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## CONGRESS PASSED BILL AVERTS FISCAL CLIFF TAX CONSEQUENCES



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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" (ATRA). 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. On January 2nd 2013, President Barack Obama has signed a bill that boosts taxes on the wealthiest Americans, while preserving tax cuts for most American households.

The bill, which averts a looming fiscal cliff that had threatened to plunge the nation back into recession, also extends expiring jobless benefits, prevents cuts in Medicare reimbursements to doctors and delays for two months billions of dollars in across-the-board spending cuts in defense and domestic programs.

### Highlights of the Act are as under:

#### Individual Tax Provisions-

#### Individual Income Tax Rates

ATRA permanently retains the 10%, 15%, 25%, 28%, and 33% income tax brackets. The 35% tax bracket ends at \$400,000 for single filers. Above this threshold, there's a new 39.6% tax bracket. Thresholds for the new 39.6% bracket for 2013 will be:

- Married Filing Jointly : \$450,000 of taxable income,
- Qualifying Widow(er) : \$450,000 of taxable income,
- Head of Household : \$425,000 of taxable income,
- Single : \$400,000 of taxable income,
- Married Filing Separately : \$225,000 of taxable income.

#### Capital Gains/Dividends

ATRA permanently retains the 0% and 15% tax rates on qualified dividends and long-term capital gains, and adds a new 20% tax rate that would apply to taxpayers who fall within the new 39.6% tax bracket. The new capital gains tax rates for 2013 and future years will be as follows:

- 0% for a person in the 10% and 15% tax brackets,
- 15% for a person in the 25%, 28%, 33%, or 35% tax brackets, and
- 20% for a person in the 39.6% tax bracket. When accounting for Code Sec. 1411's 3.8% surtax on investment-type income and gains for tax years beginning after 2012, the overall rate for higher-income taxpayers will be 23.8%

Qualified dividends for all taxpayers continue to be taxed at capital gains rates, rather than ordinary income tax rates as prior to 2003.

#### Alternative Minimum Tax (AMT)

ATRA provides the following AMT exemption amounts for 2012:

- Married Filing Jointly : \$78,750
- Qualifying Widow(er) : \$78,750
- Single : \$50,600
- Head of Household : \$50,600
- Married Filing Separately : \$39,375

These threshold amounts would be indexed for inflation for years after 2013.

#### Estate Tax Rates

ATRA permanently extends the \$5 million exclusion, indexed to inflation, and unified exemption amount with portability. The new top tax rate for estates is 40%.

### Limitations on Deductions and Exemptions

**Itemized Deductions** will be limited. The total amount of itemized deductions that are allowable as a deduction will be reduced by the lesser of 3% of the taxpayer's adjusted gross income (AGI) over the threshold amount or by 80% of otherwise allowable itemized deductions.

Similarly, **Personal Exemptions** will be limited. Taxpayers would see their total personal exemptions reduced by two percent for each \$2,500 (or fraction thereof) by which adjusted gross income exceeds the threshold.

The threshold amounts beyond which itemized deductions and personal exemptions would start to reduce, as mentioned above are as follows:

- Married Filing Jointly : \$300,000 of AGI
- Qualifying Widow(er) : \$300,000 of AGI
- Head of Household : \$275,000 of AGI
- Single : \$250,000 of AGI
- Married Filing Separately : \$150,000 of AGI

These threshold amounts would be indexed for inflation for years after 2013.

### Other Individual Tax Deductions

- The student loan interest deduction is permanently extended. ATRA eliminates the rule that the deduction can be claimed only during the first 60 months of repayment.
- The classroom expenses deduction of up to \$250 is temporarily extended through the end of 2013.
- Mortgage insurance premiums will continue to be deductible as part of the mortgage interest deduction through the end of 2013.
- The sales taxes deduction, in lieu of a deduction for state income taxes, is temporarily extended through the end of 2013.
- The charitable deduction for contributing real property for qualified conservation purposes is temporarily extended through the end of 2013.
- The above-the-line tuition and fees deduction is temporarily extended through the end of 2013.

### Various Individual Tax Credits

- The child tax credit remains unchanged and is permanently extended. The maximum amount of the child tax credit is \$1,000, and the credit is partially refundable. However, the provision reduces the earnings threshold for the refundable portion of the child tax credit to \$3,000 will expire at the end of 2017.
- The dependent care tax credit remains unchanged and is permanently extended. Day-care expenses up to \$3,000 for one child and \$6,000 for two or more children qualify for the tax credit, and these amounts are not indexed for inflation.
- The adoption credit is permanently extended. The credit is worth up to \$10,000 (indexed for inflation).
- Also permanently extended is the earned income tax credit for families with three or more dependents.
- The American opportunity tax credit is extended temporarily through the end of 2017.

### Business Tax Provisions-

Many popular but temporary tax extenders relating to businesses are included in the American Taxpayer Relief Act.

#### Code Sec 179 - Small Business Expensing

The American Taxpayer Relief Act extends through 2013, enhanced Code Sec. 179 small business expensing. The Code Sec. 179 dollar limit for tax years 2012 and 2013 is \$500,000 with a \$2 million investment limit. The rule allowing off-the shelf computer software is also extended.

#### Bonus Depreciation

The American Taxpayer Relief Act extends 50 percent bonus depreciation through 2013. Some transportation and longer period production property is eligible for 50 percent bonus depreciation through 2014.

#### Research Tax Credit

The American Taxpayer Relief Act extends through 2013, the Code Sec. 41 Research Tax Credit, which expired after 2011. The incentive rewards taxpayers that engage in qualified research activities with a tax credit.

### Work Opportunity Tax Credit

The American Taxpayer Relief Act extends through 2013, the Work Opportunity Tax Credit (WOTC), which rewards employers that hire individuals from targeted groups with a tax credit.

### More Business Tax Extenders

A number of other business tax extenders expire after 2011 and they are extended through 2013 under the American Taxpayer Relief Act. They include among others-

- New Market Tax Credit
- Employer Wage credit for activated military reservists
- Subpart F Exception for active financing income.
- Look through rule for related controlled foreign corporation payments
- Rail Road track maintenance credit.
- Seven Year recovery period for motorsports entertainment complexes.
- 100 percent exclusion for gain on sale of qualified small business stock.
- Reduced the recognition period for S corporation built-in gains tax
- Enhanced deduction for charitable contributions of food inventory.
- Tax incentives for empowerment zones
- Indian employment credit
- Accelerated depreciation for business property on Indian reservations.
- Special expensing rules for qualified film and television productions.
- Mind rescue team training credit.
- Election to expense advanced mine safety equipment.
- Qualified Zone academy bonds.
- Low Income Tax Credits for non federally subsidized new buildings.
- Low income housing tax credits treatment of military housing allowances.
- Treatment of dividends of regulated investment companies (RICs)
- Treatment of RICs as qualified investment entities.
- S Corporations making charitable donations of property
- New York liberty zone tax exempt bond financing
- Economic development credit for American Samoa.

Source : RIA Checkpoint, CCH

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