

Tax Relief or Just Tax Confusion

This is part two of a two part article that addresses selective provisions of the Jobs and Growth Tax Relief Reconciliation Act of 2003 (the New Act) that relate to individuals.

Marriage Penalty Relief

The standard deduction for married taxpayers filing jointly was increased to equal twice the standard deduction for a single taxpayer which seems quite fair; however, this provision only applies for 2003 and 2004, then the deduction is reduced to 180% of the standard deduction for single taxpayers.

Also included in the New Act in an effort to reduce the marriage penalty, the fifteen percent tax rate was expanded to twice the range for single taxpayers, but again, this provision only applies for 2003 and 2004. In 2005, the expansion is reduced to 180% of the range for single taxpayers.

Acceleration of previously enacted tax benefits

The Economic Growth Tax Relief Reconciliation Act of 2001 (The 2001 Act) included a variety of tax benefits and rate reductions that were scheduled to apply in years after the year of enactment. The New Act accelerated several of those tax benefits.

1. Reduction of ordinary income tax rates

The 2001 Act reduced most marginal ordinary income tax rates by two percent, but the reductions were not scheduled to apply until 2006. The New Act causes those reduced rates to apply for tax years 2003 through 2010. As a result of the fact that the rate cuts are retroactive to January first of this year, tax withholding tables need to be adjusted and taxpayers are entitled to have less federal income tax withheld from their wages. However, in 2011, the old rates that applied prior to the 2001 Act again apply.

Additionally, the 2001 Act provided for an expansion of the ten percent tax bracket for all taxpayers. This provision, originally scheduled to apply for tax years 2007 through 2010, applies to 2003 through 2010 as a result of the New Act. However, it only saves single taxpayers \$50 per year and married taxpayers \$100 per year, and in 2011 the old rates that applied prior to the 2001 Act again apply.

2. Child Tax Credit

Under the 2001 Act, the Child Care Credit was scheduled to gradually increase to \$1,000 by the year 2010. The New Act, increases the maximum child care credit to \$1,000 for the years 2003 and 2004, but then the maximum credit is decreased to \$700 for 2005 and then gradually increases back to \$1,000 by 2010. The New Act continues the income phase out limitations of the 2001 Act. If you were entitled to the maximum credit on your

2002 return, a \$400 check will be sent as an advance of the credit for 2003. It is unclear why the government will refund an amount that has no relation to the amount of a credit to which you “may” be entitled on your 2003 return.

The Act certainly adds confusion to the preparation of your tax return, but it also provides opportunities for investors. Because the tax rate on dividends is now up to 20% less than the tax rate on interest, it may be prudent to trade in some corporate bonds for preferred stock. Additionally, the after-tax rate of return on municipal bonds has decreased which may make US Treasury Bonds a better alternative. As always, I recommend that you see your tax attorney, CPA or preparer for specific tax advice.

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