

2013 Tax Provisions in the New Health Care Laws

3.8% Surtax on Net Investment Income

What Will Be Considered Investment Income?

Investment Income

Interest, Dividends, Capital Gains (long and short)
 Annuities (but not annuities in IRAs or company plans)
 Royalty Income
 Passive Rental Income
 Other Passive Activity Income

NOT Investment Income

Wages and Self-Employment Income
Active Trade or Business Income (including interest, dividends, capital gains)
 Distributions from IRAs, Roth IRAs, and Company Plans
 Excluded Gain from the Sale of a Principal Residence
 Municipal Bond Interest
 Proceeds of Life Insurance Policies
 Veterans' Benefits
 Gains on the Sale of an Active Interest in a Partnership or S Corporation

Taxable income from items that are **NOT** investment income can push taxpayers over the income threshold and cause investment income to be subject to the 3.8% surtax.

MAGI Threshold Amounts for 3.8% Surtax on Net Investment Income

Married Filing Joint	\$ 250,000.00
Individuals	\$ 200,000.00
Married Filing Separate	\$ 125,000.00
Trusts and Estates	\$12,000.00*

* Trusts are hit hard – The 3.8% surtax kicks in at much lower income levels for trusts. The threshold for trusts and estates is the amount at which the top trust tax bracket takes effect. This amount is \$11,200 in 2010, but by 2013 will be approximately \$12,000 since it is indexed for inflation. All other threshold amounts are NOT indexed for inflation.

Effective in 2013:

The 3.8% surtax applies to net investment income when MAGI exceeds these threshold amounts

For this purpose, MAGI is a taxpayer's regular AGI, plus any foreign income excluded from AGI

The 3.8% Medicare tax is imposed on the lesser of (1) net investment income or (2) the amount of MAGI over the threshold amount.

Taxpayers with income below these MAGI levels will not be subject to the tax

Other Health Care Tax Provisions Effective in 2013:

* Additional 0.9% Medicare tax on wages and self-employment income over the threshold amounts

* Medical expenses must exceed 10% of AGI (up from 7.5%) to be deductible (if age 65 or older, effective in 2017) – the 10% also applies to the medical expense exception to the 10% penalty on early IRA or plan withdrawals

- Tax Planning Points -

1 - Taxes on high income individuals and trusts will be increasing in 2011-2012 and again in 2013 when the 3.8% and 0.9% taxes become effective

2 - Planning needs to begin NOW to prepare for future tax increases, especially for taxpayers and trusts at the top tax brackets

3 - IRA and plan distributions are exempt from the 3.8% surtax on net investment income, but taxable distributions from these accounts can push income over the threshold amounts causing other investment income to be subject to the tax

4 - 2010 Roth conversions are now more valuable as a means to eliminate future taxable income and eliminate future RMDs from traditional IRAs before higher tax rates become effective

5 - Taxpayers who have named a discretionary trust as their IRA beneficiary should consider Roth conversions to avoid potential harsh trust tax rates at low trust income levels

6 - Salary deferrals (401(k), 403(b), etc.) can reduce MAGI for the 3.8% surtax but cannot reduce earned income for the 0.9% additional Medicare tax