On Thursday, December 6, 2012,

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responded to a request from the MBBA, Metro, Board of Directors to present a summary of the post-election Federal Tax situation. Although still a 'work in progress' at the time of Brian's presentation, the following scenarios were offered as part of his momentary assessment of what could happen to various tax payers if the 'fiscal cliff' did not encounter some relief and revision from the legislature.

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C. Analysis of possible scenarios.

1. Four potential scenarios comparing approximate 2012 results to projected 2013 results are analyzed below.

   a. Example 1: Low income taxpayer with no tax and refundable credits.

   b. Example 2: Low income taxpayer with positive taxable income.

   c. Example 3: Schedule C proprietor with net income near OASDI maximum and large asset purchases.

   d. Example 4: High income taxpayer with earned income and investment income.

2. **Caution:** Because of the interaction of many provisions and the yet unannounced tax brackets and other amounts for 2013, the scenarios necessarily use approximations in their computations. Results shown are intended to be illustrative, rather than exact.

Example 1 — Low income taxpayer with no tax and refundable credits

FACTS:

- Married couple filing a joint return.
- Three dependent children; standard deduction.
- Form W-2 = $20,000.

POSSIBLE FACTORS:

- 2% payroll tax holiday on FICA not extended for 2013.
- Reduction in child tax credit from $1,000 to $500 per child.
- Change in refundable child tax credit in 2013 to only allow refund to extent FICA of taxpayer exceeds earned income credit (refundable in 2012 at a 15% rate to extent earned income exceeds $3,000).
- Reduction in earned income credit from 45% rate to 40% rate for three or more children.

RESULTS:

	2012	2013
• Employee FICA on wages [4.2%/6.2% x $20,000]	$ 840	$ 1,240
• Income tax	0	0
• Earned income credit (@45%/40% rate)	(5,891)	(5,300)
• Refundable child tax credit	(2,550)	0
Total Tax Result	$ (7,600)	$ (4,060)

Approximate Increase in Tax $ 3,540

Example 2 ***Low income taxpayer with positive taxable income***

FACTS:

- Married couple filing a joint return.
- Three dependent children; standard deduction.
- Form W-2 = $48,000.

POSSIBLE FACTORS:

- 2% payroll tax holiday on FICA not extended.
- Elimination of 10% tax bracket.
- Reduction in standard deduction amount from 200% to 167% of single deduction.
- Reduction in child tax credit from $1,000 to $500 per child.
- Reduction in earned income credit from 45% rate to 40% rate for three or more children.

RESULTS:

	2012	2013
• Employee FICA on wages	$ 2,016	$ 2,976
• Income tax	1,600	2,700
• Child tax credit	(1,600)	(1,500)
• Earned income credit	(222)	0
• Refundable child tax credit	(1,400)	0
Total Tax Result	$ 400	$ 4,200
Approximate Increase in Tax	$ 3,800	

Example 3 ***Schedule C with net income near OASDI maximum and large asset purchases***

FACTS:

- Married couple filing a joint return.
- No children; standard deduction.
- 2012 Schedule C net income of $110,000 (after depreciation and $139,000 Section 179 deduction).
- Asset purchases during year = $300,000, with maximum Section 179 used.

POSSIBLE FACTORS:

- 2% payroll tax holiday on self-employment income not extended.
- Elimination of 10% tax bracket and compression of 15% bracket.
- Reduction in standard deduction amount from 200% to 167% of single standard deduction.
- Reduction in Section 179 amount in 2013 to $25,000 maximum.

RESULTS:

	2012	2013
• AGI	$ 102,200	$ 210,200
• SE tax on Schedule C	13,500	19,500
• Income tax	12,600	48,000
Total Tax Result	$ 26,000	$ 67,500
Approximate Increase in Tax	$ 41,500	

Example 4 High income taxpayer with earned income and investment income

FACTS:
- Single taxpayer, age 60, wealthy but in nursing home.
- Form W-2 = $400,000.
- Interest income = $100,000.
- Qualified dividends = $100,000.
- Long-term capital gains = $100,000.
- Nursing home expenses = $100,000 (taxpayer requires nursing home care for rehabilitation, but is of sound mind and is still involved in critical business decisions to justify wage income).
- Charitable contributions = $10,000.

POSSIBLE FACTORS:
- 2% payroll tax holiday on self-employment income not extended.
- Elimination of 10% tax bracket.
- Qualified dividends taxed at ordinary rates.
- Long-term capital gains taxed at 20%.
- Medical expenses deductible only to extent of 10% of AGI, rather than 7.5%.
- Phase-out of Schedule A itemized deductions.
- Phase-out of personal exemption.
- Compression of other tax brackets and increase of highest tax rates to 28%, 31%, 36%, and 39.6%.
- Application of 3.8% Medicare surtax to net investment income.
- Application of additional 0.9% Medicare tax.

