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## Taxing Matters

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Even its name is a mouthful: “The Tax Increase Prevention and Reconciliation Act” (TIPRA). But what does this massive piece of legislation, approved in May by both houses of Congress, mean to you? Most people will feel the impact in one of a very few areas and, for the most part, will pay less tax than if TIPRA had been passed. Here’s our summary.

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### **CAPITAL GAINS**

As one might expect, capital gains came in for special treatment under this legislation. In general, the favorable provisions enacted over the past five years have been extended through 2010. These include:

❖ **Lower rates on capital gains.**

If you’re a noncorporate taxpayer, your adjusted net capital gain will continue to be taxed at a *maximum* rate of 15%. If your ordinary income would be taxed at 15% or 10%, the maximum capital gains tax rate is 5%. This goes down to 0% for tax years after 2007. All of this is a substantial savings over the 8% - 20% rates previously in effect – and scheduled to be reactivated in 2008.

❖ **Lower rates on qualified dividend income.**

Noncorporate taxpayers will be allowed to treat qualified dividend income as adjusted net capital gain, rather than as ordinary income. The same rates apply as described above.

❖ **Capital gain treatment for self-created musical works.**

If you own a copyright to a musical work you created yourself, the income will now be taxed at the lower rate applied to capital gains. It used to be that income from the sale of copyrights of musical works was treated as ordinary income and taxed at the applicable higher level.

### **ALTERNATIVE MINIMUM TAX**

Earlier in the year, there was a great deal of press on the alternative minimum tax and how it was going to ensnare an increasing number of people beginning with 2006. Essentially, before TIRPA, exemptions would have dropped back to 2000 levels, with no adjustments for inflation. To deal with this, Congress has adopted a one-year patch, boosting the AMT exemption amounts over 2005 levels.

❖ **Married individuals filing jointly and surviving spouses.**

The exemption is \$62,550, less 25% of AMTI exceeding \$150,000 (0 exemption when AMTI is \$400,200)



#### ❖ **Unmarried individuals**

The exemption is \$42,500, less 25% of AMTI exceeding \$112,500 (0 exemption when AMTI is \$282,500)

#### ❖ **Married individuals filing separately**

The exemption is \$31,275, less 25% of AMTI exceeding \$75,000 (0 exemption when AMTI is \$200,100). However, over \$200,000 the AMTI of married individuals filing separately is increased by the lesser of \$31,275 or 25% of the excess of AMTI without regard to the exemption reduction.

#### **THE “KIDDIE TAX”**

The so-called “kiddie tax” now applies to unearned income for minors up to age 18. From time immemorial, a common approach to lessen tax and other liabilities has been for parents to transfer assets to their children. The window for doing this has been steadily closing over the last several years as Congress has implemented a “kiddie tax,” mandating that children under 14 with investment income would be taxed at the same marginal tax rate as their parents. As part of TIRPA, the window closed altogether. For 2006, the kiddie tax begins to apply when the child has more than \$1,700 in unearned income.

Exceptions are made for children who are married and filing a joint return for the tax year. There is also an exception for distributions for certain qualified disability trusts.

#### **ROTH IRA CONVERSIONS**

The AGI ceiling of \$100,000 has been lifted for conversions of regular IRAs to Roth IRAs for tax years beginning in 2010. Additionally, if you have a six-figure income and opt to convert a regular IRA to a Roth IRA in 2010, you can spread the income and resulting tax payments on the converted funds over 2011 and 2012.

#### **THE BOTTOM LINE**

The new law holds a number of opportunities – and some pitfalls – particularly for the affluent. And, like most tax laws, this one contains various complications and nuances. In general, we recommend that you:

- ❖ Review the formula for calculating adjusted net capital gain.
- ❖ Ensure that you know what constitutes qualified dividend income.
- ❖ Strategize now to see if you are likely to fall under the AMT in the next few years and evaluate your options – if any – for avoiding it.
- ❖ Examine alternatives to asset transfer for protecting some of your wealth for your children.
- ❖ Explore the benefits of the two types of IRA and decide which is likely to be of greater benefit to you.

Call us today to discuss your specific situation and concerns.

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