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ESTATE PLANNING NEWS & UPDATES:
POTENTIAL TAX ISSUES FOR 2013

Greetings! The waning daylight, falling snow and debating politicians means a new year will soon be upon us, so we at Manley & Brautigam wanted to take the time to alert you to some potential tax issues as 2012 draws to a close. We know that the hustle and bustle at this time of year does not always afford the time for estate and tax planning, but paying attention to these issues could be well worth your time.

Year end tax planning is always complicated by the uncertainty that the following year may bring and 2013 is no exception. This may be the most challenging year in a while because of the expiration of the extension of the Bush-era tax cuts and the imposition of more than 21 new or higher new taxes by the Obama administration. Thus, 2012 year end tax planning has become even more challenging and important.

Potential 2013 Tax Issues
Investment Income
Capital Gains and Dividends
Estate/Gift Tax
3.8% Medicare Surtax
Medicare Tax
Individual Mandate Tax
Employer Mandate Tax
Investment Income Surtax
Medical Devices
Health Insurance Plan Excise Tax
Alternative Minimum Tax
The Medicine Cabinet Tax
Medical Itemized Deduction Increase
The Flexible Spending Account (FSA) Cap
Health Savings Account (HSA) Withdrawal Tax
American Opportunity Tax Credit
Coverdell Education Savings Accounts
Bonus Depreciation

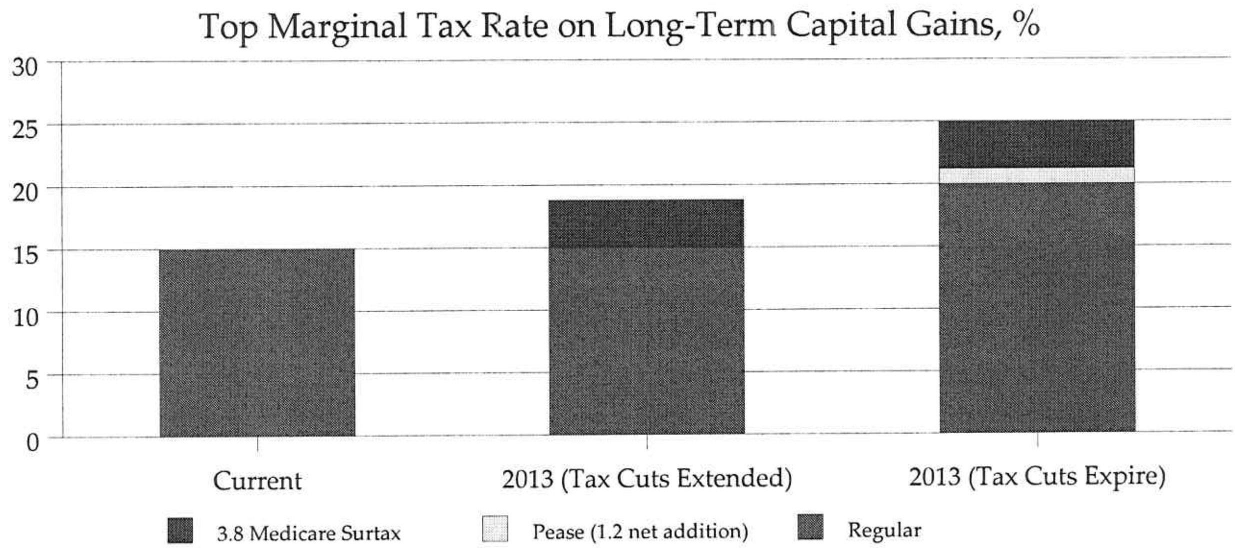
Manley & Brautigam wants to tell you and your family and/or business about some of these changes that are coming. Under the current administration's tax policy, we can expect to see the following new taxes and tax rate increases taking effect after 2012.

General Income Tax

1. Investment Income Taxes. With the expiration of the current tax laws, the tax rates on qualified capital gains will increase from 15% to 20%. Dividends, currently taxed at 15%, will be taxed at normal ordinary income tax rates, as high as 39.6%. In addition, for those earning more than $250,000 if filing jointly, $125,000 if married and filing separately or $200,000 for all other filing statuses, the capital gains tax rate will increase to 23.8% and the

dividend income tax rate will raise to 43.4% due to the Medicare Surtax. Finally, the limitation on itemized deductions (Pease) which cuts itemized deductions by 3% of adjusted gross income above specified thresholds and the personal exemption phaseout (PEP) which reduces the value of each personal exemption by 2% for each $2,500 above specified thresholds are set to expire with the Bush-era tax cuts as well.

