Q. What did the American Taxpayer Relief Act of 2012 do?

A. The American Taxpayer Relief Act of 2012 made permanent most of the income tax cuts enacted between 2001 and 2010 and extended other temporary tax provisions for between one and five years.

Numerous tax cuts enacted between 2001 and 2010 were scheduled to expire after 2012, part of the "fiscal cliff" that threatened to cut short nascent recovery from the Great Recession. The expirations involved four tax acts:

- The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) phased in income tax cuts for most taxpayers but scheduled all of the cuts to expire after 2010 to avoid conflict with Senate rules (Joint Committee on Taxation 2001).
- The Jobs and Growth Tax Relief Reconciliation Act of 2003 accelerated the phase-in of some EGTRRA provisions, but retained their expiration dates and lowered tax rates on capital gains and qualifying dividends, also with sunset dates (Joint Committee on Taxation 2003).
- The American Recovery and Reinvestment Tax Act of 2009 (Division B, Title I of the American Recovery and Reinvestment Act, or ARRA) provided a number of temporary tax cuts designed to stimulate the economy, all of which were to sunset by the end of 2010 (Altshuler et al. 2009).
- The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 extended most provisions of those three acts through 2012 (Urban-Brookings Tax Policy Center 2010).

(Another tax law, the Temporary Payroll Tax Cut Continuation Act of 2011, extended through 2012 a cut in employees' share of the payroll tax funding Social Security, from 6.2 percent to 4.2 percent. The American Taxpayer Relief Act did not extend that provision.)

The Tax Policy Center's analysis of the scheduled expirations found that failure to extend them (including the temporary payroll tax cut) would have raised taxes by more than $500 billion in 2013—an average of almost $3,500 per household. Roughly 90 percent of Americans would have seen their tax bills rise (Williams et al. 2012).

Congress passed the American Taxpayer Relief Act of 2012 (ATRA) early on January 1, 2013, to prevent most of the sunsetting tax cuts from expiring. Most 2001 and 2003 income tax cuts were made permanent for all but the highest-income taxpayers. ATRA extended three ARRA provisions through 2017, while permanent changes to the estate tax and the alternative minimum tax reduced the number of people affected and indexed those provisions for inflation.

Some Background

What did the American Taxpayer Relief Act of 2012 do?

TAX PROVISIONS MADE PERMANENT

Income Tax Provisions

- *Tax Rates*: ATRA maintained the basic marginal tax rate structure of 10, 15, 25, 28, 33, and 35 percent for taxable income under $400,000 ($450,000 for married taxpayers filing jointly); the thresholds were indexed for inflation after 2013. Taxpayers with taxable income above the thresholds face a 39.6 percent marginal tax rate.
- *Pease and PEP:* The limitation on itemized deductions (Pease) and the personal exemption phaseout (PEP) applies only to taxpayers with adjusted gross incomes of $250,000 or more ($300,000 for married taxpayers filing jointly); the thresholds are indexed for inflation after 2013.
- *Child Credits*: The child tax credit equals $1,000 per child and is refundable up to 15 percent of earnings above $10,000 (indexed for inflation after 2001). Another ATRA provision temporarily reduced the refundability threshold to $3,000. The child and dependent tax care credit rate begins at 35 percent on eligible expenses up to $3,000 per child (to a maximum of $6,000) and phases down to 20 percent between adjusted gross incomes of $15,000 and $43,000.
- *Marriage Penalty*: The standard deduction and the 10 percent and 15 percent brackets for joint filers equal twice those for single filers. (ATRA also temporarily extended the higher earned income tax credit phaseout threshold for joint filers.)
- *Education Tax*: ATRA maintained higher annual contribution limits for Coverdell education savings accounts and higher phaseout ranges for the student loan interest deduction.
- *Capital Gains and Dividends:* ATRA retained 15 percent tax rates on long-term capital gains and qualified dividends (0 percent for those who would otherwise be in the bottom two tax brackets) for taxpayers in all but the top income tax bracket; the law also sets a 20 percent rate for those in the top bracket.
- *Alternative Minimum Tax*: ATRA set the 2012 alternative minimum tax exemption at $50,600 ($78,750 for married taxpayers filing jointly) and indexes the exemption amount, the exemption phaseout threshold, and the future tax brackets for inflation.

The "Making Work Pay" Tax Credit

Effective for 2009 and 2010, the Making Work Pay (MWP) tax credit accounted for half of individual tax cuts. The credit equaled 6.2 percent of earned income up to a maximum of $400 ($800 per couple) and phased out at 2 percent of income over $75,000 ($150,000 for couples). As a result, individuals with earnings between about $6,450 and $75,000 (between about $12,900 and $150,000 for couples) could get the maximum credit. Those with incomes exceeding $95,000 ($190,000 for couples) received no credit (Urban-Brookings Tax Policy Center 2009).

