

**February 2012**

*From evolving market trends to new legislation, change is a constant in our industry. M Marketing Intelligence Reports are designed to support Member Firms with insightful commentary that addresses these changes, and their impact on the life insurance market, and adds value to client and advisor relationships.*

## Scheduled Inflation Adjustments for 2012

### Background & History

On December 17, 2010, President Obama signed into law the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the 2010 Tax Relief Act). The Act, which took effect on January 1, 2011, contains a two-year extension of income and capital gains tax law changes that were introduced with the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), the Jobs and Growth Tax Relief Reconciliation Act, and subsequent legislation. In addition, the 2010 Tax Relief Act reintroduced the estate tax with a \$5 million exemption and a 35 percent top tax rate and reunified the estate and gift tax systems.

The following changes are scheduled to apply for 2012 under current law. It is worth noting that, absent any additional legislative action, many of the core provisions of the tax code affecting income, estate, gift, and generation skipping taxes are scheduled to change substantially on January 1, 2013. This includes significantly higher tax rates and reductions in both exemptions and deductions. Careful attention will be required throughout 2012 as to the effect developing legislation may have on planning decisions.

### Federal Income Taxes

Marginal income tax rates in 2012 will remain unchanged from 2011 levels. The taxable income amounts within the brackets will be slightly indexed upward (a two to three percent increase). There was no adjustment for the Alternative Minimum Tax.

2012 Tax Brackets, Incremental by Taxable Income				
Tax Bracket	Married Filing Jointly	Married Filing Separately	Head of Household	Single
10% Bracket	\$0 – \$17,400 <i>\$0 – \$17,000 in 2011</i>	\$0 – \$8,700 <i>\$0 – \$8,500 in 2011</i>	\$0 – \$12,400 <i>\$0 – \$12,150 in 2011</i>	\$0 – \$8,700 <i>\$0 – \$8,500 in 2011</i>
15% Bracket	\$17,400 – \$70,700 <i>\$17,000 – \$69,000 in 2011</i>	\$8,700 – \$35,350 <i>\$8,500 – \$34,500 in 2011</i>	\$12,400 – \$47,350 <i>\$12,150 – \$46,250 in 2011</i>	\$8,700 – \$35,350 <i>\$8,500 – \$34,500 in 2011</i>
25% Bracket	\$70,700 – \$142,700 <i>\$69,000 – \$139,350 in 2011</i>	\$35,350 – \$71,350 <i>\$34,500 – \$69,975 in 2011</i>	\$47,350 – \$122,300 <i>\$46,250 – \$119,400 in 2011</i>	\$35,350 – \$85,650 <i>\$34,500 – \$83,600 in 2011</i>
28% Bracket	\$142,700 – \$217,450 <i>\$139,350 – \$212,300 in 2011</i>	\$71,350 – \$108,725 <i>\$69,975 – \$106,150 in 2011</i>	\$122,300 – \$198,050 <i>\$119,400 – \$193,950 in 2011</i>	\$85,650 – \$178,650 <i>\$83,600 – \$174,400 in 2011</i>
33% Bracket	\$217,450 – \$388,350 <i>\$212,300 – \$379,150 in 2011</i>	\$108,725 – \$194,175 <i>\$106,150 – \$189,575 in 2011</i>	\$198,050 – \$388,350 <i>\$193,950 – \$379,150 in 2011</i>	\$178,650 – \$388,350 <i>\$174,400 – \$379,150 in 2011</i>
35% Bracket	Over \$388,350 <i>Over \$379,150 in 2011</i>	Over \$194,175 <i>Over \$189,575 in 2011</i>	Over \$388,350 <i>Over \$379,150 in 2011</i>	Over \$388,350 <i>Over \$379,150 in 2011</i>

## Inflation Adjustments for 2012 (continued)

### Personal Exemption and Standard Deduction

The personal exemption in 2012 will increase by \$100 to \$3,800.

The standard deduction, claimed by taxpayers who don't itemize deductions, will increase by \$300 for married couples (to \$11,900) and by \$150 for singles and married people filing separately (to \$5,950). The standard deduction for head of household will be \$8,700 in 2012 (an increase of \$200).

