IRS Inflation Adjustments and Tax Legislative Update
March 2023

Overview
In late December, Congress passed a significant omnibus budget bill. Included was the Setting Every Community Up for Retirement Enhancement 2.0 Act of 2022 (“Secure Act 2.0”), which contains various retirement and other changes that practitioners and their clients need to be aware of. It provides new incentives for employers to offer retirement plans to their employees and for employees to participate and improve their retirement security.

Secure Act 2.0 aims to help employees and their beneficiaries, owner-employees, small businesses, and retirees, and ease costs, administrative burdens, and penalties for inadvertent mistakes. It will also require most plans to be amended to comply with some of its provisions. The 2023 omnibus bill containing the new provisions was signed into law by President Biden on December 29, 2022. Highlights of the new legislation are included in this memorandum after a summary of the many new IRS inflation adjustments that apply to various tax items in 2023.

Key Tax Rates
The 2023 standard deduction for single taxpayers that do not itemize is now $13,850. Married couples filing joint returns that do not itemize will have a standard deduction of $27,700 in 2023. For itemizers, state and local tax (SALT) deductions continue to remain capped at $10,000.

The following tables reflect applicable ordinary income, long and short-term capital gains, qualifying dividends and net investment income tax brackets for 2023 compared to 2022.

2022 Federal Income Tax Brackets					
Single	Married Filing Jointly	Married Filing Separate	Head of Household	Estates & Trusts	Marginal Rate
Up to $10,275	Up to $20,550	Up to $10,275	Up to $14,650	Up to $2,750	10%
$10,276 to $41,775	$20,551 to $83,550	$10,276 to $41,775	$14,651 to $55,900	NA	12%
$41,776 to $89,075	$83,551 to $178,150	$41,776 to $89,075	$55,901 to $89,050	NA	22%
$89,076 to $170,050	$178,151 to $340,100	$89,076 to $170,050	$89,051 to $170,050	$2,751 to $9,850	24%
$170,051 to $215,950	$340,101 to $431,900	$170,051 to $215,950	$170,051 to $215,950	NA	32%
$215,951 to $539,900	$431,901 to $647,850	$215,951 to $323,925	$215,951 to $539,900	$9,851 to $13,450	35%
Over $539,900	Over $647,850	Over $323,925	Over $539,900	Over $13,450	37%

2023 Federal Income Tax Brackets					
Single	Married Filing Jointly	Married Filing Separate	Head of Household	Estates & Trusts	Marginal Rate
Up to $11,000	Up to $22,000	Up to $11,000	Up to $15,700	Up to $2,900	10%
$11,001 to $44,725	$22,001 to $89,450	$11,001 to $44,725	$15,701 to $59,850	NA	12%
$44,726 to $95,375	$89,451 to $190,750	$44,726 to $95,375	$59,851 to $95,350	NA	22%
$95,376 to $182,100	$190,751 to $364,200	$95,376 to $182,100	$95,351 to $182,100	$2,901 to $10,550	24%
$182,101 to $231,250	$364,201 to $462,500	$182,101 to $231,250	$182,101 to $231,250	NA	32%
$231,251 to $578,125	$462,501 to $693,750	$231,251 to $346,875	$231,251 to $578,100	$10,551 to $14,450	35%
Over $578,125	Over $693,750	Over $346,875	Over $578,100	Over $14,450	37%

Source: Internal Revenue Service

2023 Top Federal Income Tax Rates	
Ordinary earned income, not including short-term capital gains or passive income [1]	37.0%
Ordinary income including net investment income (interest, short-term capital gains, non-qualified dividends and other passive income) [2]	40.8%
Long-term capital gains [3]	23.8%
Qualified dividends [4]	23.8%

Notes:
1 Medicare surcharge of 0.9% applied to wages and self-employment income that exceeds $200K for singles and $250K for couples
2 Includes interest, dividends, royalties, net rental income and other passive income
3 Includes 3.8% surtax on net investment income over $200K for singles and over $250K for couples
4 Includes 3.8% surtax on net investment income over $200K for singles and over $250K for couples

