Supplement to J.K. Lasser’s New Tax Law Simplified 2011

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How do you write a book about new tax law and not include some of the biggest tax changes of the year? You write the book (with alerts about possible developments), wait for Congress to make additional changes, and then post an online Supplement explaining these changes. Since publication of J.K. Lasser’s New Tax Law Simplified, Congress enacted the Tax Relief, Unemployment Benefits Reauthorization, and Job Creation Act, which can impact your 2010 return as well as tax planning for years to come. The courts and the IRS have also made decisions and rulings that create tax changes you should know about. Here are key developments since the publication of the book.

The changes presented in this Supplement are tied to the chapters in the book.

Introduction

New law. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, signed into law on December 17, 2010, adds $800 billion in tax breaks for individuals and businesses. Many, but not all, of the provisions that expired at the end of 2009, as well as those set to expire at the end of 2010, have been extended for a year or two. The Bush-era tax cuts that were scheduled to expire at the end of 2010 have been extended through 2012. The estate and gift tax rules have been dramatically changed for 2010, 2011, and 2013.

Chapter 1—New Rules for Your Home and Family

First-time homebuyer credit. The general first-time homebuyer credit of up to $8,000 as well as the long-term resident credit of up to $6,500, which applied to homes purchased through April 30, 2010 (September 30, 2010, for homes in contract at the end of April), have not been extended.

However, the DC homebuyer credit for first-time homebuyers in the District of Columbia, which had expired at the end of 2009, has been extended through 2011. The credit is up to $5,000 of the purchase price.

Homeowners qualifying for the first-time homebuyer or long-term resident credit on 2010 returns must attach certain documentation (such as a HUD-1 statement for first-time homebuyers) to prove eligibility for the credit. Your tax return cannot be filed electronically; you must file a paper return and attach the required documentation to Form 5405 to claim the credit.

Energy improvements. The residential energy property credit for making certain improvements, such as adding insulation or installing energy-efficient windows and exterior doors, expired at the end of 2010. This credit had allowed 30% of qualified costs to be a tax credit up to $1,500 over 2009 and 2010; it has not been extended.
However, for 2011, the former residential energy property credit, which had applied in 2007, will again be effective. This credit is limited to 10% of qualifying costs up to a maximum credit of $500. The $500 limit must be reduced by any such credits claimed after 2005.

Also, for purposes of the $500 credit, additional dollar limits apply to certain types of improvements, so that no more than the following amounts can be taken into account:

- $50 for any advanced main air-circulating fan
- $150 for any qualified natural gas, propane, or oil furnace or hot water boiler
- $200 for windows
- $300 for any item of energy-efficient building property

Qualified improvements must meet criteria established by the 2009 International Energy Conservation Code and the 2009 Consortium for Energy Efficiency.

The IRS has ruled that for purposes of the 2010 home energy credit, the improvements must be installed by December 31, 2010. Merely making a purchase of a qualified improvement by that date is not sufficient to claim the credit.

**Real estate taxes.** The additional standard deduction for real estate taxes of up to $500 (or $1,000 for joint filers) expired at the end of 2009; it has not been extended for 2010. Only homeowners who itemize their personal deductions can write off their property taxes.

**Real estate tax rebate for volunteer responders.** Volunteer firefighters and emergency medical responders were able to exclude from income a property tax reduction or rebate and up to $360 per year in payments or reimbursements. These breaks expired at the end of 2010; they have not been extended.

**Personal and dependency exemptions.** The old phase-out for personal exemptions for high-income taxpayers had been set to reapply after 2010; Congress extended the elimination of the phase-out for 2011 and 2012.

### Chapter 2—Changes for Health Care and Education

**American Opportunity credit.** The credit of up to $2,500 (40% of which is refundable) had been set to expire at the end of 2010 and revert to the old Hope credit; the American Opportunity credit has been extended through 2012. In the president’s State of the Union Address in January 2011, he asked that Congress make this credit permanent to give families up to $10,000 of tax relief when paying for higher education.

**Tuition and fees deduction.** The above-the-line deduction for tuition and fees of up to $4,000 had expired at the end of 2009; it has been extended through 2011.

**Distributions from 529 plans for computer technology.** Such distributions were tax free in 2010; this rule has not been extended for 2011.

