The Big Tax Questions of 2013

How will Congress resolve these issues?

Decisions must be made. In the next couple of months, Congress will address several major tax matters. Here are the big questions looming.

The Bush-era income tax cuts. Will the current 10%-15%-25%-28%-33%-35% federal tax rate structure give way to 15%-28%-31%-36%-39.6% tax brackets in 2013? After the election, some analysts feel a compromise will be struck to maintain some of the Bush-era cuts for another year. In 2013, you may see the 10%, 15%, 25% and 28% brackets being retained while the wealthy face higher taxes.[1]

Tax rates on capital gains & dividends. Right now, dividends and most long-term capital gains are taxed at either 0% or 15% (depending on the income tax bracket you fall into). In 2013, dividends are scheduled to be taxed as regular income (cf. 15%-39.6% tax brackets above) and the capital gains tax rates are set to increase to 10% and 20%. So will dividend taxes and capital gains taxes only increase for the rich in 2013? That may very well turn out to be the case.[2]

Estate & gift taxes. President Obama's proposal has the U.S. returning to a top estate tax rate of 45% with a $3.5 million exemption. In other words, estate taxes would return to 2009 levels as opposed to 2001 levels (55% top rate, $1 million exemption), which is what would happen if the Bush-era cuts simply expired. While Sen. Orrin Hatch (R-UT) and others in Congress have called for an end to estate taxes, many analysts think they will return to 2009 levels as a byproduct of Obama's re-election. Will we see a unified gift and estate tax in 2013? That is a possibility, though not a given. It could be that the lifetime gift tax exemption becomes $3.5 million in 2013 (it is currently $5.12 million per individual with the unused portion of an individual exemption portable between spouses) with gifts past the exemption taxed at 35%. That would be better than the alternative: a scheduled $1 million exemption, along with a 55% maximum gift tax rate.[2,3]

The payroll tax holiday. Months ago, the consensus was that this would not survive into 2013. Yet last month, Rep. Christopher Van Hollen, the top Democrat on the House Budget Committee, told C-SPAN that it should be extended. Former Treasury Secretary and Obama administration economic advisor Larry Summers agrees. So it may live on for another year.[4]

The marriage penalty. Our federal tax code has a longstanding quirk: occasionally, married couples pay more in tax than they would if they were single filers. The Economic Growth and Tax Relief Reconciliation Act of 2001 attempted to lessen the penalty in two ways. It made the standard deduction for married joint-filing couples twice what it was for singles, and it made the bottom two tax brackets for those married and filing jointly twice as broad as for singles. In 2013, the marriage penalty could become more severe: the standard deduction for joint filers will be only about 167% of the standard deduction for singles and those widened joint-filer tax brackets are slated to narrow. As middle-income couples will probably face higher payroll taxes in 2013, retaining the current softer penalty seems likely.[2]

Child & childcare tax credits. Both of these credits are set to shrink next year. The child tax credit is supposed to be halved to $500, and the maximum childcare credits available to most parents ($600 for one child aged 12 or younger, $1,200 for more than one) are poised to drop to $480 and $960. Extending these credits into 2013 could amount to good PR for a disdained Congress.[5]

The American Opportunity Credit. In 2009, the up-to-$1,800 Hope tax credit was supercharged into the AOC: an up-to-$2,500 education credit which could be claimed for four tax years that include college education rather than two. In 2013, the AOC is scheduled to disappear with an $1,800 (or possibly $1,900) Hope credit slated to reappear. The AOC may be extended into 2013; again, it would be a popular move at a time when Congress is riding a wave of unpopularity.[5,6]

College expense deduction. Back in 2011, you could write off as much as $4,000 in tuition on your federal return. Some legislators would like to see this deduction made available again in 2013 and perhaps even made retroactively available for 2012. It would be a popular move and it could prove a nice "sweetener" on any bill addressing tax issues for the coming year.[5]

Charitable IRA gifts. Universities and retirees found the IRA charitable rollover quite useful, but it faded away at the end of 2011. Many in the education community (and some in Congress) would like to see it return for 2013, and given that tax hikes seem to be imminent next year, a big tax break like this might be offered pursuant to a Congressional compromise.[5]

IDLs & PEPs. In 2010, itemized deduction limits and personal exemption phase-outs were repealed. In 2013, they may return as the federal government seeks much-needed tax revenues.[2]

Citations.

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