### Federal Estate and Gift Taxes

Both the estate and gift tax exemption amount will be subject to an inflation adjustment in 2012 that increases the amount from \$5 million to \$5.12 million, representing a 2.4 percent increase. The annual exclusion will remain unchanged at \$13,000.

The amount of the annual gift tax exclusion for gifts to a spouse who is not a U.S. citizen will rise to \$139,000 (up from \$136,000 in 2011). The amount of a gift from a foreign person required to be reported under IRC Sec. 6039F will increase from \$14,375 in 2011 to \$14,723 in 2012.

### Generation Skipping Taxes

Along with estate and gift tax exemptions, the generation skipping tax exemption will also increase from \$5 million to \$5.12 million.

### Capital Gains and Dividends

Long-term capital gains and qualified dividends will continue to be taxed at a maximum of 15 percent. Short-term capital gains will continue to be taxed at ordinary income tax rates.

### Individual Retirement Accounts (IRAs)

Although the maximum annual contribution to a traditional IRA remains unchanged at \$5,000, modified adjusted gross income (MAGI) limits that determine if a traditional IRA contribution is deductible have increased by two to three percent.

If 2012 federal income tax filing status is:	IRA deduction is reduced if MAGI is between:	Deduction is eliminated if you MAGI is:
Single or head of household	\$58,000 – \$68,000 <i>(up from \$56,000 in 2011)</i>	\$68,000 or more
Married filing jointly or qualifying widow(er)*	\$92,000 – \$112,000 (combined) <i>(up from \$90,000 in 2011)</i>	\$112,000 or more (combined)
Married filing separately	\$0 – \$10,000	\$10,000 or more

*\*If not covered by an employer plan but a spouse is, the deduction is limited if the MAGI is \$173,000 to \$183,000, and eliminated if the MAGI exceeds \$183,000.*

MAGI limits that determine how much can be contributed to a Roth IRA account have also increased.

If 2012 federal income tax filing status is:	IRA contribution is reduced if MAGI is between:	Contribution is eliminated if you MAGI is:
Single or head of household	More than \$110,000 but less than \$125,000 <i>(up from \$107,000 in 2011)</i>	\$125,000 or more
Married filing jointly or qualifying widow(er)	More than \$173,000 but less than \$183,000 (combined) <i>(up from \$169,000 in 2011)</i>	\$183,000 or more (combined)
Married filing separately	More than \$0 but less than \$10,000	\$10,000 or more

### Retirement and Pension Plans

The maximum annual elective deferral contributions to a 401(k) plan has increased from \$16,500 in 2011 to \$17,000 in 2012. This increase also applies to 403(b), 457(b), and SAR-SEP plans.

The maximum annual amount that can be allocated to a defined contribution plan has increased from \$49,000 in 2011 to \$50,000 in 2012, plus age-50 catch up contributions. The annual benefit limit for defined benefit plans will increase from \$195,000 to \$200,000.

The compensation limit for determining benefits and contributions will increase from \$245,000 to \$250,000. Additionally, the definition of a highly compensated employee will go from \$110,000 to \$115,000 in 2012.

### Social Security

In February of this year, Congress passed an extension of the 2011 social security tax rate reduction, which will keep the two percentage-point rate reduction at 4.2 percent for employees and 10.4 percent for self-employed persons throughout 2012. The social security wage base will rise from \$106,800 in 2011 to \$110,100 in 2012. The threshold for coverage under social security and medicare for domestic employees will be \$1,800 in 2012, up from \$1,700 in 2011.

### Conclusion

It is important to acknowledge that the scheduled adjustments described above for 2012 are subject to change, pending possible actions by the IRS and the U.S. government. As 2011 draws to an end, the necessity for broad-based tax reform continues to be debated in Congress. Now is an excellent time to consider the importance of careful planning, and to emphasize flexibility so that appropriate adjustments can be made as the situation evolves.

## For More Information

To learn more about the inflation adjustments of 2012, please contact a member of M Financial's Advanced Markets or Sales Support teams.

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