Chapter 6: New Legislation

Three Percent Withholding Repeal and Job Creation Act ... A215
Middle Class Tax Relief and Job Creation Act of 2012 ... A220
Expiring Tax Provisions ... A221

Corrections were made to this workbook through January of 2013. No subsequent modifications were made.

THREE PERCENT WITHHOLDING REPEAL AND JOB CREATION ACT

On November 21, 2011, President Obama signed into law the Three Percent Withholding Repeal and Job Creation Act (HR 674). The tax-related portions of this Act are described below.

REPEAL OF WITHHOLDING ON GOVERNMENT PAYMENTS

Old Law. As part of the Tax Increase Prevention and Reconciliation Act of 2005, payments made to private contractors by federal, state, and local government entities would be subject to 3% withholding. As originally enacted, the provision was to become effective for payments made after December 31, 2010. Subsequent legislation delayed the effective date until January 1, 2012, and IRS regulations further delayed implementation until January 1, 2013. The regulations further stipulated that payments less than $10,000 were not subject to the withholding requirement.

New Law. HR 674 repealed the government withholding requirement as if it had never been enacted. The provision is effective for payments made after December 31, 2011.

WORK OPPORTUNITY TAX CREDIT FOR VETERANS

Old Law. The work opportunity tax credit (WOTC), except as modified by HR 674, is not available for individuals who begin work for an employer after December 31, 2011.

New Law. HR 674 extends the WOTC **only for qualified veterans** who begin work for an employer on or before December 31, 2012. A **qualified veteran** for purposes of the WOTC is expanded to include veterans who begin work after November 21, 2011, and before January 1, 2013, and have aggregate periods of unemployment of at least four weeks in the year prior to being hired. A qualified veteran is a veteran who falls into **one** of the four following targeted categories.[1]

- A member of a family receiving assistance under the Supplemental Nutrition Assistance Program (food stamps) for at least three months during the 15-month period ending on the hiring date
- Unemployed for at least six months in the 1-year period ending on the hiring date
- Entitled to compensation for a service-connected disability and hired within one year after being discharged or released from active duty
- Entitled to compensation for a service-connected disability and unemployed for at least six months in the 1-year period ending on the hiring date

1. Instructions for Form 8850.

The credit amount depends on a number of factors, including the length of the veteran's unemployment, hours the veteran works, and the amount of first-year wages paid. Employers who hire veterans with a service-related disability may be eligible for the maximum credit.[2]

WOTC Available to Tax-Exempt Organizations

HR 674 amends IRC §§52 and 3111 to make the WOTC available to qualified tax-exempt organizations that hire qualified veterans on or after November 22, 2011. These organizations can claim the credit against the employer share of social security tax.

Ineligible Individuals

Wages paid to certain employees do not qualify for the credit even if the employee is a member of one of the targeted categories. Ineligible individuals include the following.

1. Persons related to the employer[3] (For this purpose, relatives include all the relationships qualifying under the dependency exemption except for unrelated people who only qualify because they live with the taxpayer for the entire tax year. If the employer is a corporation or other entity, the employee must not be related to anyone with more than 50% ownership or control of the employer.)
2. Dependents of the business owner[4]
3. Prior employees[5]
4. Individuals who work fewer than 120 hours[6] for the employer
5. Individuals hired as replacement workers during a strike or walkout[7]
6. Individuals who receive no more than half of their total wages from the employer for working in the employer's trade or business[8]

WOTC Certification

Employers must obtain certification for potential employees from the **state workforce agency** (e.g., Illinois Department of Employment Security), in order to qualify for the WOTC. The following steps are required for WOTC certification.

1. The employer prescreens potential employees by completing Form 8850, *Pre-Screening Notice and Certification Request for the Work Opportunity Credit.* If the employer believes the applicant is a member of a targeted group, the form must be completed no later than the day the job offer is made. Form 8850 must then be submitted to the state workforce agency no later than the 28th day after the job applicant begins work for the employer.
2. One of the following forms must be completed and sent to the state WOTC coordinator.
   a. ETA Form 9062, *Conditional Certification Form,* if the job applicant received this form from a participating agency, such as the Jobs Corps
   b. ETA Form 9061, *Individual Characteristics Form,* if the applicant did not receive conditional certification
3. The state WOTC coordinator must certify that the job applicant is a member of a targeted group.

