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ECONOMIC GROWTH AND TAX RELIEF RECONCILIATION ACT OF 2001, H.R. 1836: SUMMARY OF SELECTED PROVISIONS–PART II
— by Roger A. McEowen* and Neil E. Harl**

Individual income tax rates

The act provides a new ten percent regular income tax bracket applicable to the first $6,000 of taxable income for single persons, $10,000 of taxable income for heads of households and $12,000 for married couples filing joint returns. The provision is made applicable for taxable years beginning after December 31, 2000. The $6,000 and $12,000 amounts increase to $7,000 and $14,000 respectively for 2008 and thereafter. The taxable income levels for the new low-rate bracket will be adjusted annually for inflation for taxable years beginning after 2008, and the bracket for single persons and married persons filing separately will be 50 percent of that of joint returns. Act. Sec. 101, amending I.R.C. § 1.

The Act adds a new provision creating a rate reduction credit for 2001 and which operates in lieu of the new 10 percent bracket for 2001. Taxpayers will be entitled to a credit in tax year 2001 of five percent of the amount of the income that would have been eligible for the new 10 percent rate. The Treasury is instructed to issue checks by October 1, 2001, to taxpayers who timely filed their 2000 returns. Act. Sec 101, adding I.R.C. § 6428.

The Act specifies that the 15 percent bracket is modified to begin at the end of the new 10 percent income tax bracket and ends at the same level as under present law. The present law regular income tax rates are reduced after June 30, 2001 as follows: the 28 percent rate is reduced to 27.5 percent in years 2001, to 27 percent in 2002 and 2003, to 26 percent in years 2004 and 2005, and 25 percent in 2006 and later. The 31 percent rate is reduced to 30.5 percent in 2001, to 30 percent in 2002 and 2003, 29 percent in 2004 and 2005, and 28 percent in 2006 and later. The 36 percent rate is reduced to 35.5 percent in year 2001, and 35 percent in 2002 and 2003, 34 percent in years 2004 and 2005 and 33 percent for year 2006 and later. The 39.6 percent rate is reduced to 39.1 percent in 2001, 38.6 percent in 2002 and 2003, 37.6 percent for 2004 and 2005, and 35 percent in 2006 and later. Act Sec. 101(a)(i)(2), amending I.R.C. § 1.

Phaseout of personal exemptions

The Act provides for a five-year phase-in of the repeal of the personal exemption

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phaseout, whereby the otherwise personal exemption phaseout is reduced by one-third in taxable years beginning in 2006 and 2007, and is reduced by two-thirds in taxable years beginning in 2008 and 2009. The repeal is fully effective for taxable years beginning after December 31, 2009. The effective date of the phaseout, whereby the otherwise personal exemption phaseout is referred to as Act Sec. 102, amending I.R.C. § 151(d).

**Phaseout of overall limitation on itemized deductions**

A phased-in repeal of the overall limitations on itemized deductions for all taxpayers is provided as follows: the applicable limitation on itemized deductions is reduced by one-third in taxable years beginning in 2006 and 2007, and by two-thirds in taxable years beginning in 2008 and 2009. For taxable years beginning after December 31, 2009, the overall limitation is repealed. The provision is effective for tax years beginning after December 31, 2005. Act Sec. 103, amending I.R.C. § 68.

**Child tax credit**

The Act increases the child tax credit to $1,000, effective for taxable years beginning after December 31, 2000. The increase is phased in as follows: $600 for calendar years 2001-2004; $700 for calendar years 2005-2008; $800 for 2009; and $1,000 for 2010 and later. The credit is refundable to the extent of ten percent of the taxpayer’s earned income in excess of $10,000 for calendar years 2001-2004 and the percentage is increased to 15 percent for calendar years 2005 and thereafter. The $10,000 amount is indexed for inflation starting in 2002. Families with three or more children are allowed a refundable credit for the amount by which the taxpayer’s social security taxes exceed the earned income credit, if that amount is greater than the refundable credit based on the taxpayer’s earned income in excess of $10,000. The refundable portion of the credit does not constitute income and will not be treated as resources for purposes of determining eligibility or the amount or nature of benefits or assistance under any federal program or state or local program financed with federal funds. Act Sec. 201, amending I.R.C. § 24(a).

**Adoption credit**

The Act provides a credit against tax of $10,000 or a gross income exclusion of $10,000 for employer-provided adoption assistance. For the adoption of special needs children, the Act provides a credit against tax for qualified adoption expenses limited by an aggregate amount of $10,000 in qualified adoption expenses. The Act also provides for a gross income exclusion up to $10,000 for employer-provided adoption assistance. The Act increases the income limitation at which phase-out begins to $150,000 (from $75,000), and makes permanent the use of the credit against alternative minimum tax. Act Sec. 202, amending I.R.C. § 23(a)(1).

