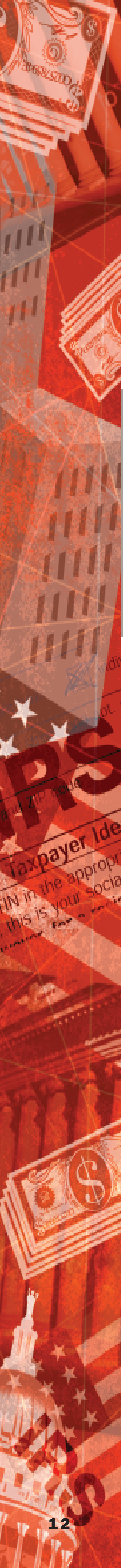

By Anthony P. Curatola, Editor

Individual Taxpayer Provisions of the 2010 Tax Act

For individual taxpayers, the 2010 Tax Act extended several income tax provisions, including the extension of the 2010 income tax rate brackets, the doubling of the 15% tax rate bracket for married taxpayers filing a joint tax return, and many others.

Last month's column addressed the major business provisions extended by The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (PL 111-312) signed into law on December 17, 2010. This month, we'll take a look at some of the individual taxpayer income tax provisions that expired on December 31, 2009, or were set to expire on December 31, 2010, and were extended by the Act.

Tax Rates

Probably the most controversial tax provision included in the Act was the extension of the individual income tax rates. In general, the sticking point was whether to extend some or all of the 2010 tax rate brackets (10%, 15%, 25%, 28%, 33%, and 35%) and, in particular, whether to bring back the 36% and 39.6% tax rate brackets for upper-income taxpayers. When the final vote occurred, the 2010 income tax rate brackets were extended for tax years 2011 and 2012. The permanency of these rates—and the rates for upper-income taxpayers—is likely to be a major issue during the 2012 Presidential election.

The Act also extended the doubling of the 15% tax rate bracket for married taxpayers filing a joint tax return. This provision provides a level tax field between married couples with two wage-earners and unmarried couples earning the same income. The same leveling isn't true for other tax brackets.

For 2009 and 2010, the Making Work Pay credit provided a tax credit of 6.2% on taxpayers' earned income (up to $400 for individuals or $800 in the case of a joint tax return). This credit didn't apply to all taxpayers since it was reduced by 2% of a taxpayer's modified adjusted gross income (MAGI) exceeding $75,000 ($150,000 for a joint filing). Though the Act didn't extend this credit, it did introduce a somewhat equivalent tax reduction to the payroll taxes paid by all taxpayers in 2011. Payroll taxes consist of two taxes: old-age, survivor, and disability insurance tax (Social Security tax) and hospital insurance tax (Medicare tax). The Act provides a 2% reduction to the employee's portion of the Social Security tax rate. Thus, all employees will pay 4.2% (instead of 6.2%) on earned income, the self-employed will pay an effective 10.4%, and employers will continue to pay 6.2%.

Deductions

The standard deduction amount for taxpayers filing a joint tax return will continue to be double the inflation-adjusted amount applicable to taxpayers filing as single (or married separate) for both 2011 and 2012. Historically, the difference between the two standard deduction amounts (66.67%) was seen as a marriage penalty.

The return of the phaseout of a person's itemized deductions and personal/dependency exemptions amounts for those taxpayers with a MAGI above a threshold amount is delayed until 2013. Hence, all taxpayers are able to deduct all itemized deductions and all personal/dependency exemption amounts during 2011-2012 as long as the alternative minimum tax (AMT) rules aren't applicable to the taxpayer.

The option to take an itemized deduction for state and local general sales taxes instead of the state income tax has been retroactively extended from 2009 for tax years 2010 and 2011 (but not for 2012). This is seen as a leveling provision for those itemizing taxpayers living in states that don't have a state income tax (or have a low one).

Teachers weren't forgotten in this patchwork legislation. The above-the-line deduction for up to $250 of teacher classroom expenses is extended for both 2011 and 2012 (in lieu of a miscellaneous itemizing deduction). This provides minimal tax relief to those educators with at least 900 hours teaching in grades K-12. Yep—that means college, tech, and preschool educators can't participate.

