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The American Taxpayer Relief Act of 2012 makes permanent many otherwise expiring tax provisions. The following is my summary of what I believe to be relevant provisions:

Ordinary income above a certain threshold is taxed at a higher rate. The thresholds are: taxable income of $400,000 (for an unmarried taxpayer), $425,000 (for a head of household), and $450,000 (for a taxpayer who is married and filing jointly).

The new law extends the current maximum 15% tax rate on long-term capital gains and qualified dividends for individuals who have taxable income up to $400,000 (for a unmarried taxpayer), $425,000 (for a head of household), and $450,000 (for a taxpayer who is married and filing jointly). For capital gain and dividend income above the applicable threshold, the rate increases to 20%. With the new 3.8% Medicare surtax for unmarried and head of household taxpayers with modified adjusted gross income ("MAGI") over $200,000 and married taxpayers with MAGI over $250,000, the capital gain and qualified dividend rate has become more complex.

The 3.8% "Medicare surtax" effective January 1, 2013, under the health care reform law passed in 2010 is still being deployed. This new tax applies to certain types of investment income for unmarried taxpayers with MAGI above $200,000 and married couples above $250,000. The tax applies to the lesser of the individual's net investment income or MAGI in excess of the threshold amounts. In addition, high-income earners will be subject to an additional payroll tax of 0.9% on wages received in excess of those threshold amounts.

The $5 million estate, gift and generation-skipping transfer ("GST") tax exemptions are now permanent and adjusted for inflation from 2011. It also makes permanent the "portability" provision between spouses, which allows a surviving spouse to use a deceased spouse's unused exemption on lifetime gifts and/or transfers at death. GST exemption, however, is not portable. For 2013, the exemption amount is projected to be $5.25 million. The Act sets the rate for all transfers in excess of the exemption amount (for all three taxes) at 40%. The federal credit for state death taxes is now permanently repealed. However, an estate may continue to deduct state estate or inheritance taxes for purposes of computing the federal estate tax. A variety of beneficial GST tax provisions that were scheduled to expire have been made permanent, including the automatic allocation of a taxpayer's GST exemption to certain transfers, provisions permitting the "qualified severance" of a trust into two trusts, one of which is exempt from the GST tax and one of which is not; and relief for a late allocation of GST exemption.

The alternative minimum tax ("AMT") patch, which historically had been passed each year by Congress to lessen the burden of AMT on millions of middle-income households is now permenant and will be adjusted for inflation. Under the Act, the AMT exemption amount for 2012 is $50,600 for unmarried taxpayers and heads of household, $78,750 for taxpayers who are married and filing jointly, and it is indexed for inflation going forward. The 2013 exemption amounts are projected to be $51,900 for unmarried taxpayers and heads of household, and $80,750 for married taxpayers filing jointly.

The personal exemption phase-out ("PEP") provision, which had been suspended under prior law, returns under the Act. It phases out the personal exemption for taxpayers with adjusted gross income ("AGI") over $250,000 (for an unmarried taxpayer), $275,000 (for a head of household), and $300,000 (for a taxpayer who is married and filing jointly).

In the past, a law known as the "Pease provision" limited itemized deductions for high-income taxpayers. The Pease provision was suspended for 2010 through 2012, which allowed taxpayers to deduct 100% of their itemized deductions regardless of their income (subject to other applicable restrictions). The Act reinstates the Pease provision for taxpayers with AGI above the following thresholds: $250,000 (for an unmarried taxpayer), $275,000 (for a head of household), and $300,000 (for a taxpayer who is married and filing jointly). The Pease provision phases out itemized deductions by the lesser of (i) 3% of the excess of AGI over the threshold or (ii) 80% of the otherwise allowable deductions. While the Act did not directly address the mortgage interest or charitable deductions, the Pease provision has the effect of limiting the amount of these deductions that a taxpayer may take if his or her income exceeds the applicable threshold.

The payroll tax "holiday" enacted in 2010 has been allowed to expire. Under the payroll tax holiday, the 6.2% social security tax paid by all wage earners was temporarily cut to 4.2%. The expiration of the holiday will cause wage earners to pay 2% more in social security taxes on all wages up to $113,700.

The Act extends the ability of a taxpayer to exclude from income gain on the sale of certain qualified small business stock ("QSBS"), as long as the stock was held for more than five years before sale. The exclusion is generally 50%, but was increased to 75% for QSBS acquired after February 17, 2009, and before September 28, 2010; and to 100% for QSBS acquired after September 27, 2010, and before January 1, 2012. The Act extends the 100% gain exclusion to QSBS acquired after September 27, 2010 and before January 1, 2014. Note that the QSBS exclusions are generally limited to the greater of (i) $10 million of gain or (ii) ten times the taxpayer’s cost basis in the stock sold in that year. In addition, gain subject to the 100% exclusion rule is not a preference item for alternative minimum tax purposes.

The Act extends the ability of a taxpayer age 70½ or older to exclude up to $100,000 from gross income for distributions made directly from a traditional or Roth IRA to a qualified charity. This provision expired after 2011; it is now extended for 2012 and 2013. The Act contains two time-sensitive provisions giving taxpayers flexibility with respect to the 2012 tax year. First, if a taxpayer took a required minimum distribution ("RMD") in December of 2012, he or she can elect to treat some or all of that RMD as a qualified charitable contribution to the extent that the distribution (up to $100,000) is transferred in cash to a qualifying charitable organization before February 1, 2013, and meets the other charitable rollover requirements. Second, a qualified charitable contribution made in January of 2013 may be treated as having been made on December 31, 2012.

Pease provision applied to charitable contributions. As described above, the Pease provision may limit the value of the charitable contribution deduction to a high-income taxpayer. Specifically, the Pease provision phases out the income tax deduction for a charitable gift by the lesser of (i) 3% of the excess of AGI over the threshold level of $250,000 (for an unmarried taxpayer), $275,000 (for a head of household) or $300,000 (for a married taxpayer filing jointly), or (ii) 80% of the otherwise allowable deduction. (As noted above, the Pease provision also applies to most other itemized deductions.) The threshold levels are indexed for inflation. The threshold amounts in the Act are a taxpayer-favorable increase from the law previously scheduled to apply in 2013 (under which a threshold of only $174,450 was projected to apply to most individuals and married couples).

Property contributed for conservation purposes. A donor's deduction for a charitable gift of long-term capital gain property is generally limited to 30% of the donor's AGI. However, for the years 2006 through 2011, a special provision allowed a deduction of up to 50% of the donor's AGI for contributions of "qualified conservation property." The Act extends this provision through December 31, 2013.

Regards

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