BARRETT
ASSET MANAGEMENT, LLC
SINCE 1937

The New Tax Law and You

Congress took us to the edge of the "Fiscal Cliff" as the clock struck midnight on New Year's Eve. Hours later, they approved the American Taxpayer Relief Act of 2012. We wonder if the name of this law was meant to elicit a chuckle as few people, if any, will experience any true tax relief. We offer you a review on how the new tax law may affect you.

For all wage earners

Regardless of how much you earn, whether it be $6,000 per year or $600,000 per year, income earners across the board will see a paycheck that is 2% less than the previous year as the payroll tax holiday was allowed to expire. This means the full 6.2% of Social Security will now be withheld from your pay as opposed to the previous 4.2%. The tax holiday lasted two years. The wage ceiling on which Social Security is taxed has also been increased to $113,700 from $110,100. The 1.45% Medicare tax is unlimited, but if you earn more than $200,000 an additional 0.9% will also be withheld on income in excess of that amount as a result of the Affordable Care Act of 2010 (commonly referred to as "Obamacare").

Income Earners over $200,000

The Obamacare Medicare surtax will also result in an additional 3.8% tax on net investment income. This tax applies to taxpayers with modified adjusted gross income that exceeds a threshold ($250,000 for married filers and $200,000 for singles). It is important to note that these surtaxes apply to income over the threshold rates, not all of your income.

Income Earners over $250,000

Dependent and Personal Exemptions Decreased

Beginning in 2013, taxpayers with AGI (adjusted gross income) in excess of the levels listed below will lose some or all of their exemption deductions.

- Singles at $250,000
- Married jointly at $300,000
- Head of household at $275,000
- Married filing separately at $150,000

Reduction of Some Itemized Deductions

The same income guidelines apply to itemized deductions. Earners can lose up to 80% of their Schedule A deductions such as mortgage interest, charitable contributions, property taxes, and state income taxes paid.

For Income Earners over $400,000

Tax Rates on Standard Taxable Income

For a large percentage of taxpayers, tax rates will remain the same as 2012. For single filers with taxable income above $400,000, married filers with income over $450,000, married filing separately over $225,000 and heads of household with taxable income over $425,000, the new 39.6% rate will replace the 35% tax rate for income over these amounts. All other tax rates on income will remain the same.

Tax Rate	Single	Married Filing Joint
10%	Up to $8,950	Up to $17,900
15%	$8,951 – $36,250	$17,901 – $72,500
25%	$36,251 – $87,850	$72,501 – $146,400
28%	$87,851 – $183,250	$146,401 – $223,050
33%	$183,251 – $398,350	$223,051 – $398,350
35%	$398,351 – $400,000	$398,351 – $450,000
39.6%	Over $400,000	Over $450,000

Source: IRS

Capital Gains and Dividend Income

If you happen to fall into the highest income bracket on the tax table ($400,000+ income), your marginal capital gains and dividend income tax rate increases from 15% to 20%. Do bear in mind that not all income is created or taxed equally. Depending on the source of income, it can be subject to different tax rates and different bracket thresholds. The American Taxpayer Relief Act of 2012 makes it much more difficult to calculate your overall tax liability.

Estate and Gift Taxes

Taxpayers will be able to leave an extra $130,000 to their heirs free of estate taxes this year under cost-of-living adjustments announced by the IRS. The estate-tax exemption, lifetime gift tax exemption and generation skipping transfer tax exemption for 2013 will be $5.25 million for individuals, up from $5.12 million in 2012. The new legislation also preserves the "portability" feature which allows for any unused portion of a spouse's exemption to be used by the surviving spouse. So for married couples, the combined threshold is $10.5 million. The top estate tax rate will be 40% up from 35%.

Special planning will be required for state estate taxes in some states. To date, none of the states that have enacted a freestanding state estate tax have made the state estate tax exemption portable between married couples. This means that in states where there is a difference between the state estate tax exemption and federal estate tax exemption, married couples will need to include special planning in their estate planning documents in order to take advantage of both spouses' state estate tax exemptions.

Special planning will be required for generation skipping trusts. While the estate tax exemption has been made portable between married couples, the generation skipping transfer tax exemption has not. This means that in order for married couples to take advantage of both spouses' generation skipping transfer tax exemptions, special planning will be required in married couples' estate planning documents.

There is some good news. The annual gift tax exclusion has been increased from $13,000 to $14,000. So you may make gifts of $14,000 to as many people as you wish without having to file a gift tax return or pay gift tax.

Next Steps

Barrett Asset Management has always embraced the notion of tax-advantaged investing. It's not what you make, it's what you keep. Your portfolio manager can help you make sense of this new tax law as it relates to your investment income. We can help you determine if further consultation with your accountant or estate planning attorney is warranted. We also have an in-house financial planner to answer any of your other questions.

Christina Bater, CFP®