Tax law changes you should know for 2013

David Bekedam for *Progressive Dairyman*

The fiscal cliff has come and gone, and the nation has survived. I'm sure many of you were up late on New Year's Eve glued to the TV awaiting a decision from Congress on a plan that would save the country from financial ruin. When the negotiating and politicking was over and the dust settled, we ended up with exactly what we expected from our government: a short-term fix to a long-term problem. The American Taxpayer Relief Act of 2012 was signed into law on January 2, 2013. Let's discuss some of the changes you should be aware of in 2013.

For most Americans, the tax rates and brackets will remain unchanged as those from the Bush-era tax cuts were made permanent. However, Congress has added another bracket for those single filers earning more than $400,000 and $450,000 for joint filers. Income over these amounts will be taxed at the top rate of 39.6 percent.

The payroll tax holiday from 2011 and 2012 is now over for 2013. This was a 2 percent reduction in the employee's Social Security portion of the FICA tax. For 2013, this goes back to 6.2 percent from 4.2 percent. For self-employed individuals, the FICA tax increases from 10.4 percent to 12.4 percent on self-employment income up to $113,700 for 2013.

One of the biggest areas of speculation was what would be done with the capital gains rate, which was lowered to 15 percent as a result of the Bush tax cuts. Many thought the capital gains rate would revert back to 20 percent. Capital gains rates, the rate you pay on the long-term capital gains resulting from cow sales, was held at 15 percent for single taxpayers earning less than $400,000 and married taxpayers earning less than $450,000. For taxpayers with earnings in excess of these amounts, the capital gains rate jumps to 20 percent. Better yet, if your taxable income falls within or below the 15 percent tax bracket, the tax rate is 0 percent on long-term capital gains. Careful planning is necessary to avoid paying the higher rates.

Bonus depreciation at 50 percent, which was set to expire at the end of 2012, has been extended through the end of 2013. This allows a depreciation deduction of 50 percent of the cost of new farm buildings and equipment purchased in 2012 and 2013. The other 50 percent of the asset is depreciated over its normal useful life, starting in the year of purchase. Bonus depreciation can be used to create a loss within an entity when needed to offset income from other sources.

The Section 179 depreciation allowance was also raised. Section 179 allows for a full deduction of the cost of qualifying capital asset purchases in the first year. For all of 2012, the Section 179 depreciation allowance was $139,000 with phase-out beginning at $560,000. On January 2, 2013, Congress increased the Section 179 depreciation allowance to $500,000 with phase-out beginning at $2,000,000 in qualified capital purchases and made it effective for 2012 and 2013. So, where you may have been phased out from this deduction under the law that was in place for all of 2012, you may be able to take advantage of it under the new law. The Section 179 deduction is available for new and used equipment. Section 179 cannot be used to create

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or increase a business' taxable loss.

Another closely watched area of discussion was regarding the estate tax. The lifetime exemption was set to revert back to $1 million with a tax rate of 55 percent on estate value over that amount. The new law prevented this and made permanent the exemption level of $5 million (as indexed for inflation – $5.25 million in 2013). The top federal estate and gift tax rate was raised from 35 percent in 2012 to a permanent rate of 40 percent. The portability feature, which allows an unused exclusion of the first to die to transfer to the surviving spouse, was continued as well.

Precise tax planning becomes additionally important as a result of the passing of the new law. There are increased Medicare taxes imposed on higher-income individuals, personal exemption phase-outs, itemized deduction limitations, etc. Not to mention additional taxes imposed at the state level on those high-income individuals, such as in California.

While we were encouraged to see Congress make many of the Bush-era tax cuts permanent, we have more to look forward to this year. The debt ceiling issue will soon come to the table again. And this year we get to deal with all of the burdensome record-keeping responsibilities, reporting requirements and fees of Obamacare. Make sure you have a competent CPA to assist you in using the new laws to your advantage and avoid falling into traps that could have you paying more than necessary. **PD**

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