

## The Cost-of-Living Dollar Limits

### for 2001 Tax Year

401(k) deferral limit \$10,500

Annual compensation limit \$170,000

Defined contribution IRC Sec 415 limit \$35,000

Compensation limit for SEP eligibility \$450

Deferral limit for SIMPLE \$6,500

IRC Section 179 \$24,000

Unified Credit Exclusion \$675,000

Self-employed health insurance AGI deduction 60%

Business mileage rate \$0.345/mile

Medical mileage rate \$0.12/mile

Charitable mileage rate \$0.14/mile

Automobile depreciation limit: first year \$3,060\*

Second year \$4,900\*

Third year \$2,950\*

Each succeeding year \$1,775\*

(\*Unchanged from 2000)

## JENNIFER A. JONES, CPA, LTD.

### Tips, Tricks & Tools

Volume 2, Issue 3

A Quarterly Newsletter

July 2001

### New Tax Law Enacted

The recently enacted Economic Growth & Tax Relief Reconciliation Act of 2001 promises to deliver tax savings to nearly every American. The \$1.35 trillion federal tax cut, which is to be phased in over the next decade, includes tax-rate reductions, child credit increases, marriage penalty relief, education incentives, estate tax repeal, retirement plan provisions, alternative minimum tax relief, and other changes.

Although the list of changes is too extensive for this newsletter and space does not permit full discussion of their implications, we will add a comprehensive discussion to our website soon. We will also have booklets available soon that will provide an overview of the tax law changes. What follows are highlights, as space permits.

### Individual Rate Reductions

**Tax Rate Changes.** Until this new law, we had five regular tax rates: 15%, 28%, 31%, 36%, and 39.6%. The new law introduces a new 10% tax rate for the years 2002 and after. Rather than incorporating the 10% rate into the 2001 tax rate schedules, the US Treasury has been directed to mail a "rebate" check to most individual taxpayers who filed a return for 2000, providing an immediate tax benefit. The "rebate" amounts will be up to \$600 for joint filers, up to \$500 for head of household filers, and up to \$300 for single and married filing separately filers

The remaining tax rates will also be reduced, starting July 1, 2001. By 2006, when the reduction is completely phased in, the previous rates (listed above) will be reduced to 15%, 25%, 28%, 33%, and 35%, respectively.

Starting in 2005, the 15% bracket is expanded for joint filers to relieve some of the marriage penalty.

**Itemized Deduction Reduction and Personal Exemption Phaseout Repealed.** Higher income taxpayers have had to reduce their deductions for the itemized deductions and personal exemptions if their adjusted gross income exceeded certain thresholds. The new law gradually repeals the itemized deductions reduction and personal exemption phaseout. Effective after 2009, these current provisions are completely repealed.

### Social Security

Wage Base for 2001 \$80,400

Retirees under 65 may earn up to \$10,680 (\$890 a month). For each \$2 earned over the amount for the year, the retiree loses \$1 in benefits. Retirees turning 65 in 2001 can earn up to \$25,000 a year without losing benefits, counting only earnings before the month they turn 65. For each \$3 earned over this limit, the retiree loses \$1 in benefits. No limit if 65 or over, effective January 1, 2000.

As you work and pay Social Security taxes, you earn "Credits", up to a maximum of 4 for each year. The amount of earnings it takes to earn a credit changes each year. In 2001, you earn one credit for each \$830 of your earnings. So if you have earned at least \$3,320 during the year, you get the maximum 4 credits.

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### Child-Related Provisions

**Child Tax Credit.** Currently, eligible taxpayers may claim a \$500 tax credit for each qualifying dependent under age 17. Under the new law, the child tax credit is increased to \$1,000, phased in over 10 years, starting in 2001. For 2001-2004 the credit per child is \$600. The new law also has a provision that makes the child tax credit refundable to the extent of 10% of the taxpayer's earned income in excess of \$10,000.

**Dependent Care Credit.** Effective for years starting after 2002, the maximum credit percentage increases to 35% and the maximum amount of eligible expenses rises to \$3,000 for one and \$6,000 for two or more qualifying dependents.