The ability to deduct mortgage insurance premiums as mortgage interest is extended, but only for one year (i.e., 2011).

Needless to say, there are some deductions that weren't included in this legislation. The exclusion of the first $2,400 of unemployment compensation isn't extended; thus, all unemployment compensation is includible in gross income. The increased standard deduction for real estate taxes isn't extended; this provision was beneficial to those taxpayers unable to itemize (e.g., retirees with paid-off mortgages). The itemized deduction or increased standard deduction for state or local sales or excise taxes on new car purchases was also left out of the legislation. And finally, the $500 reduction per incident for personal and casualty losses reverts to its pre-2010 level of $100.

AMT Provisions

We can't get into all of the individual tax provisions in the Act because of space limitations, but there is one other that should be mentioned: the AMT exemption-amount provision, which is retroactively extended for 2010 and 2011. Table 1 shows the exemption amount increases by year.

Table 1. **AMT Exemption Amounts by Year**

	Married filing jointly	Married filing separate	Unmarried	Estate & Trust
2010	$72,450	$36,225	$47,450	$22,500
2011	$74,450	$37,225	$48,450	$22,500
2012	$45,000	$22,500	$22,500	$22,500

Education

A number of provisions for educational costs were included. The ability to exclude up to $5,250 of employer-sponsored qualified educational costs is available for both 2011 and 2012. Qualified costs include, but aren't limited to, tuition, fees, and other related educational costs such as books, supplies, and equipment for both graduate and undergraduate courses.

The above-the-line deduction for qualified tuition and related expenses (i.e., fees) is retroactively extended for 2010 and 2011. Taxpayers can't double dip by taking a deduction here and excluding amounts reimbursed by an employer-sponsored plan. This deduction also has both a dollar and AGI limitation. The dollar limitation is $4,000 for taxpayers with a MAGI that doesn't exceed $65,000 ($135,000 for married filing jointly) and $2,000 for taxpayers with a MAGI that doesn't exceed $80,000 ($160,000 for married filing jointly). This provision doesn't have a phaseout range. It is a cliff—you either qualify or you don't; there are no partial amounts.

The deductibility of up to $2,500 of qualifying interest on student loans is extended for 2011 and 2012, but it has a phaseout range that applies to taxpayers with MAGI amounts of $60,000 to $75,000 ($120,000 to $150,000 for married filing jointly). Thus, taxpayers with MAGI amounts in excess of $75,000 ($150,000 for married filing jointly) don't qualify for this deduction. In addition, the reinstatement of the 60-month limit for claiming the deduction once the taxpayer begins paying back the loan is delayed to 2013.

For 2010, the Coverdell Education Savings Account (Coverdell) permits an annual nondeductible contribution of $2,000 per beneficiary who is under 18 years of age by year-end. The Act extends this contribution amount through 2012, which means the contribution amount reverts to the $500 annual limit for 2013. The contribution limit of the Coverdell is phased out if the contributor's MAGI falls between $190,000 through $220,000 for taxpayers filing married jointly and $95,000 through $105,000 for all others. Since the phaseout applies to the contribution, some tax planning within the family may be neces-

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sary as to who can or should contribute.

Finally, the American Opportunity Tax Credit (AOTC) is extended through 2012. The AOTC provides a credit up to $2,500 per year for the first four years of post-secondary education and is calculated as 100% on the first $2,000 of educational costs and 25% on the second $2,500 of costs. This credit is phased out where the taxpayer's MAGI amount is between $160,000 and $180,000 for married filing jointly and between $80,000 and $90,000 for all other taxpayers. For 2009 through 2012, the credit is applicable to qualified tuition, fees, and course-related material.

The Future

Interestingly, there are several tax legislative bills pending in both the House and Senate, including fair tax reform, homeowner tax fairness, job creation, medical device access and innovation protection, permanent marriage penalty relief, and a permanent extension of the election to deduct state and local sales taxes. Naturally, we shouldn't expect any tax legislation until December or maybe January to make tax filing next year more challenging. **SF**

Anthony P. Curatola is the Joseph F. Ford Professor of Accounting at Drexel University in Philadelphia, Pa., and a member of IMA's Greater Philadelphia Chapter. You can reach Tony at (215) 895-1453 or curatola@drexel.edu.