tax rate overview

The effective rate of federal tax on income ranges from 0% to 56% for the tax year 2017. For 2018, the top effective rate is reduced to just over 53%.

EISNERAMPER

As a result of the American Taxpayer Relief Act of 2012 ("ATRA"), the Bush-era tax cuts were extended and made permanent for married taxpayers with taxable income below $470,700 in 2017 and single taxpayers with income below $418,400 in 2017. These amounts are adjusted for inflation in the future.

The rate of tax you pay on your income — as well as the benefit you receive from your deductions — can vary from no tax at all to a rate of approximately 56% in 2017 (53% in 2018) depending on many factors, including:

- What is the nature of your income? Is it ordinary income, qualifying dividend income or net long-term capital gain income?
- Are you losing the advantage of the lower long-term capital gains rate because of netting rules?
- Are you subject to the AMT?
- Are you subject to the Medicare Contribution Tax on net investment income?
- Are you subject to the Medicare Wage Surcharge?
- Is any of your income subject to self-employment tax?
- For 2017, how much of your miscellaneous itemized deductions and total itemized deductions are being limited? As a result of the Tax Cuts and Jobs Act, these items are suspended from January 1, 2018 through December 31, 2025.
- For 2017, are your personal exemptions being phased out? As a result of the Tax Cuts and Jobs Act, personal exemptions are repealed from January 1, 2018 through December 31, 2025.
- Is any of your income eligible to be excluded from your taxable base?
- Are credits available to offset your tax?

The most common federal tax rates (exclusive of the Medicare Contribution Tax on net investment income) are:

- 20% for net long-term capital gains and qualified dividends for taxpayers in the 39.6% tax bracket, such as for married taxpayers with 2017 taxable income over $470,700 ($418,400 for single filers). For 2018, the 20% tax rate for net long-term gains and qualified dividends are applicable to taxpayers with taxable income over $479,000 for married filing joint and $425,800 for single individual taxpayers.
- 28% for ordinary income subject to the AMT.
- For 2017, 39.6% maximum rate for ordinary income, including short-term capital gains for married taxpayers with taxable income over $470,700 and $418,400 for single filers. For 2018, the 37% highest rate for ordinary income, such as short-term capital gains for married filers with taxable income over $600,000 and for single taxpayers with taxable income over $500,000.
- The 2017 top rate for the first $127,200 of wages earned in 2017 ($128,400 in 2018) is approximately 48% and 56% for self-employment income. For 2018, the top rate drops to 45% and 53% for self-employment income. The portion of Social Security FICA tax that employees pay remains unchanged at 6.2% on the first income listed herein (12.4% for self-employed individuals). The Medicare portion of the FICA tax remains unchanged at 1.45% on all income earned for employees. For the self-employed, the rate is 2.9% of all self-employment income. Also, there is another 0.9% Additional Medicare Tax (or Hospital Insurance Tax) paid by those earning more than $200,000 ($250,000 for married taxpayers and $125,000 for married taxpayers filing separately).

ORDINARY INCOME RATES

Ordinary income primarily includes wages, business and self-employment income, interest income, nonqualifying dividend income, taxable retirement plan distributions, rental income, taxable Social Security benefits, alimony, and your distributive share of ordinary income passing through to you from a partnership, LLC or S corporation.

For 2017, net short-term capital gains are subject to the same rate as ordinary income and, therefore, could be taxed at a rate as high as 43.4%, inclusive of the Medicare Contribution Tax on net investment income. For 2018, this rate drops to 40.8%. Chart 1 shows the different tax brackets that apply to ordinary income in 2017 and 2018 for married filing jointly and single taxpayers.

CAPITAL GAIN AND DIVIDEND INCOME RATES

Long-term capital gains and qualified dividend income are eligible to be taxed at lower maximum tax rates than ordinary income. This is discussed in detail in the chapter on capital gains and dividend income. But here are the basic rules:

- Net long-term capital gains are taxed at a maximum rate of 20% (if your taxable income exceeds certain thresholds) for both the regular tax and the AMT — with several notable exceptions to be chart 1

2017 AND 2018 FEDERAL TAX RATE SCHEDULES

2017 FEDERAL TAX RATE SCHEDULES

Taxable Income	Base Tax	Marginal Tax Rate (Tax on Next Dollar)
Married Filing Jointly or Qualifying Widow(er)		
$ 0	$ 0	10%
18,650	1,865.00	15%
75,900	10,452.50	25%
153,100	29,752.50	28%
233,350	52,222.50	33%
416,700	112,728.00	35%
470,700	131,628.00	39.6%
Single		
$ 0	$ 0	10%
9,325	932.50	15%
37,950	5,226.25	25%
91,900	18,713.75	28%
191,650	46,643.75	33%
416,700	120,910.25	35%
418,400	121,505.25	39.6%

