INFORMATION THAT WORKS FOR YOU
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2013 Year-End Planning For Individuals

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Congress is forever extending some tax laws, letting others expire, and creating altogether new ones. In 2013, the American Taxpayer's Relief Act (ATRA) was enacted and various provisions of the Patient Protection and Affordable Care Act of 2010 (ACA) are scheduled to take effect. The release of significant new IRS rules on many pressing issues will also affect you in 2013.

Below we have set forth a sampling of the changes, the new laws and the expiring laws. Gaining a full understanding of those that affect your specific circumstances will help you more effectively manage and potentially reduce the amount of tax you pay. At Scribner, Cohen and Company, we are available to help you make the best choices for your unique circumstances.

Tax Rate Changes:

For 2013 and subsequent years, the individual income tax rates are amended to include an additional top bracket of 39.6 percent. The starting points for taxable income subject to the 39.6 percent bracket are stated below and they are adjusted for inflation annually.

	2013	2014
Married Filing Joint	$450,000	$457,600
Heads of Household	$425,000	$432,200
Single	$400,000	$406,750
Married Filing Separate	$225,000	$228,800

Trusts reach the highest tax bracket of 39.6 percent when taxable income reaches $11,950 for 2013 and $12,150 for 2014. Therefore, assuming all other tax related and non-tax related factors have been properly considered, trustees may want to consider distributing trust income to beneficiaries to reduce the tax costs at the trust level.

Starting in 2013 a 20 percent tier was added to the capital gain and qualified dividend rates. This top rate is aligned with the same income levels as the 39.6 tax bracket. Year-end planning should therefore include a review of your income and gains to avoid unexpected results.

New 3.8% Surtax on Net Investment Income

The new 3.8% Medicare Contribution Tax went into effect in 2013 as a result of the passage of the Affordable Care Act. The surtax equals 3.8 percent of the lessor of net investment income or the amount that the taxpayer's modified adjusted gross income exceeds the following threshold amount:

- $250,000 married couples filing joint returns
- $200,000 single or head of household individuals
- $125,000 married couples filing separate returns

Net investment income includes:

- ❖ Capital gains, interest, dividend income
- ❖ Royalties
- ❖ Income received from a business in which the taxpayer is a passive participant
- ❖ Income received from a business that trades in financial instruments or commodities
- ❖ Rental income
- ❖ Gain on sale of a business or business asset when you have actively participated in the business

0.9% Medicare Withholding Tax

Starting in 2013, there is an additional 0.9% Medicare Withholding Tax on wages or self-employment income in excess of

- ❖ $250,000 for a married couple filing jointly
- ❖ $200,000 for single individuals and heads of household.

Employers are responsible to withhold and pay this surtax on wages in excess of $200,000. This may result in unexpected additional tax due for married couples filing joint whose individual wages or self-employment income are below the threshold but whose combined income exceeds the threshold.

Alternative Minimum Tax

The American Taxpayer Relief Act permanently increased the exemption amount for AMT purposes and provides that it will be indexed annually for inflation. For 2013, the exemption amount is $51,900 for single individuals and heads of households and $80,800 for married couples filing a joint return. Taxable income that exceeds the exemption amount is subject to a 26 percent AMT rate on the first $175,000 of alternative minimum taxable income and 28% over $175,000. There are many types of income and deductions that increase exposure to AMT, including state income and real estate taxes, some of which may be mitigated with tax planning, others not.

Reinstatement of the Itemized Deduction Limitation (Pease) and the Personal Exemption Phase-out

ATRA reinstated a modified version of the "Pease" limitation on itemized deductions and the phase-out of the personal exemption for higher income taxpayers as follows:

The itemized deduction limitation reduces the deductible amount of certain itemized deductions by 3% of the amount by which the taxpayer's adjusted gross income exceeds an applicable threshold. However, the amount of itemized deductions is not reduced by more than 80 percent. Medical expenses, investment interest expenses and casualty and theft deductions are not affected by this limitation.

The personal exemption phase-out reduces the deductible amount by 2% for each $2,500 or a portion thereof by which the taxpayer's adjusted gross income exceeds the applicable threshold.

The Child Tax Credit

The $1,000 child tax credit became permanent for 2013 and subsequent years. It is not indexed for inflation.

Medical Expense Deduction

Medical expenses are deductible as itemized deductions to the extent they exceed a threshold. For 2013 and forward, the threshold has been increased from 7.5% to 10% of adjusted gross income, except for taxpayers who are age 65 or older before the close of the tax year. The age 65 or older taxpayer can continue to apply the 7.5% threshold until the year 2016.

FYI: Payments made by credit cards before year-end qualify for the medical expense deduction in the current year.

Health Flexible Spending Arrangements

For 2013, The Affordable Care Act (ACA) limited the maximum annual contribution to a health flexible spending arrangement account to $2,500. The amount will be indexed for inflation. The amount contributed reduces the taxpayer's reportable wages.

The following tax law "extenders" are set to expire at the end of 2013, unless Congress acts to extend them.

- The election to deduct state and local sales taxes in lieu of state and local income taxes.
- The $250 above-the-line deduction for qualified unreimbursed education expenses.
- The exclusion of cancellation of principal residence mortgage debt of up to $2 million.
- The deduction for mortgage insurance premiums.
- The ability to make charitable donations directly from individual retirement accounts.

