THE SMALLBIZ BUILDER

PADGETT THE SMALL BIZ PROS

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Taxmageddon!

Taxpayers (and tax professionals) are facing a unique set of challenges as the November Presidential election approaches and end-of-the-year tax planning looms. If Congress and the White House fail to act by December 31st, favorable Bush-era tax cuts will expire, along with a variety of business and investment tax breaks, raising income tax rates to levels last seen in 2001. Unfortunately, our current political and legislative environment only adds to the uncertainty as Republicans and Democrats are both hesitant to act until they know who will occupy the White House next year. This political gridlock combined with a fragile economy and the possibility of rising tax rates has been dubbed by many as "Taxmageddon." So what does all this mean for taxpayers? How will the 2012 tax filing season be affected and what approach should taxpayers take for tax planning in 2013?

Our best advice is to stay informed of the possible changes that may affect your business and your personal tax position.

"Staying in the Know"

Many favorable tax provisions expired at the end of 2011. Unless Congress acts and passes retroactive changes by December 31st, many taxpayers will be affected by the following **expired** provisions when filing their 2012 income tax returns. Historically, many of these temporary provisions have been extended, but this year there is no guarantee that Congress will take action in time.

- Increase in the alternative minimum tax exemption (AMT Patch),
- Deduction for state and local tax for itemized filers,
- Deduction for PMI (premium mortgage insurance) for itemized filers,
- Provision for Tax - free IRA withdrawals for charitable donations (for those over age 70 ½).

Another handful of provisions are set to **expire by the end of 2012,** and it is unlikely that Congress will address these provisions until after the Presidential election. The IRS warns that late-year law changes make for an administrative nightmare and often result in delayed filings. While taxpayers (and the IRS) remain hopeful for tax reform, we may not see progress until late December making tax planning nearly impossible. Expiring provisions include the following:

- Bush-era tax cuts in marginal income tax rates,
- Reduced tax rates on dividends and long-term capital gains,
- Marriage penalty relief provisions,
- Expanded refundable credits for the child tax, adoption and earned income credit
- The moratoria on the phase outs of itemized deductions,
- The payroll tax cut, which reduced an employee's share of Social Security taxes by two percentage points, and
- A variety of previously extended temporary tax provisions (tax extenders) which affect individuals, businesses, charities, energy, community development, and disaster relief.

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We provide accounting, tax planning and preparation and business consulting to small business owners and individuals

"What's New For 2013?"

Despite the uncertainty of what will happen to the expired and expiring tax provisions, the recent Supreme Court ruling to uphold the "Affordable Care Act" will affect taxpayers beginning January 1, 2013. This ruling requires all Americans to purchase health insurance or pay a penalty beginning in 2014. To fund this health care mandate, the following two items will be effective in 2013. (We will address the 2014 health care mandate in another issue of the Small Biz Builder).

Medicare Tax Increase: Beginning in 2013, higher-income taxpayers will be subject to an additional 0.9% tax on earned income. The tax applies to income in excess of a single person's wage and self-employment income over $200,000, or a married couple exceeding $250,000. There is no employer match as this tax increase is entirely paid by the employee or the self-employed individual. There will be employer withholding, but if you are self-employed, you will need to build this into your quarterly tax estimates.

Investment Tax Increase: Beginning in 2013, higher income individuals with net investment income will be subject to a 3.8% tax of the lesser of two amounts: net investment income or the excess of the taxpayer's modified adjusted gross income over a $200,000/$250,000 threshold amount. Net investment income includes Interest, dividends, annuities, royalties, and rents, income from a passive business, capital gains and other net gains from the sale of property.

"So, now what?"

So what does all this mean for you as a taxpayer and how will this impact your tax planning for 2012 and 2013? The threat of Taxmageddon is "real" and will likely affect every American household, regardless of income. It's important for each taxpayer to understand that the outcome of the Presidential election coupled with the potential tax law changes make for a foggy and unpredictable future.

Today, due to this uncertainty, your trusted tax advisor may not have answers to all of your tax questions and tax concerns. Padgett is active in Washington DC, explaining to lawmakers the problem this uncertainty is causing and encouraging them to give small business some predictability in the tax laws they must comply with. While Padgett may not be successful in changing Washington, we can however ensure your concerns are heard and keep you informed once the rules are known. So what should you be doing today in these uncertain times?

While taking the most conservative planning approach, by assuming all of the laws will expire or will not be extended, may cause you to pay higher than necessary estimated tax payments or to withhold too much federal tax from your wages, taking a more aggressive approach could cause you to have an unprecedented tax liability at the end of the tax year, as well as additional penalties. Taking a middle ground approach, may put you into either one of the aforementioned predicaments. In the end, it all comes down to being flexible and "staying in the know" so that whatever the outcome, you are prepared, ready to act quickly, and can make educated decisions. For more information regarding how these potential tax laws can affect your tax position, contact your local Padgett Office to set up an appointment.