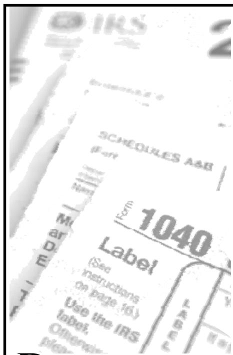


BATSON
ACCOUNTING & TAX, P.A.

TAX NEWSLETTER

DISASTER AVERTED....

OK, we made it past the fiscal cliff. But at a price that most of us will begin paying in 2013. As expected, tax rates will climb and the rules will be as complicated and confusing as ever. For everyone, there is a tax increase.

The American Taxpayer Relief Act increases individual tax rates for those with taxable incomes over $400,000 ($450,000 for families), revives certain credits that were scheduled to expire, maintains a $5,000,000 exclusion for estate taxes but at a 40% max rate, and permanently "patches" the alternative minimum tax (AMT).

You may say, "I don't make $400k so this doesn't bother me." Don't feel left out because payroll taxes on all wages & salaries will go up 2% and there is a new Medicare tax of 3.8% on net investment that will affect individuals with gross income over $200,000 ($250,000 MFJ). To boot, phase outs of itemized deductions and personal exemptions return for the 2013 year.

There's plenty for each of us to dislike. On the other hand, the Act did avoid draconian sunset provisions that would have changed all tax rates, capital gains treatments, child credits, estate taxes and more. The cost of no action would have been far worse than what we got.

INSIDE THIS ISSUE:

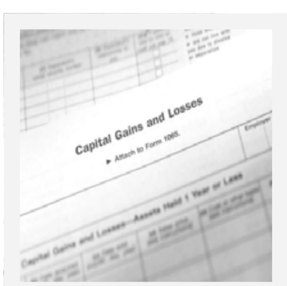
INDIVIDUAL TAX RATES

Effective for 2013, the American Taxpayer Relief Act makes the Bush-era rates permanent for those with taxable incomes less than $400,000 single, $425,000 head of household, $450,000 MFJ. Income above these rates will now be taxed at 39.6% up from the 35% prior bracket. Rates did not change for 2012.

The same brackets (10%, 15%, 25%, 28%, 33% and 35%) will apply for 2013. But the 39.6% bracket will be added as the top rate.

CAPITAL GAINS/DIVIDENDS

For individuals in the same threshold group mentioned above ($400k area), the top rate for capital gains and dividends raises to 20% from the prior 15% max rate. All other taxpayers will still use the 15% max rate and, surprisingly, the zero percent rate for capital gains will still apply to capital gains and dividends to the extent income falls below the top of the 15% income tax bracket.



Capital gains from installment sale profits will be subject to the rates and rules in place in the year of the payment, not the year of sale. So someone selling on an installment basis in 2012 may elect to pay tax on all capital gains in that year to avoid the higher rates in years ahead.

The Act does not affect sale of principal residence gains, which are still tax free generally up to $250,000 per individual, $500,000 married filing jointly.

ITEMIZED DEDUCTION LIMITATION (PHASE OUTS)

Mortgage interest expense, income taxes, property taxes, charitable contributions, medical expenses (subject to limits), mortgage insurance premiums (subject to limits), and miscellaneous items are still deductible as itemized deductions, as well as the personal exemption. For 2010 and 2011, you were able to deduct these without phase outs due to higher incomes.

> "THE HARDEST THING IN THE WORLD TO UNDEDRSTAND IS THE INCOME TAX."
>
> -ALBERT EINSTEIN

However, the phase out of deductions begins again in 2013. Essentially, itemized deductions begin to be phased out at income levels of $300,000 MFJ, $250,000 single and $150,000 MFS. Phase outs will also apply to personal exemptions.

The effect of this obviously is to raise tax revenue for higher income taxpayers without raising rates. And it adds more complexity to the filing of returns.

NEW 3.8% MEDICARE SURTAX – EFFECTIVE 2013

For those with modified gross income of $250,000 MFJ, $200,000 single, $125,000 MFS, a 3.8% tax will apply to net investment income. Net investment income is generally to be considered interest, dividend and capital gain income. This tax provision was actually passed in 2010 to help cover the cost of health care reform.

Again, those in lower income categories won't be affected by this.

But for those individuals whose taxable incomes are over the thresholds, the effective maximum tax rates for capital gains and dividends will go up by as much as 8.8% (5% capital gain rate increase plus 3.8% Medicare surtax). That is significant.

ADDITIONAL .9% MEDICARE TAX – EFFECTIVE 2013

Currently, the Medicare withholding tax is 1.45% of wage and salary income, and this amount is matched by employers for a total of 2.9%.

Effective in 2013, however, an additional .9% Medicare tax is required to be withheld from employee wages and salaries exceeding $200,000. The employer does not have to match this.

This is going to become tricky for 2013 filing because the .9% tax will be required when married couples' incomes exceed $250,000. For example, John may earn $190,000 and Mary may earn $150,000 and neither will be subject to the .9% withholding. However, on their 2013 tax filing, their combined salary income is $340,000. $90,000 will be subject to .9% Medicare tax ($340,000 less $250,000 threshold) which they will pay with the income tax return.

