Thomas, Judy, and Tucker, P.A.

Welcome to the June 2003 Thomas, Judy & Tucker, P.A. newsletter. If you prefer to have this newsletter e-mailed, please call our office at (919) 571-7055 and give us your e-mail address, or e-mail it to us at heather.dickson@tjtpa.com

President Bush signed into law on May 28, 2003 the **"Jobs and Growth Tax Relief Reconciliation Act of 2003,"** which contains significant tax cuts for stockholders, individual taxpayers, couples and businesses. This newsletter is dedicated to giving you a summary of the highlights of this legislation, which begins on the following page.

STAFF NEWS

Our journey through life is often made a little easier by the help of others. For many here at Thomas, Judy & Tucker, P.A., a name that will always be at the top of the list is **Gilbert Smith**. Gilbert passed away on December 8, 2002 after a long battle with melanoma. While we mourn his passing, he will always be remembered here for his giving nature and as a mentor to many. Even as his health was deteriorating, his faith enabled him to overcome his own discomfort and focus on helping and encouraging others. Gilbert, a retired CPA, was also a role model in his commitment to community organizations. He was a director for Camp Oak Hill, director for the Raleigh Rescue Mission, director and treasurer for the Foundation for Hope for Research and Treatment for Mental Illness, and on the finance committee for the Lucy Daniels foundation. It is our hope that we will honor Gilbert's memory by helping others in the same way that he helped us.

- We now have a CERTIFIED FINANCIAL PLANNER™ practitioner on our staff. **Michael Feldbusch** achieved the CFP™ designation on December 16, 2002. Michael, who is a senior staff member on our tax team, has completed rigorous coursework and experience requirements as well as successfully passing the exam to attain this designation. We congratulate Michael on his achievement and are very exited about a new breadth of knowledge he brings to our clients.
- We also have a new CPA on staff. **Will Vaughn** , who joined the firm in October 2001, successfully passed the CPA exam in November and has been approved by the NC Board of CPA examiners to receive his license. This is a well-deserved achievement for Will and we congratulate him!

AFRs FOR JUNE 2003

The Applicable Federal Rates for June 2003 have been announced. Selected rates are as follows:

Term	Compounding Monthly	Compounding Annual
Short-term (0-3 years)	1.48%	1.49%
Mid-term (4-9 years)	3.02%	3.06%
Long-term (over 9 years)	4.56%	4.65%

GET YOUR TAX REFUND STATUS ON THE INTERNET!

The IRS is encouraging taxpayers to check the status of their refunds over the internet. The service, "Where's My Refund", is quick, easy and safe, and is available on the IRS website at www.irs.gov.

The IRS determines if a return has been received and is in processing; the mailing date or direct deposit date of the refund; or whether the refund has been returned to the IRS because it could not be delivered. This is a secure site, meeting the IRS security and privacy certifications.

Taxpayers without internet access can get refund information by calling the automated refund services at (800) TAX-4477 or by using the new IRS refunds hotline at (800) TAX-1954.

FOR INDIVIDUALS: ACCELERATION OF CERTAIN PREVIOUSLY ENACTED TAX BENEFITS AND REDUCTIONS

An important component of the 2003 Jobs and Growth Act speeds up previously enacted tax benefits and reductions that were scheduled to be phased in over the next several years. (For employees, your federal tax withholding will be adjusted no later than July 1, 2003 to reflect the rate and tax bracket changes.) These acceleration provisions include:

Acceleration of 10% individual income tax rate bracket expansion. The expansion in the width of the 10% rate bracket for single and joint filers is accelerated from 2008 to 2003. The change in the 10% tax bracket limit for 2003 is:

	2003 – 2005	2002
Single (and Married Filing Separately)	$7,000	$6,000
Married Filing Jointly	$14,000	$12,000

For 2004, both these figures will be indexed for inflation. The endpoint of the 10% bracket for heads of household remains unchanged at $12,000. From 2005 through 2007, the end point of the 10% bracket will revert to the $12,000/$6,000 levels (and under prior law, will go up to $14,000/$7,000 for 2008 through 2010).

