

## *Yet More Federal Tax Changes*

In May, President Bush signed into law the Tax Increase Prevention and Reconciliation Act (TIPRA) and in August, he signed into law The Pension Protection Act of 2006 (PEPRA). Both statutes contain wide reaching changes to federal tax rules. Below is an overview of selected provisions of these tax acts that will impact a large percentage of Americans.

### Increased Age for Kiddie Tax

Unearned income such as interest, dividends and capital gains of a child under age 14 is taxed at the marginal income tax rate of such child's parent to the extent it exceeds \$1,700. The age limit for tax years after 2005 is now 18. Even though the tax statute was not signed until August of this year, the change is effective as of January 1, 2006.

### AMT Relief

The alternative minimum tax catches more and more taxpayers each year, many by surprise. The exemption amounts from such tax were increased as part of the 2001 Tax Act, but the increased exemptions were to apply only through 2005. The new tax statute extended the increased exemptions but only through 2006. For 2006, a married couple filing jointly, will have a \$62,550 exemption from alternative minimum tax.

### Receipts required for ALL charitable contributions

Another broad reaching change is to the substantiation requirement for charitable contribution deductions. For tax years after 2006, all contributions must be evidenced by a cancelled check, a receipt or a letter from the charity. This change will effectively deny a deduction for a cash contribution made outside a supermarket to a town sports team, unless a receipt is received.

Previously, some latitude was given during an audit for cash contributions, but now, unless the documentation, which must have been received by the time the tax return was filed, exists, the deduction will be denied. Some taxpayers abused the government's latitude, so the government decided to solve the problem by killing the proverbial ant with a sledgehammer.

### Extension of reduced tax rate to long term Capital Gains and Qualified Dividends

The reduced tax rates applicable to long term capital gains and qualified dividends have been extended through 2010. They were previously scheduled to expire for tax years after 2008. Thus, the highest tax rate on long term capital gains and qualified dividends will remain at 15%. For those taxpayers in the 10 or 15 percent tax brackets, the 5% tax rate applies through 2007 and then the rate is reduced to 0.

### IRA withdrawals directly to Charity

A unique planning opportunity was created for those who are required to take distributions from Individual Retirement Accounts. A taxpayer age 70 ½ years old or older can have a distribution made directly from his/her IRA to a qualified charity and not have the withdrawal included in gross income. There is no deduction for the

contribution though. This rule solves, from a federal tax standpoint, the income tax that often resulted when a distribution was included in income and then the same amount deducted as a contribution.

You should be aware of the state tax implications though. If your state does not permit a deduction for contributions to charity, such as Massachusetts, you may end up with a state tax due on money you never received. Massachusetts solved this problem with Technical Information Release 06-20 in which the federal exclusion was adopted for Massachusetts income tax purposes, but if you are not a resident of Massachusetts, be sure to research the state tax implications before having a distribution sent to a charity.

The above is only a brief explanation of selected provisions of TIPRA and PEPRA. As always, I recommend that you consult with your CPA for an explanation of all provisions of these acts that impact you.

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