Chart of the Month

November 2012

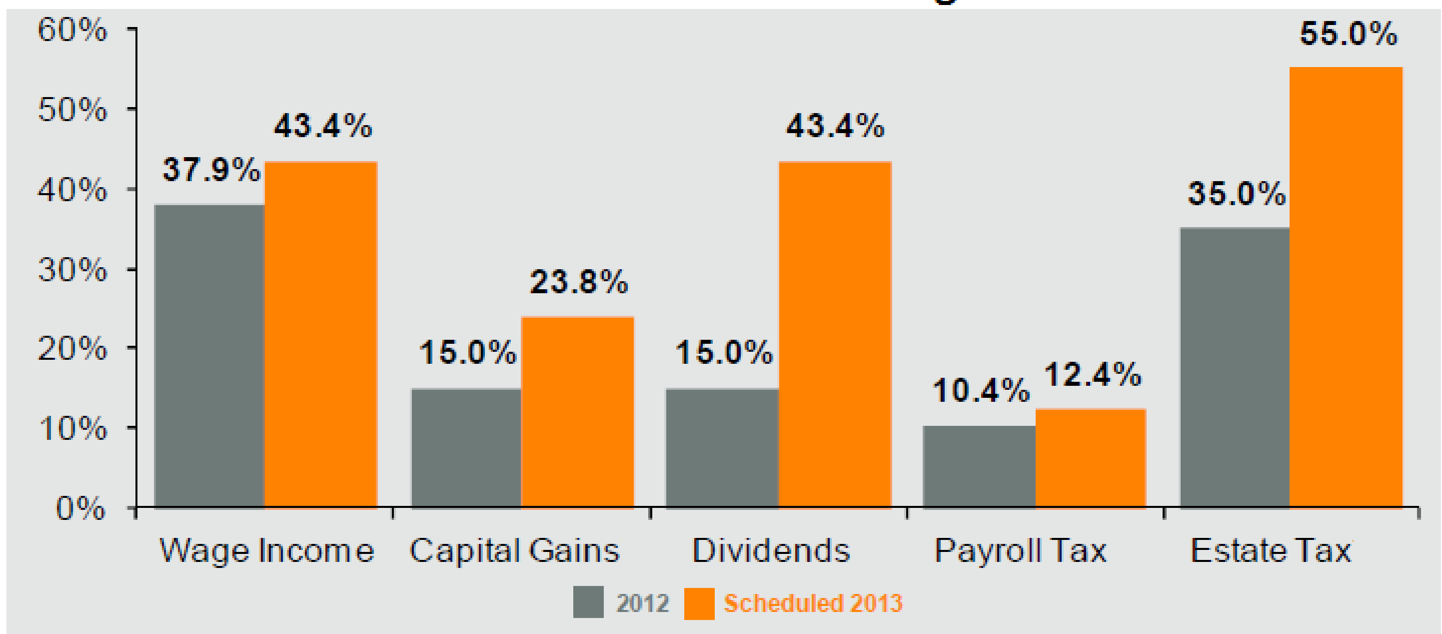
If the so-called Bush tax cuts expire on December 31, 2012, tax rates on wages, interest, dividends, and capital gains will rise across all income brackets to their prior levels. Specifically, the current 10% bracket will go away and the lowest new bracket will jump to 15%. The existing 25% bracket will move up to 28%, the 28% bracket will go to 31%, the 33% bracket will rise to 36%, and the 35% bracket will return to 39.6%. Meanwhile, the maximum federal rate on long-term capital gains will increase from 15% to 20% while the maximum rate on dividends will skyrocket from 15% to 39.6%.

Due to the Healthcare Act, capital gains and gross income from interest, dividends, annuities, royalties, and rents will also be subject to an additional 3.8% tax (equalizing the new Medicare tax on employee compensation), raising the maximum rates on wages and dividends to 43.4% and capital gains to 23.8%.

Furthermore, the combined employer and employee payroll tax will revert to 12.4% while the estate tax exemption will fall from $5.12 million to $1 million and the tax rate on estates over $1 million will jump from 35% to 55%.

As a result of the passage of Proposition 30, California residents will also be subject to higher state taxes on incomes over $250,000. Lastly, the phase-out on personal exemptions and itemized deductions for mortgage interest, state and local taxes, and charitable donations will be back in full force in 2013.

While hopeful that meaningful tax and spending reform will be enacted shortly before or after the end of the year, we believe a temporary fix is the most likely outcome. That said, it is important for our leaders to recognize that should they decide to "kick the can down the road" once again, the markets will eventually force them to deal with our fiscal crisis. Therefore, lawmakers need to work together sooner rather than later.



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