax and are fully taxable when withdrawn.

Therefore, maximizing your "after tax" money in mutual funds is now an even better strategy.

Conclusion

Due to limited space, we have briefly covered only some of the major and a few of the minor points of all of the tax bills. While most of the legislation involving individuals is summarized in some fashion, self-employed and corporate changes were given little (if any) space.

It is also worthwhile considering that major tax reform replacing the income tax system completely is now being discussed.

This is the fourth major bill of the 4 year Bush presidency. Minor bills have also passed, including the elimination of the loophole for teachers wanting their spouse's Social Security benefits.

Handouts in our packet discuss the Windfall Elimination Provision (offset of a retiree's Social Security).

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NOTE - Changes brought about by all of these tax bills may complicate your tax preparation. For information more specific to your income tax planning and preparation, please **visit a Certified Public Accountant in your area or contact our office at 800.950.1829.**

ADDITIONAL HELP can also be obtained through various books which should be available at bookstores soon, updated to reflect these new laws (i.e. Ernst & Young's Guide to Your Taxes and J. K. Lasser Income Tax Guide).

To Contact the IRS

IRS Website - www.irs.gov - This site can be used to check the status of a refund, learn about electronic filing and download forms and publications

IRS Forms/Publications - 800.829.FORM (3676) - Call for forms and/or publications to be mailed to you

IRS Help Line - 800.829.1040 - Normally a long hold before speaking to a representative

Tele-Tax Line - 800.829.4477 - Automated topics; another way to check on the status of a refund—"user friendly"

Your Local IRS Office - Your local office is designed to help you in specific current and past matters, as well as printouts of prior year information. They are often busy but can be quicker in off-peak times/dates. You can obtain the address/telephone number of your local office by calling 800.829.1040, visiting the IRS website or consulting your local telephone book.