RESULTS:	2012	2013
• Employee FICA on wages	$ 10,420	$ 12,620
• Tax on qualified dividends	15,000	39,600
• Tax on long-term capital gains	15,000	20,000
• Increased tax due to lower medical expense ded.	0	7,000
• Incr. tax from phase-out of Sch. A itemized deductions	0	5,000
• Incr. tax from phase-out of personal exemptions	0	1,600
• Compression of other tax brackets/increase in tax rates (i.e., tax w/out qual divs and LTCGs)	120,000	134,000
• 3.8% Medicare surtax on net investment income	0	11,400
• Additional 0.9% Medicare tax	0	1,800
Total Tax Result	$ 160,420	$ 233,020
Approximate Increase in Tax		$ 72,600

D. Comparison chart.

1. The following chart summarizes individual rates and related tax provisions, comparing 2012 (as things are now) to 2013 with the expiration of EGTRRA.

Item	2012 (as things are now)	2013 w/ EGTRRA Expiration
Tax rates and tax brackets for joint returns (amounts rounded to nearest $1,000)	$0 – $17k 10% $17k – $71k 15% $71k – $143k 25% $143k – $217k 28% $217k – $388k 33% Over $388k 35%	$0 – $58k 15% $58k – $141k 28% $141k – $214k 31% $214k – $383k 36% Over $383k 39.6%
Capital gain rate	15%	20%
Dividend income rate	15%	Normal tax rate
Marriage penalty – standard deduction on joint return	$11,900 (2.00 x single deduction)	$9,940 (1.67 x single deduction)
Phase-out of Schedule A	No phase-out	In excess of joint AGI of approximately $180,000
Phase-out of personal exemptions	No phase-out	In excess of joint AGI of approx. $180K single/ $265K jt.
Child tax credit	$1,000/child	$500/child

Provisions which expired or will expire in 2012. Except as otherwise noted, all of the following provisions expire on 12/31/2012.

1. Temporary payroll tax cut [Sec. 1001 of P.L. 112-96].

2. Increase of the size of 15% rate bracket for married filers to double that of unmarried filers [Sec. 1(f)(8) and Sec. 901 of P.L. 107-16].

3. Reduce capital gain rates for individuals [Secs. 1(h), 55(b), 57(a)(7), 1445(e)(1), 7518(g)(6)(A) and Sec. 303 of P.L. 108-27].

4. Dividends of individuals taxed at capital gain rates [Secs. 1(h)(11), 163(d)(4)(B), 854(a) and (b), and 857(c) and Sec. 303 of P.L. 108-27].

5. 10% individual income tax rate [Sec. 1(i) and Sec. 901 of P.L. 107-16].

6. Reduction in other individual income tax rates: Size of 15% rate bracket modified to reflect 10% rate, and 28%, 31%, 36%, and 39.6% rates are reduced to 25%, 28%, 33%, and 35%, respectively [Sec. 1(i)(2) and Sec. 901 of P.L. 107-16].

7. Dependent care credit: Increase of dollar limit on creditable expenses from $2,400 to $3,000 ($4,800 to $6,000 for two or more children), increase of applicable credit percentage from 30% to 35%, increase of beginning point of phase-out range from $10,000 to $15,000 [Secs. 21(a)(2) and 21(c) and Sec. 901 of P.L. 107-16].

8. Adoption credit and adoption assistance exclusion: Increased to $10,000 for maximum credit and maximum exclusion, special needs adoptions deemed to have $10,000 eligible expenses for purposes of credit and exclusion, increase the beginning and ending points of phase-out range for credit and exclusion, allow the credit against AMT [Secs. 23 and 137 and Sec. 901 of P.L. 107-16].

9. Child credit: Increase from $500 to $1,000, expand eligibility for refundable portion of the credit, AMT relief, provide that child credit not treated as income or resources for purposes of benefit or assistance programs financed in whole or in part with Federal funds [Secs. 24(a), (b)(3), and (d) and Secs. 203 and 901 of P.L. 107-16].

10. American opportunity tax credit [Sec. 25A(i)].

11. Earned income tax credit (EITC): Increase in the beginning point of the phase-out range for joint returns, modification of EITC treatment of amounts not includible in income, repeal of reduction of EITC for AMT liability, expansion of math error authority [Secs. 32(b)(2), (c)(2)(A)(i), (h), and 6213(g)(2) and Sec. 901 of P.L. 107-16].

12. Earned income tax credit: Credit percentage of 45% for three or more qualifying children [Sec. 32(b)(3)(A)] and phase-out threshold for marriage penalty relief [Sec. 32(b)(3)(B)].

13. Cellulosic biofuel producer credit [Sec. 40(b)(6)(H)].

14. Credit for employer-provided child care [Sec. 45F and Sec. 901 of P.L. 107-16].

15. Work opportunity tax credit targeted to hiring qualified veterans [Sec. 51(c)(4)(B)].

16. Credit for prior year minimum tax liability made refundable after period of years [Sec. 53(e)].

17. Increase of the standard deduction for married filers to double that of unmarried filers [Sec. 63(c)(2)(A) and Sec. 901 of P.L. 107-16].