**Coverdell education savings accounts.** Favorable rules for these accounts, allowing contributions up to $2,000 annually and tax-free distributions for costs in K–12 plus higher education, were set to expire at the end of 2010; they have been extended through 2012.
Chapter 4—New Investment Opportunities and Traps

Build America bonds. These bonds, created by the American Recovery and Reinvestment Act, were taxable municipal bonds with a potential tax credit of 35% of the bond interest. The rule applied to bonds issued in 2009 and 2010; the special rule has not been extended.

Savings bonds. You can opt to apply your federal tax refund to the purchase of U.S. savings bonds, Series I, up to a maximum of $5,000. You make the request by completing Form 8888, Direct Deposit of Refund to More than One Account. The request must be in multiples of $50.

Capital gain rates. The general capital gain rate, which had been 15% (zero for taxpayers in the 10% or 15% tax bracket) in 2010, has been extended through 2012.

Small business stock. There is a 100% exclusion for stock acquired after September 27, 2010, and before January 1, 2012 (a 75% exclusion applies to stock issued after February 17, 2009, and before September 28, 2010). The stock must be held at least 5 years in order to qualify for zero capital gain tax on the sale. The 100% exclusion applies for both regular tax and the alternative minimum tax. The Administration announced that it would propose a permanent extension of the 100% exclusion in its fiscal 2012 budget.

Chapter 5—New Ways to Boost Your Take-Home Pay

Making work pay credit and FICA tax changes. This tax credit of up to $400 ($800 for joint filers) expired at the end of 2010; it has not been extended. Instead, for 2011 only, there is a 2% reduction in Social Security portion of FICA taxes paid on wages and other taxable compensation. This reduction is built into the withholding tables to boost your take-home pay throughout the year.

$250 educator deduction. The $250 deduction from gross income for educators, which expired at the end of 2009, has been extended for 2010 and 2011. This deduction can be claimed whether or not you itemize other personal deductions. The Tax Court has allowed a coach who paid for athletic equipment to claim this deduction on the grounds that the athletic field was his classroom.

Chapter 6—Other Money-Saving Tax Breaks

Additional standard deduction amounts. The additional standard deduction amounts for real estate taxes (up to $500 or $1,000 for joint filers) and for net disaster losses expired at the end of 2009; they have not been extended for 2010. Many taxpayers who used Schedule L in 2009 may not need it for 2010.

Itemized deductions. The limitation on high-income taxpayers, which was scheduled to reapply starting in 2011, has been postponed; there is no limitation on itemized deductions by high-income taxpayers in 2010, 2011, and 2012.

Option for state and local sales taxes. For those who itemize their personal deductions, there had been an option in 2009 to deduct either state and local income taxes or state and local sales taxes. This option has been extended through 2011.
**IRA transfers to charity.** The tax-free transfer to a public charity of IRA funds up to $100,000 annually by those age 70½ expired at the end of 2009; it has been extended through 2011.

Because the extension was enacted so late in 2010, the law allowed transfers made through January 31, 2011, to be treated as having been made on December 31, 2010. This extension was helpful to taxpayers who failed to take their required minimum distributions for 2010 before the end of 2010 because the direct transfer to charity avoided the 50% penalty that would have applied to the failure to take the distribution. However, those who took distributions before the extension of the charitable transfer opportunity were not given a do-over; funds could not be recontributed to their IRAs and then transferred to charity.

**Real estate donated for conservation purposes.** The favorable percentage limitations on donations of realty for conservation purposes, which had expired at the end of 2009, have been extended through 2011. This means the limit on donations of qualified property for conservation purposes is 50% of the contribution base (100% for farmers and ranchers).

**Alternative minimum tax.** The alternative minimum tax (AMT) exemption amounts have again been “patched” for 2010:

- $72,450 for married filing jointly
- $47,450 for single taxpayers and heads of households
- $36,225 for married filing separately

For 2011, the “patch” in the exemption amounts:

- $74,450 for married filing jointly
- $48,450 for single taxpayers and heads of households
- $37,225 for married filing separately

**Tax credit offsets to the AMT.** Nonrefundable personal tax credits, such as the lifetime learning credit and the dependent care credit, can be used to offset not only regular income tax, but also the alternative minimum tax through 2011. After 2011, the only nonrefundable personal credits that can offset AMT will be the adoption credit, the child tax credit, and the retirement saver’s credit unless Congress continues the current rule.