**Dependent care credit**

The applicable dollar limit for dependent care credits is increased to $3,000 (for one qualifying person) and $6,000 (for two qualifying persons). The Act increases the applicable percentage to 35 percent (from 30 percent), but reduces the rate (but not below 20 percent) by one percentage point for each $2,000 (or fraction thereof) by which the taxpayer’s adjusted gross income for the taxable year exceeds $15,000 (from $10,000). The provision applies to taxable years beginning after December 31, 2002. Act Sec. 204, amending I.R.C. § 21.

**Employer expenses for child care assistance**

A tax credit for employer-provided child care is provided equal to 25 percent of the qualified expenses for employee child care and 10 percent of the qualified expenses for child care resource and referral services, up to a limit of $150,000 per taxable year. The Act provides that such credits are subject to recapture for the first 10 years after the qualified child care facility is placed in service, reduced as a percentage of the credit over the 10-year period, if the taxpayer ceases operation of the facility as a qualified child care facility or disposes of its interest in the facility and the person acquiring the interest in the facility does not agree in writing to assume the taxpayer’s recapture liability. The provision is effective for taxable years beginning after December 31, 2001. Act Sec. 205, amending I.R.C. §§ 38, 1016 and adding I.R.C. § 45F.

**“Marriage penalty”**

The size of the 15 percent bracket for a married couple filing jointly is increased to twice the size of the corresponding rate bracket for taxpayers filing as a single person by 2008. The increase is phased over four years beginning in 2005. The Act specifies that the end point of the 15 percent bracket for a married person filing a separate return will be one-half of the end point of the 15 percent bracket for a married couple filing a joint return. The provision is effective for tax years beginning after 2004. Act Sec. 302, amending I.R.C. § 1(f).

**Earned income credit**

Beginning in 2002, the amount of reduction of the earned income credit by the amount of the alternative minimum tax is repealed. The earned income amount used to calculate the EIC for married taxpayers filing jointly is increased to 110 percent of the amount for all other taxpayers eligible for the EIC. The definition of earned income for EIC purposes is amended to exclude nontaxable earned income amounts. The beginning and ending amounts of the EIC phase-out range for married taxpayers filing jointly is increased by $1,000 in taxable years beginning in 2002-2004, by $2,000 in taxable years beginning in 2005-2007, and by $3,000 in taxable years beginning in 2008. The $3,000 amount will be adjusted for inflation annually beginning in 2009. The definition of “qualifying child” for EIC purposes is expanded, and the calculation of the EIC is changed by replacing “modified adjusted gross income” with “adjusted gross income.” Act Sec. 303, amending I.R.C. § 32.

**Education IRAs**

The annual limit on contributions to an education IRA is increased from $500 to $2,000. The definition of qualified education expenses that may be paid tax-free from an education IRA is expanded. The phase-out range for marrieds filing jointly is increased so that it is twice the range for single taxpayers, resulting in a phase-out range of $190,000 to $220,000 of modified adjusted gross income. The Act specifies that various age limitations do not apply to special needs beneficiaries, and clarifies that corporations and other entities are permitted to make contributions to education IRAs, regardless of the income of the corporation or entity during the year of the contribution. Taxpayers are allowed to claim a HOPE Credit or Lifetime Learning Credit for a tax year and to exclude from gross income amounts distributed (both the contributions and earnings portions) from an education IRA on behalf of the same student as long as the distribution is not used for the same educational expenses for which a credit was claimed. Repealed is the excise tax on contributions made by any person to an education IRA on behalf of a beneficiary during any taxable year in which any contributions are made by anyone to a qualified state tuition...

Qualified tuition programs

The Act expands the definition of “qualified tuition program” to include certain prepaid tuition programs established and maintained by one or more eligible educational institutions that satisfy the requirements of I.R.C. § 529. Distributions made in taxable years from qualified state tuition programs are excluded from gross income to the extent the distribution is used to pay for qualified higher education expenses. A taxpayer can claim a HOPE Credit or Lifetime Learning Credit for a tax year and can exclude from gross income amounts distributed from a qualified tuition program on behalf of the same student as long as the distribution is not used for the same expenses for which a credit was claimed. Eliminated is the penalty on distributions not used for higher education expenses. That provision is replaced with the same additional tax that applies to educational IRAs. Assets of qualified tuition plans of private institutions must be held in trust. The provision is effective for taxable years beginning after December 31, 2001, except that the exclusion from gross income for certain distributions from a qualified tuition program established and maintained by an entity other than a state is effective for tax years beginning after December 31, 2003. Act. Sec. 402, amending I.R.C. § 529.

