



WHY THE TAX INCREASE PREVENTION AND RECONCILIATION ACT IS GOOD NEWS FOR INVESTORS

By Charles Falk, Esq.

The Tax Increase Prevention and Reconciliation Act (“TIPRA”) was signed last week by President Bush. It has several important provisions for investors:

- **Extension of Dividend and Capital Gain Rate Cuts:** The tax centerpiece of President Bush’s administration was the reduction to 15% in 2003 as the highest rate on dividends and long-term capital gains. It has also been the most controversial. Assailed by critics as a “welfare plan for the rich,” its supporters have equally argued that it has provided a strong stimulus for the economy. The 15% rate was scheduled to expire at the end of 2008, but the TIPRA extends the rate cut to the end of 2010.
- **Alternative Minimum Tax Relief:** The Alternative Minimum Tax (“AMT”) is the genie that won’t go back into the bottle. First enacted in 1969 and modified in 1986 with a different name, the AMT has been described as “one of the major nightmares of taxpayer burden in the Code.” Long ignored by most taxpayers because the AMT did not affect them, the AMT now is a multi-headed dragon that affects many taxpayers. Further, it is a stealth tax because it is difficult to anticipate until it is too late. It is especially hard for employees with employee business expenses and taxpayers living in high tax states (i.e. New Jersey and New York). The TIPRA extends the current temporary exemption amount through 2007 to \$62,550 for taxpayers filing joint returns and \$42,500 for single taxpayers. Without this extension, it is estimated that an additional 15 million taxpayers would have felt the sting of the AMT.
- **Changes to Roth IRAs:** TIPRA eliminates the ceiling of \$100,000 of adjusted gross income for converting a traditional IRA to a Roth IRA for tax years after 2009. The conversion, however, is treated as a taxable distribution but is not subject to the 10% early withdrawal penalty. Also, taxpayers who convert in 2010 can elect to recognize the income in 2010 or average it over the next two years. In a traditional IRA, taxpayers recognize the untaxed portion as they take it out. In a Roth IRA, no deduction is allowed for the contribution but earnings are not taxed when distributed. Because of this change,

many taxpayers are planning to start non-traditional IRAs between 2006 and 2009 and convert them in 2010. This is a tax break that everyone should look into.

- **Kiddie Tax Changes**: The “kiddie tax” requires a child’s unearned income (such as dividends and interest) in excess of \$1,700 to be taxed at the parent’s rate, which is almost always higher than the child’s rate. TIPRA raised the child’s maximum age for being subject to the “kiddie tax” to less than 18 years of age (from less than 14). Thus, additional taxes will be collected because the group subjected to this rule is now more comprehensive. Ironically, within a week of after enactment of this provision, a bill was introduced in Congress to eliminate this change and return the age to under 14 years.
- **Sale of Musical Works and Copyrights**: The TIPRA allows creators of musical works to treat the sale of such works as capital assets, effective for tax years after 2011. This is an important provision because musical works were specifically excluded from capital asset treatment in the hands of its creator. Thus, the creator could never receive the special long-term capital gains rates on such compositions.
- **More on the Way**: A number of important provisions were not included in the legislation that was signed. These are being bundled up in a new bill that is nearly ready to be proposed—stay tuned!!!

About the Author:

Charles Edward Falk is a Professor of Taxation, Seton Hall University, N.J. He holds the following degrees/designations: LL.M (in taxation), New York University School of Law (1981); LL.M in Corporation Law (bankruptcy and securities laws), New York University School of Law (1991); LL.M in Trade Regulation (intellectual property and antitrust laws), New York University School of Law (1995); J.D., Washington and Lee School of Law (1979); M.S. (in accounting), The University of Virginia (1976); B.A. (in economics), University of Kansas (1970); Member New Jersey and Virginia Bars; Certified Public Accountant New Jersey and Virginia; Author, Tax Planning for the Development and Licensing of Patents and Know How, Tax Management #557, Bureau of National Affairs; Author, Tax Planning for the Development and Licensing of Copyrights, Computer Software, Trademarks and Franchises, Tax Management #558; Board of Advisors, Tax Management and BNA's Bankruptcy Law Reporter.