

## **Tax Relief: Some Important Changes**

*By Timothy D. Lott, CPA, CVA*

There have been many tax law changes that may have affected you for 2002 and maybe even 2001. You should be aware of them and take the necessary steps to ensure that you receive maximum tax savings.

You are probably aware of the major tax bill that passed in early 2001 that included some changes for 2001, as well as many changes for future years. There have been some changes due to September 11, 2001 along with some other changes that haven't received much media attention. In fact, two changes took effect in 2001 that were not even part of the 2001 tax act. I won't dwell on any one tax bill in this article, nor will I dwell on any one issue; however, I will make you aware of the changes that haven't been widely publicized.

First, as of January 2001, you could use a standardized table to determine your required minimum distribution if you were at least 70 ½ years old. In many cases, using this new table would lower your required minimum distribution, thereby lowering your tax liability and extending the life of the IRA or qualified retirement plan account. In addition, upon the death of the IRA owner, the beneficiary could take distributions over their life expectancy, NOT over five years as was the old rule. You also have until December 31<sup>st</sup> of the year following the date of death to determine the IRA beneficiary. This does not mean you can add beneficiaries after death; however, with proper planning and using contingent beneficiaries, you now have the opportunity to do some postmortem planning. Everyone should review their beneficiary designations of their IRA's.

Second, as part of the Taxpayer Relief Act of 1997, individuals were given the opportunity to make an election on their 2001 tax return to "deem sale" certain appreciated assets as of January 2, 2001 to begin the new 5-year holding period on those assets. While it generally would not make sense to make this election, I personally had two clients where it did make sense and we made the election. For those who have extended their 2001 individual tax returns it's not too late.

There are two other changes that took effect in 2001 that were not finalized and communicated to the public until early March 2002. Therefore, if you were one of the diligent taxpayers that filed returns early, you should talk to your tax advisor about these changes and decide if an amended return makes sense for you.

The first change is an added depreciation deduction that is available for taxpayers who purchased certain furniture, equipment and leasehold improvements after September 10, 2001. Taxpayers can elect to take an additional 30% "bonus" depreciation in addition to any Section 179 expensing election. This even applies to vehicles used in your business. In addition to the maximum vehicle depreciation you get with a new vehicle, you could get up to \$4,600 more under this change.

The second change affects those that may have a net operating loss (NOL) for 2001. The current law limited certain NOL carryback's to two previous years (for a 2001 NOL, you could only go back to 1999). However, you can now carry that loss back five years, or back to 1996.

Below are some of the changes for 2002 that you should plan to take advantage of, if possible:

1. You can contribute up to 25% of earnings for Profit Sharing and SEP retirement plans, an increase of 10% from prior law.
2. If you created a new retirement plan and it took effect as of January 1, 2002, you may be entitled to a tax credit.
3. The maximum dollar amount you can contribute to qualified retirement plans is now \$40,000 (subject to other limitations) and \$3,000 for IRA's.
4. The maximum dollar deferral for 401(k) plans is now \$11,000 and the percentage limit is increased to 100% of earnings (with other possible limitations).
5. For those of you over fifty years old there are new "catch-up" contributions you can make in addition to these new limits. For 401(k) deferrals you can add another \$1,000 in 2002 for a total of \$12,000. For IRA's and SIMPLES you can add \$500 for a total of \$3,500 and \$7,500 respectively.
6. You can now contribute to a Coverdell IRA (formerly called Educational IRA's) and a Section 529 Qualified Tuition plan for the same beneficiary. Under old law you could not contribute to both in the same year.
7. You also have until April 15<sup>th</sup> of the following year to make the Coverdell contribution, just like regular IRA's. The old rule was that it had to be made by December 31<sup>st</sup> of the year of contribution.
8. Section 529 Qualified Tuition plan distributions are now tax-free when used for higher education expenses and Coverdell distributions can be used for educational expenses for grades 1-12 as well as college and for private and religious schools. They've also expanded the definition of what qualifies as an educational expense under the Coverdell IRA.
9. If you were directly or indirectly affected by the 9/11 attacks, there are other tax relief measures for the victims of the attacks and you should consult with your tax advisor.

As I mentioned, this only scratches the surface of the many tax law changes that have been enacted since January 2001. You should plan to meet with your advisors to ensure that proper planning is implemented in order to maximize your tax savings.

*Timothy D. Lott, CPA, CVA is a partner with Naden/Lean, LLC, a CPA and business consulting firm in Timonium, Maryland.*