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AMERICAN TAXPAYER RELIEF ACT OF 2012

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American Taxpayer Relief Act Summary

With 2012 behind us, Americans feared that the country had been plunged over the widely publicized “fiscal cliff” when they awoke on New Year’s Day 2013. However, Congress passed, and President Obama signed, the American Taxpayer Relief Act of 2012 (“The Act”) on January 1, 2013, marking the end (at least temporarily) of a hotly debated legislative process that saw brinksmanship from both sides of the aisle. The Act is the product of a compromise between Senate Republicans and Vice President Joe Biden and it permanently extends the Bush-era income tax rates for lower- and middle-income taxpayers, but allows the top rates on earned income, investment income, and estate and gifts to increase from their 2012 levels for wealthier Americans.

Major provisions of the Act include:

- Permanent extension of most individual income tax relief first introduced during the administration of George W. Bush for unmarried taxpayers with income of $400,000 or less and married taxpayers with $450,000 income or less.
- A new top marginal tax rate of 39.6% for unmarried taxpayers with income of $400,000 or more and married taxpayers with $450,000 income or more.
- An increase in the AMT exemption to $50,600 for unmarried filers and $78,750 for married filers in 2012. In addition, the legislation permanently indexed these amounts for inflation.
- A new maximum rate on certain investment income (capital gains and qualified dividends) at 20% for unmarried taxpayers with income of $400,000 or more and married taxpayers with $450,000 income or more.
- Reinstatement of the phase-outs for personal exemptions and the limitation on itemized deductions for single taxpayers with adjusted gross income in excess of $250,000 and joint filers with AGI over $300,000. Like the AMT exemption, these AGI thresholds will be indexed for inflation going forward.
- The extension of a variety of business tax provisions, including the research and development credit and special bonus depreciation rules.

The Act does not, however, extend the payroll tax cut that was in effect for 2011 and 2012, meaning that American workers with W-2 income will see a drop in their take home pay in 2013. The Act also did not do anything to alter the provisions from Patient Protection and Affordable Care Act of 2010 set to take effect in 2013, most notably the 3.8% surtax on net investment income.

Americans across all income levels will likely feel the impact of the Act’s passage, though more than 90% of the tax increases will fall on households with income of $1 million or more according to the Wall Street Journal. Indeed, David Kautter, a tax expert at American University, estimates that a couple with one child and $1 million of income, including $250,000 of itemized deductions, would see a tax increase of approximately $37,000 from 2012.

Despite claims that the Act's passage will help America avoid the "fiscal cliff", there are a number of unresolved issues that will need to be addressed, including the debt ceiling. Most policy experts believe the stage is set for an intense debate on fundamental tax reform and deficit reduction that could endure for the rest of the year and into 2014.