A nontax provision extended "economic recovery payments" to certain individuals who did not qualify for the MWP credit. Payments totaling an estimated $14.2 billion went to recipients of Social Security, supplemental security income, railroad retirement benefits, and veterans' disability compensation or pension benefits (Urban-Brookings Tax Policy Center 2009).

The Alternative Minimum Tax Patch

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What did the American Taxpayer Relief Act of 2012 do?

A one-year extension of the alternative minimum tax (AMT) "patch" temporarily raised the AMT exemption. The cost: about $70 billion over 10 years. The patch saved affected taxpayers an estimated average of about $2,400. Under permanent AMT law, roughly 30 million taxpayers would have owed the additional levy (Urban-Brookings Tax Policy Center 2009).

Other Individual Tax Provisions

Other major provisions in the American Recovery and Reinvestment Act replaced the HOPE education credit with the more generous and more refundable American opportunity credit (at a 10-year cost of $14.8 billion), increased the refundability of the child credit ($13.9 billion), boosted the earned income tax credit (EITC—$4.7 billion), and temporarily suspended taxation of the first $2,400 of unemployment benefits ($4.7 billion). All gave taxpayers more money to spend and thus help boost the economy. Two other provisions—the automobile sales tax credit ($1.7 billion) and the homeownership tax credit ($6.6 billion)—subsidized the purchase of cars along with homes for first-time buyers, thus targeting benefits for two industries hit hard by the Great Recession (Urban-Brookings Tax Policy Center 2009).

Business Tax Provisions

A broad range of provisions included incentives for the production of "clean" energy ($20 billion), funding to finance infrastructure development ($19.6 billion), tax benefits for business investment ($8 billion), and other economic recovery tools ($6.5 billion). The largest single provision extended tax incentives to produce electricity from renewable fuels for three years at an estimated cost of $13 billion. Among a variety of infrastructure development tools, school construction bonds ($10 billion), Build America bonds ($4.3 billion), and help for financial institutions ($3.2 billion) provided the most assistance. Special allowances for business investment in 2009 ($6 billion) and provisions related to net operating losses ($3.2 billion) gave additional assistance to firms.

TAX RELIEF UNEMPLOYMENT INSURANCE REAUTHORIZATION AND JOB CREATION ACT OF 2010

Faced with the scheduled sunset of all provisions of the 2001 and 2003 Bush tax cuts and the 2009 stimulus act (as well as several other tax laws), and unable to agree on permanent changes, Congress temporarily extended many provisions in the Tax Relief Unemployment Insurance Reauthorization and Job Creation Act of 2010. The law had diverse effects on the tax code:

- It extended all of the 2001 and 2003 individual income tax cuts for two years through 2012.
- It extended selected provisions of the 2009 act for two years through 2012, including
    - the higher EITC phaseout threshold for married couples filing jointly ($5,000 above the threshold for single filers, indexed for inflation);
    - the 45 percent EITC phase-in rate for families with three or more children;
    - the $3,000 threshold (unindexed) for refundability of the child tax credit; and
    - the American Opportunity Tax Credit for higher education.
- It set an effective exemption of $5 million and a 35 percent tax rate for the estate tax for 2011 and 2012, and replaced the state death tax credit with a deduction.
- It reduced the Social Security tax rate on employees to 4.2 percent for 2011 and the self-employment

What did the American Taxpayer Relief Act of 2012 do?

tax rate by 2 percentage points for 2011. (However, the act did not reduce the amount of self-employment tax that taxpayers could deduct on their income tax returns.)

- It raised the AMT exemption to $47,450 for single filers and $72,450 for married couples filing jointly for 2010 and to $48,450 and $74,450, respectively, for 2011.
- It extended other expiring tax provisions, including the deduction for state and local general sales taxes, the above-the-line deduction for education expenses, and the educator expense deduction, through 2011.

The temporary reduction in the Social Security tax effectively replaced the MWP credit from the 2009 stimulus. That swap reduced the tax savings for low-income workers—single people with earnings under $20,000 and couples with earnings under $40,000—and provided large new tax breaks for high earners. Recall that single workers with income over $95,000 and couples with income over $190,000 got no MWP credit. In contrast, the cut in the Social Security tax rate saved high earners—those with earnings at or above the $106,800 cap on earnings subject to the tax in 2011—$2,136 in payroll taxes and double that for high-earning couples.

A Tax Policy Center analysis showed that, while about two-thirds of households in the lowest income quintile (income under about $18,000) would have gotten either credit, their average MWP credit would have been twice their payroll tax savings—$371 versus $178. Meanwhile, nearly 90 percent of households in the top quintile (income over about $105,000) got an average payroll tax cut of about $2,250, compared with just 60 percent who would have gotten MWP credits averaging about $650.

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Data Sources

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Further Reading

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Some Background

What did the American Taxpayer Relief Act of 2012 do?

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