

TAX LETTER

New Year, New Tax Rules

Dear Clients and friends,

Regardless what happened to the so called “Fiscal Cliff”, the following new tax rules are here with us:

Federal

A) Regarding Social Security (OASDI) Taxes

For both employee and employer the OASDI portion of the FICA tax for 2013 will be 6.2% for employee and 6.2% for employer. This flat tax will be assessed for salary and/or wages up to \$113,700.

For self-employed individual, it will be 12.4% of net self-employment income, max at the same threshold as for employee.

B) Regarding Medicare Taxes

The basic Medicare tax rate will remain at 2.9% (1.45% for employee and 1.45% for employer) on unlimited salary and/or wages. This basic Medicare tax will be the same for self-employ individual.

C) Regarding the new additional Medicare tax

For earning from salary/wages exceeding \$200,000, there will be an additional 0.9% (total 2.35%) Medicare tax assessment. Regardless the employee’s earning/deduction/marital situation, employer must withhold an additional 0.9% from the employee. However, employer will not be required to pay this additional 0.9%. Any over withholding due to individual employee’s total earning and marital status, the employee will be allowed to make a credit against total income tax due or claim a refund

For self-employed individual, if their Modified AGI (Adjusted Gross Income) is greater than \$200,000 single and \$250,000 married filing jointly, the additional 0.9% will be assessed on earning or profit in excess of the allowed threshold.

D) Regarding the new 3.8% Medicare Surtax

This 3.8% Surtax is an additional tax on top of all other taxes that a taxpayer has to pay.

For individuals, this 3.8% surtax will be assessed on the **lesser of** (i) net investment income (NII), or (ii) Amount of Modified AGI in excess of \$200,000 for single and \$250,000 for married filing jointly.

Net investment income (NII) for individual including interest, dividend, annuity, royalty, rent net of allowable expenses and net gain from sale or exchange of tangible and/or real property. Tangible and real property held in or by a trade or business will be exempted from this surtax [re: IRC Section 1411 (c)] .

Further, for the purpose of this surtax, ordinary income/profit from a trade or business conducted by a sole proprietor, partnership or S corporation will not be included as part of NII.

However, income generated by a trade or business (i) from an IRC Section 469 passive activity and (ii) from trading in financial instrument and/or commodity will be included as part of NII.

Other than for individual, there are rules which will be applicable to different type/nature of Trust and Estate. Currently, the IRS is in process of promulgating more rules and regulations. Once they are clear, we will make another attempt to explain.

California

In November 2012, California voters passed Proposition 30 which increased the individual income tax rates and the State sales tax. From 2013 to 2016, the State sales tax will be increased by 0.25%.

(E) Regarding Individual Income Tax

Effective **retro-actively** back to January 1, 2012, will be modified as follows:

<u>Single Taxpayer</u>	<u>Married Filing Joint</u>	<u>2012 retroactive Marginal tax Rate</u>
Below 48,943	Below 97,885	Same as for 2011
48,943 - 250,000	97,885 - 500,000	9.3% (2011 Max rate)
250,001 - 300,000	500,001 - 600,000	10.3%
300,001 - 500,000	600,001 - 1,000,000	11.3%
500,001 or more	1,000,001 or more	12.3%
More than 1,000,000	More than 1,000,000	13.3% *
* (1% Mental Health Surtax for taxable income in excess of 1,000,000)		

2012 problem - the quarterly deposit and/or State income tax withheld, for some higher income (say single wage earner \$250,000 or more) taxpayers may not be sufficient. Certain catch up may be necessary.

F) Regarding Net Operating Loss ((NOL) carry over from prior year(s)

The California NOL carry over **Suspension** was not extended to 2012. As a result individual and business with qualified NOL from prior years which could not be used in 2011 and earlier years due to the Suspension, now can be carried over to 2012. This is a good news.

Sincerely,

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An Accountancy Corporation