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2. IRS News Rel. IR-2012-17 (Feb. 9, 2012).
3. IRC §51(i)(1)(A).
4. IRC §51(i)(1)(C).
5. IRC §51(i)(2).
6. IRC §51(i)(3)(B).
7. IRC §51(c)(3).
8. IRC §51(f)(1).

Calculating the Credit

The tax preparer must know how many hours each employee worked, their hire date, wages paid during the year to each employee, and in which group each employee was certified. They must then complete Form 5884, *Work Opportunity Credit,* or Form 5884-C, *Work Opportunity Credit for Qualified Tax-Exempt Organizations Hiring Qualified Veterans.*

Qualified wages for purposes of the credit include all compensation included as wages for federal unemployment tax (FUTA) purposes. If the work performed by an employee during more than half of any pay period qualifies under FUTA as agricultural labor, that employee's wages subject to social security and Medicare taxes are qualified wages. Qualified wages must be reduced by any work supplementation payments received under the Social Security Act for the employee.

Generally, the credit is 40% of the applicable first-year wages for an employer that is not tax-exempt. However, if the employee has worked at least 120 hours but less than 400 hours for the employer, the credit is limited to 25% of the applicable first-year wages.

For a qualified tax-exempt employer, the credit is 26% of the qualified first-year wages if the veteran performs at least 400 hours of service for the organization. If the veteran performs at least 120 hours of service but less than 400 hours, the credit is 16.25% of the qualified first-year wages. Furthermore, the organization can only take into account the wages paid to a qualified veteran for services in furtherance of activities related to the purpose or function of the organization under IRC §501. Wages for services in an unrelated trade or business are not counted for purposes of the credit.[9]

6

The **qualified first-year wages** that can be taken into account for a **qualified veteran** is limited to the following.

1. **$6,000** for a qualified veteran certified as being either:
   a. A member of a family receiving assistance under the Supplemental Nutrition Assistance Program for at least a 3-month period during the 15-month period ending on the hiring date, or
   b. Unemployed for at least four weeks but less than six months in the 1-year period ending on the hiring date.
2. **$12,000** for a qualified veteran certified as being entitled to compensation for a service-connected disability and either:
   a. Hired not more than one year after being discharged or released from active duty in the U.S. Armed Forces, or
   b. Began work before November 22, 2011, and was unemployed for at least six months in the 1-year period ending on the hiring date.
3. **$14,000** for a qualified veteran who began work after November 21, 2011, and was certified as being unemployed for at least six months in the 1-year period ending on the hiring date
4. **$24,000** for a qualified veteran who began work after November 21, 2011, and was certified as being entitled to compensation for a service-connected disability and unemployed for at least six months in the 1-year period ending on the hiring date

After calculating the amount of the credit, the deduction for wages paid must be reduced by the amount of the credit.

9. IRS Notice 2012-13, 2012-9 IRB 421.

Example 1. Bob Taylor is the owner of Taylor Express, a trucking company. After consulting with his accountant, he hires the following individuals who are certified by the state workforce agency as qualified veterans.

Name	Hire Date	2012 Wages Paid	Hours Worked	Additional Information
Jessica Fynch	3/1/2012	$ 7,000	350	Unemployed for two months in the year ending on the hiring date
Drew Barry	4/2/2012	15,000	600	Unemployed for seven months in the year ending on the hiring date
Antonio Bennett	5/7/2012	2,500	100	Unemployed for eight months in the year ending on the hiring date

Bob's accountant Marilyn uses the above information to determine the amount of qualified wages for purposes of the WOTC credit.

Step 1. Marilyn looks for employees who do not qualify for the credit. She observes that Antonio Bennett's wages do not qualify because he worked less than 120 hours for the company.

Step 2. Marilyn looks for employees who qualify for less than the full credit because they worked less than 400 hours. She determines that Jessica Fynch falls into this category.

Step 3. Marilyn determines the amount of the wages that can be taken into account for the credit is as follows.

