CLIENT LETTER
2013 First Quarter Federal Tax Developments

Dear Client:

April 15 has come and gone but it's not time to stop thinking about taxes and strategic tax planning opportunities. Since the start of 2013, there have been many new federal tax developments, which will impact tax planning for this year and beyond. As 2013 unfolds, many changes made to the Tax Code by the American Taxpayer Relief Act of 2012 (ATRA) take effect. Additionally, there are new taxes to take into account because of the health care reform package, along with enhancements to many tax credits and deductions. Now is a good time to revisit these developments and explore how they will affect your strategic tax plans. Planning today can help maximize your tax savings going forward. As always, please give our office a call or email if you have any questions.

Tax planning and ATRA

Returns just filed (or that will be filed under extension by October 15, 2013) reflect the tax laws as they existed in 2012 (with some expired provisions renewed retroactively for 2012 by ATRA). Looking ahead, your 2013 return to be filed in 2014 will reflect the many changes to the Tax Code made by ATRA. Because the new law was passed at the beginning of the year, it was overshadowed by the filing season. However, its provisions impact every taxpayer and it's vital to take time to gauge how they will affect you. The list of changes made by ATRA is long: many generous tax incentives, such as the $1,000 child tax credit, enhanced adoption credit, and enhanced earned income credit, are made permanent. ATRA also permanently "patches" the alternative minimum tax (AMT), which definitely will impact planning for taxpayers liable for the AMT. The new law also extends permanently the Bush-era tax rate cuts for individuals except taxpayers with taxable income above $400,000 ($450,000 for married couples filing a joint return). Income above these levels is taxed at 39.6 percent effective January 1, 2013. ATRA also increased the tax rates on qualified capital gains and dividends for higher income taxpayers. All these changes and more are set in motion by ATRA.

New proposals to consider

Looking ahead, some new proposals could impact tax planning in 2013 and beyond. President Obama has proposed to reduce the value to 28 percent of certain deductions and exclusions that would otherwise reduce taxable income in the 33, 35 or 39.6 percent tax brackets. The President also re-proposed the so-called Buffett Rule, now referred to as the "Fair Share Tax" for taxpayers with incomes above $1 million (with full phase-in above $2 million). Moreover, the President has proposed to limit contributions and accruals on tax-favored retirement benefits, including IRAs, qualified plans, tax-sheltered annuities, and deferred compensation plans. The limit generally would apply when a taxpayer accumulates total retirement amounts that exceed the amount necessary to provide the maximum annuity permitted for a defined benefit plan. The President's proposals are expected to be debated in Congress as lawmakers and the White House try to reach an agreement on tax reform and deficit deduction. President Obama has said he wants an agreement before August, which could significantly change your tax planning for 2013 and beyond. Our office will keep you posted of developments.

NII surtax takes effect

The 3.8 percent Medicare surtax on net investment income (NII) became effective January 1, 2013. The NII surtax on individuals equals 3.8 percent of the lesser of: Net investment income for the tax year, or the excess, if any of the individual's modified adjusted gross income (MAGI) for the tax year, over the threshold amount. The threshold amount in turn is equal to $250,000 in the case of a taxpayer making a joint return or a surviving spouse, $125,000 in the case of a married taxpayer filing a separate return, and $200,000 in any other case.

The IRS issued proposed regulations in 2012 intending them to be "reliance regulations." Nonetheless, taxpayers continue to be confused over certain sections. Although final regulations are promised "within 2013" so they would be available for the 2013 tax year and 2014 filing season, current misinterpretation of the proposed regulations can impact on tax strategies now being put into motion in 2013. Any misinterpretation can also bear on 2013 estimated tax that may be due to cover any 3.8 percent NII surtax liability. Our office will keep you posted of developments.

Vehicle depreciation limits increase for 2013

Tax planning for 2013 is helped by the IRS's release of inflation-adjusted limitations on depreciation deductions for business-use of passenger automobiles, light trucks, and vans first placed in service during calendar year 2013. Some of the depreciation limits are identical to the limits for 2012; other ceilings have increased by $100. The 2013 dollar limits reflect the inflation adjustments both with the extension of bonus depreciation by ATRA and without. If bonus depreciation is allowed to lapse after 2013, as President Obama has proposed, the dollar limits for 2014 would be lower but would still be adjusted for inflation. The maximum depreciation limits under Code Sec. 280F for passenger automobiles first placed in service during the 2013 calendar year are: $11,160 for the first tax year ($3,160 if bonus depreciation does not apply); $5,100 for the second tax year; $3,050 for the third tax year; and $1,875 for each succeeding tax year. The maximum depreciation limits under Code Sec. 280F for trucks and vans first placed in service during the 2013 calendar year are slightly higher. Keep in mind that SUVs and pickup trucks with a gross vehicle weight rating (GVWR) in excess of 6,000 pounds continue to be exempt from the luxury vehicle depreciation caps based on a loophole in the operative definition.

IRS audits of business property write-offs on "stand-down"

The IRS announced in March that it had updated its 2012 directive that generally instructs employees to discontinue audits of costs to maintain, replace or improve tangible property. The updated directive tells employees not to begin examining those issues for tax years beginning on or after January 1, 2012 and before January 1, 2014. The directive retains the "stand-down" of audit activity in this area beginning in 2012. The IRS also advised that it intends to make changes to temporary regulations regarding certain de minimis rules, routine maintenance and more.

Prepare for employer and individual mandates under PPACA

The IRS issued long-awaited proposed reliance regulations on the employer mandate under the Patient Protection and Affordable Care Act (PPACA). An applicable large employer is an employer that employed an average of at least 50 full-time employees during the preceding calendar year, including full-time equivalent (FTE) employees. The statute defines a full-time employee as an employee who on average was employed for at least 30 hours of service per week.

The PPACA also generally requires individuals, unless exempt, to carry minimum essential health insurance coverage after 2013 or make a shared responsibility payment. The IRS has issued proposed regulations on the individual mandate. The proposed regulations, the IRS explained, are intended to mitigate the affordability test for related individuals.

IRS ramps up oversight of foreign accounts

The Foreign Account Tax Compliance Act (FATCA) gives the agency new tools to discover tax evasion. In January, Treasury and the IRS issued final regulations under FATCA that describe the requirements for foreign financial institutions (FFIs), nonfinancial foreign entities (NFFEs), and other taxpayers to comply with FATCA's reporting and withholding regimes on U.S. and foreign account holders. The 544-page regulation package seeks to harmonize the United States' regulatory requirements with the use of intergovernmental agreements (IGAs) to implement FATCA.

Simplified safe harbor for claiming home office deduction

The home office deduction is one of the most complex in the Tax Code. In response, the IRS announced a simplified safe harbor method for claiming the home office deduction for tax years beginning on or after January 1, 2013. Under the safe harbor, taxpayers determine the amount of deductible expenses for qualified business use of the home for the tax year by multiplying the allowable square footage by the prescribed rate. The allowable square footage cannot exceed 300 square feet and the prescribed rate is $5.00, which provides a maximum deduction under the safe harbor of $1,500. The IRS indicated it may revisit the prescribed rate amount in the future.

If you have any questions about these or any other federal tax developments and their impact on tax planning, please contact our office.

Sincerely yours,

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