2. Estate/Gift Tax. The federal estate and gift tax through 2012 is set at a maximum rate of 35%



with a $5.12 million exemption. Without an extension the maximum rate will return to 55% with a $1 million exemption.

"Obamacare" Taxes

With the passage of The Patient Protection and Affordable Care Act ("Obamacare") and its implementation in 2014, you can expect to see the following taxes:

3. Medicare Surtax 3.8%. Starting January 1, 2013, a new 3.8% "unearned income Medicare contribution" tax on higher income individuals, estates and trusts is imposed. The Medicare Surtax is one of the most important new areas of concern. It will be imposed on the taxpayer's "net investment income" (NII) and will generally apply to passive income.[1] The Medicare surtax also will apply to capital gains from the disposition of property.[2] It

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[1] "Net investment income" includes interest, dividends, royalties, annuities, rents, income from passive business activities, income from trading in financial instruments or commodities, and gains from assets held for investment like stock and other securities. (Gains from assets held for business purposes are not subject to the extra tax.)

[2] The sale of a primary residence will continue to excluded from gross income in the amounts of $250,000 for single filers and $500,000 for joint filers under Internal Revenue Code § 121.

will not apply to income derived from a trade or business, or from the sale of property used in a trade or business. For individuals, the Medicare Surtax will apply to the lesser of the taxpayer's NII or the amount of the "modified" adjusted gross income.

4. <u>Medicare Tax</u>. Starting January 1, 2013, Employers will be required to withhold an additional 0.9% Medicare Tax on high-income taxpayers whose compensation is in excess of the $250,000/$125,000/$200,000 threshold.

5. <u>The Individual Mandate Tax</u>. Starting in 2014, anyone not buying "qualifying" health insurance must pay an income surtax between 1% and 2.5% of adjusted gross income above the applicable threshold for filing taxes for that year. Thus, in 2014 a married couple will pay the higher of a base tax of $285 per year, or 1.0% of adjusted growth income above the threshold. This is the lowest base tax and will rise to $695 per adult and $347.50 per child (up to $2,085 for a family) or 2.5% of AGI above the threshold by 2016.

6. <u>The Employer Mandate Tax</u>. Starting in 2014, a new tax is imposed on employers with 50 or more employees who do not provide health insurance for their employees. The tax imposed on the employer is equal to $2,000 for each full-time employee, and can increase to $3,000 under certain facts. If an employer offers insurance but requires a waiting period to enroll in coverage of 30-60 days, there is a $400 tax per employee ($600 if the period is 60 days or longer).

7. <u>The Investment Income Surtax</u>. Effective January 1, 2013, for those earning more than the $250,000/$125,000/$200,000 threshold, the capital gains tax rate will increase from 15% to 23.8%, the dividend income tax rate will raise from 15% to 43.4%. In addition, for those with earnings from Sub-S corporations, the tax rate on "other investment income" will rise from 35% to 43.4%.

8. <u>Medical Devices</u>. Effective January 1, 2013, a new "Medical Device Manufacturers" excise tax of 2.3% is imposed on the U.S. sales of all medical devices retailing for more than $100.

9. <u>Health Insurance Plan Excise Tax</u>. Also known as the "Cadillac" Health Insurance Plan Tax, this new 40% excise tax is imposed on employers that provide extensive (too much) health insurance and pay all or part of the premium for its employees. This is effective in 2018 because most unionized workers are covered by plans that fall under this definition and a deferral was made to spare union members from this tax for at least a period of time.

10. <u>Charitable Hospital Excise Tax</u>. A $50,000 excise tax on charitable hospitals that fail to meet new "community health assessment needs," "financial assistance" and other rules set by the Health and Human Services Dept.

11. Alternative Minimum Tax. Each year a taxpayer must pay the greater of an Alternative Minimum Tax (AMT) or regular tax, therefore the AMT should be examined to determine a taxpayer's potential liability. Congress has not yet enacted a "patch" for 2012.

2013 Tax Parameters

Taxable Income Over	Taxable Income But Not Over	Pre-2011 (Bush Tax Cuts Expire)	Obama Proposal (FY 2013 Budget)	Romney Proposal	Current Policy (Bush Tax Cuts in Place)
Single					
0	8,900	0.15	0.10	0.08	0.10
8,900	36,150	0.15	0.15	0.12	0.15
36,150	87,550	0.28	0.25	0.20	0.25
87,550	182,600	0.31	0.28	0.224	0.28
182,600	212,850	0.36	0.33	0.264	0.33
212,850	397,000	0.36	0.36	0.264	0.33
397,000	---	0.396	0.396	0.28	0.35
Married Filing Jointly					
0	17,800	0.15	0.10	0.08	0.10
17,800	60,350	0.15	0.15	0.12	0.15
60,350	72,300	0.28	0.15	0.12	0.15
72,300	145,900	0.28	0.25	0.20	0.25
145,900	222,300	0.31	0.28	0.224	0.28
222,300	266,100	0.36	0.33	0.264	0.33
266,100	397,000	0.36	0.36	0.264	0.33
397,000	---	0.396	0.396	0.28	0.35
Head of Household					
0	12,700	0.15	0.10	0.08	0.10
12,700	48,400	0.15	0.15	0.12	0.15
48,400	125,000	0.28	0.25	0.20	0.25
125,000	202,450	0.31	0.28	0.224	0.28
202,450	239,500	0.36	0.33	0.264	0.33
239,500	397,000	0.36	0.36	0.264	0.33
397,000	---	0.396	0.396	0.28	0.35

