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HIGHLIGHTS OF THE TAX REDUCTION ACT OF 1975

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The Tax Reduction Act of 1975 contains many provisions that are effective for the 1975 tax year only, others are effective for a two year period and a few are permanent.

More emphasis in this discussion will be placed on changes that will affect your 1975 Tax Return rather than the 1974 tax rebate. Generally most taxpayers will or have received a rebate of 10% of their 1974 tax liability with a maximum of $200 and a minimum of $100 or their actual tax liability whichever is less. There is a reduction in the rebate if your adjusted gross income is over $20,000 and those with $30,000 or more AGI will receive $100.

STANDARD DEDUCTION CHANGES

The standard deduction has been increased for 1975 to 16% of the adjusted gross income with a maximum of $2,300 for single persons and $2,600 for joint returns. Previously it was 15% with a maximum of $2,000 for a joint return.

The low income allowance was increased from $1,300 to $1,600 for single persons to $1,900 for joint returns or surviving spouses and $950 for a married person filing a separate return.

PERSONAL EXEMPTION TAX CREDIT

This credit is available for 1975 only. This tax credit is to be computed by multiplying $30 by the number of exemptions (other than those for age and blindness) that the taxpayer claims on his 1975 return for himself, his spouse, and his dependents. The credit is subtracted directly from tax liability.

EARNED INCOME CREDIT

Individuals who maintain a household in the United States for themselves and one or more of their dependent children may receive a refundable credit equal to 10% of earned income up to a maximum of $400. If earned income exceeds $4,000 the credit is reduced by 10% of the amount above $4,000. This applies to the earned income or adjusted gross income whichever is higher. Thus, at the $8,000 adjusted gross income level (or earned income level), the credit will be eliminated. If the amount of the credit is greater than the taxpayer's liability, the excess will be treated as an overpayment and will be refunded to the taxpayer. Thus it will operate similar to the negative income tax. It has been estimated that eight to ten million additional tax returns will be filed because of this provision.

Earned income is compensation for personal services, including wages, salaries, tips and other employee compensation. It also includes net earnings from self-employment, including farming. It does not include pensions and annuities.

HOME PURCHASE CREDIT

Taxpayers purchasing qualified homes are eligible for a tax credit equal to 5% of the purchasers tax basis, up to a maximum credit of $2,000. It must be purchased as a principal residence, summer homes do not qualify. If the taxpayer sells his old home and buys a new home the purchase price of the new home will be reduced by the amount of the unrecognized gain on the old home.

The credit applies to purchase of new houses, including mobile homes, condominiums, and cooperative housing units. The construction must have been started prior to March 26, 1975. Also the home must have been purchased and occupied after March 12, 1975 and before January 1, 1977. You must be the first occupant to live in the home. A binding contract for purchase of the residence must be entered into before January 1, 1976, except in the case of self-construction.

A certification by the seller must be attached to the taxpayers return stating that the purchase price is the lowest price at which the residence was ever offered for sale. It may also be to the purchasers advantage to have the certification state that construction began prior to March 26, 1975. A special form 5405, "Credit for Purchase or Construction of New Principal Residence," must be attached to the form 1040.

If the taxpayer builds his own home work done prior to March 13, 1975 does not count for credit purposes.

If a new home buyer sells within three years from the date of purchase the credit will be recaptured. If, however, he reinvests within the required time there is no recapture. A casualty or death does not trigger a recapture.

INVESTMENT CREDIT

The investment credit is increased from seven to ten percent for eligible property acquired and placed in service after January 21, 1975, and before January 1, 1977. Purchases between January 1 and January 21 will continue to be eligible for seven percent investment credit.

Self-constructed property qualifies for the 10% investment credit for that portion completed after January 21, 1975 and before January 1, 1977.

Corporate taxpayers may qualify for 11% credit if an amount equal to one percent of the qualified investment is contributed to an employee ownership plan.

The Act increases for two years the dollar limit on the cost of used property for investment credit. The amount is increased from $50,000 to $100,000 (From $25,000 to $50,000 for a married person filing separately.) It applies for 1975 and 1976.

One permanent change was made about investment credit. It applies to eligible property that requires at least two years to complete. The investment credit is available as progress payments are made during the construction period.

LOWER CORPORATE TAX RATES

For tax years ending in 1975 the corporate surtax exemption is increased from $25,000 to $50,000 of taxable income. The tax rate on the first $25,000 of taxable income is reduced from 22 to 20 percent. The next $25,000 will be taxed at 22 percent with amounts over $50,000 taxed at 48% (22 percent "normal" tax plus 26 percent surtax).

The increase and decrease in this exemption are to be treated as changes in the tax rates in the case of fiscal-year corporations. As a result, the fiscal-year corporations will compute its tax by a proration formula based on the number of days of its tax year in 1974 and 1975.

A permanent change applies to accumulating surplus. The new law raises the accumulated surplus from $100,000 to $150,000 before becoming liable for the tax on accumulated earnings. However, as before, corporations may be able to accumulate larger amounts free of the tax if such amounts can be based on reasonable business needs.

REPLACEMENT PERIOD FOR HOME

Homeowners get six additional months in which to replace a home sold at a gain with a new home and defer the tax on the gain. This change is permanent, it extends the time from 12 to 18 months for replacing a home and from 18 to 24 months where the taxpayer constructs his new residence.

CHILD CARE DEDUCTION

The income limitations on child and dependent care deductions have been raised from $18,000 to $35,000. The full deduction will be available to taxpayers whose gross income does not exceed $35,000. This deduction, which can amount to $4,800 per year, is for expenses incurred which meet the requirements listed below:

1. You must have been gainfully employed during the period the expenses were incurred;
2. You must have maintained a household that included one or more qualifying individuals;
3. Your expenditures must have been necessary to enable you to be gainfully employed;
4. Your payments for the service must

have been to other than relatives (except cousins) or dependent members of your household; and

5. If you are married and living with your spouse, you both must have been gainfully employed (unless one of you was disabled) substantially full-time and must file a joint return.

PENSION PLAN CONTRIBUTIONS

For H.R. 10 (Keogh) Plans, a provision permits cash basis taxpayers to treat contributions made on or before the due date of his return (including extensions) as if they had been made on the last day of the taxable year to which the return relates. This provision applies to plan years beginning after December 31, 1974.

DEPLETION ALLOWANCE

The law repealed the 22 percent depletion allowances after December 31, 1974 with two exceptions as follows:
(1) The 22% depletion rate will continue to apply to regulated natural gas and gas sold under a fixed contract. (2) Small producers and royalty owners are exempt to the extent that their average daily production does not exceed 2,000 barrels or 12 million cubic feet of natural gas in 1975.

The quantity is phased down in later years. The depletion rate will also phase down. For example in 1981 the rate will be 20% and by 1984 it will reduce to 15%. There are other exclusions for producers who own or control retail outlets.

OTHER ITEMS

There are several other items in the law such as incentive payments for the employment of certain A F D C recipients. Employers hiring qualified welfare recipients as business or non-business qualify for a 20% credit for salaries. There is a $1,000 annual limitation on non-business salaries.

There are changes in taxation of foreign oil and gas. Also tax changes for utilities were included. Other miscellaneous changes were included.

See your tax accountant if you have questions or desire more information about these changes.

AMENDMENT TO HOUSING CREDIT

On June 30, 1975, President Ford signed H.R. 6900 which liberalizes the tax credit on a new home.

Under the revised rules a new home is eligible property if it was purchased at the lowest price it was offered for sale after February 28, 1975.

Under the old rules, the purchase price had to be the lowest price the home was ever offered for sale.

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