COROMANDEL WEALTH MANAGEMENT

Planning Ahead: A Look at Taxes for 2013

George Gagliardi, CFP®, MBA

You can spend the remainder of 2012 preparing for some major tax law changes scheduled to take place in 2013, or you can wait to see what will be passed into law that effects the scheduled income tax rate changes. These tax law changes will impact many investors, and should make for a very interesting and complicated 2013 tax season. With this also being a Presidential election year, there is a lot to watch for over the remainder of the year.

While new issues will likely arise in the coming months, this is an opportune time to focus on what we know currently, and those changes for which taxpayers should consider planning. This article is focused on the major pending changes to income tax rates.

Income Taxes

Looking ahead to 2013, without any Congressional action, the rates for Federal income taxes on ordinary income will change. The following table sets forth the scheduled rate increases:

Marginal Income Tax Rates

2012	2013
10%	**15%**
15%	**15%**
25%	**28%**
28%	**31%**
33%	**36%**
35%	**39.6%**

For those in the highest bracket, the combined marginal Federal income tax rate together with the Medicare contribution surtax will create a 43.4% marginal tax rate on unearned income.

Summary of Key Scheduled Income Tax Changes for 2013

- ✓ **Expiration of the Bush Tax Cuts of 2001 and 2003**
  - Top tax brackets rise from 33% to 36% and from 35% to 39.6%
  - Long-term capital gains tax rate maximum of 15% rises to 20%
  - Dividends will be taxed at ordinary income-tax rates (i.e. qualified dividend tax rate of 15% ends)
- ✓ **A new Medicare tax of 3.8% on net investment income for high income families**
- ✓ **Expiration of the payroll-tax cuts that were passed in late 2010**
- ✓ **Expiration of the Alternative Minimum Tax “Patch”**

Long-Term Capital Gain Rates

The maximum rate on long-term capital gain is scheduled to increase from 15 to 20 percent in 2013. Individual taxpayers in the 10 and 15 percent ordinary income tax brackets currently pay no tax on long-term capital gains. These taxpayers are scheduled to be subject to a 10 percent long-term capital gain rate in 2013. Those in higher income brackets will have their capital gains rate increase to 20%, plus an additional 3,8% for high income families.

Maximum Rates	2012	2013	2013 (including Medicare contribution tax)
Long-Term Capital Gain	15%	20%	**23.8%**

Dividend Income Tax Rates

The Bush tax cuts included "qualified dividend income," which currently allows dividends received from domestic corporations and certain foreign corporations to be taxed at the taxpayer's long-term capital gain rate. Additionally, qualified dividend income earned by stocks, mutual funds and exchange-traded funds may be distributed to shareholders and treated as qualified dividend income by the shareholder. Prior to the Bush tax cuts, all dividend income was taxed as ordinary income. If Congress fails to extend these provisions, the qualified dividend income provisions will expire, and the impact will be that all dividends will once again be taxed as ordinary income. Most notably, taxpayers in the highest marginal income tax bracket who currently enjoy the 15 percent rate on qualified dividend income will be taxed at 39.6 percent for dividends received from the same issuer in 2013. Additionally, the 3.8 percent Medicare contribution surtax discussed below will increase the effective rate of tax on dividend income for certain higher-income taxpayers to as high as 43.4%. The following table reflects the scheduled dividend tax rate increases:

Maximum Rates	2012	2013	2013 (including Medicare contribution tax)
Qualified Dividend Income	15%	39.6%	**43.4%**
Ordinary Dividend Income	35%	39.6%	**43.4%**

New Medicare Contribution Tax

A new 3.8 percent Medicare contribution tax on certain unearned income of individuals, trusts, and estates is scheduled to take effect in 2013. This provision, which was enacted as part of the Patient Protection and Affordable Care Act (PPACA), will happen regardless of whether Congress extends the Bush tax cuts. For individuals in 2013, the 3.8 percent tax will be imposed on the lesser of the individual's net investment income or the amount by which the individual's modified adjusted gross income (MAGI) exceeds certain thresholds ($250,000 for married individuals filing jointly or $200,000 for unmarried individuals). For purposes of this tax, investment income generally includes: interest, dividends, income from trades or businesses that are passive activities or that trade in financial instruments and commodities, and net gains from the disposition of property held in a trade or business that is a passive activity or that trades in financial instruments and commodities. Investment income generally excludes distributions from qualified retirement plans and as well as items that are taken into account for self-employment tax purposes. Any taxpayer who believes that their MAGI will exceed the thresholds described above should consider consulting a qualified tax adviser to plan for the applicability of this tax.

Do You Have A Plan?

For 2013, tax planning will be a critical part of a comprehensive financial plan. Does your investment professional review your tax return?

Not getting the correct advice during tax season can be costly and result in a huge tax headache. If you are not sure whether you have the right information to know whether you are accurately examining all of the opportunities to reduce your tax bill, please take the quick quiz below.

In today's highly complex and rapidly changing world, you are faced with an incredible array of investment choices. Making good investment choices is important, but that's just one part of achieving your overall personal and financial goals.

Make sure that your financial advisor is able to review all of the critical financial planning areas – taxes, estate planning, insurance, retirement, Social Security, investments – and has access to other professionals in these areas (CPAs, estate planning attorneys) who can coordinate with them.

Tax planning should be considered as part of a comprehensive financial plan. Some strategies that individuals might consider for 2012 include:

- ✓ Realizing capital gains prior to 2013.
- ✓ Re-balancing portfolios with a careful review of all investments that produce dividends.
- ✓ Saving for retirement through tax deferred or tax free accounts.
- ✓ Analyzing when to take certain deductions in order to increase their value.

In conclusion, the primary purpose of tax planning is to understand your choices so that you can make investment and planning decisions that help you maximize your income and after-tax investment returns.

Do You Have a Tax Plan for 2013?		
Is the tax basis for all of your existing investments readily obtainable?	***Yes***	***No***
Does your non-retirement account custodian provide you with a list of all of your completed transactions along with the tax losses or gains?	***Yes***	***No***
Does your investment professional do a full review of your tax forms and show you how your investments are impacting your taxes?	***Yes***	***No***
Does your investment professional review your retirement withdrawals to see whether you are using a tax-efficient withdrawal strategy?	***Yes***	***No***
Do you receive reports on the steps investors can take to reduce their taxes?	***Yes***	***No***
Does your investment professional consider tax consequences and alternatives when making new investment recommendations?	***Yes***	***No***

If you answered *NO* to two or more of these questions, then you may not be maximizing your tax strategies.

Reminder: *Always seek out the advice of a qualified financial professional and tax expert to make sure that your taxes are properly planned on your specific terms.*

As a financial planning firm, our goal is to help clients formulate financial strategies for our clients. If you have any questions about yours, please give us a call.

George Gagliardi, CFP®, MBA, is a financial planner with Coromandel Wealth Management in Lexington, MA, and works with clients to develop and implement retirement and investment strategies. He is affiliated with Trust Advisory Group, Ltd., a Registered Investment Advisor, and can be reached at george@CoromandelWM.com or (781) 728-9001.

Complimentary Financial Check-up

If you are not currently a client of Coromandel Wealth Management, we would like to offer you a complimentary one-hour private consultation. To schedule your financial check-up, please call George Gagliardi at: (781) 728-9001.

Coromandel Wealth Management
15 Muzzey Street
Lexington, MA 02421

Phone: 781.728.9001
info@CoromandelWealthMgmt.com
www.CoromandelWealthMgmt.com