ALTERNATIVE MINIMUM TAX

AMT was originally intended to ensure that wealthy taxpayers paid a "minimum tax" rather than using loopholes to escape taxes altogether. Over the years, because of lack of inflation indexing, AMT has snared millions of taxpayers Congress probably never intended to penalize. It causes taxes to be higher than they would be under the usual rules. Yet, the revenue generated is significant so it hasn't been revised.

Fortunately for 2012 and going forward, "patches" have been made to AMT in the form of increased exemptions and promises to index for inflation. While these won't make AMT go away, these patches will reduce the effects on many and will reduce the number of people who would otherwise have been subject to AMT.

AMT is neither simple nor easily predictable. We will, however, always determine whether your filings are subject to AMT and will let you know the effects.

AUTO EXPENSES AND STANDARD MILEAGE RATES

If you use your personal vehicle for business purposes, the standard mileage rate can be used to simplify record keeping and to allow for adequate reimbursement of expense. For 2012, the rate was 55.5 cents per mile. For the year 2013, the rate is 56.5 cents. Rates for medical, moving, and charitable mileage are different and are listed in the box to the right.

It is important that you maintain a log of your business mileage to include date, places travelled, business reason and mileage. If you are audited, IRS will require that you provide a copy of the log; if it isn't available, they can deny the deduction.

MILEAGE RATES

TYPE	2012	2013
Business	55.5	56.5
Medical/ Moving	23	24
Charitable	14	14

SMALL BUSINESS EXPENSING

The new act does extend Section 179 small business expensing of capital assets purchased. For years 2012 and 2013, up to $500,000 of capital assets acquired may be expensed in the year of purchase ($2,000,000 investment limit). This provision exists to encourage business purchases of assets and would have been significantly reduced without the new act.

Additionally, the Act extends 50% bonus depreciation through 2013.

To be eligible for Sec 179 expensing, acquired property can generally be new or used assets. But to be eligible for bonus depreciation, the property must be new.

ESTATE TAX

Federal transfer taxes (estate, gift and generation-skipping transfer (GST) taxes) seem to have been in a constant state of flux in recent years. The American Taxpayer Relief Act aims to provide some certainty. Effective January 1, 2013, the maximum estate, gift and GST tax rate is generally 40 percent, which reflects an increase from 35 percent for 2012. The exclusion amount for estate and gift taxes is unchanged for 2013 and subsequent years at $5 million (adjusted for inflation). The GST exemption amount for 2013 and beyond is also $5 million (adjusted for inflation).

TAX CREDITS AND DEDUCTIONS

Like the Bush-era income tax cuts, many popular tax credits and deductions were scheduled to expire after 2012 (in some cases, they expired after 2011). The Act makes some of these incentives permanent and extends others. One of the most widely used tax credits, the $1,000 child tax credit, is made permanent. If Congress had not acted, the $1,000 child tax credit would have decreased to $500 per qualifying child for 2013 and beyond. The $1,000 amount is not, however, indexed for inflation.

Other popular tax credits and deductions for individuals made permanent or extended by the new law are listed in the box to the right:→

- Enhanced adoption credit/exclusion (permanent)
- Enhanced child and dependent care credit (permanent)
- Enhanced student loan interest deduction (permanent)
- American Opportunity Tax Credit (through 2017)
- Higher education tuition deduction (through 2013)
- IRA distributions to charitable organizations (through 2013)
- Transit benefits parity (through 2013)
- Cancellation of indebtedness on principal residence (through 2013)
- Code Sec. 25C residential energy efficient property credit (through 2013)
- Teachers' classroom expense deduction (through 2013)

AUDIT STATISTICS

In March 2012, the IRS released audit rates for fiscal year (FY) 2011, which show a general show an uptick in audits, especially of higher income taxpayers. Individual taxpayers were collectively audited as a 1.1 percent rate over the FY 2011 period. The audit rate for individuals with adjusted gross incomes (AGI) between $200,000 and $500,000 was 2.66 percent in FY 2011 compared to 1.92 percent in FY 2010. The audit rate for individuals with AGI between $500,000 and $1 million was 5.38 percent in FY 2011 compared to 3.37 percent in FY 2010. For individuals with AGI between $1 million and $5 million, the audit rate increased from 6.67 percent in FY 2010 to 11.80 percent in FY 2011.

"THE WAGES OF SIN ARE DEATH, BUT BY THE TIME TAXES ARE TAKEN OUT, IT'S JUST SORT OF A TIRED FEELING."
-- COMEDIAN

AUDIT ACTIVITY IN OUR PRACTICE

To our knowledge, none of our clients became newly engaged in field audits during 2012, thankfully.

However, three of our clients who had adopted children in prior years had to prove the expenses they paid in order to keep their adoption credits. In one case, a federal refund of about $6,000 was held up by IRS until the taxpayer proved adoption expenses incurred in a prior year. This was a tedious exercise as the receipts were written in a foreign language, exchange rates had to be proven, legal adoption papers had to be interpreted, and passport information for the child was complicated. Ultimately in all of these cases, however, our clients won and there were no adjustments. IRS had to pay interest on the money owed on the refund delayed.