Source: Internal Revenue Service

Capital Gains Tax Rates

2022 Total Income		2023 Total Income		Long Term Capital Gains Rate
Single Filers	Married Filing Joint	Single Filers	Married Filing Joint	
Up to $41,675	Up to $83,350	Up to $44,625	Up to $89,250	0%
$41,676 to $459,750	$83,351 to $517,200	$44,626 to $492,300	$89,251 to $553,850	15%
More than $459,750	More than $517,200	More than $492,300	More than $553,850	20%

Source: Internal Revenue Service

Net Investment Income Tax (NII)

2022 Net Investment Income Tax (MAGI Thresholds)		2023 Net Investment Income Tax (MAGI Thresholds)	
Single Filers	Married Filing Joint	Single Filers	Married Filing Joint
Over $200,000	Over $250,000	Over $200,000	Over $250,000

Source: Internal Revenue Service

Under the former version of the Build Back Better Act, which was being considered by Congress in 2021 and the beginning of 2022, the NII surtax would have been expanded to cover NII derived in the ordinary course of a trade or business for joint filers with modified AGI over $500,000, single or head-of-household filers with modified AGI over $400,000, and married people filing a separate return with a modified AGI over $250,000. The proposed legislation would have clarified that the surtax doesn't apply to wages on which Social Security and Medicare payroll taxes (i.e., FICA taxes) are already imposed. The Build Back Better Act was never passed by Congress and is not likely to be passed given the change in control of the House as a result of the recent mid-term elections.

Estate, Gift and Generation-Skipping Adjustments

The exemption amounts for the estate, gift and generation-skipping taxes increase to $12.92 million in 2023. ($25.84 million per couple). The annual exclusion amount for gifts increases from $16,000 to $17,000 per year. These changes provide high net worth individuals a significant planning window to make gifts, set up irrevocable trusts and analyze strategies to swap high basis assets included in their taxable estate with low basis assets currently titled in irrevocable trusts.

State Trust Tax Survey Chart

Now that Colony Trust Company can offer trust administration in both North Carolina and Tennessee, there could be opportunities to transfer certain administrative functions from less tax friendly states to one of Colony Trust Company's offices, either in NC or TN. The chart below provides a survey of a handful of states in the Mid-Atlantic and Southeastern regions and how they impose taxation. For example, moving the principal place of administration of a non-grantor trust from SC or MS to NC or TN, could generate significant state income tax savings.

State	Taxing Statute	Top Tax Rate	Under What Conditions Does The State Tax a Non-Grantor Trust?
AL	Ala. Code 40-18-1(33)	5.00%	If the trust is set up by the Will of an AL resident or settlor was an AL resident at time trust became irrevocable and an AL resident is a beneficiary or trustee for more than seven months during the tax year
FL	No tax	0.00%	No tax
GA	O.C.G.A. 48-7-22	5.75%	If there is trust property located in GA or if the trustee is "managing funds for the benefit of a resident of" GA (but see *Kaestner* where US Supreme Ct ruled unconstitutional if only connection is NC beneficiary without other factors)
MS	Miss. Code Ann. 27-7-5(1)	5.00%	If the trust is administered in MS
NC	N.C. Gen Stat. 105-160.2	4.99%	If there is a NC beneficiary (but see *Kaestner* where US Supreme Ct ruled unconstitutional if only connection is NC beneficiary without other factors)
SC	S.C. Code Ann. 12-6-30(5)	7.00%	If the trust is administered in SC
VA	Va. Code Ann. 58.1-302	5.75%	If the trust is set up by the Will of a VA resident, or if a trust was created by a settlor who was a VA resident, or a trust which is being administered in VA
TN	No tax	0.00%	No tax
DE	30 Del. Code. 1601(8)-(9)	6.60%	If the trust is set up by the Will of a DE resident, or settlor of trust was a DE resident, or the majority of the trustees are DE residents for more than ½ the year; in all of such cases only if there is a DE beneficiary

Source: Steve Oshins - state trust charts

Alternative Minimum Tax (AMT)

The AMT is a separate tax calculation that requires individual taxpayers, estates and trusts to add back certain deductions that would otherwise be deductible against their regular tax calculation. The AMT tax rate is generally lower than the highest regular income tax rate, but the base upon which the tax is applied is higher due to the addback of various deductions.