## DEADLINES

### July

15

Monthly-filers Form 941 federal tax deposit due

DC sales tax return and payment due, quarterly and monthly filers

Maryland income tax withheld return and payment due, monthly filers

20

Virginia and Maryland sales tax return and payment due, quarterly and monthly filers

DC income tax withheld return and payment due, quarterly and monthly filers

31

Form 941 due

Virginia income tax withheld return and payment due, quarterly and monthly filers

Maryland income tax withheld return and payment due, quarterly and monthly filers

State unemployment tax returns and payment due

DC Personal Property Tax Return and payment due

Form 940 federal tax deposit due

Form 5500 Annual Return/Report of Employee Benefit Plan due

### August

15

Monthly-filers Form 941 federal tax deposit due

DC sales tax return and payment due, monthly filers

Maryland income tax withheld return and payment due, monthly filers

Federal, DC and Maryland Individual Income Tax Returns due, if Form 4868 or first extension request was filed

20

Virginia income tax withheld return and payment due, monthly filers

DC income tax withheld payment return and payment due, monthly filers

Virginia and Maryland sales tax return and payment due, monthly filers

### September

1

Virginia Individual Income Tax return due, if Form 760-E was filed

15

Monthly-filers Form 941 federal tax deposit due

DC sales tax return and payment due, monthly filers

Form 1040-ES voucher #3 with payment due DC, Virginia and Maryland individual estimated tax payment #3 due

Maryland income tax withheld return and payment due, monthly filers

20

Virginia income tax withheld return and payment due, monthly filers

DC income tax withheld payment return and payment due, monthly filers

Virginia and Maryland sales tax return and payment due, monthly filers

## Education Provisions

**Education IRAs.** Starting after 2001, the annual limit on contributions to an Education IRA is increased to \$2,000 per designated beneficiary; the contribution phaseout range for joint filers is increased to twice the range for single filers; the definition of qualified education expenses is expanded; the age 18 and age 30 limitations are eliminated for "special needs" beneficiaries; among other provisions.

**Section 529 Plans.** Starting after 2001, educational institutions are allowed to sponsor plans; the definition of "member of the family" is expanded; and tax-free transfers from one qualified plan to another are permitted. Starting in 2002 for state programs, and in 2004 for other qualified tuition programs, distributions or education benefits received are excludable from income.

**Student Loan Interest.** After 2001, the 60-month limit is repealed and the income phaseout ranges increase.

**Deduction for Higher Education Expenses.** For 2002-2005, a deduction for qualified higher education expenses may be claimed whether or not the taxpayer itemizes deductions. This deduction may not be claimed in a year in which a HOPE or Lifetime Learning Credit has been claimed for the same student. For 2002-2003 the maximum deduction is \$3,000 for taxpayers with AGI not exceeding \$65,000 (\$130,000 for joint filers).

## Retirement Provisions

**IRAs.** The new law increases the maximum IRA contribution: \$3,000 for 2002-2004; \$4,000 for 2005-2007, and \$5,000 (adjusted for inflation) for 2008 and after. These annual limits are increased by \$500 for 2002-2005 and \$1,000 for 2006 and after, for individuals who have reached the age of 50 by the end of the tax year and who meet the AGI limits.

**401(k) Limits Increased.** The amount that may be contributed to a 401(k), 403(b), SAR-SEPs, SIMPLE, and 457 plans have been increased. Beginning in 2002, these annual limits are increased even further for individuals who have reached the age of 50 by the end of the tax year.

**Employer Provisions.** The limit on annual additions will increase from \$35,000 to \$40,000 for years after 2001. The maximum salary taken into account will increase from \$170,000 to \$200,000 for 2002 and after. After 2001, the 401(k) elective deferrals will not be considered employer contributions subject to the 15% deduction limit and the limit on employer contributions to a profit sharing plan will be increased from 15% to 25%. Faster vesting schedules will take effect for 401(k) matching contributions.

## Estate and Gift Taxes

Starting in 2002, the top estate and gift tax rates will be reduced, and the unified credit effective exemption amount will increase in steps. In 2010, the estate and generation-skipping transfer taxes are repealed. The top gift tax rate will be equal to the highest individual income tax rate, scheduled to be 35%.

Starting in 2010, the old stepped-up basis rule for transfers at death is replaced with a modified carryover basis rule. In general, the basis of property received from a decedent will be the *lesser* of the decedent's adjusted basis or the fair market value on the date of death. There is a provision that permits an estate to step up the basis of assets acquired at a decedent's death within limits: an estate will be permitted to increase the basis of assets transferred up to a total of \$1.3 million, plus another \$3 million for property transferred to a surviving spouse.

Your will and estate plan should be reviewed by your estate attorney.