18. Repeal of overall limitation on itemized deductions [Sec. 68(g) and Sec. 901 of P.L. 107-16].

19. Discharge of indebtedness on principal residence excluded from gross income of individuals [Sec. 108(a)(1)(E)].

20. Employer-provided educational assistance: Expansion to graduate education and making the exclusion permanent [Sec. 127(c)(1) and Sec. 901 of P.L. 107-16].

21. Repeal of the personal exemption phase-outs for high-income taxpayers [Sec. 151(d)(3)(F) and Sec. 901 of P.L. 107-16].

22. Additional first year depreciation for 50% of basis of qualified property [Secs. 168(k)(1) and (2)].

23. Election to accelerate AMT credits in lieu of additional first-year depreciation [Sec. 168(k)(4)].

24. Increase in dollar limitations for expensing to $125,000/$500,000 (indexed) [Secs. 179(b)(1) and (2), (c)(2), and (d)(1)(A)(ii)].

25. Student loan interest deduction: Increase and indexation for inflation of the phase-out ranges, repeal of the limit on the number of months that interest payments are deductible, repeal of the rule that voluntary payments of interest are not deductible [Sec. 221 and Sec. 901 of P.L. 107-16].

26. Repeal of collapsible corporation rules [Sec. 341 and Sec. 303 of P.L. 108-27].

27. Education Individual Retirement Accounts (Coverdell education savings accounts): Increase of maximum annual contribution from $500 to $2,000, expansion of definition of qualified education expenses, increase in the size of the phase-out range for married filers to double that of unmarried filers, provision of special needs beneficiary rules, contributions by corporations and other entities, and contributions until April 15 permitted [Secs. 530(b)(1), (b)(2), (b)(4), (c)(1), (d)(2) and Sec. 901 of P.L. 107-16].

28. Reduced rates under accumulated earnings tax and personal holding company tax [Secs. 531 and 541 and Sec. 901 of P.L. 107-16].

29. Estate, gift and generation-skipping transfer tax provisions [Sec. 901 of P.L. 107-16]:

    a. Reduction in the maximum estate and gift tax rate at 35% [Secs. 2001 and 2502].

    b. Modifications of estate and gift taxes to reflect differences in credit resulting from different tax rates [Secs. 2001(b)(2), 2001(g), and 2505(a)].

    c. Increase in estate and gift tax exemption to $5 million (indexed for inflation in years after 2011) [Sec. 2010].

d. "Portability" rules permitting a surviving spouse to use the deceased spousal unused exclusion amount [Sec. 2010(c)].

e. Estate tax deduction for State death taxes paid [Secs. 2011, 2053, 2058, 2102, 2106, and 2604].

f. Expansion and clarification of estate tax conservation easement rules [Secs. 2031(c)(2) and (c)(8)(A)(i)].

g. Repeal of the qualified family-owned business deduction [Sec. 2057].

h. Modifications to generation-skipping transfer tax rules regarding deemed allocations of exemption to certain transfers in trust, severing of trusts, valuation, and relief for late elections [Secs. 2632(c) and 2642(a)(3), (b)(1) and (b)(2)(A)].

i. Modifications to estate tax installment payment rules [Secs. 6166(b)(1)(B)(ii), (b)(1)(C)(ii), (b)(8)(B), (b)(9)(B)(iii)(I), and (b)(10)].

Topic 19I Summary of New Taxes under ACA

A. New taxes under ACA.

2010

1. **10% tax on indoor tanning services.** Effective for amounts paid for indoor tanning services performed on or after July 1, 2010, a new 10% excise tax applies [Sec. 5000B(a)(1)].

2011

2. **Elimination of ability to reimburse over-the-counter medicines.** Effective for tax years beginning after 2010, reimbursements for a medicine or drug out of a pre-tax health FSA, HSA or Archer MSA or from an employer-provided HRA, are permitted only if the medicine or drug is a prescribed drug or is insulin [Secs. 106(f), 220(d)(2)(A) and 223(d)(2)(A)].

3. **Nonqualifying HSA withdrawals.** Effective for distributions after December 31, 2010, the penalty for HSA withdrawals not used to pay for qualified medical expenses was increased from 10% to 20% [Sec. 223(f)(4)(A)].

2013

4. **3.8% surtax on net investment income.** See Topic 11B.

5. **0.9% increase in Medicare HI tax for higher income wage earners.** See Topic 11C.

6. **Higher Schedule A itemized-deduction hurdle for medical expense deductibility.** See Topic 10B.

7. **Health FSA contributions capped at $2,500.** See Topic 14B.

8. **2.3% excise tax on medical device manufacturers.** See Topic 19H.

2014

9. **Penalty for individuals who do not purchase health insurance.** See Topic 19C.

10. **Penalty for large employers who do not provide affordable health coverage.** See Topic 19D.

2018

11. **40% tax on high cost health care plans.** Starting in 2018, providers of health care plans which cost more than $10,200 for individuals or $27,500 for families will be required to pay a 40% tax on the excess premium amount [Sec. 4980I(a)]. The tax is imposed on the health insurance issuer in the case of a group health plan, on the employer in the case of an employer-funded HSA or MSA, and on the plan administrator in the case of other employer-sponsored coverage [Sec. 4980I(c)(2)].