- $6,000 of Jessica's wages because she was unemployed for at least four weeks but less than six months in the 1-year period ending on the hiring date
- $14,000 of Drew's wages because he was unemployed for at least six months in the 1-year period ending on the hiring date and he did not have a service-connected disability

Step 4. Marilyn enters the qualified wages on Form 5884, which is shown next. The $7,100 credit is then entered on Form 3800, *General Business Credit*.

> **Note.** This example uses a 2011 form because the draft 2012 form was not yet available at the time this book went to press.

For Example 1

Form **5884** Department of the Treasury Internal Revenue Service	**Work Opportunity Credit** ▶ Attach to your tax return.		OMB No. 1545-0219 2011 Attachment Sequence No. 77
Name(s) shown on return: **Taylor Express**			Identifying number: **32-0123456**
1	Enter on the applicable line below the total qualified first- or second-year wages paid or incurred during the tax year, and multiply by the percentage shown, for services of employees who are certified as members of a targeted group.		
a	Qualified first-year wages of employees who worked for you at least 120 hours but fewer than 400 hours . $ **6,000** × 25% (.25)	**1a**	**1,500**
b	Qualified first-year wages of employees who worked for you at least 400 hours . . . . $ **14,000** × 40% (.40)	**1b**	**5,600**
c	Qualified second-year wages of employees certified as long-term family assistance recipients . . . . . . $ ______ × 50% (.50)	**1c**	
2	Add lines 1a, 1b, and 1c. See instructions for the adjustment you must make to salaries and wages	**2**	**7,100**
3	Work opportunity credit from partnerships, S corporations, cooperatives, estates, and trusts	**3**	
4	Add lines 2 and 3. Cooperatives, estates, and trusts, go to line 5. Partnerships and S corporations, stop here and report this amount on Schedule K. All others, stop here and report this amount on Form 3800, line 4b	**4**	**7,100**
5	Amount allocated to patrons of the cooperative or beneficiaries of the estate or trust (see instructions)	**5**	
6	Cooperatives, estates, and trusts, subtract line 5 from line 4. Report this amount on Form 3800, line 4b	**6**	

Controlled Groups

Employees of corporations that are members of the same controlled group (as defined in IRC §52(a)) are treated as being employed by a single employer. The WOTC for each corporation is based on its proportionate share of the wages giving rise to the credit.

Employees of partnerships, proprietorships, etc., that are under common control are treated as being employed by a single employer.[10] Each business's portion of the WOTC is based on its proportionate share of the wages giving rise to the credit.

Successor Employers[11]

In the case of an employer determined to be a successor employer for federal unemployment tax purposes, the successor employer may continue to claim the credit for employees who were certified by the predecessor employer. No recertification is necessary.

10. IRC §52(b).

11. IRC §51(k)(1).

CONTINUOUS LEVY

Old Law. The IRS can levy specified payments to or received by a taxpayer continuously from the date the levy is first made until the levy is released. The levy may attach to up to 15% of any specified payment due to the taxpayer, or up to 100% of any specified payment due to a vendor of goods or services sold or leased to the federal government.

New Law. HR 674 expands the IRS's continuous levy authority to apply to all payments due to a vendor of the federal government. Effective November 21, 2011, payments for property, as well as goods or services, are subject to levy.[12]

MODIFICATION OF PREMIUM ASSISTANCE CREDIT

Old Law. The Patient Protection and Affordable Care Act provides a premium assistance credit for eligible individuals who purchase health insurance through an exchange after 2013. The premium assistance credit is available to qualified individuals whose modified gross income (MAGI) is between 100 and 400% of the federal poverty level.

New Law. HR 674 modifies the definition of MAGI for purposes of calculating the premium assistance credit to include the portion of an individual's nontaxable social security benefits.[13]

> **Note.** For detailed information about the premium assistance credit, see 2012 Volume A, Chapter 7: Healthcare Reform Act.

MIDDLE CLASS TAX RELIEF AND JOB CREATION ACT OF 2012

On February 22, 2012, the president signed into law the Middle Class Tax Relief and Job Creation Act of 2012 (HR 3630). The centerpiece of this legislation is an extension of the "payroll tax holiday" for employees through the end of 2012. It also adjusts the timing of estimated tax payments required to be made by certain large corporations.

