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Newsletter – Winter 2012

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Final 2012 Newsletter

Well here it is-the last newsletter before we start yet another tax season. We will be sending out a preferred appointment letter again this year but please note it will go out via email so if you are having any problem at all receiving this newsletter let us know so we can be sure we can get you the appointment and time you want. That is the whole reason for us sending out those letters. Well we are going to get into the body of this newsletter right away. This entire newsletter will be devoted to one topic- The Fiscal Cliff so we are off to Obama's second term which is not starting out so good.

The Cliff

You know with my luck this whole fiscal cliff will resolve itself before I send this newsletter to you. It takes me about a week from start to finish to get this to you. So we will see what happens. Now the rumor mill is this. The president wants us to go over the cliff. The reason is he will get much of what he wants if we do. The other benefit he sees is right now the majority of the public will blame the republicans if we do fall off the cliff. The only drawback is republicans do hold the key to raising the debt ceiling and if that doesn't happen then all of Obama's entitlement programs that got him his second term will end abruptly. So we will see. But what exactly is the cliff? It is a combination of 2 things. The first is all of the Bush tax cuts of which several were extended time and time again, are all going to end on 1/1/13. The second is in August of 2011 when the spending limit was raised the last time, there was never any agreement as to what else should happen to compensate for the cost of the increased spending. So the cuts to the budget were postponed to- yep- you guessed it-1/2/13. So this collision will take place unless an agreement is worked out. So what specifically does this mean? The first area is estate taxes. When this was a big issue in 2010 I put tongue in cheek and said if you are going to die do it in 2010 because that was the one year estate taxes were to be eliminated. I am not going to do that again because that turned out to be the year my mother died. But I can tell you this; if we go over the cliff don't die in 2013. The estate exemption will go from 5,120,000 in 2012 to 1,000,000 in 2013. This means that most of you that could forget about estate tax planning are right back in the middle of it. And to make matters worse the estate rate will go from 35% to 55% with a 5% kicker for estates in excess of 10 MIL. And a big improvement to estate law was the introduction of portability. This allowed the transfer of the estate credits between husband and wife. If we go over the cliff this would be gone. Now the republicans want to eliminate estate taxes all together. The reason is the revenue brought in by the estate tax is less than 2% if the total revenue received by our government and the estate taxes cause over 2/3 if all IRS court cases-by far the highest cost for some of the lowest income. Obama on the other hand views this as a break for the wealthy (which is by the way what he is- wealthy but he just doesn't tell us that because it would not be good for him politically) and is unwilling to let this go. What he wants will kill most estate plans put in place and cause many more of us to be forced to enter this complicated issue in the future. Also regular tax rates will go from 10%, 15%, 25%, 28%, 33%, and 35% for 2012 to 15%, 28%, 31%, 36%, and 39.6% which in effect really will be 42-45% (more later). You will also notice the lower income levels are affected 1st with everyone losing the 10% first tax bracket. This is a direct and major hit to lower income families.

- The 2% reduction in FICA tax will be gone. Unfortunately this looks like it is gone no matter what since neither side is looking to put this back in.
- The marriage penalty relief passed some years ago which really only covered part of the marriage penalty will be gone. Maybe that is just wishful thinking on our presidents part that he wants all couples to get divorced and live together as two single taxpayers. I guess I shouldn't complain as my revenues would just about double.
- Capital gains will go up to 20% and that doesn't include the new 3.8% tax increase already in place
- The break for taxable dividends would be gone and instead of being treated as capital gains (which they really are) they would be treated just like your W-2
- We would go back to the phase out and therefore loss of itemized deductions. We would also lose the personal exemption again (anybody missing those Clinton days?) what is getting traction is the area in limiting both of these to a fixed rate. Right now the most popular number is 28% and if your income tax bracket is higher then that- tough!!! It is amazing that everybody screams tax simplification and then they think of things that will only add a great amount of complexity and yes I will have to charge more to report this mess.
- Again if you think this is only going to affect those earning over $250,000 people well guess again. Earned Income credit will change and will be reduced by AMT (every newsletter has something about AMT in it) also child tax credit will get cut in ½ but there is more bad news for all of you no matter what your income.
- Adoption credit is set to die in 2013 and the child care credit- you know that credit you take so you can do something like let's say WORK so you can pay all of your taxes- will be cut by 20%
- Student loan interest deduction will be gone in 2013 as so will be the discharge of debt for your residence. Won't that be fun as you are going to get ripped on taxes on that short sale you tried so hard to never have happen.
- All that bonus depreciation-gone (anybody sick yet) For business the 179 deductions for writing off of assets will drop from 139,000 in 2012 to 25,000 in 2013.
- And ok yes the king of them all-Alternative minimum tax (AMT) the only issue with this is it is schedule to clobber us this year if nothing is done. If this doesn't change there will be a lot more people wanting to leave the old union jack. That is why that issue with earned income credit not offsetting AMT is so big. With the exemption amount about cut in half many lower income people that depend on the EIC will have to do with out.

