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TAX ALERT – January 2013

On January 1, Congress finally passed - and President Obama signed - the American Taxpayer Relief Act. This Act will prevent many tax hikes that were scheduled to go into effect this year and retain many favorable tax breaks that were scheduled to expire. **This Tax Alert is a short overview of what you need to know about the retroactive provisions for 2012 taxes** - and well as some of the many changes that will impact your 2013 taxes and also income and investments as we move into the new year. A more detailed analysis will be in our upcoming Strauss Report for Winter 2013.

It is important to note that in no way did this bill simplify taxes; in fact, many of the changes created still more forms and worksheets as well as did not generate nearly enough new income - or cut enough spending - so it is expected that the tax fight will continue in Congress for 2013 and beyond.

Here is what the new law means to you right now:

- **The 2% reduction in payroll (Social Security tax withheld from your pay)** - from 6.2% to 4.2% was allowed to expire. This means a tax hike or less take home pay for every worker - or about $100 less take home pay/month for an individual earning $100,000.
- **Unemployment Benefits** for the long term unemployed were extended through the end of 2013.
- **Tax free distributions from IRAs - given directly to charity - are now revived both for 2012 and 2013**. Because 2012 has already passed, a **special rule permits 2012 distributions taken in December 2012 and donated to charities before February 1, 2013 to count as 2012 transfers**. Another special rule permits certain **2013 IRA distributions directly transferred to a charity made by January 31, 2013 to be deemed as made on December 31, 2012.** Call us for more detail - so you get it right - if you decide to donate from your IRA this month.
- **The option to deduct State and Local Sales Taxes as itemized deductions on Schedule A** is revived for 2012 and continued through 2013.
- **The Educators Expense adjustment to income ($250)** is revived for 2012 and continued through 2013.
- **The Tuition and fees Adjustment to Income** is now revived for 2012 and continued through 2013. The big American Opportunity Tax Credit (maximum of $2500) has been extended for 5 years!
- **The Deduction for Mortgage insurance premiums** (deductible as qualified residence interest) is revived for 2012 and continued through 2013.

- **The AMT "patch" or exemption amounts have been retroactively made permanent** at $50,600 for individuals and $78,750 for joint filers. In addition, starting in 2013, it indexes these exemption amounts for inflation.
- **Energy Tax Credits have been retroactively extended for 2012 and 2013**. This means your residential energy property expenditures (including furnaces, water heaters, air conditioners and I believe insulation) are available for the 10% credit with a lifetime credit limit of $500 ($200 for windows and skylights) are available for 2012 on Form 5695 so long as you have not "used up" your lifetime credit in prior years.
- **Extended the enhanced (and refundable) Child Credit and the Earned Income Credit for five years- through tax year 2017.**
- **Estate and Gift tax provisions retained:** The exemption - now permanent - is still $5 million (indexed for inflation) and continues the portability feature that allows the first spouse to die to transfer his/her unused exclusion to the surviving spouse. The top rate for taxable estates was permanently increased from 35 to 40%. Most of us will be exempt from any estate or "death" transfer tax.

So what is happening to the rates for 2013 and beyond?

- Beginning in 2013**, the regular tax rates** will remain at 10%, 15%, 25%, 28% and 35% but with a 39.6% rate applying for income above $400,000 for Singles and $450,000 for Married Joint filers.
- Beginning in 2013, **rates for qualified dividends and long term capital gains** will remain at -0- and 15% for most of us. For higher income taxpayers (see above), these rates will permanently rise to 20%. With the new Medicare surcharge on net investment income from the new health care legislation beginning in 2013, income taxes on the **excess** investment income if AGI is over $200,000 ($250,000 Married Jointly) would rise to 18.8% for Singles and 23.8% for Married jointly. Net investment income is defined as:

  Interest, dividends, annuities, royalties, and rents

  Income from a business in which the taxpayer does not personally, materially participate, and business income from trading and financial instruments or commodities

  Capital gains and other net gains from the sale of property

- **Phase-outs are back beginning in 2013**. Both the limitations on itemized deductions and personal exemptions which had previously been suspended, have been reinstated - with a starting threshold of $300,000 for joint filers and $250,000 for single taxpayers.
- Beginning in 2013, a **Medicare surtax of .9 percent** will be applied for wages and self-employment income over $200,000 for Singles and $250,000 combined for Married jointly. This may or may not be withheld by your employer and we will need to review earned income of both spouses at tax time if see if this applies to you in 2013.