PAYROLL TAX CUT

Old Law. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 reduced the employee share of the old-age, survivors, and disability insurance (OASDI) tax from 6.2% to 4.2% for calendar year 2011 only. The employer's share of the OASDI tax was unchanged at 6.2%. The payroll tax cut was extended through the end of February 2012 by the Temporary Payroll Tax Cut Continuation Act of 2011, which was enacted on December 23, 2011.

Self-employed individuals also benefit from a comparable rate reduction in the social security portion of the self-employment tax. OASDI taxes for the self-employed are reduced from 12.4% to 10.4%.

New Law. HR 3630 extends the reduction in OASDI taxes for employees and self-employed individuals through December 31, 2012. The reduction for 2012 applies to the first $110,100 of wages and net self-employment income received by an individual; thus, the maximum benefit to be derived is $2,202 ($110,100 × 2%).

HR 3630 also **repealed** the recapture tax that was included in the December legislation that effectively capped the amount of wages eligible for the payroll tax cut at $18,350 (the 2-month equivalent of the $110,100 social security earnings limit). Without this repeal, the recapture tax would have been payable when the taxpayer filed their 2012 tax return.

> **Note.** For more information about the reduction in social security taxes, see pages 269–270 in the 2011 *University of Illinois Federal Tax Workbook.*

12. IRC §6331(h)(3).

13. IRC §36B(d)(2)(B)(iii).

CORPORATE ESTIMATED TAX PAYMENTS

Old Law. Several pieces of legislation in recent years have accelerated the due date for future estimated tax payments required to be made by certain large corporations (those with assets of at least $1 billion) from one quarter into the previous quarter. None of these timing differences have occurred yet. These measures were enacted by Congress to fulfill certain budgetary requirements by shifting revenue from one fiscal year into another.

New Law. HR 3630 **repeals** the shifts in the timing of estimated tax payments mandated by recent legislation. The payment schedule that applied prior to the enactment of the following laws is restored.

- The Corporate Estimated Tax Shift of 2009
- The Hiring Incentives to Restore Employment Act
- The United States–Korea Free Trade Agreement Implementation Act
- The United States–Columbia Trade Promotion Agreement Implementation Act
- The United States–Panama Trade Promotion Agreement Implementation Act

EXPIRING TAX PROVISIONS

The following tables list selected tax provisions scheduled to expire in 2011–2013.[14] The entire list can be found on the Joint Committee on Taxation's website at **www.jct.gov.** At the time this table was prepared, these provisions were not extended beyond the dates shown.

Provisions that Expired in 2011

IRC Section	Expired Provisions	Expiration Date
36(h)(3)	First-time homebuyer credit for individuals on qualified official extended duty outside United States	Apr. 30, 2011
3301(1)	FUTA surtax of 0.2%	Jun. 30, 2011
25C(g)	Credit for certain nonbusiness energy property	Dec. 31, 2011
26(a)(2)	Personal tax credits allowed against regular tax and AMT	Dec. 31, 2011
36C and 137	Expanded adoption credit and adoption assistance programs	Dec. 31, 2011
45G(f)	Credit for certain expenditures for maintaining railroad tracks	Dec. 31, 2011
45L(g)	Credit for construction of new energy efficient homes	Dec. 31, 2011
45M(b)	Credit for energy efficient appliances	Dec. 31, 2011
45P	Employer wage credit for activated military reservist	Dec. 31, 2011
51(c)(4)	Work opportunity tax credit	Dec. 31, 2011
55(d)(1)	Increased AMT exemption amount	Dec. 31, 2011
62(a)(2)(D)	Deduction for certain expenses of elementary and secondary school teachers	Dec. 31, 2011
163(h)(3)	Premiums for mortgage insurance deductible as qualified residence interest	Dec. 31, 2011
164(b)(5)	Deduction for state and local general sales taxes	Dec. 31, 2011