What to do, What to do

So what are the wise men of these upcoming dark days saying? Assuming of course we wake up on 12/22/12.

- Stay single- yes I have seen this more than once in fact many are saying get divorced in 2013 to save taxes. Please note this is only true if you both work or earn income. One income families can save the court cost.
- Sell your stock that has gone up in value- then if you really like the investment buy it back. This is really good if you are in the 15% tax bracket because the tax rate you will pay in 2012 will be zero- yes zero. I can tell you will never see that again.

- Accelerate income and defer expenses. Yes it took me 29 years in business but this is the year it finally came true that I have completely reversed myself. Note this you have and hopefully will never see this advice from me again
- Elect out of the installment sale. This one could be tough because it could force you to pay tax on money you don't have. (thinking of you Jeff)
- If you are thinking about giving a large gift do it in 2012. This includes donations of appreciated property.

Health Care 2013

On top of this portions of the Health care bill become effective in 2013. Many parts of this bill phase in over the next couple of years. One part is high income earners will see their Medicare tax go up 62%. Also I mentioned the 3.8% tax your investment income which by the way included interest, dividends, rents and royalties. So what does that mean if you get a dividend and you are in the 39 % bracket for 2013. The tax rate of that dividend (or interest) will be at the 43.4 % rate. Also the floor for everyone under age 65 for medical expenses goes from 7.5% to 10% in 2013. That means before you can deduct $1 of your medical you have to exceed 10% of your income in medical expenses. But don't worry- Health care also puts a 2.3% tax on all medical devices sold in 2013

Items already gone for 2012

- $250 deduction for teachers
- deduction for Mortgage Insurance Premiums
- deduction for state sales tax
- Tuition and fees deduction
- …and a few minor ones.

So now that you know what the fiscal cliff is-anybody interested in finding a real cliff to jump off?

One more thing you don't want to hear

Seven years ago I made a promise to you our clients that I would not raise our fees until we are out of the horrible economic times we were in. I did not think it was going to last this long but a promise is a promise. In that time our fees have been fixed and accordingly our buying power has decreased considerably. If you even consider just a 2 or 3% inflation rate over 7 years that adds up a lot. Now I do hear you saying but my fee went up- why? There are 2 ways your fee could have gone up. First is you just had me do more work on your return. Second and this has happened a lot over the past 7 years, the government reporting requirements have increased. A good example is the ridiculous new reporting requirements for capital gains last year. Everyone I talked to in my profession consider this one of the dumbest things they have seen. But yet it is still there and still needs to be done. And don't forget the state. Remember when you could file the state return on 1 page that I charged $10 for. Now nobody can file the state on 1 page and most state returns are 6-8 pages long. I would say this accounted for about 80% of all of you that saw their fee go up. Well the public has spoken. According to the majority we are out of the woods and in recovery and the voters of Illinois are even more convinced of this by the numbers that reelected our President. Therefore we are going to raise our fees this year. The average per return will be 6-7%. We are also going to increase our fees for appointment time (not tax appt) and research time. While many of you may not agree with the majority who voted of the solidness of our current path, we are a democracy and the people has spoken

I could go into my publications to see if I can find some stupid thing the IRS did in the last month but I think even that would be hard to laugh at after all this. The only thing I have seen is the IRS is saying they won't be ready for this tax season because of the cliff. What that will mean is all of you that come in early to get your refund- just like 2 years ago you will have to wait. But do you think they will extend tax season deadline. Well that might be something you can laugh at. So for everyone have a Great Christmas and Happy New Year and we will see you all in month or 2.

Tom & Dorothy
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