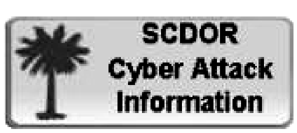
More commonly nowadays, the correspondence audit is being used. IRS computers will identify areas to be questioned and letters will be issued requesting proof of deductions or information regarding income. Our experience is that many of these are more annoying than substantive, but nevertheless the taxpayer is required to respond by mailing copies of receipts and proof of payment or other information.

SC CYBER ATTACK & ELECTRONIC FILING

The hacking of South Carolina's Department of Revenue data files continues to alarm us and as of this writing, there is still no assurance the State has a fix. We have been told by SCDOR that as of January 30th, e-filing with the State will be "safe". Exactly what that means was not defined but we intend to monitor developments.

For federal purposes we are required to file your returns electronically unless you opt out, which you have the right to do. Despite the state problem in 2012, e-filing will still get your refund paid faster. And the hacking has already been done.

For more information regarding the cyber attack and to enroll in the state provided identity protection program, visit the SCDOR website at: www.sctax.org and click on the image shown here:



DELAYED FILING

Because of the late passage of the American Taxpayer Relief Act, IRS is having to reprogram its computers or change forms in a number of areas. IRS has announced that filing may begin on January 30, 2013 for returns whose forms aren't affected.

However, IRS says that several forms won't be completed until late February or March. These include Form 4562 (Depreciation and Amortization), Form 5695 (Residential Energy Credits) and Form 3800 (General Business Credits). If your returns require these forms, your filing will be delayed.

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AUTHORIZED IRS e-file PROVIDER

SCACPA

NSA National Society of Accountants

A NOTE FROM PAUL...

At the beginning of every year as we prepare for the very busy time, I reflect gratefully on relationships that have been developed with so many of you over the years. In one way or another we are all "graying" together, some of us literally and some of us aspiring. Over the years and to this day, it is a pleasure for all of us at Batson Accounting to work with you, to advise you and to plan ahead.

This filing season will be challenging as we all absorb the changes, but we will do our best to make it as painless as possible for you. Can't promise your taxes will be less, but we'll do the best we can with the rules we are given.

To all of you, I express my thanks for your confidence, your friendship and your continued reliance on our knowledge and service. I look forward to seeing you soon.

Best wishes to all,

Paul Batson

Paul O. Batson, III

DISCLOSURE OF INFORMATION

Regulations with regard to our providing copies of tax returns to outside parties are causing an increased bureaucratic workload. In order to provide copies of your returns to any outside party, we are required to have your specific written consent in advance stating the purpose of the disclosure. We'll continue to assist you and will help with the paperwork.

Questions often asked…

"Does the new tax act allow me to donate to charity directly from my IRA?"

Yes, the Act extends for two years, through December 31, 2013, the provision allowing tax-free distributions from individual retirement accounts to charities by individuals age 70 ½ or older, up to a maximum of $100,000 per year.

"In 2012, my mother gave me the proceeds from a certificate of deposit she owned. It was $100,000. How much tax will I owe on this?"

None. Gifts received do not constitute income so long as they are truly gifts, i.e., no expectation of services or items in exchange. Gifts received are not includable on your tax filing nor are they taxable. However, in certain cases, the giver may be required to file a Gift Tax return.

"My wife and I divorced in 2011 and she has custody of our child. If I paid for the cost of day care, may I claim the dependent care credit on my tax return?"

No. Your child must be your dependent in order to claim the dependent care credit or the child tax credit.

"I sold my primary residence in 2012 and had to spend a lot of money on repairs prior to the sale and I also lost money on the sale. How do I deduct these costs?"

You may not deduct the cost of repairs for a principal residence nor may you deduct the loss. However, gains from sale of principal residences are still excluded from taxation up to $250,000 per person ($500,000 MFJ).

"During 2012, my rental property required a lot of maintenance such as painting, cleaning, deck repair and other work. I kept a detailed log of the hours I spent doing the work. May I deduct the value of my labor as a repair?"

No. Only what you actually paid for labor and materials is potentially deductible. IRS prohibits deducting the value of our own labor.

"A family member died in 2012 and I inherited her house. Late in 2012, I sold the house for $180,000. How much tax do I have to pay?"

Likely no tax. You must first determine your cost basis in the property, which will be the fair market value at the time of the death of your family member. If the property sold for less than that amount, you'll have a loss and no tax. If the property sold for more than the cost basis, you would have a gain and would pay tax on the gain. However, you'll pay no tax on the inherited asset itself.

"I contributed a lot more money to my church this year than usual. I don't want to create any red flags on my return so should I just not deduct all of it?"

Deduct all of it. We don't know all the triggers that cause audits, but we should never be afraid to take legitimate deductions. As long as you have receipts and evidence of payment, you are covered and should not fear IRS.