14. Joint Committee on Taxation, *List of Expiring Federal Tax Provisions,* 2010–2020 (JCX-1-12) (Jan. 6, 2012).

Provisions that Expired in 2011 *(continued)*

IRC Section	Expired Provisions	Expiration Date
168(e)(3)(E)(iv), (v), (ix), 168(e)(7)(A)(i) and (e)(8)	15-year straight-line cost recovery for qualified leasehold improvements, qualified restaurant buildings and improvements, and qualified retail improvements	Dec. 31, 2011
168(k)(5)	Additional first-year (bonus) depreciation for 100% of basis of qualified property	Dec. 31, 2011
170(b)(1)(E) and 170(b)(2)(B)	Special rules for contributions of capital gain real property made for conservation purposes	Dec. 31, 2011
170(e)(3)(C)	Enhanced charitable deduction for contributions of food inventory	Dec. 31, 2011
170(e)(3)(D)	Enhanced charitable deduction for contributions of book inventories to public schools	Dec. 31, 2011
170(e)(6)(G)	Enhanced charitable deduction for corporate contributions of computer equipment for educational purposes	Dec. 31, 2011
179(b)(1) and (2) and 179(f)	Increased expensing to $500,000/$2,000,000 and expanded definition of §179 property	Dec. 31, 2011
222(e)	Above-the-line deduction for qualified tuition and related expenses	Dec. 31, 2011
408(d)(8)	Tax-free distributions from individual retirement plans for charitable purposes	Dec. 31, 2011
871(k)(1)(C) and (2)(C), and 881(e)(1)(A) and (2)	Treatment of certain dividends of regulated investment companies	Dec. 31, 2011
1202(a)(4)	Special rules for qualified small business stock	Dec. 31, 2011
1367(a)	Basis adjustment to stock of S corporations making charitable contributions of property	Dec. 31, 2011
1374(d)(7)	Reduced S corporation recognition period for built-in gains tax	Dec. 31, 2011
601 of PL No. 111-312	Temporary payroll tax cut	Dec. 31, 2011

Note. The temporary payroll tax cut was originally set to expire in 2011. It was extended to expire on December 31, 2012.

Provisions Expiring in 2012

IRC Section	Expiring Provisions	Expiration Date
1(f)(8)	Increase the size of 15% rate bracket for married filers to double that of unmarried filers	Dec. 31, 2012
1(h), 55(b), 57(a)(7), 1445(e)(1), 7518(g)(6)(A)	Reduced capital gain rates for individuals	Dec. 31, 2012
1(h)(11), 163(d)(4)(B), 854(a) and (b), and 857(c)	Dividends of individuals taxed at capital gain rates	Dec. 31, 2012
1(i)	10% individual income tax rate	Dec. 31, 2012
1(i)(2)	Reduced individual income tax rates — size of 15% rate bracket modified to reflect 10% rate, and 28%, 31%, 36% and 39.6% rates are reduced to 25%, 28%, 33%, and 35%, respectively	Dec. 31, 2012
21(a)(2) and 21(c)	Dependent care credit — increase of dollar limit on creditable expenses from $2,400 to $3,000 ($4,800 to $6,000 for two or more children), increase of applicable credit percentage from 30 to 35%, increase of beginning point of phaseout range from $10,000 to $15,000	Dec. 31, 2012
23 and 137	Adoption credit and adoption assistance exclusion — increase to $10,000 for maximum credit and maximum exclusion, special needs adoptions deemed to have $10,000 eligible expenses for purposes of credit and exclusion, increase the beginning and ending points of phaseout range for credit and exclusion, allow the credit against AMT	Dec. 31, 2012
24(a) and (b)(3)	Child tax credit — increase from $500 to $1,000, expand eligibility for refundable portion of the credit, AMT relief, provide that child tax credit not treated as income or resources for purposes of benefit or assistance programs financed in whole or in part with federal funds	Dec. 31, 2012
24(d)	Refundable child tax credit floor amount at $3,000	Dec. 31, 2012
25A(i)	American opportunity credit	Dec. 31, 2012
32(b)(2), (c)(2)(A)(i), (h), and 6213(g)(2)	Earned income credit (EIC) — increase in the beginning point of the phaseout range for joint returns, modify EIC treatment of amounts not includible in income, repeal reduction of EIC for AMT liability, expand math error authority	Dec. 31, 2012
32(b)(3)(A)	EIC credit percentage of 45% for three or more qualifying children	Dec. 31, 2012
32(b)(3)(B)	Phaseout threshold for marriage penalty relief	Dec. 31, 2012
45F	Credit for employer-provided child care	Dec. 31, 2012
53(e)	Credit for prior-year minimum tax liability made refundable after period of years	Dec. 31, 2012
63(c)(2)(A)	Increase the standard deduction for married filers to double that of unmarried filers	Dec. 31, 2012
68(g)	Repeal of overall limitation on itemized deductions (Pease limitation)	Dec. 31, 2012

