Tax Law Changes For 2013 and beyond

Although Congress averted many of the consequences of a possible tumble over the fiscal cliff with last-minute action, we would like you to be aware of the impact of the bill that was passed — known as the American Taxpayer Relief Act of 2012 — signed into law January 2.

We have compiled an overview of the key provisions of this new law. We encourage you to review them and call us if you have any concerns about how your tax situation will change as we prepare your returns for this filing season.

- **Income Tax and Capital Gains Rates in 2013 and beyond.** Although most taxpayers avoided a tax increase, rates did rise for top earners. Taxpayers (including those who receive income through partnerships and S corporations) who earn more than $400,000 ($450,000 for married taxpayers filing jointly) have a marginal tax rate of 39.6%. All other existing rates remain the same. The same individuals who are subject to the new 39.6% top rate on income now face a 20% rate on capital gains and dividends, up from 15%. Taxpayers in the 10% and 15% income brackets have a zero capital gains rate and those in the middle will continue to pay 15%.

- **New Health Care-Related Taxes.** The health care reform legislation enacted in 2010 contains tax provisions that are scheduled to take effect in 2013. As a result. a new Medicare tax of 3.8% applies to interest (tax exempt is excluded), dividends, rents, royalties and capital gains earned by taxpayers to the extent an individual's adjusted gross income exceeds $200,000 ($250,000 for married filing jointly).

- **Personal Exemptions and Itemized Deductions Phase-out Levels.** Itemized deductions (excluding investment interest, medical expenses and casualty and theft losses) and the personal exemption will be reduced for individuals with adjusted gross income exceeding $300,000 for married couples and surviving spouses and $250,000 for individuals. These itemized deductions will be reduced by 3% of the amount by which adjusted gross income exceeds these levels, and the personal exemption will be reduced by $50 for each $2,500 that the adjusted gross income exceeds these levels.

- **Permanent AMT Inflation Indexing.** After years of last-minute AMT "patches," the new law permanently indexes the AMT to inflation starting in tax year 2012. For income you earned in 2012, the exemptions are $50,600 for individuals and $78,750 for married taxpayers filing jointly.

- **Restoration of the Full Rate for Social Security and Medicare Taxes.** The law did not extend the 2% cut for the employees' portion of the Social Security payroll tax, which means it will go back to the full rate of 6.2% on income up to $113,700 in 2013.

- **Clarity on Estate and Gift Taxes.** After years of uncertainty in this area, the new law holds the estate and gift-tax exclusion at $5 million, indexed for inflation ($5.12 million in 2012). The top tax rate jumped to 40% from 35% as of January 1, 2013, but without this change, it would have soared to 55% with a $1 million exclusion amount. The act made permanent the estate tax portability election, which allows a surviving spouse to use a deceased spouse's unused exemption amount.

- **Marriage Penalty Relief Retained.** Certain taxpayers filing jointly will no longer have to worry about paying more than if they filed as single taxpayers; joint filers also will enjoy a larger standard deduction.

- **Education Tax Benefits Extended.** Many deductions for education expenses were set to expire at the end of last year, but they will remain in place under the new law. For example, the law extends the deduction for qualified education expenses through 2013 and retroactively for the 2012 tax year.

- **Conversions to Roth Retirement Plans.** The new law allows participants in an employer-sponsored 401(k) to transfer any amount to a Roth 401(k) — the funds will be taxed upon conversion.

- **Tax Relief for Mortgage Loan Modifications.** Taxpayers struggling to pay their mortgages, or whose home values have fallen below their purchase price, were given another year of tax relief on any qualifying "indebtedness income" they may receive as a result of a loan modification or short sale on their principal residence.

- **Extension of Qualified Charitable Distributions from IRAs**. The 2012 Act extended Qualified Charitable Distributions (QDCs) from Individual Retirement Accounts (IRAs) for 2012 and 2013.

We can help you understand the effect that these changes will have on your tax situation. In addition to preparing your return in a way that maximizes your tax advantages, we are also available after tax season to advise on strategies and planning decisions that will help you minimize taxes and meet your financial goals.

Please don't hesitate to contact us today at 314-962-7447 to schedule an appointment to begin discussing your options.