**Chapter 7—Tax-Saving Changes for the Self-Employed**

**Bonus depreciation.** After September 8, 2010, and before January 1, 2012, eligible property can qualify for 100% bonus depreciation; 50% bonus depreciation applies to eligible property placed in service after December 31, 2009, and before September 9, 2010.

**Correction on page 130.** Bonus depreciation applies to qualified leasehold improvements; it does not apply to restaurant or retail improvements.

**Business travel per diem rates.** The maximum federal per diem rate for travel from October 1, 2010, through September 30, 2011, covering lodging and meals and incidental expenses (M&IE) within the continental United States (CONUS) in most locations is
$123 per day ($77 for lodging and $46 for M&IE)—up from $116 ($70 for lodging and $46 for M&IE) that had applied to the prior 12-month period. A number of the rates to certain areas have changed. These rates can be found at www.gsa.gov (click on “Per Diem Rates”).

The high-low substantiate rates for high-cost and all other areas within CONUS for the period October 1, 2010, through September 30, 2011, is $233 for travel to high-cost localities and $160 for travel to all other areas with CONUS. Of these rates, the meal portion is $65 for high-cost areas and $52 for all other areas within CONUS. These rates are slightly lower than the rates for the prior 12-month period.

**Employment-related tax credits.** The Work Opportunity credit has been extended through 2011. The Empowerment Zone employment credit, Indian employment credit, and the wage differential payment credit, all of which expired at the end of 2009, have also been extended through 2011. The community renewal employment tax credit, which expired at the end of 2009, has not been extended.

**Research credit.** The 20% credit, which had expired at the end of 2009, has been extended through 2011.

**Health insurance premiums by self-employed individuals.** In 2010 these premiums are subtracted from net earnings from self-employment in order to figure self-employment tax. In effect, there is no self-employment tax on these premiums. This rule is set to run only for 2010. For income tax purposes, the premiums continue to be deductible from gross income; no itemizing of personal medical expenses is required.

**W-2 forms.** The IRS has ruled that reporting the value of health coverage on W-2 forms for employees in 2011 is voluntary; it will be mandatory in 2012.

**General business credit carryback.** The carryback for the general business credit usually is one year. However, for credits of small businesses arising in 2010, the carryback period is 5 years. The carrybacks can offset both regular tax and the alternative minimum tax.

A “small business” for this purpose is a privately held corporation, partnership, or sole proprietorship with average gross receipts in the 3 prior years not exceeding $50 million.

**Note:** For partnerships and S corporations, the gross receipts test must be met at both the entity and owner levels.

**Chapter 8—Estate, Gift, and Generation-Skipping Transfer Taxes**

There have been dramatic changes to estate, gift, and generation-skipping transfer taxes starting in 2010. Here are the key points to note:

**Exemption amounts.** For 2010, the gift tax exemption is $1 million per person, while the exemption for estate and generation-skipping transfer taxes is $5 million per person.

For 2011 and 2012, the exemption amount for married couples is “portable.” This means that if one spouse dies without using the full exemption amount, the surviving spouse gets to use it. Say a husband with an estate of $3 million dies in 2011, leaving all of his
property to his children from a former marriage. His surviving spouse now has an exemption amount of $8 million (her $5 million, plus the unused $2 million from the husband).

**Tax rates.** The maximum tax rate on transfers is 35%. There is no tax on generation-skipping transfers made in 2010.

**Basis for heirs.** Assets inherited from a person dying in 2010, 2011, or 2012 is stepped up to the value for estate tax purposes (i.e., the value on the date of death). No one will ever pay tax on the appreciation in assets up until the time of death.

**Special rule for people who died in 2010.** Because of the late enactment of these new estate tax rules, estates of those who died in 2010 can make a special election to use the rules that had been scheduled to apply in 2010, rather than the rules outlined above. The old rules were:

- No estate tax, regardless of the size of the estate

A modified carryover basis rule for heirs. Basis can only be stepped up to the value at the time of death up to $3 million for assets passing to a surviving spouse, plus $1.3 million of assets passing to anyone. The IRS has released a draft of Form 8939 to be used in making the allocation of basis under the modified carryover basis rule.