Source: The Tax Policy Center; http://www.taxpolicycenter.org/taxtopics/2012-Election-CompareRates-2013.cfm

12. Payroll Tax Holiday. The Old-Age, Survivors, and Disability Insurance taxes which fund Social Security have been reduced from 6.2% to 4.2% for the past two years. On January 1,

2013, the employee share of these taxes is set to revert back to 6.2% causing an estimated $95 billion increase in 2013 alone.

13. The "Medicine Cabinet Tax." This new tax took effect in 2011, and prohibits reimbursement of expenses for over-the-counter medicine (except insulin) from an employees pre-tax dollar funded Health Saving Account (HSA), Flexible Spending Account (FSA) or Health Reimbursement Account (HRA). This provision hurts middle class earners particularly hard since they earn enough to actually pay federal taxes, but not enough to make this restriction negligible.

14. Medical Itemized Deduction Increase. Currently, one can deduct excess medical expenses if they are greater than 7.5% of adjusted gross income (AGI). Effective 01/01/2013, the amount is increased to 10% of AGI. For example: consider a family with AGI of $80,000 and $8,000 of medical expenses. Currently, that family can get some relief from being able to take a $2,000 deduction (7.5% X $80,000 = $6,000; $8,000 –$6,000 = $2,000). The increase to 10% will eliminate the deduction; and if that family pays at a 25% federal tax rate, the real cost of that lost deduction would be $500.

15. The Flexible Spending Account (FSA) Cap. Effective January 1, 2013, there is a new cap of $2,500 per year (which is now unlimited) on the amount of pre-tax dollars that could be deposited into a FSA. This impacts many, but especially those who currently use those accounts to pay for special needs education for special needs children. Tuition rates for this type of special education can easily exceed $14,000 per year and the use of pre-tax dollars helps many middle income families.

16. Health Savings Account (HSA) Withdrawal Tax Hike. Effective, January 1, 2013, the additional tax on non-medical early withdrawals from an HSA increases from 10% to 20%.

17. Additional and Miscellaneous Taxes.

- Elimination of the tax deduction for employer-provided prescription drug coverage for Medicare recipients.

- A $60 billion tax on health insurers.

- A $2.4 billion tax on the paper industry to control a pollutant known as black liquor.[3]

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[3] "Black liquor" is a byproduct of the wood-pulping process at paper mills. The companies have burned black liquor to generate power since the 1930s.

- A $2.3 billion-a-year tax on drug companies.

- Indoor Tanning Services Tax. Effective in 2010, a new 10% excise tax on people using tanning salons.

Education

1. American Opportunity Tax Credit. The American Opportunity Tax Credit ("AOTC") was extended by the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 and currently provides a maximum credit of $2,500 for expenses incurred for the first four years of post-secondary education. The Hope education credit is available if the AOTC is not extended but is a less generous credit that only applies to expenses related to the first two years of postsecondary education.

2. Coverdell Education Savings Accounts. Currently, the maximum annual contribution to a Coverdell ESA is $2,000 and unless this is extended past 2012, the annual contribution will drop to $500.

Business Property

3. Bonus Depreciation. In order to encourage economic growth, a special 50% first year bonus depreciation allowance is provided for qualified property. This bonus is set to expire in 2012.

4. Code Sec. 179 Expensing. Code Sec. 179 allows a taxpayer to deduct the cost of qualified property as an expense, rather than requiring the cost of the property to be capitalized and depreciated. The limitation for 2012 is $139,000 with a $560,000 investment ceiling on all other qualifying property. In 2013, these limits are set to drop to a $25,000 limitation and a $200,000 ceiling.

As you can see, these changes are extensive and can have major effects on the financial situation of yourself, your business, your trust or your estate. If they are going to affect you, please do not hesitate in contacting us and setting up a consultation. Time is getting short. In all honesty, new taxes means more work for us. But as one person said, "let's stop talking about new taxes and start talking about creating more taxpayers with higher incomes."

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