Acceleration of reduction in individual income tax rates. The change that will affect the widest number of taxpayers is an immediate reduction of the marginal tax brackets paid by all but the lowest earners. The taxable income changes are:

Married filing jointly	Single	2003 - 2005	2002
$14,000 - $56,800	$7,000 - $28,400	15 %	15 %
$56,800 - $114,650	$28,400 - $68,800	25 %	27 %
$114,650 - $174,700	$68,800 - $143,500	28 %	30 %
$174,700 - $311,950	$143,500 - $311,950	33 %	35 %
$311,950	$311,950	35 %	38.6 %

These rate reductions were scheduled for 2006 under 2001 EGTRRA. After 2010, rates above 15% will revert to the pre-2001 law levels (i.e., to 28%, 31%, 36%, and 39.6%)

Acceleration of marriage-penalty relief. The 2003 law reduces so-called marriage penalties (i.e., tax-law provisions that force two-income couples to pay more in taxes each year merely because they are married). The basic standard deduction amount for joint returns and those in the 15% tax bracket will be double the basic standard deduction amount for single returns.

	Standard Deduction		15% Tax Bracket	
	MFJ	Single	MFJ	Single
2002	$7,850	$4,700		
2003	$9,500	$4,750	$14,000	$7,000
2004	2 x Single rate	Adjust for inflation	2 x Single rate	Adjust for inflation
2005	174% Single rate	Adjust for inflation	180% Single rate	Adjust for inflation

Acceleration of increase in child tax credit.

2002	$600	(Per qualifying dependent child under age 17)
2003 – 2005	$1,000	
2006 – 2008	$700	

What's more, for 2003, the increased amount of the child tax credit will be paid in advance beginning in mid-July over a period of three weeks. **Thus, a typical qualifying family will receive an advance payment check for up to $400 per qualifying child who is under age 17 as of the end of 2003.** Note that the income limits related to the child tax credit are unchanged by the 2003 Jobs and Growth Act. This means the credit allowable is reduced or eliminated by $50 per $1,000 for taxpayers with adjusted gross income (AGI) over certain levels: $75,000 for singles and $110,000 for married couples. However, taxpayers who didn't qualify in the past for the child tax credit because of AGI limitations may now qualify for a portion because of the increased credit (even though they won't get an advance payment).

Minimum tax relief to individuals. The 2003 Act also includes some relief from the alternative minimum tax, or AMT. With income tax rates decreasing and the AMT rate staying the same, more individuals may find themselves paying AMT. The increase in the AMT exemption amount is as follows:

Tax Year	MFJ	Single
2002	$49,000	$35,750
2003 – 2004	$58,000	$40,250
2005	$45,000	$33,750

TAX CHANGES FOR BUSINESS AND CORPORATIONS

Liberalized Section 179 expensing election. The 2003 law significantly liberalizes the expensing election, which permits small businesses to expense (i.e., deduct immediately rather than depreciate over several years) a certain amount of the cost of tangible depreciable personal property purchased and placed in service during the tax year in an active trade or business. All of the following expensing changes are effective for tax years beginning after 2002 and before 2006:

- The maximum annual expensing amount is $100,000 (up from $25,000).
- The maximum annual expensing amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the tax year exceeds a specified dollar level. This dollar level is increased to $400,000 (from $200,000).
- The above increased dollar amounts will be inflation-indexed for tax years beginning after 2003.
- Off-the-shelf computer software is made eligible for expensing.
- Taxpayer revocation of expensing elections will no longer require IRS consent.
- Equipment can be new or used equipment.

More bonus depreciation. A second major change affecting businesses is an increase and extension of bonus first-year depreciation. In general, before the 2003 Jobs and Growth Act, a 30% additional first-year depreciation allowance applied to the non-expensed portion of qualified property (which included most new MACRS property) if:

- Its original use commenced with the taxpayer after Sept. 10, 2001
- The asset was acquired by the taxpayer after Sept. 10, 2001 and before Sept. 11, 2004
- Placed in service by the taxpayer before 2005 (before 2006 for some property with longer production periods).

