GET THE FACTS ON 3.8% TAX

We understand that taxes, especially new tax laws, can be confusing. We put together this fact sheet so we can provide you with the most critically important details real estate professionals need for interpreting the new 3.8% tax on investment income.

•Beginning January 1st 2014 all taxpayers are subject to a 3.8% Medicare tax on:
1.The taxpayer's net investment income, or
2.The taxpayer's *modified adjusted gross income*

•Married individuals filing jointly only pay this tax on total income – from all sources – exceeding $250,000

•Those filing separately pay on total income exceeding $200,000

•Married and filing separately – the 3.8% threshold is $125,000

•For income received by *trusts* and *estates* the threshold is $11,950

•If any of these situations does not exceed the applicable threshold – they are exempt from the new tax

•The 3.8% will always be applied to the net investment income, or the modified adjusted gross income which exceeds the applicable threshold amount

•The new 3.8% medicare tax does not apply as a *transfer tax* for any property transactions: meaning it will never be part of closing costs on home, or land sales

•The 3.8% tax does not apply to home and investment property sales

•Sale of your primary residence remain eligible for the full advantage of $250,000 for single filers, and $500,000 for married filers filing jointly – exclusion on the selling price

•Capital gains on primary residence sales exceeding these thresholds must be included on your tax return form 1040 – as income

•However – if these capital gains still do not result in income exceeding the 3.8% total income thresholds – then taxpayers are still exempt from the new tax

•Income totals exceeding the 3.8% threshold are subject to a formula partially protecting investments

•Beyond real estate income, the new tax also applies to other investment proceeds: when your income exceeds the $200,000/$250,000 base thresholds, the standard tax formula will apply for capital gains – dividend proceeds – interest returns – as well as net rental income after expenses

•If you no dot receive any investment income during a particular year from such categories as dividend, rents, interest, and other capital gains – regardless of how much other income you receive – you are *exempt* from the 3.8% tax

•The first year you will have to pay any amount on the 3.8% tax will be in 2014 for income on capital gains earned in calendar year 2013.

•All future payments of the 3.8% tax will be made in the year following the year investment income was earned

•The new 3.8% tax will utilize a formula that only applies to amounts over the thresholds of $200,000/$250,000. For example, if you earn $210,000, you will be subject to pay the 3.8% on just the $10,000 which exceeds the threshold

•While taxpayers will be required to pay the 3.8% tax on all rental incomes, this only applies to *net* rental income. This means that depreciation amounts, interest, property taxes, along with maintenance and utility expenses can all be deducted from your gross rental proceeds

•Any rental, trade, or business income is derived from activities deemed to be passive under IRS regulations, then the combined net income from these sources *is* subject to the 3.8% tax – but only if the taxpayer's modified adjusted gross income exceeds the 3.8% the applicable threshold amounts

•All of these provisions pertain specifically to IRS title 26 - code section 1411

•The new tax is part of the provisions providing funding for the Affordable Care Act passed in 2010, and as such is just one of the support pillars for this important legislation

Keep in-mind that each of these provisions is subject to change - or delayed application – so it is important to stay watchful for any adjustments that may take effect before April 15, 2014. Please don't hesitate to contact us with any questions you may have on how the 3.8% tax may affect your business.

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