

What the New Tax Law Means for You

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- ▶ Despite the name of the new federal tax law (American Taxpayer Relief Act of 2012), it neither relieved the existing tax burden Americans incur nor was it passed into law in 2012 (it was actually signed into law shortly after we fell over "the fiscal cliff").
- ▶ All workers who pay into the Social Security system are paying a 2% higher tax in 2013 than in 2012 and higher earners will pay meaningfully more taxes as outlined in this article.

As you prepare to file your 2012 tax returns, your tax burden may be top of mind. If you are presently working, you probably have already seen the impact of higher taxes in your recent paychecks. Despite statements from Congressional leaders that taxes were raised on the "rich," however defined, in reality, if you pay into the Social Security system, your taxes increased by 2% with the advent of the New Year.

The American Taxpayer Relief Act of 2012, signed into law on January 2, not only increased taxes on nearly every wage earner, but also increased the complexity of the federal tax code, despite ongoing pronouncements from Congress that simplifying the tax code remains a goal.

Taxes Increased for Workers

If you work and contribute to the Social Security system through the FICA tax, your tax increased as of January 1 from 4.2% to 6.2% on the first \$113,700 in wages. This tax, frequently called the "payroll tax," had been reduced by 2% for 2011 and 2012 in an effort to reduce workers' tax burden.

However, the Social Security system has been woefully underfunded for years, so it did not make practical sense, from the perspective of the Social Security system, to reduce the tax revenue that supports the system. This 2% tax increase beginning in 2013 has a marginally negative impact on the economy since consumers will now have less money available for consumption.

Taxes Increased for Higher Earners

In addition to the 2% payroll tax increase imposed on workers, those with higher incomes will pay more taxes this year.

For adjusted gross income in excess of \$200,000 for individuals and \$250,000 for couples, filing jointly, the Patient Protection and Affordable Care Act, which was passed in 2010 and is commonly referred to as Obamacare, imposes a 3.8% Medicare tax beginning in 2013 on the lesser of all net investment income or

the income in excess of the threshold. (The details of the calculation are beyond the scope of this article.) An additional 0.9% Medicare surtax is imposed on wages and self-employment income above the same \$200,000 and \$250,000 thresholds, respectively.

For adjusted gross income in excess of \$250,000 for individuals and \$300,000 for couples, filing jointly, you will incur the tax changes indicated above, plus limitations on itemized deductions and a phase out of personal exemptions. For 2012, limitations on itemized deductions and the phase out of personal exemptions had been suspended, but are now reinstated for 2013, which effectively increase the taxes you will pay at this income level.

And finally, for taxable income in excess of \$400,000 for individuals and \$450,000 for couples, filing jointly, you will be impacted by the taxes, limitations, and phase outs already reviewed, plus the following tax increases in 2013: (1) marginal federal income tax rate increases from 35% to 39.6%; (2) long-term federal capital gain tax rate increases from 15% to 20%; and (3) qualified federal dividend income tax rate increases from 15% to 20%.

Other Changes

A variety of other changes were also made as part of the American Taxpayer Relief Act, including (1) a permanent fix for the Alternative Minimum Tax (AMT) exemption amount so that it is automatically indexed for inflation and (2) the federal estate tax exemption was maintained at \$5 million per individual, indexed to inflation (\$5.25 million for 2013), but the federal estate tax rate was increased from 35% to 40%.

This is just a summary of some of the tax changes that have been imposed. Contact us or your tax preparer to determine how these changes impact your situation.