Provisions Expiring in 2012 *(continued)*

IRC Section	Expiring Provisions	Expiration Date
108(a)(1)(E)	Discharge of indebtedness on principal residence excluded from gross income of individuals	Dec. 31, 2012
127(c)(1)	Employer-provided educational assistance — expansion to graduate education and making the exclusion permanent	Dec. 31, 2012
151(d)(3)(F)	Repeal of the personal exemptions phaseouts for high-income taxpayers	Dec. 31, 2012
168(k)(1) and (2)	Additional first-year (bonus) depreciation for 50% of basis of qualified property	Dec. 31, 2012
168(k)(4)	Election to accelerate AMT credits in lieu of additional first-year (bonus) depreciation	Dec. 31, 2012
179(b)(1) and (2), (c)(2), and (d)(1)(A)(ii)	Increase dollar limitations for expensing to $125,000/500,000 (indexed)	Dec. 31, 2012
221	Student loan interest deduction — increase and index phaseout ranges for inflation, repeal the limit on the number of months that interest payments are deductible, repeal the rule that voluntary payments of interest are not deductible	Dec. 31, 2012
530(b)(1), (b)(2), (b)(4), (c)(1), (d)(2)	Coverdell education savings accounts — increase maximum annual contribution from $500 to $2,000, expand definition of qualified education expenses, increase the size of the phaseout range for married filers to double that of unmarried filers, provision of special needs beneficiary rules, contributions by corporations and other entities, and contributions until April 15th, permitted	Dec. 31, 2012
531 and 541	Reduced rates under accumulated earnings tax and personal holding company tax	Dec. 31, 2012
2001 and 2502	Reduced the maximum estate and gift tax rate to 35%	Dec. 31, 2012
2001(b)(2), 2001(g), and 2505(a)	Modified estate and gift taxes to reflect differences in credit resulting from different tax rates	Dec. 31, 2012
2010	Increase estate and gift tax exemption to $5 million (indexed for inflation in years after 2011)	Dec. 31, 2012
2010	"Portability" rules permitting a surviving spouse to use the unused estate and gift tax exemptions of the last deceased spouse	Dec. 31, 2012
2011, 2053, 2058, 2102, 2106, and 2604)	Estate tax deduction for state death taxes paid	Dec. 31, 2012
2031(c)(2) and (c)(8)(A)(i)	Expanded and clarified estate tax conservation easement rules	Dec. 31, 2012
2057	Repeal of the qualified family-owned business deduction	Dec. 31, 2012
2632(c) and 2642(a)(3), (b)(1), and (b)(2)(A)	Modified GSTT rules regarding deemed allocations of exemption to certain transfers in trust, severing of trusts, valuation, and relief for late elections	Dec. 31, 2012
6166(b)(1)(B)(ii), (b)(1)(C)(ii), (b)(8)(B), (b)(9)(B)(iii)(I), and (b)(10)	Modified estate tax installment payment rules	Dec. 31, 2012

Provisions Expiring in 2013

IRC Section	Expiring Provisions	Expiration Date
35(a)	Credit for health insurance costs of eligible individuals	Dec. 31, 2013
42(b)(2)	Determination of low-income housing credit rate	Dec. 31, 2013
168(e)(3)(A)	Three-year depreciation for race horses two years old or younger	Dec. 31, 2013
179D(h)	Energy efficient commercial buildings deduction	Dec. 31, 2013
420(b)(5)	Transfer of excess pension assets to retiree health accounts	Dec. 31, 2013