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PUBLISHED: JANUARY 3, 2013

Pulling U.S. Back from the Cliff, Congress Approves Tax and Spending Policies

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Late on Jan. 1, 2013, the U.S. House passed the American Tax Relief Act of 2012 by a 257-167 vote after the Senate passed identical legislation (commonly known as the “fiscal cliff agreement”) earlier in the morning by an 89-8 vote. President Barack Obama, who had returned to Hawaii to resume his family vacation, signed the bill on Jan. 2 by use of autopen, which he had used twice before to sign legislation into law while travelling. The new law will bring changes to U.S. tax and spending policies, including the following highlights:

Tax Policy

Marginal rates: The law will permanently extend the current policy for single people who make up to $400,000 and $450,000 for married couples.

Capital gains and dividends: The law makes permanent the 15 percent tax rate on capital gains and dividends for individuals making up to $400,000 and $450,000 for married couples, with an increase to 20 percent above those thresholds. A provision in the Patient Protection and Affordable Care Act will raise the capital gains rate to 23.8 percent because of an additional 3.8 percent tax on investment income for people making more than $200,000 ($250,000 for couples).

Estate tax: Estates will be taxed at a top rate of 40 percent, with the first $5 million exempted for individual estates and $10 million for family estates, which is an increase of five percent over 2012 levels.

Personal exemption phase-out (PEP) and limitation on itemized deductions (Pease): Individuals making under $250,000 and married couples who make under $300,000 will avoid the caps on itemized deductions and the phase-out of the personal exemption.

Alternative minimum tax (AMT): Permanently indexes the AMT for inflation to prevent middle- and upper-middle-income taxpayers from receiving higher tax bills.

Bonus depreciation: The law provides a one-year extension of accelerated bonus depreciation of business investments in new property and equipment.

Wind tax credit: The wind tax credit was extended through January 1, 2014. The tax credit is worth 2.2 cents per kilowatt-hour of energy produced by new wind installations for their first 10 years of operation.

Temporary payroll tax cut: The 2 percent cut in the payroll tax ends. Social Security is financed by a 12.4 percent tax on wages up to $113,700, with employers paying half and workers paying the other half. President Obama and Congress had reduced the share paid by workers from 6.2 percent to 4.2 percent for 2011 and 2012. As of January 1, 2013, workers will again be required to pay 6.2 percent of their wages as a payroll tax.

Spending Policy

Debt limit: No increase in the debt limit, which remains at $16.394 trillion.

Sequester: Sequester is turned off for two months and paid for with a reduction in discretionary spending cap for 2013 and 2014 and expanding eligibility for Roth conversion.

Unemployment insurance: Extends jobless benefits for the long-term unemployed for one year.

Medicare “doc fix”: A one-year extension is paid for by reducing Medicare spending. This would stop a scheduled 27 percent payment cut in Medicare physician payments to doctors.

Farm bill: Provides for a one-year extension of the Food, Conservation and Energy Act of 2008 at no additional cost to the taxpayer.

CLASS Act repealed: The CLASS Act was enacted as part of the 2010 Patient Protection and Affordable Care Act. It was a new national, voluntary long-term care insurance system. Actuaries have found that, without substantial changes, the program's premiums would be far too expensive for most buyers and projected it would be financially unsustainable.

Contact Info

We have been closely following developments regarding this legislation. We will continue to follow the future debate on tax and spending policy as it unfolds in Washington this year. If you have any questions concerning these matters, please contact your Husch Blackwell attorney or Kyle Gilster at 202.378.2303.

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