Alternative Minimum Tax (AMT)	2023
Maximum AMT exemption amount	Married Filing Joint $126,500 Single $81,300
Exemption phaseout threshold	Married Filing Joint $1,156,300 Single $578,150
26% rate applies to AMT income (AMTI) at or below this amount (28% rate applies to AMTI above this amount)	Married Filing Joint $220,700 Single $220,700

Source: Internal Revenue Source

While there are several factors that could contribute to a taxpayer being subject to AMT, a combination of: (i) significant long-term capital gains, (ii) exercise of incentive stock options, and/or (iii) accelerated depreciation deductions, will typically trigger an AMT liability since the deduction for state and local taxes is capped at $10,000.

To the extent that a taxpayer is subject to AMT, a common practice is to consider deferring certain deductions (preference items) into the subsequent year and/or accelerating income into the current year if doing so is favorable when factoring in the lower AMT tax rates versus the higher regular tax rates.

Retirement Plan and IRA Key Numbers

The following tables reflect IRS elective deferral limits, IRA contribution limits and income phase-out ranges for traditional and Roth IRAs.

Elective Deferral Limits	2022	2023
401(k), 403(b), 457(b), Profit-Sharing Plans	Lesser of $20,500 or 100% of participant's compensation ($27,000 if age 50 or older)[2]	Lesser of $22,500 or 100% of participant's compensation ($30,000 if age 50 or older)[2]
Defined Contribution Plans, SEPs	Lesser of $61,000 or 25% of participant's compensation	Lesser of $66,000 or 25% of participant's compensation
SIMPLE 401(k) plans and SIMPLE IRA plans[1]	Lesser of $14,000 or 100% of participant's compensation ($17,000 if age 50 or older)	Lesser of $15,500 or 100% of participant's compensation ($19,000 if age 50 or older)

1 Must aggregate employee deferrals to all 401(k), 403(b) and SIMPLE plans of all employers; 457(b) contributions are not aggregated.
2 Special catch-up limits may also apply to 403(b) and 457(b) plan participants.

Source: Internal Revenue Service

The chart below compares the 2022 and 2023 IRA contribution limits.

IRA contribution limits	2022	2023
Traditional and Roth IRAs	Lesser of $6,000 or 100% of earned income ($7,000 if age 50 or older)	Lesser of $6,500 or 100% of earned income ($7,500 if age 50 or older)

Income phaseout range for determining deductibility of traditional IRA contributions for taxpayers:	2022	2023
1. Covered by an employer-sponsored plan and filing as:		
Single/Head of household	$68,000 - $78,000	$73,000 - $83,000
Married filing jointly	$109,000 - $129,000	116,000 - $136,000
2. Not covered by an employer-sponsored retirement plan, but filing joint return with a spouse who is covered by a plan	$204,000 - $214,000	$218,000 - $228,000

Income phaseout range for determining ability to fund a Roth IRA for taxpayers filing as:	2022	2023
Single/Head of household	$129,000 - $144,000	$138,000 - $153,000
Married filing jointly	$204,000 to $214,000	$218,000 - $228,000

Source: Internal Revenue Service

Spousal IRA Planning

A contribution to a Traditional or Roth IRA is allowed only if the taxpayer has earned income. An exception exists for non-working spouses as long as the couple has at least $13,000 of combined earned income. This allows the working spouse to contribute $6,500 to their own IRA and $6,500 to their spouse's IRA. Deductible contributions for 2023 are allowed until the return due date (April 2024 plus extensions).

Secure Act 2.0 Highlights

The following highlights are not exhaustive. The omnibus bill included other technical tax provisions for small business owners and qualified plan sponsors as well as addressed certain conservation easement arrangements that are not discussed in this memorandum.

