

Forum Wealth Management

Office: 623-236-9263

Fax: 623-242-9814

learnmore@forumwealthmgt.com

www.forumwealthmgt.com



High-Income Individuals Face New Medicare-Related Taxes



November 12, 2014

Page 1 of 4, see disclaimer on final page



High-Income Individuals Face New Medicare-Related Taxes

The health-care reform legislation enacted in 2010 included new Medicare-related taxes that first took effect in 2013. These new taxes target high-income individuals and families. Here are the basics:

Additional Medicare payroll tax

If you receive a paycheck, you probably have some familiarity with the Federal Insurance Contributions Act (FICA) employment tax; at the very least, you've probably seen the tax deducted on your paystub. The old age, survivors, and disability insurance ("OASDI") portion of this FICA tax is equal to 6.2 percent of covered wages (up to \$117,000 in 2014). The hospital insurance or HI portion of the tax (commonly referred to as the Medicare payroll tax) is generally equal to 1.45 percent of covered wages, and is not subject to a wage cap. FICA tax is assessed on both employers and employees (that is, an employer is subject to the 6.2 percent OASDI tax and the 1.45 percent HI tax, and each employee is subject to the 6.2 percent OASDI tax and the 1.45 percent HI tax on wages as well), with employers responsible for collecting and remitting the employees' portions of the tax.

Self-employed individuals are responsible for paying an amount equivalent to the combined employer and employee rates on net self-employment income (12.4 percent OASDI tax on net self-employment income up to the taxable wage base, and 2.9 percent HI tax on all net self-employment income), but are able to take a deduction for the employer portion of the self-employment taxes paid.

Beginning in 2013, the hospital insurance (HI) tax on high-wage individuals increased by 0.9 percent (to 2.35 percent). Who is subject to the additional tax? If you're married and file a joint federal income tax return, the additional HI tax applies to the extent that the combined wages of you and your spouse exceed \$250,000. If you're married but file a separate return, the additional tax applies to if your wages exceed \$125,000. For everyone else, the threshold is \$200,000 of wages. So, a single individual with wages of \$230,000 will owe HI tax at a rate of 1.45 percent on the first \$200,000 of wages, and HI tax at a rate of 2.35 percent on the remaining \$30,000 of wages for the year.

Employers are responsible for collecting and remitting the additional tax on wages that exceed \$200,000. (Employers do not factor in the wages of a married employee's spouse.) You are responsible for the additional tax if the amount withheld from your wages is insufficient (if too much is withheld, you're entitled to a credit on your federal income tax return). The employer portion of the HI tax remains unchanged (at 1.45 percent).

If you're self-employed, the additional 0.9 percent tax applies to self-employment income that exceeds the dollar amounts above (reduced, though, by any wages subject to FICA tax). If you're self-employed, you won't be able to deduct any portion of the additional tax.

Medicare contribution tax on unearned income

A 3.8 percent Medicare contribution tax also first became effective in 2013. Referred to as the "unearned income Medicare contribution tax," or the "net investment income tax" it is imposed on the unearned income of high-income individuals (the new tax is also imposed on estates and trusts, although slightly different rules apply). The tax is equal to 3.8 percent of the lesser of your net investment income (generally, net income from interest, dividends, annuities, royalties and rents, and capital gains, as well as income from a business that is considered a passive activity or a business that trades financial instruments or commodities), or your modified adjusted gross income (basically, your adjusted gross income increased by any foreign earned income exclusion) that exceeds \$200,000 (\$250,000 if married filing a joint federal income tax return, \$125,000 if married filing a separate return).

So, effectively, you're only subject to the additional 3.8 percent tax if your adjusted gross income exceeds the dollar thresholds listed above. It's worth noting that interest on tax-exempt bonds, veterans' benefits, and excluded gain from the sale of a principal residence that are excluded from gross income are not considered net investment income for purposes of the additional tax. Qualified retirement plan and IRA distributions are also not considered investment income.

Both taxes can apply

You can be subject to both taxes, but not on the same income. In other words, if your wages exceed the dollar threshold that applies to your filing status, you're subject to the new additional Medicare payroll tax. If you also have unearned income, that unearned income may (assuming your modified adjusted gross income exceeds the relevant threshold) be subject to the new



Medicare tax on unearned income.

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual. To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing. All performance referenced is historical and is no guarantee of future results. All indices are unmanaged and cannot be invested into directly.

The information provided is not intended to be a substitute for specific individualized tax planning or legal advice. We suggest that you consult with a qualified tax or legal advisor.

LPL Financial Representatives offer access to Trust Services through The Private Trust Company N.A., an affiliate of LPL Financial.

The LPL Financial Registered Representatives associated with this site may only discuss and/or transact securities business with residents of the following states: AZ, CA, CO, MI, MN, OH, and WA.

Securities and Advisory services offered through LPL Financial, a Registered Investment Advisor. Member FINRA/SIPC www.finra.org / www.sipc.org

Forum Wealth Management
Office: 623-236-9263
Fax: 623-242-9814
learnmore@forumwealthmgt.com
www.forumwealthmgt.com