The 2003 Jobs and Growth Act makes the following changes:

- 50% bonus first-year depreciation applies to qualified property if
  - Its original use commences with the taxpayer after May 5, 2003
  - The asset is acquired by the taxpayer after May 5, 2003 and before 2005 (there can't be a written binding contract for acquisition in effect before May 6, 2003).
  - It is placed in service by the taxpayer before 2005 (before 2006 for certain property with longer production periods).
- Taxpayers can elect on a class-by-class basis to claim 30% instead of 50% bonus first-year depreciation for qualifying property, or elect not to claim bonus first-year depreciation at all. Two situations in which a taxpayer would likely consider making an election to claim smaller bonus first-year depreciation (or to elect out of it entirely) are where the taxpayer (1) has about-to-expire net operating losses, or (2) anticipates being in a higher tax bracket in future years.
- Note that there still is no AMT depreciation adjustment for the entire recovery period of qualified property recovered under the bonus first-year depreciation rules (50% or 30%).

Late estimated tax payment allowed for 25% of September 15, 2003 payments. Another change for corporations affects only the estimated tax payment rules for 2003. Despite the general rule that estimated tax payment installments must be made no later than Apr. 15, June 15, Sept. 15 and Dec. 15, 25% of the amount of any required installment of corporate estimated tax which is otherwise due in Sept. 2003 will not be due until Oct. 1, 2003. This change affects corporations using (1) the calendar year (third installment of estimated tax would have been due on Sept. 15, 2003); (2) a fiscal year ending Mar. 31, 2004 (second installment would have been due on Sept. 15, 2003); (3) a fiscal year ending May 31, 2004 (first installment would have been due on Sept. 15, 2003); and (4) a fiscal year ending Sept. 30, 2003 (last installment would have been due Sept. 15, 2003). The due dates for all other corporate estimated tax payments are not changed by the 2003 Jobs and Growth Act provision.

TAX ACT MAY IMPACT INDIVIDUAL ESTIMATED TAX PAYMENTS

The second installment of 2003 estimated tax payments for individuals is due on June 16, 2003. The new tax law may reduce the amount you need to pay. For an analysis of how it affects your individual estimates for 2003, please call our office and we will be glad to recalculate.

NORTH CAROLINA EFFECT OF NEW FEDERAL LAW UNCERTAIN

While North Carolina tax law follows the federal in many respects, there is no assurance that in this economically difficult time the state will be able to accept these changes. The legislature will have to address this issue. We will keep you updated on the status of conforming North Carolina law to the federal changes.

DIVIDENDS AND CAPITAL GAINS: REDUCTION IN TAX RATES

An important component of the 2003 Jobs and Growth Act, particularly if you are an investor, is a reduction in the taxes on dividends and capital gains. These lower rates can mean considerable tax savings for taxpayers. Keep in mind that they are not permanent, since they will cease to apply after 2008, barring additional Congressional action to extend them. Here are more details regarding dividends and capital gains under the Act.

Capital gains rates reduced. Under the 2003 Jobs and Growth Act, effective for sales and exchanges (and installment payments received) after May 5, 2003 and before Jan. 1, 2009, the 10% and 20% rates on adjusted net capital gain are reduced to 5% (zero in 2008) and 15%, respectively, for both regular tax and the alternative minimum tax (AMT). The lower rates apply to sales of capital assets held more than one year. Because this 5% drop in the capital gains rate is more than the 3.6% drop in the top individual rate under the 2003 Jobs and Growth Act and the 2% drop in other individual rates, the advantage of long-term capital gains over other types of taxable income is even greater for high earners than it was before.

Note, however, that there is no cut in the 28% capital gains rate affecting collectibles and certain small business stock and the 25% rate affecting gains representing depreciation claimed recapture.

Tax rates on dividends reduced. For dividends received in tax years beginning after 2002 and before 2009, dividends received by an individual shareholder from domestic corporations are treated as adjusted net capital gain for purposes of applying the capital gain tax rates. In other words, the dividends are taxed at rates of 5% (zero in 2008) and 15% for both regular tax and AMT purposes. This results in substantial tax savings for dividend recipients given the fact that, under pre-2003 Jobs and Growth Act law, the dividends were taxed as ordinary income at rates up to 38.6%.

