Overview of the tax provisions in the 2012 American Taxpayer Relief Act (1/2/2013)

The recently enacted 2012 American Taxpayer Relief Act is a sweeping tax package that includes, among many other items, permanent extension of the Bush-era tax cuts for most taxpayers, revised tax rates on ordinary and capital gain income for high-income individuals, modification of the estate tax, permanent relief from the AMT for individual taxpayers, limits on the deductions and exemptions of high-income individuals, and a host of retroactively resuscitated and extended tax breaks for individual and businesses. Here's a look at the key elements of the package:

- *Tax rates.* For tax years beginning after 2012, the 10%, 15%, 25%, 28%, 33% and 35% tax brackets reflecting the Bush tax cuts will remain in place and are made permanent. This means that, for most Americans, the tax rates will stay the same. However, there will be a new 39.6% rate, that will apply for income over: $400,000 (single), $425,000 (head of households), $450,000 (joint filers and qualifying widow(er)s), and $225,000 (married filing separately). These dollar amounts will be inflation-adjusted for tax years after 2013.
- *Estate tax.* The new law prevents steep increases in estate, gift and generation-skipping transfer (GST) tax that were slated to occur for individuals dying and gifts made after 2012 by permanently keeping the exemption level at $5,000,000 (as indexed for inflation). However, the new law also permanently increases the top estate, gift, and GST rate from 35% to 40% It also continues the portability feature that allows the estate of the first spouse to die to transfer his or her unused exclusion to the surviving spouse. All changes are effective for individuals dying and gifts made after 2012.
- *Capital gains and qualified dividends rates.* The new law retains the 0% tax rate on long-term capital gains and qualified dividends, modifies the 15% rate, and establishes a new 20% rate. Beginning in 2013, the rate will be 0% if income falls below the 25% tax bracket; 15% if income falls at or above the 25% tax bracket but below the new 39.6% rate; and 20% if income falls in the 39.6% tax bracket. It should be noted that the 20% top rate does not include the new 3.8% surtax on investment-type income and gains for tax years beginning after 2012, which applies on investment income above $200,000 (single) and $250,000 (joint filers) in adjusted gross income. So actually,

the top rate for capital gains and dividends beginning in 2013 will be 23.8% if income falls in the 39.6% tax bracket. For lower income levels, the tax will be 0%, 15%, or 18.8%.

- *Personal exemption phaseout.* Beginning in 2013, personal exemptions will be phased out (i.e., reduced) for adjusted gross income over $250,000 (single), $275,000 (head of household) and $300,000 (joint filers). Taxpayers claim exemptions for themselves, their spouses and their dependents. Last year, each exemption was worth $3,800.
- *Itemized deduction limitation.* Beginning in 2013, itemized deductions will be limited for adjusted gross income over $250,000 (single), $275,000 (head of household) and $300,000 (joint filers).
- *AMT relief.* The new law provides permanent alternative minimum tax (AMT) relief. Prior to the Act, the individual AMT exemption amounts for 2012 were to have been $33,750 for unmarried taxpayers, $45,000 for joint filers, and $22,500 for married persons filing separately. Retroactively effective for tax years beginning after 2011, the new law permanently increases these exemption amounts to $50,600 for unmarried taxpayers, $78,750 for joint filers and $39,375 for married persons filing separately. In addition, for tax years beginning after 2012, it indexes these exemption amounts for inflation.
- *Tax credits for low to middle wage earners.* The new law extends for five years the following items that were originally enacted as part of the 2009 stimulus package and were slated to expire at the end of 2012: (1) the American Opportunity tax credit, which provides up to $2,500 in refundable tax credits for undergraduate college education; (2) eased rules for qualifying for the refundable child credit; and (3) various earned income tax credit (EITC) changes.
- *Cost recovery.* The new law extends increased expensing limitations and treatment of certain real property as Code Section 179 property. It also extends the bonus depreciation provisions with respect to property placed in service after Dec. 31, 2012.
- *Tax break extenders.* Many of the "traditional" tax extenders are extended for two years, retroactively to 2012 and through the end of 2013. Among many others, the extended provisions include the election to take an itemized deduction for state and local general sales taxes in lieu of the itemized deduction for state and local income taxes, the $250 above-the-line deduction for certain expenses of elementary and secondary school teachers, and the research credit.
- *Pension provision.* For transfers after Dec. 31, 2012, in tax years ending after that date, plan provision in an applicable retirement plan (which includes a qualified Roth contribution program) can

allow participants to elect to transfer amounts to designated Roth accounts with the transfer being treated as a taxable qualified rollover contribution.

- *Payroll tax cut is no more.* The 2% payroll tax cut was allowed to expire at the end of 2012.

I hope this information is helpful. If you would like more details about these provisions or any other aspect of the new law, please do not hesitate to call.zz