In the early morning hours of Jan. 1, 2013, the Senate, by a vote of 89-8, passed H.R.8, the "American Taxpayer Relief Act" (the 2012 Taxpayer Relief Act). Late on that same day—hours after the government had technically gone over the "fiscal cliff"—the House of Representatives, by a vote of 257 to 167, also passed the bill. The 2012 Taxpayer Relief Act, prevents many of the tax hikes that were scheduled to go into effect this year and retain many favorable tax breaks that were scheduled to expire. However, it also increases income taxes for some high-income individuals and slightly increases transfer tax rates. Below, is an overview of the 2012 Taxpayer Relief Act's key provisions.

Tax rates

For most individuals, the legislation permanently extends the lower federal income tax rates that have existed for the last decade. That means most taxpayers will continue to pay tax according to the same six tax brackets (10%, 15%, 25%, 28%, 33%, and 35%) that applied for 2012. The top federal income tax rate, however, will increase to 39.6% beginning in 2013 for individuals with income that exceeds $400,000 ($450,000 for married couples filing joint returns).

Generally, lower tax rates that applied to long-term capital gain and qualifying dividends have been permanently extended for most individuals as well. If you're in the 10% or 15% marginal income tax bracket, a special 0% rate generally applies. If you are in the 25%, 28%, 33%, or 35% tax brackets, a 15% maximum rate will generally apply. Beginning in 2013, however, those who pay tax at the higher 39.6% federal income tax rate (i.e., individuals with income that exceeds $400,000, or married couples filing jointly with income that exceeds $450,000) will be subject to a maximum rate of 20% for long-term capital gain and qualifying dividends.

Alternative minimum tax (AMT)

The AMT is essentially a parallel federal income tax system with its own rates and rules. The last temporary AMT "patch" expired at the end of 2011, threatening to dramatically increase the number of individuals subject to the AMT for 2012. The American Taxpayer Relief Act permanently extends AMT relief, retroactively increasing the AMT exemption amounts for 2012, and providing that the exemption amounts will be indexed for inflation in future years. The Act also permanently extends provisions that allowed nonrefundable personal income tax credits to be used to offset AMT liability.

2012 AMT Exemption Amounts

	Before Act	After Act
Married filing jointly	**$45,000**	**$78,750**
Unmarried individuals	**$33,750**	**$50,600**
Married filing separately	**$22,500**	**$39,375**

Estate tax

The Act makes permanent the $5 million exemption amounts (indexed for inflation) for the estate tax, the gift tax, and the generation-skipping transfer tax--the same exemptions that were in effect for 2011 and 2012. The top tax rate, however, is increased to 40% (up from 35%) beginning in 2013.

The Act also permanently extends the "portability" provision in effect for 2011 and 2012 that allows the executor of a deceased individual's estate to transfer any unused exemption amount to the individual's surviving spouse.

Phaseout or limitation of itemized deductions and personal exemptions

In the past, itemized deductions and personal and dependency exemptions were phased out or limited for high-income individuals. Since 2010, neither itemized deductions nor personal and dependency exemptions have been subject to phaseout or limitation based on income, but those provisions expired at the end of 2012.

The new legislation provides that, beginning in 2013, personal and dependency exemptions will be phased out for those with incomes exceeding specified income thresholds. Similarly, itemized deductions will be limited. For both the personal and dependency exemptions phaseout and the itemized deduction limitation, the threshold is $250,000 for single individuals ($300,000 for married individuals filing joint federal income tax returns).

Other expiring or expired provisions made permanent

·"Marriage penalty" relief in the form of an increased standard deduction amount for married couples and an expanded 15% federal income tax bracket;

·Expanded tax credit provisions relating to the dependent care tax credit, the adoption tax credit, and the child tax credit; and

·Higher limits and more generous rules of application relating to certain education provisions, including Coverdell education savings accounts, employer-provided education assistance, and the student loan interest deduction;

Temporary extensions

·Provisions relating to increased earned income tax credit amounts for families with three or more children are extended through 2017;

·American Opportunity credit provisions relating to maximum credit amount, refundability, and phaseout limits are extended through 2017;

·The $250 above-the-line tax deduction for educator classroom expenses, the limited ability to deduct mortgage insurance premiums as qualified residence interest, the ability to deduct state and local sales tax in lieu of the itemized deduction for state and local income tax, and the deduction for qualified higher education expenses are all extended through 2013;

·Charitable IRA distributions (IRA holders over age 70½ are able to exclude from income up to $100,000 in qualified distributions made to charitable organizations) are extended through 2013; (*special rules apply for the 2012 tax year*)

·Exclusion of qualified mortgage debt forgiveness from income provisions extended through 2013;

·Exclusion of 100% of the capital gain from the sale of qualified small business stock extended to apply to stock acquired before January 1, 2014;

·50% bonus depreciation and expanded Section 179 expense limits extended through 2013;

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

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