



Working Families Tax Relief Act of 2004 (HR 1308)

September 2004

Congress passed HR 1308, Working Families Tax Relief Act of 2004.

HR 1308 extends several provisions that expired at the end of 2003 or were scheduled to expire at the end of 2004. It also contains some new provisions and technical corrections. Here is a summary of the new and extended provisions.

Provisions Retroactive to January 21, 2004

Alternative Minimum Tax (AMT)

Through 2005, the following personal nonrefundable credits will continue to be allowed against AMT as well as regular tax. These credits are:

- Child and Dependent Care Credit
- Credit for the Elderly and Permanently and Totally Disabled
- Mortgage Interest Credit
- Hope and Lifetime Learning Credits

Child Tax Credit

Beginning in 2004, earned income for purposes of the child tax credit includes excludable combat pay.

Earned Income Tax Credit (EITC)

For 2004 and 2005, military personnel who receive excludable combat may elect to include excludable combat as earned income for EITC purposes. Individuals whose EITC would be increased should make the election. We expect guidance regarding how the election is to be made.

Archer Medical Savings Accounts (MSAs)

MSAs may continue to be established through 2005, or until the statutory limit for the number of accounts is met, whichever is earlier. The trustee report required to be made on August 1, 2004, shall be treated as timely if made before the close of the 90-day period beginning on the date of the enactment of this Act.

Educator Expenses

An above-the-line deduction of up to \$250 is allowed for qualifying classroom expenses. Full-time primary and secondary education teachers and certain other school personnel can claim the deduction. Extended through 2005.

Work Opportunity Credit

Up to 40 percent (25 percent in certain circumstances) credit of first-year wages, up to \$6,000 of wages per eligible employee. Up to \$3,000 of qualifying summer employment is eligible for the credit. The New York Liberty Zone Work Opportunity Credit is also extended. These credits were extended through 2005.

Research Credit

The business credit for research expenses is extended through 2005. The credit was scheduled to expire June 30, 2004.

Welfare-To-Work Credit

The welfare-to-work credit allowed to employers who hire qualifying welfare recipients. Employers may claim a 35 percent credit of the first \$10,000 of eligible wages in the first year of employment plus a 50 percent credit for the first \$10,000 of eligible wages in the second year of employment. Extended through 2005.

Percentage Depletion

The temporary suspension of the income limitation for claiming percentage depletion is extended through 2005.

Electric Vehicle Credit

The scheduled phase-out of the credit is postponed until 2006. Under prior law, 75 percent of the credit would have been allowed in 2004 (50 percent in 2005, 25 percent in 2006, and 0 percent thereafter).

Deduction for Clean-Fuel Vehicles

The scheduled phase-out of the deduction is postponed until 2006. Under prior law, 75 percent of the credit would have been allowed in 2004 (50 percent in 2005, 25 percent in 2006, and 0 percent thereafter).

District Of Columbia

- **First-Time Homebuyer Credit.** The D.C. first-time homebuyers credit is the lesser of (1) \$5,000 or (2) the purchase price of the residence. The credit is phased out based on modified adjusted gross income. This credit is extended through 2005.
- **D.C. Enterprise Zone.** D.C. Enterprise Zone benefits are extended including, but not limited to, the D.C. wage credit and the \$20,000 additional section 179 expense allowance.
- **Tax-Exempt Economic Development Bonds.** These bonds can continue to be issued through 2005.
- **Zero Percent Capital Gains Rate.** This provision applies to qualifying DC Zone business stock, partnership interest, or business property held longer than five years. Qualifying property must be acquired prior to January 1, 2006. Qualified gains must be incurred prior to January 1, 2010.

Charitable Contributions of Computer Technology And Equipment Used For Educational Purposes



For qualifying contributions (IRC section 170(e)(6)), this provision limits the reduction of the allowed contribution based on other-than-long-term capital gain. Extended through 2005.

Environmental Remediation Costs

Qualifying environmental cleanup costs (IRC section 198) may continue to be expensed. Extended through 2005.

Credit for Energy Produced from Renewable Resources

This credit is extended through 2005.

Extensions for 2005 and Later Years

Alternative Minimum Tax (AMT)

The expanded AMT exemption amounts that were due to expire in 2004 are extended for one year, through 2005.

Marriage Penalty Relief

The 15 percent rate bracket for MFJ remains at twice that of single filers through 2010. The standard deduction for MFJ remains twice the single standard deduction through 2010.

10 Percent Rate Bracket Expansion

The 10 percent rate bracket remains at \$7,000 for Single and MFS filers and \$14,000 for MFJ filers through 2010. The amount will be adjusted for inflation.

Child Tax Credit

The child tax credit remains \$1,000 per child through 2010. In addition, the refundable portion of the credit is determined by using 15 percent of earned income rather than 10 percent. This provision applies to families with earned incomes in excess of \$11,000 (2005). The additional child tax credit is the lower of (1) the unused child tax credit or (2) (taxable earned income - \$11,000) x 15 percent. This will increase the child tax credit for many low-income families.

Indian Employment Tax Credit

This credit is extended through 2005.

Accelerated Depreciation for Business Property on Indian Reservation

This provision is extended through 2005.

Provisions Not Extended

Bonus Depreciation

The rules allowing 30 percent and 50 percent bonus depreciation do not apply after 2004 unless these provisions are included in a later bill.

IRS User Fees

Unless included in a later bill, the IRS may not assess user fees for letter ruling requests, determination letters, etc. after 2004.

Unified Definition of Child (effective 2005)

The new law creates a uniform definition of qualifying child for the tax benefits that relate to children. Under the new law, a qualifying child must meet only three tests, relationship, residence, and age. These rules are summarized below.

Relationship

The child must be the taxpayer's son, daughter, stepchild, sibling, stepsibling, or a descendant of such individuals. Foster children placed with the taxpayer by authorized placement agencies would satisfy the relationship test. If the child is the taxpayer's sibling, stepsibling or a descendant of any such individual, the taxpayer must care for the child as if the child were his or her own child.

Residence

The child must live with the taxpayer in the same principal place of abode in the United States for over half the year. Military personnel on extended active duty outside the United States would be considered to be residing in the United States. As under current law, the taxpayer and child are considered to live together even if one or both are temporarily absent due to special circumstances such as illness, education, business, vacation, or military service.

Age

The child must be under the age of 19, a full-time student if over age 18 and under age 24, or totally and permanently disabled. However, as under current law, qualifying children (who are not disabled) must be under age 13 for purposes of the child and dependent care tax credit and under 17 (whether or not disabled) to qualify for the child tax credit.

A tiebreaker rule similar to the current EITC tiebreaker applies if more than one qualifying taxpayer claims a benefit for the same child.

This new rule affects the following tax benefits.

- The dependency exemption.
- The child tax credit.
- The earned income credit.
- The dependent care credit.
- Head of household filing status.

Notes

The prior-law rules are retained for individuals to whom the uniform definition does not apply.

If a child files a joint return the uniform definition rules do not apply. Prior-law rules may be used instead.

Do not hesitate to contact your Freed Maxick & Battaglia tax advisor for assistance in taking advantage of this new legislation.