

Overview of tax changes in the 2004 Working Families Act

Congress recently passed the 2004 Working Families Act, which provides a package of tax cuts for middle income families and extends more than 20 expired business-related tax provisions. Here's what you need to know right now about this important new legislation:

Family tax relief.

Child credit.

The child credit, which is \$1,000 per child for 2004 but was scheduled to drop to \$700 for 2005 through 2008 and to rise to \$800 for 2009, will stay at \$1,000 through 2010. Also, the 15% refundability percentage of the child credit is accelerated so that it applies for tax years beginning after 2003 (instead of after 2004).

Marriage penalty relief.

Two provisions that provide a measure of relief from the marriage penalty are extended by the Act. The provision setting the basic standard deduction for joint filers at twice that of single taxpayers, and the provision that increases the size of the 15-percent rate bracket for married couples filing joint returns, both of which were due to expire at the end of 2004, are extended through 2010.

10-percent bracket.

The scheduled reduction in the amount of income subject to the 10% tax bracket is repealed, effective through 2010.

Extension of relief from the alternative minimum tax (AMT).

Higher exemption amount extended.

In recent years, Congress has provided a measure of relief from the AMT by raising the AMT "exemption amounts," thereby reducing the likelihood of an AMT liability. However, this partial relief was set to expire for tax years beginning after 2004, and the exemption amounts were scheduled to revert to the lower amounts allowed under prior law. The Act preserves this partial relief from the AMT by extending the higher exemption amounts to 2005. Also, the availability of nonrefundable personal credits to offset AMT has been extended through 2005 (instead of expiring after 2003 tax years).

Uniform definition of child.

In a major tax simplification measure, the Act replaces a series of different eligibility tests for child-related benefits with a uniform definition of a child. For tax years beginning after 2004, the Act establishes a uniform definition of a qualifying child for purposes of the dependency exemption, the child credit, the earned income credit, the dependent care credit, and head of household filing status. Under the uniform definition, in general, a child is a qualifying child of a taxpayer if the child (1) has the same principal place of abode as the taxpayer for more than one half the taxable year; (2) has a

specified relationship to the taxpayer; (3) has not yet attained a specified age; and (4) meets a support test.

Assistance to military families in combat zones.

The Act provides assistance to low-income military families in combat zones by (1) increasing the child credit for families by allowing them to include tax-free combat pay when calculating their refundable child credit; and (2) increasing the earned income credit (EIC) for military families in 2004 and 2005 by giving them the option to include combat pay when calculating the EIC. These provisions are expected to provide an additional \$199 million of assistance to military families in combat zones.

Extension of business-related tax relief.

The Act extends the life of more than 20 expired or expiring business-related tax provisions. The tax provisions that get a new lease on life include:

- The research credit, extended for amounts paid or incurred after June 30, 2004 and before 2006.
- The work opportunity tax credit and the welfare-to-work credit, extended for wages paid or incurred for individuals beginning work after 2003 and before 2006.
- The enhanced deduction for a corporation's qualified computer contributions, extended for contributions made in tax years beginning after 2003 and before 2006.
- The above-the-line deduction for certain expenses of eligible educators, extended to tax years beginning in 2004 and 2005.
- Expensing of environmental remediation costs, extended for expenses paid or incurred after 2003 and before 2006.
- The credit for producing electricity from certain renewable resources, extended to facilities placed in service after 2003 and before 2006.
- The suspension of the net-income limitation on percentage depletion for marginal wells, effective for tax years beginning after 2003 and before 2006.
- The full credit for qualified electric vehicles and the full deduction for qualified clean fuel vehicle property are allowed for vehicles placed in service before 2006, repealing the phase-downs of the credit and deduction scheduled for 2004-2005.
- Archer medical savings accounts-new contributions to these accounts OK for 2004 and 2005.
- The Indian employment tax credit, extended through 2005.
- District of Columbia Enterprise Zone designation and related tax incentives, extended through 2005.
- First-time D.C. homebuyer credit, extended to property purchased on or before Dec. 31, 2005.

Give us a call at your earliest convenience for more details on how you may be affected by this important tax legislation.