
CCH Reviews Tax Proposals in Obama Budget

By Editor Test *Wed, Feb 10, 2010*

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President Obama's proposed budget has tax proposals for 2011 that reflect a heightened concern with job creation and the rising deficit. CCH issued a Special Tax Briefing on the measures. The administration wants to:

Reinstate former top marginal rates

The president proposes reinstating the top marginal income tax rates of 36% and 39.6% rates for single individuals with incomes over \$200,000 and married couples filing jointly with incomes over \$250,000.

The \$200,000 amount would be reduced for the standard deduction and one personal exemption and indexed for inflation for 2011. The \$250,000 amount would be reduced for the standard deduction and two personal exemptions and indexed for inflation for 2011.

The 39.6% rate would start at the inflation-adjusted level now in place for the 35% rate, which for 2010 is \$373,650. The president would also make permanent the 10%, 15%, 25% and 28% percent tax brackets, which are due to expire after 2010.

Levy 15 bps fee on big banks' "covered liabilities"

The president's 2011 budget also includes his "financial crisis responsibility fee," a tax on the liabilities of financial institutions with at least \$50 billion in consolidated assets. The rate of the fee applied to covered liabilities would be approximately 15 basis points. The fee would be effective as of July 1, 2010.

"This is one of the more controversial elements in the budget," Luscombe noted.

Restore 20% capital gains tax

Those in the top two brackets would also see an increase in their capital gains rates, to 20% from the current 15% after 2010. However, rather than taxing qualified dividends as ordinary income beginning in 2011, as under current law, Obama would retain their treatment as capital gains.

"Upper-income taxpayers would actually fare somewhat better under Obama's proposals than they would under current law, which would repeal almost all the Bush-era tax cuts as of 2011," said CCH Principal Federal Tax Analyst Mark Luscombe, JD, LLM, CPA.

"Retaining the 10% and 25% brackets benefits them as well as other taxpayers, as does retaining of the treatment of dividends as capital gains. However, they would not fare as well as they have in the past."

Reinstate estate tax

While the federal estate tax has officially expired for 2010 and is officially set to return in 2011 at pre-2001 levels, the president's FY 2011 baseline budget assumes a retroactive reinstatement of the estate tax to January 1, 2010, at 2009 levels.

That's the thrust of the Permanent Estate Tax Relief for Families, Farmers, and Small Businesses Bill of 2009 (H.R. 4154) to permanently extend the estate tax at 2009 exemption rates, passed by the House last year. The bill would impose a 45% tax on estates above \$3.5 million per individual and \$7 million for married couples. The bill is now in the Senate where, at press time, no action has yet been taken.

Establish "Saver's Credit"

Establish the planned "Saver's Credit" but change the credit to a 50% match on contributions up to \$500 (\$1,000 for joint filers). The matched would phase out at a rate of 5% of adjusted gross income (AGI) in excess of \$32,500 (\$65,000 for married couples filing jointly). The \$500 amount and the AGI amounts would be indexed annually for inflation for tax years beginning with the 2012 tax year.

Require small businesses that employ 10 or more people and that don't offer a retirement plan to enroll their employees in an IRA to be funded by a payroll deduction, although the employees could opt out.

Reintroduce "Pease" limitation

This year also sees a repeat of the proposal to reintroduce the limitation on itemized deductions, known as the "Pease" limitation, and the personal exemption phase-out, known as PEP, for those above the \$200,000/\$250,000 income thresholds.

Whenever itemized deductions would reduce taxable income in the revived 36% and 39.6% brackets, the tax value of those deductions would be limited to 28%. The proposal would apply to itemized deductions after they have been reduced by the reinstated Pease limitation.

Continue AMT "Patch"

The 2011 fiscal year budget assumes that Congress will continue to "patch" the alternative minimum tax (AMT) as it did for 2009 and then index it for inflation—or continue one-year "patches" in the future.

Miscellaneous items

As in last year's budget, the administration is also proposing changes to rules regarding valuation, basis and grantor retained annuity trusts to correct what are seen as abusive practices.

A major initiative for businesses in the budget is \$33 billion in small business jobs and wages tax credits. The measure would provide a \$5,000 tax credit for every net new employee hired by a qualified small business in 2010, capped at \$500,000 for any one firm.

The proposal would also reimburse small businesses that increase wages or hours for existing employees for the Social Security payroll taxes they pay on real increases in their payrolls, up to the current Social Security maximum wage base of \$106,800.

Another new item is a proposal to remove cell phones from their current classification as “listed property.” This would lift the strict substantiation requirements for business use and make depreciation of cell phones easier. In addition, an employee could exclude the fair market value of personal use of a cell phone provided predominantly for business purposes from gross income.

“The current rules date back to when a cell phone was an expensive novelty,” Luscombe said.

As in the 2010 budget, the administration again proposes to raise the exclusion currently available on gain realized on qualified small business stock from 75% to 100%. The exclusion is intended to help small businesses raise capital. The administration would eliminate as an AMT preference item the excluded portion of the gain, as well.

“This would be an attractive investment for someone who otherwise might be facing a 20-percent capital gains tax in the future,” Luscombe noted.

The administration also proposes extending the Section 179 expensing and bonus depreciation provisions for 2009 through 2010.

The budget reiterates a number of revenue raisers from last year, including a repeal of the LIFO inventory method, taxation of carried interest as ordinary income and a package of international taxation “reforms.” The president also proposes to revive Superfund taxes for 10 years commencing with tax years beginning after December 31, 2010.

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