Known Unknowns
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The time is near when Americans may once again suffer from the indecision that grips our representatives in Washington, D.C. The tax cuts of 2001 and 2003 will disappear on January 1 without explicit action from Congress and the President. This do-nothing option is estimated to cost 83 percent of U.S. families an average annual tax increase of $3,701 according to the non-partisan Tax Policy Center.

We witnessed a fundamental shift last summer in the faith Americans maintain in their elected representatives to put the right decision ahead of politics when the need is dire. The stock market's reaction in late July of last year tells the story of how we were all caught off guard by the downgrade of our country's once sacred AAA credit rating, which resulted from the inability of Congress to reach terms over the debt ceiling limit. We needed our leaders to reach a compromise but they failed us.

The tone regarding a resolution to "Taxmaggedon" before year end grows darker every day. We learned last year that our representatives are willing to call each other's bluffs at our collective expense, so we must commit to achieving the best outcomes in the context of an uncertain future.

Every U.S taxpayer should understand the likelihood of their tax rates increasing next year. Both political parties have stated commitments to ensure this does not happen, but they have staked out different positions. The Republican Party's plan is to continue with current rates for all taxpayers. Democrats would maintain current rates for those earning under $250,000, while letting the rate cuts of 2001 and 2003 sunset for those above that threshold. Therefore, higher income households need to weigh their options with urgency.

What does this mean in terms of action?

Higher income earners who expect a bonus for 2012 to be paid in 2013 should find out whether they can elect to use a corporate deferred compensation plan. Nearly all Fortune 500 corporations offer this type of tax deferral plan, but rules vary from plan to plan. The election must be made well in advance and generally comes with many stipulations, so it is important to understand the features of each particular plan. Specifics aside, those in the top two income tax brackets should plan on increasing regular contributions to tax deferred accounts if their rates move higher in 2013.

Any payroll deduction that can be made on a pre-tax basis – from retirement plans to parking or public transportation – will also reduce your overall tax obligation.

Let's also consider the implications for our taxable investments. The long term capital gains tax rate will increase from 15 to 20 percent next year, plus another 3.8 percent Medicare Tax for filers with an adjusted gross income higher than $200,000 individually or $250,000 jointly. That represents an almost 40 percent tax increase on investments.

The good news? If you have capital loss carry forwards, they will be worth 10 to 25 percent more in 2013 since they can be used to offset capital gains that would otherwise be taxed at the new higher rate. So if your loss carry forwards exceed your gains then it probably makes sense to sit tight for now.

Those without offsetting losses, however, must make a decision based on incomplete information. Do you wait and hope a favorable resolution is negotiated or do you harvest your current gains and pay this year's lower rates? The wait-and-see approach presents more downside than harvesting gains in 2012 and the upside potential of waiting is limited, so it makes more sense to book capital gains this year under most circumstances.

One final set of changes that's important to address are those regarding tax deductions. The opportunity to claim personal exemptions and itemize specific deductions has provided relief to parents and created incentives to make decisions like financing a home purchase, giving to charity and much more.

Personal exemptions reduced taxable income by $3,800 for each dependent claimed by a taxpayer in 2012. As of the New Year, those married couples earning $261,450 and individuals earning $209,150 will see their ability to claim personal exemptions begin to diminish. Adjust gross incomes at and above $383,950 and $331,650, respectively, will completely lose the benefit these exemptions currently provide. This would affect taxpaying families with multiple dependents most.

Itemized deduction benefits, meanwhile, are also scheduled for reduction in 2013. Taxpayers with adjusted gross incomes of $174,450 would see this benefit begin to decrease. Deductions would then be reduced by three cents for every dollar above these income thresholds, and are limited to an 80 percent reduction from their original benefit to taxpayers.

No two families have the same blend of incomes and expenses, nor do they usually capitalize on itemized deductions in the same manner. The current changes set to take place in 2013 and the uncertainty shrouding the ultimate outcome will affect every tax payer differently, and the best approach to minimizing each of our tax burdens is likely to be just as unique.

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