– *Tax-free rollovers from 529 accounts to Roth IRAs*. After 2023, the Act permits beneficiaries of 529 college savings accounts to make up to $35,000 of direct trustee-to-trustee rollovers from a 529 account to their Roth IRA without tax or penalty. The 529 account must have been open for more than 15 years, and the rollover is limited to the amount contributed to the 529 account (and its earnings) more than five years earlier. Rollovers are subject to the Roth IRA annual contribution limits but are not limited based on the taxpayer's AGI.

– *Age increased for required distributions.* Under the Act, the age used to determine required distribution beginning dates for IRA owners, retired employer plan members, and active-employee 5%-owners increases, in two stages, from the current age of 72 to age 73 for those who turn age 72 after 2022, and to age 75 for those who attain age 74 in 2032.

– *Bigger catch-up contributions permitted.* Starting in 2025, the Act increases the current elective deferral catch-up contribution limit for older employees from $7,500 for 2023 ($3,500 for SIMPLE plans) to the greater of $10,000 ($5,000 for SIMPLE plans), or 50% more than the regular catch-up amount in 2024 (2025 for SIMPLE plans) for individuals who attain ages 60-63. The dollar amounts are inflation-indexed after 2025.

– *More penalty-free withdrawals permitted.* The Act adds an exception after 2023 to the 10% pre-age-59½ penalty tax for one distribution per year of up to $1,000 used for emergency expenses to meet unforeseeable or immediate financial needs relating to personal or family emergencies. The taxpayer has the option to repay the distribution within three years. No other emergency distributions are permissible during the three-year period unless repayment occurs.

– *Long term care exception*. Beginning December 29, 2025, retirement plans may make penalty-free distributions of up to $2,500 per year for payment of premiums for high quality coverage under certain long term care insurance contracts.

– *Reduced penalty tax on failure to take RMDs.* For tax years beginning after December 29, 2022, the Act reduces the penalty for failure to take required minimum distributions from qualified retirement plans, including IRAs, or deferred compensation plans under Code Section 457(b) from the current 50% to 25% of the amount by which the distribution falls short of the required amount. It reduces the penalty to 10% if the failure to take the RMD is corrected in a timely manner.

– *Favorable surviving spouse election.* For plan years after 2023, the surviving sole spousal designated beneficiary of an employee who dies before RMDs have begun under an employer qualified retirement plan may elect to be treated as if the surviving spouse were the employee for purposes of the required minimum distribution rules. If the election is made distributions need not begin until the employee would have had to start them. This provision allows a designated spousal beneficiary to receive a similar distribution period for lifetime distributions under an employer plan as is permitted if the surviving spouse rolled the amount into an IRA. The IRS will prescribe the time and manner of the election, which once made may not be revoked without IRS' consent.

– *Employer match for student loan payments.* To assist employees who may not be able to save for retirement because they are overwhelmed with student debt and are missing out on available matching contributions for retirement plans, the Act allows them to receive matching contributions by reason of their student loan repayments. For plan years after 2023, it allows employers to make matching contributions under a 401(k) plan, 403(b) plan, or SIMPLE IRA for "qualified student loan payments."

– *More qualify for ABLE programs.* States may establish tax-exempt ABLE programs to assist persons with disabilities. Under current law, an individual must become disabled or blind before age 26 to be eligible to establish an ABLE account. The Act raises the age threshold from 26 to 46. The change is effective for tax years beginning after 2025.

– *Return of excess contributions.* The Act specifies that earnings attributable to excess IRA contributions that are returned by the taxpayer's tax return due date (including extensions) are exempt from the 10% early withdrawal tax. The taxpayer must not claim a deduction for the distributed excess contribution. This applies to any determination of, or affecting, liability for taxes, interest, or penalties made on or after December 29, 2022.

– *Time limit on excess contribution excise tax.* The Act provides that the statute of limitations for the assessment of excise taxes on excess contributions to tax-favored accounts and accumulations on qualified retirement plans begins to run on the filing of the taxpayer's income tax return for the year of the violation and runs for three years (six years in the case of excess contributions). The starting point no longer depends on the plan's filing an excise tax return.

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