Willson & Pechacek, P.L.C. Newsletter

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THE LOOMING FISCAL CLIFF: WHAT ARE THE POTENTIAL OUTCOMES?

Now that the election is over, and the players remain exactly the same, it remains to be seen what will happen with regards to the fiscal cliff the taxpayers of the United States are peering over as January 1, 2013 nears. If Congress does nothing, the United States will plunge over the fiscal cliff in less than 2 months, taxes will rise for 90% of Americans due to automatic increases in income, payroll and other tax law changes. According to the Tax Policy Center, it is predicted that taxes will rise by $500 billion in 2013, or an average of almost $3,500.00 per household, if there is no change and the laws as currently written do take effect on January 1, 2013. The fiscal cliffs looms because the Bush ordinary income tax rate cuts will expire on December 31, 2012. If Congress does nothing, the income tax rates will change to 15%, 28%, 31%, 36%, and 39.6% from the present levels of 10%, 15%, 25%, 28%, 33% and 35%.

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HEALTHCARE REFORM AND NEW TAXES

The Patient Protection and Affordable Care Act was passed by Congress in 2010 and is still in the process of being implemented. Over each of the next two years, new taxes will be imposed. Here is how they will work:

Beginning January 1, 2013 a new 3.8% surtax will be imposed on investment income for those taxpayers whose income exceeds $250,000 ($200,000 for singles) and only to the extent their net investment income exceeds those thresholds. For example, if you are a joint filer with income of $260,000 of which $50,000 is investment income you will pay the surtax on $10,000 of investment income.

Investment income subject to the rule generally includes passive income while excluding retirement income or income derived from a trade or business. For example, in a sale of farmland, a passive landlord who sells the underlying farm property would potentially be subject to the surtax; however, a selling farmer who was active with the farming operation would be excluded.

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This is an average rate increase of 3 to 5% across all the tax brackets.

In addition to the income tax brackets, the Bush tax cuts on capital gain income and dividend income will also expire at the end of the year. If no action is taken, the long term capital gain rate will raise to 20% from the current 15% for the top four tax brackets. At the bottom, they will rise to 10% from 0%. The dividend rate will also rise to the ordinary income tax rates for each tax bracket or as high as 39.6% for top earners. Dividends are now taxed at a 15% maximum tax bracket rate, and the lower brackets are taxed at a 0% rate.

In addition, under the current Obamacare Healthcare Law, regardless of what happens to the fiscal cliff, investment income above $200,000.00 for single filers, and $250,000.00 for married filing joint filers will also be subject to the new 3.8% tax under Obama's Healthcare Law. Therefore this means that dividends will effectively be taxed at a 43.4% rate for the highest income tax bracket (39.6 + 3.8).

The current cut in the payroll tax that funds the Social Security Pension Program was extended earlier this year in an effort to boost the economy. The current 4.2% rate paid by employees, down from the previous 6.2% rate, expires on December 31, 2012 also. Therefore, if there is no change to the current law, every employee and self employed individual will be subject to a 2% payroll tax increase starting January 1, 2013.

There is even a bigger cliff looming for the Federal Estate Tax and the exemption available. Under the current law, the first $5,120,000.00 worth of assets are exempt, anything over the $5,120,000.00 exemption is currently taxed at a 35% maximum rate. On January 1, 2013, the exemption will drop down to $1,000,000.00 and the tax rate will increase to a maximum 55% rate. For example, a farmer with $5,120,000.00 worth of farmland will pay no Federal Estate tax if he passes away in December, 2012. That same farmer with a $5,120,000.00 estate that passes away in January, 2013 will pay over $2,000,000.00 in federal estate tax. — a dramatic difference in federal estate tax liability.

If you have any questions how to best plan for the upcoming uncertainty, please do not hesitate to contact us. There are still planning opportunities regardless of what the Tax Code will be starting January 1, 2013.

BY LONNY L. KOLLN II

IOWA'S LAW ON MECHANIC'S LIENS CHANGES

Effective January 1, 2013, there are some significant changes with regard to how mechanic's liens are filed in the state of Iowa. The most important change is that general contractors, subcontractors, and owner-builders will no longer perfect their mechanic's liens by filing with the clerk of the district court. Instead, they will post information on their liens to a state construction registry internet website.

The Secretary of State's office will maintain the state construction registry internet website and be responsible for its administration. One of the duties of the Secretary of State's office will be to send out various notices to homeowners regarding liens on their home.

In order to perfect a mechanic's lien, contractors must post to the website a verified statement of account setting forth the amount of the demand due as well as the following: (a) the date when material was first furnished or labor as first performed and the date when material was last furnished or the last of the labor performed; (b) the legal description of the property charged with the lien; (c) the name and last known mailing address of the owner of the property; (d) the address of the property or a description of the location of the property if the property cannot be reasonably identified by address; and (e) the tax parcel identification number.

The new law also provides that general contractors or owner-builders who contract with subcontractors to provide labor or furnish material shall post a notice of commencement of work to the website within ten days of the commencement of work.

In the event a general contractor or owner-builder fails to post the notice, the subcontractor may post the notice in conjunction with the filing of the required preliminary notice to the website. As long as the subcontractor posts the preliminary notice before the balance due is paid to the general contractor or owner-builder, the lien is effective as to all labor, service, equipment and material furnished to the property by the subcontractor.

When the mechanic's lien is satisfied by payment of the claim, the general contractor, subcontractor or owner-builder shall acknowledge satisfaction thereof.

If you have any questions regarding the changes to Iowa's law on mechanic's liens, feel free to contact our attorneys for more information.

BY KYLE A. MARCUM

The second tax beginning January 1, 2013 for those households whose income exceeds $250,000 ($200,00 for singles) is a .9% increase in Medicare tax for wage earners and the self-employed. This is an additional "employee share" to be withheld from paychecks. Other items beginning in 2013 include a new $2,500 limit to contributions to employer provided flexible spending accounts. These accounts let individuals save pre-tax dollars for use for medical expenditures for the year. The penalty for making non-medical withdrawals also increases from 10% to 20%.

Beginning January 1, 2014, everybody must have health insurance or pay a penalty tax. The amount of the tax is phased in to the full amount by 2016, but begins in 2014 with $95, but can be as much as $2,085 by 2016.

As you can see, the new taxes are complicated and may affect individuals differently depending on their circumstances. If you would like to discuss these tax matters further, feel free to contact our attorneys.

BY LEE M. RANKIN

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