



# CLIENT TALK

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## 2001 TAX REFORM UPDATE

### TAX "REFORM" IS COMING!

This year's tax law changes are beginning to shape up in Congress. President Bush promised in his campaign to address four major areas of tax reduction:

- Marginal Rate Reduction on Income Taxes
- Marriage Penalty Tax Relief
- Childcare Credit Increase
- Estate Tax Reduction

The proposed \$1.35 trillion dollar tax cut (subject to constant adjustment) can address each of these issues.

### WHAT TAX REDUCTION IS NOT

This is *not true tax reform* which permanently lowers the total taxes collected. The President and Congress are intent upon massively increasing Federal spending by a minimum of 5% in the next fiscal year. The compound effect of spending increases over the next decade guarantees that the total tax revenues demanded by the Federal Government will necessarily increase. The tax revenue must come from somewhere. Therefore, serious long-term reduction of income tax will not occur.

### THIS IS NOT SIMPLIFICATION

The extreme complexity of the Internal Revenue Code, including various incentives and tricks, is maintained and made worse by tax reform. Gimmicks such as the *Alternative Minimum Tax* can nullify any rate reduction for some taxpayers and will continue to trap the unwary.

### MARRIAGE PENALTY RELIEF

The *Marriage Penalty* affects two income couples, particularly if one party could qualify for "Married Filing Separately" status. By getting married, the couple pays

*more* tax than when they were single. In some situations the penalty is as much as \$3500. President Bush and the Republicans want to correct this. Nevertheless, as long as there is a "progressive" rate structure, the marriage penalty can never be fully eliminated.

### ESTATE TAX REPEAL

Estate tax repeal will shoot a giant hole through the Federal budget. Congress has established artificial time limitations for calculating the lost revenue from estate tax repeal. The House uses a five-year period and the Senate uses a ten-year time limitation in determining lost tax revenues. The calculations intentionally ignore the eleventh year when the big reduction from the total elimination of the estate tax begins. Also, the calculations fail to include the lost income tax. Every tax lawyer is busy planning techniques to take advantage of estate tax elimination to lessen the income tax owed by the family.

### BUSINESS TAX INITIATIVES

Pension contribution increases are the focus of the business tax reform. The IRA deduction will eventually increase from \$2,000 to \$5,000. The wage base for determining pensions contributions will also increase for 401K Plans and SEP Plans. This will encourage increased funding of pension and retirement plans.

Other areas currently being addressed are restoring the full meal and entertainment percentage deduction for business, adopting accelerated depreciation or expensing of high-tech equipment and reforming Sub-Chapter S. The Internet taxation moratorium which expires in October, 2001, will most likely be extended for another five years. Capital gain reduction will probably be proposed with an increase in minimum wage rates as a separate bill from the main tax reform package.