Certain dividends do not qualify for the new rate. Generally, dividends from REITs, foreign corporations not listed on U.S. stock exchanges and certain preferred stock dividends do not qualify. Additionally, dividends from investments with a holding period of less than three months would not qualify.

Please keep in mind that these are only the highlights of the most important changes in the new law. Please give us a call at your earliest convenience for more details on how you may be affected, and whether immediate action is needed to take advantage of the tax breaks in this important tax legislation.

NEW PAYROLL WITHHOLDING TABLES ISSUED

IRS has posted on its website new lower percentage method withholding tables reflecting the 2003 Job and Growth Act's lower individual tax rates and expanded tax brackets. Publication 15-T, which contains the new tables, will be mailed to all employers by the third week in June. Employers are encouraged to use the new tables as soon as they can work them into their payroll systems, but must start to use them no later than July 1, 2003. The web address for the new tables is http://www.irs.gov/pub/irs-pdf/n1036.pdf.

MAXIMIZE REAL ESTATE DEPRECIATION DEDUCTION

When buying business real estate—for your own business occupancy or for rental to others—you should take steps that maximize the income tax depreciation deductions that you can claim for the property. Here are a few suggestions.

Separating improvements from land. Not all of the cost of acquiring real estate is depreciable. Specifically, the cost of *improvements* to land is depreciable, but the cost of the land itself is not. It is vital to identify and document, *at the time that you acquire real estate*, the part of your overall acquisition cost allocable to improvements. Thus, when you buy a property, you should either retain a qualified real estate appraiser to make an allocation between land and improvements based on a detailed written analysis, or, if you have enough valuation expertise and knowledge of the locality, write your own detailed analysis and allocation. In either case, we will be happy to review the analysis to determine whether it is in accordance with valuation techniques that are respected by the tax law. Also, regarding the allocation, you should be aware that the cost of improvements includes not only the cost of buildings, but also the cost of items such as landscaping and roads, and even some costs of grading and clearing. We can assist an appraiser (or you) in identifying which of these seemingly land-related costs are, actually, costs of improvements, and should, therefore, be reflected in the improvements portion of the allocation.

WRITE-OFF 50% OF CERTAIN NEW BUILDING COSTS

By using component depreciation to segregate personal property from the structural cost, most property with a life of less than 20 years will be eligible for the new 50% bonus depreciation discussed earlier. See the column at the right for examples of what components may qualify for this significant early write-off.

Separating personal property from buildings. Most business buildings must be depreciated over a period of 39 years, with the exception that residential rental real estate (for example, an apartment house) is depreciable over 27.5 years. On the other hand, most personal property (furniture, equipment, etc.) is depreciable over 5 years or 7 years. If a specific item is classified as personal property rather than as a part of a building, the depreciation deductions for that item will be available sooner and, in economic terms, have a greater "present value" to the property owner. Thus, in the same way that it is important to properly allocate between improvements and land, it is important to take steps to identify and document, *at the time that you acquire real estate*, the items that are personal property and the items that are building parts. For some items, the distinction follows "common sense"—an ordinary chair is personal property, a weight-bearing brick wall is part of a building. However, for many items—for example, lighting fixtures, signs, floor coverings, wall coverings, plumbing, electrical systems and heating and cooling systems—the distinctions are governed by tax rules that can be complex, can involve projections as to the future use of the items, and may even necessitate consultation with engineers or other construction experts. Also, after the personal property and building items are separately identified, they must be separately valued, either by an appraisal or a breakdown of construction costs (depending on whether the building was already on the site, or newly-constructed).

We will be pleased to work with you in implementing the above planning techniques (and any other available strategies) should you undertake a specific business real estate acquisition.

Please call us for additional information on any of the above. We are committed to keeping you informed on tax and financial developments and the opportunities they present for you and your business.

Very truly yours,

Thomas, Judy & Tucker, P.A.