Taxpayer Relief Act of 2012

The Taxpayer Relief Act of 2012 was enacted January 2, 2013, of which many provisions are retroactive for 2012 tax. We will review some the most important ones which will affect your dealership and your personal tax returns.

Business Provisions

50% bonus depreciation for new equipment was extended through December 31, 2013. Bonus depreciation allows for write off of 50% of new equipment only and does not apply to used equipment. It also includes most purchased software costs. It increases new car to $11,160 and new truck to $11,360 for first year depreciation.

Section 179 allows for immediate expensing of up to $500,000 of equipment and qualifying real estate in 2013. It was scheduled to be reduced to $139,000 for 2013. The section 179 deduction phases out as purchases exceed $2 million. Unlike 50 percent bonus depreciation, it applies to both new and used assets and is a limited deduction based on taxable income. It applies to "qualifying real property", such as leasehold improvements for third party tenants only and not a related dealership or related finance company. It qualifies for retail improvement, for example, the interior portion of nonresidential property used in the retail trade of selling personal property. It also applies to qualifying restaurant property.

The **15 year depreciation** lives for leasehold improvements and retail space improvements is also extended through December 31, 2013.

Individual Provisions

The **2% payroll reduction** is gone for employees. Effective January 1, 2013, the 2% FICA decrease which had been in existence for two years was eliminated. This means your potential customer's take home pay has been reduced by 2% for 2013 and beyond as compared to 2012.

Tax rates have been increased also for 2013. The 2012 old tax rates were 10%, 15%, 25%, 28%, 33%, and 35% for any income from $388,300 and above. The new rates for 2013 are 10%, 15%, 25%, 28%, 33%, 35%, and 39.6% for any income from $400,000 and above for singles and $450,000 for married filing jointly. While many dealers may not normally make over these amounts, income for dealers from year to year sometimes varies greatly, so it may make sense to plan for such fluctuations if possible to reduce income to below the top brackets.

Some possible options for dealers may be to review inventory market value adjustments, plan the timing of fixed asset purchases with bonus and Section 179 deductions, plan the timing of employee bonuses between years and review year end for possible receivable charge offs.

The **alternative minimum exemption tax patch** has made permanent.

The **personal and dependent exemption** phase out is back permanently for 2013. The exemption may be completely eliminated for some higher income taxpayers. The phase out starts at $250,000 for singles and $300,000 for married filing jointly.

The **itemized deductions** phase out is back permanently for 2013 also. You may lose up to 80% of your itemized deductions for 2013, as the phase out starts at $250,000 for singles and $300,000 for married filing jointly.

Obamacare Taxes

Section 1402 Medicare

Investment Income Tax is effective for tax years beginning January 1, 2013. An additional 3.8% tax will be charged on investment income over the Modified Adjusted Gross Income (MAGI) thresholds of $200,000 for singles, $250,000 for married filing jointly and $125,000 for married filing separately.

The effective top marginal federal tax rate including the tax rate changes from the Tax Reform Act of 2012 is 43.6% of investment income. In some states with high income tax rates, the total income tax rates on some high income investment earnings can be greater than 50%.

Income subject to this Medicare Investment Income Tax consists of interest income, dividend income, capital gains, annuities, net rental income, royalties and passive income.

Income not subject to this additional income tax is active trade or business income such as your dealership or related finance company, distributions from IRA's or other qualified retirement plans, other income treated as self employment and a gain on sale of an active trade of business, such as an S corporation, partnership or sole proprietorship. Although this income is not subject to the additional Investment Income Tax, this income does raise the total income and therefore may move investment income to the threshold level where it does become taxable. Possible timing of this income can help reduce the amount of investment income subject to the Medicare Investment Income Tax.

To help reduce this possible investment income tax, you may consider reducing rent paid to related parties. Reducing rent paid from related parties, such as the dealership and related finance company, will increase the dealership income and decrease rental income subject to the tax.

You can also reduce interest rates on officer notes payable in your dealership and related finance company. Generally interest rates on related party debt can set at between 1% to 1.5% interest rates for up to a nine year note. Also be sure to treat interest paid on intercompany debts as operating income and not classify it as interest income on S corporation and partnership tax returns.

Try to recognize investment income when possible in lower income years and time any possible dividends from reinsurance companies, capital gains and other income subject to this tax.

The **Medicare tax** increases 0.9% to 2.35% as of January 1, 2013 for single with earned income over $200,000 and married filing jointly over $250,000. The tax is assessed on the employee share only, but the employer withholds it. Many taxpayers may have paid themselves large bonuses at year end to pay in required tax withholdings to avoid penalties, but this will cost you the additional increase you are over the limits above. You may want to consider starting to pay quarterly estimated tax payments instead to meet your required tax withholdings.

Well we have covered some of the main changes which may affect most dealers and their dealerships. You still have time to plan and institute your income changes before year end. Not doing so may increase your income tax needlessly.

TAX TIP

Obama Administration Postpones Large Employer Health Care Mandate Until 2015

The Obama Administration has announced that it is postponing for a full year, until 2015, the Patient Protection and Affordable Care Act's (PPACA) mandatory employer and insurer reporting requirements. As a result of not obtaining this reporting information in 2014, the administration also announced that it will waive the imposition of any employer penalty payments for 2014. This effectively means that employers with 50 or more employees will not be required to provide health insurance to their employees until 2015.

In addition to the one-year delay, the administration said it is also cutting red tape and simplifying the reporting process.

Republican leaders, however, called the delay an admission that the law is a failure. Republicans further condemned the delay, saying it is a concession to big business interests while the administration still expects the middle class to comply. The announcement did not address the individual mandate that goes into effect in 2014 and requires most individuals to obtain health insurance or pay a penalty. Nor does it apparently delay implementation of marketplace exchanges.

Your ATA representative will keep you informed with any new developments with respect to the implementation of the employer health care mandate.