Welcome to:

Federal Tax Individual Update

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Agenda

- New 2013 Rates and Provisions for Some Taxpayers
- 2013 Medicare Tax Changes for Some Taxpayers

Background

- The changes come from the new law that was enacted on January 2, 2013
- The American Taxpayer Relief Act of 2012

Quick Picture of Tax Formula

Gross Income

Minus: Certain Deductions

Equals Adjusted Gross Income

Minus: Itemized Deductions and Exemptions

Equals Taxable Income

Higher Ordinary Income Tax Rates

- The 10% through 33% brackets remain (just adjusted for inflation indexing)
- The 35% bracket still exists but is very small
- The new 39.6% rate applies to taxable income of over:
  - $450,000 for married filing joint returns
  - $400,000 for unmarried

Long-Term Capital Gains & Dividends

- Maximum rate was 15% for 2012
- For 2013, it is 20%, but only if taxable income exceeds the 39.6% threshold:
  - $450,000 for married filing joint returns
  - $400,000 for unmarried
- It remains 15% for all other taxpayers

Itemized Deduction and Exemption Phaseout

- Phaseout means you lose some/all of your deductions or exemptions if your adjusted gross income exceeds a threshold:
  - $300,000 for married filing joint returns
  - $250,000 for unmarried

Higher Threshold for Deducting Medical Expenses

- In 2012: Medical expenses were deductible to the extent they exceeded 7.5% of adjusted gross income (for regular tax purposes).
- Effective in 2013, the threshold is raised to 10%
- But, for 2013 to 2016 only:
  - If age 65 at end of tax year, use 7.5% for regular tax
  - Only one spouse must be that age for a joint return

2013 Medicare Tax Changes for Some Taxpayers

- This is another change from the healthcare legislation
- There are many tax provisions in the healthcare legislation
- This one increases the Medicare tax for wages and applies the tax to net investment income for taxpayers with income over certain thresholds

The Medicare Tax: Pre-2013

- The tax applied only to wages and self-employment income
  - Employee share was 1.45%;
  - Employer share was 1.45%
  - Total tax was: 2.9%

Change for Wages and Self-Employment Income

- Only for taxpayers above certain income thresholds:
- The employee portion increased by 0.9% to 2.35% (1.45% + 0.9%)
  - The employer portion remains 1.45%
  - Total tax is 3.8% (2.35% + 1.45%)

Threshold for Higher Wage/SE Tax

- Extra 0.9% employee portion of Medicare applies on wages/SE income in excess of:
  - $200,000 for unmarried
  - $250,000 for married joint
  - $125,000 for married separate
- No indexing for inflation

New Tax on Net Investment Income

- The entire 3.8% Medicare tax applies to net investment income, if individual's income exceeds:
  - $200,000 for unmarried
  - $250,000 for married joint
  - $125,000 for married separate
- No indexing for inflation
- The tax will be computed and paid as part of Form 1040 – Using Form 8960

Net Investment Income Includes:

- Income from interest, dividends, annuities, royalties and rents
- Income from a passive trade or business
- Net gain from the disposition of property
- Income from a trade or business of trading financial instruments or commodities
- Reduce gross income by all related expenses before computing the tax

Items Not Subject to Net Investment Tax

- Income excluded from gross income for regular taxes, including:
  - Municipal bond (tax-free) interest
  - Excluded gains on sales of principal residence
- Distributions from qualified retirement plans
- Social Security benefits or alimony