Student loan interest deduction

The phase-out ranges for eligibility for the student loan interest deduction are increased to $50,000-$65,000 for singles, and to $100,000-$130,000 for married taxpayers filing jointly. The phase-out ranges are adjusted annually for inflation after 2002. The Act also repeals both the limit on the number of months during which interest paid on a qualified education loan is deductible and the restriction that voluntary payments of interest are not deductible. The provision is effective for interest paid on qualified education loans after December 31, 2001. Act Sec. 412, amending I.R.C. § 221.

Deduction for higher education expenses

Taxpayers are permitted an above-the-line deduction for qualified higher education expenses paid by the taxpayer during tax years from 2002-2005. Qualified education expenses are defined in the same manner as for the HOPE credit. For years 2002 and 2003, a taxpayer with an AGI of not more than $65,000 ($130,000 for marrieds filing jointly) is entitled to a maximum annual deduction of $3,000. In 2004 and 2005, the maximum deduction rises to $4,000. Taxpayers with higher incomes that do not exceed $80,000 ($160,000 for marrieds filing jointly) may deduct a maximum of $2,000 per year. Taxpayers with incomes exceeding the limits receive no deduction and the deduction expires for tax years beginning after December 31, 2005. The deduction and the HOPE or Lifetime Learning Credit may not be taken in the same year for the same student. Likewise, a taxpayer may not claim a deduction for amounts taken into account in determining the amount excludable due to a distribution from an education IRA or the amount of interest excludable for education savings bonds. The provision is effective for education payments made in tax years beginning after December 31, 2001 and before January 1, 2006. Act Sec. 431, redesignating I.R.C. § 222 as § 223 and inserting a new § 222.

Modifications of IRA contribution limits

The maximum annual dollar contribution limit for IRA contributions is increased to $3,000 for 2002 through 2004, $4,000 for years 2005 through 2007, and $5,000 for 2008. For years beginning after 2008, the limit is adjusted annually for inflation in $500 increments. The otherwise maximum contribution limit (before application of the AGI phase-out limits) for an individual who had attained age 50 before the end of the taxable year is increased by $500 for 2002 through 2005, and is increased by $1,000 for 2006 and thereafter. The provision is effective for taxable years beginning after December 31, 2001. Act Sec. 601, amending I.R.C. §§ 219(b) and 408.

Defined benefit plans

The Act increases the $35,000 limit on annual additions to a defined contribution plan to $40,000 and indexes it in $1,000 increments. The $140,000 annual benefit limit under a defined benefit plan is increased to $160,000, and the dollar limit is reduced for benefit commencement before age 62 and increased for benefit commencement after age 65. The Treasury Secretary is to apply rules similar to those adopted in Notice 99-44 regarding benefit increases due to the repeal of the combined plan limit under former I.R.C. § 415(e), according to the Statement of Managers for Conference Agreement on H.R. 1836. The Act also increases the dollar limit on annual elective deferrals under I.R.C. § 401(k) plans. I.R.C. § 403(b) annuities and salary reduction SEPs to $11,000 in 2002. In 2003 and thereafter, the Act increases the limits in $1,000 annual increments until the limits reach $15,000 in 2006, with indexing in $500 increments thereafter. Also increased is the maximum annual elective deferrals that may be made to a SIMPLE plan to $7,000 in 2002, $8,000 in 2003, $9,000 in 2004, and $10,000 in 2005. The limit is indexed thereafter in $500 increments. The limit is twice the otherwise applicable dollar limit in the three years before retirement. The provisions are effective for years beginning after December 31, 2001. Act Sec. § 611, amending I.R.C. §§ 402, 408, 415 and 457.

Sunset of provisions

All provisions of the Act are repealed and have no application to taxable, plan or limitation years beginning after December 31, 2010. Act Sec. § 901.

CORRECTION

On P. 83 of the last issue of the Digest, the following paragraphs should read (change in italics):

“Sunset provision

The 2001 Act, specifies that “all provisions of, and amendments made by the Act shall not apply . . . to estates of decedents dying, gifts made or generation-skipping transfers after December 31, 2010.” Act Sec. 901.

Therefore, unless amended further, the estate, gift and generation skipping transfer tax provisions will (1) be repealed after 2009 and (2) one year later revert to the status of the provisions as of the date of enactment.”