Same Sex Marriage

In June 2013 the US Supreme Court held that Section 3 of the Defense of Marriage Act that defines marriage for federal purposes as one man and one woman was unconstitutional. Consequently, the IRS announced a general rule recognizing same-sex marriages for all federal tax purposes nationwide, regardless of the jurisdiction in which the couple resides.

Wisconsin does not recognize same-sex marriage. Therefore, each individual will have to continue to file single or head of household for Wisconsin purposes. Schedule S "Allocation of Income to be Reported by Same-Sex Couples Filing a Joint Federal Return" must be submitted with the return

For tax years 2011 and earlier, same-sex couples who filed their tax returns timely may choose to amend their federal tax returns to file using a married filing separate or joint filing status provided the statute of limitations has not expired.

Estate and Gift Tax

ATRA preserved the annual gift tax exclusion, but adjusts it for inflation. This exclusion allows each individual to give an annual gift of $14,000 in 2013 to any other individual or individuals, gift tax free, and without the gift counting towards the lifetime exclusion. The annual gift tax exclusion is projected to remain $14,000 for 2014.

FYI: All gifts must clear the donor's bank by December 31st to count toward the current year's annual exclusion. If a check was written at the end of the current year, but cashed in the following year, that gift would count towards the annual exclusion for the following year.

In addition, ATRA provides for a maximum federal unified estate and gift tax rate of 40 percent with an inflation adjusted $5 million exclusion for gifts made and estate of decedents dying after December 31, 2012. For 2013 the lifetime exclusion is $5,250,000. For 2014 the lifetime exclusion is projected to be $5,340,000.

Affordable Care Act and the Individual Mandate

Effective January 1, 2014, the ACA generally requires individuals to carry minimum essential coverage for each month, qualify for an exemption or make a payment when filing his or her return. Minimum essential coverage for purposes of the individual mandate is employer-sponsored coverage, coverage through a state or federal Marketplace, Medicare, Medicaid, and other plans.

The penalty for 2014 is $95 or the flat fee of one percent of taxable income, $325 in 2015 or the flat fee of two percent of taxable income, $695 in 2016 or 2.5% of taxable income. After 2016 the $695 amount is indexed for inflation.

Higher Education Incentives Extended

The American Opportunity Tax Credit was extended through 2017 and allows eligible taxpayers to claim a tax credit for qualified post-secondary education expenses.

The Lifetime Learning Credit remains available as does the above-the-line deduction for qualified tuition and related post-secondary education expenses.

Report of Foreign Bank and Financial Assets

If you own a bank account or other financial assets located in a foreign country, if you own a flow-through entity with foreign assets, or if you have signature authority over foreign financial assets, you may have a responsibility under the Foreign Account Tax Compliance Act (FATCA) or the Bank Secrecy Act to disclose your ownership to the Treasury

Department. In recent years, the government's enforcement of these requirements has increased significantly. Failure to report foreign financial assets may result in substantial penalties starting at $10,000.

WISCONSIN TAX UPDATE

Wisconsin Tax Rates Change

Starting in 2013, the Wisconsin tax rates have been reduced to the following:

4.6% → 4.4%
6.15% → 5.84%
6.5% → 6.27%
6.75% → 6.27%
7.75% → 7.65%

Tuition Deduction

For 2013, the maximum Wisconsin subtraction for the amount paid for tuition and mandatory student fees is $6,943. The subtraction is subject to a phase-out which is increased by inflation each year.

Edvest Program

For 2013, the Edvest deduction remained the same at $3,000 per beneficiary.

Medical Care Insurance Subtraction:

The subtraction increased from 45% to 100% of the amount paid by employees whose employer pays a portion of insurance. All other categories are now at 100%

Child and Dependent Care Expenses

The subtraction increases to $2,250 for one qualified person and $4,500 if more than one qualified person.

Starting in 2014

Private School Tuition

Effective for taxable years beginning on January 1, 2014, a subtraction from federal adjusted gross income is allowed for tuition expenses paid for a dependent to attend an eligible institution. The maximum deduction for Elementary students (Grades K-8) is $4,000. The maximum deduction for secondary students (Grades 9-12) is $10,000. There is no phase-out based on income levels.

Net Operating Loss Deduction

Effective for taxable years beginning on January 1, 2014, a Wisconsin net operating loss may be carried back against Wisconsin taxable income of the previous two years and then carried forward against Wisconsin taxable income of the next 20 years.

Depreciation and Section 179 Expensing

Effective for taxable years beginning on or after January 1, 2014, for purposes of computing depreciation, depletion, and amortization on property additions placed in service in those years, Wisconsin depreciation will be computed under the law in effect on January 1, 2014 for federal purposes. The same will hold true for the computation of the Wisconsin section 179 expensing election deduction.

Because the Wisconsin and federal systems have differed for many years, the respective deductions relative to assets placed into service in prior years have differed. In order to bring the two systems together, taxpayers must consolidate the cumulative difference between adjusted federal tax basis and adjusted Wisconsin tax basis as of the last day of the tax year beginning in 2013 into a single asset account that may be amortized/depreciated at the rate of 20% per year over the next five years (tax years 2014 through 2018).

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