2018 FEDERAL TAX RATE SCHEDULES

Taxable Income	Base Tax	Marginal Tax Rate (Tax on Next Dollar)
Married Filing Jointly or Qualifying Widow(er)		
$ 0	$ 0	10%
19,050	1,905.00	12%
77,400	8,907.00	22%
165,000	28,179.00	24%
315,000	64,179.00	32%
400,000	91,379.00	35%
600,000	161,379.00	37%
Single		
$ 0	$ 0	10%
9,525	952.50	12%
38,700	4,453.50	22%
82,500	14,089.50	24%
157,500	32,089.50	32%
200,000	45,689.50	35%
500,000	150,689.50	37%

Note: *See Appendix B for detailed 2017 tax rate schedules, including tax rates for married taxpayers filing separately and taxpayers filing as head of household. See Appendix C for detailed 2018 tax rate schedules, including tax rates for married taxpayers filing separately and taxpayers filing as head of household.*

discussed in the chapter on capital gains and dividend income. In some cases, the former 15% rate may still apply. To benefit from long-term capital gains treatment, you must have held the asset for more than 12 months. There is an additional 3.8% Medicare Contribution Tax on net investment income, including net long-term capital gains.

- For 2017, dividends received from most domestic corporations and qualified foreign corporations are taxed at the same 15% rate that applies to net long-term capital gains (20% for married taxpayers with taxable income over $470,700 ($479,000 in 2018) and $418,400 ($425,800 in 2018) for single filers). Dividends that do not qualify for the preferential rate of 15% (or 20%), such as dividends from a money market fund or nonqualified foreign corporations, are subject to the higher ordinary income tax rates. There is an additional 3.8% Medicare Contribution Tax on net investment income that may also apply to dividend income.

ALTERNATIVE MINIMUM TAX

Ordinary income subject to the AMT is taxed at a maximum rate of 28%. As mentioned above, the 15% or 20% rate on net long-term capital gains and qualified dividends also applies to the AMT. While the AMT rate on ordinary income is lower than the highest regular tax rate of 39.6% for 2017 (37% for 2018), it usually applies to a higher taxable income base and frequently results in a greater tax. This was especially true for the 2017 tax year, if you live in a state with high income tax rates and high real estate taxes, and/or you have significant investment expenses in excess of 2% of your AGI, since these deductions are not allowed in computing your AMT. For 2018, the AMT exemption and exemption phase out threshold amounts have been increased. See the chapter on the AMT for a more detailed discussion.

KIDDIE TAX

The unearned income of a child under age 19, or a full-time student under age 24, is generally taxed at the parents' tax rate. This is designed to lessen the effectiveness of intra-family transfers of income-producing property that would shift income from the parents' higher marginal tax rate to the child's generally lower tax rate. For 2017, the first $1,050 of the child's unearned income is tax-free. The next $1,050 for 2017 is taxed at the child's marginal rate. Any excess of unearned income above $2,100 is then taxed at the parents' marginal rate (assuming the parents' rate is higher than the child's). To the extent that the child has earned income such as wages, that income is taxed at the child's marginal rate. Unearned income such as net long-term capital gains and qualifying dividend income is eligible for the preferential tax rate of 15% or 20% to the extent that rate applies to the parents' income. The child may also be subject to the Medicare Contribution Tax on net investment income (see below).

chart 2

SOCIAL SECURITY AND MEDICARE TAXES FOR 2017 AND 2018

Maximum Income Subject to Tax			Tax Rates/Maximum Tax Cost	
			Employer and Employee Portion	Self-Employed
Social Security	2017	$127,200	6.2%/$7,886.40 each	12.4%/$15,772.80
	2018	$128,400	6.2%/$7,960.80 each	12.4%/$15,921.60
Medicare	2017	No limit	1.45%/No limit 2.35%/No limit**	2.678%/No limit* 3.578%/No limit**
	2018	No limit	1.45%/No limit 2.35%/No limit**	2.678%/No limit* 3.578%/No limit**

** The tax rate is actually 2.9%, but only 92.35% of self-employment income is subject to the Medicare Tax.*
***Includes 0.9% Hospital Insurance Tax for amounts above certain income thresholds.*

The Tax Cuts and Jobs Act has simplified the "kiddie tax." From tax year beginning January 1, 2018 through December 31, 2025, the "kiddie tax" is simplified by applying the ordinary and capital gains rates applicable to trusts and estates to the net unearned income of a child. The child's net taxable unearned income is taxed at the trusts and estates tax brackets and rates, whereas the taxable earned income portion of the child is being taxed at the single individual's tax brackets and rates. Therefore, the "kiddie tax" calculation is no longer affected by the parent's or siblings' tax situations.

EMPLOYMENT TAXES

Your wages and self-employment income are also subject to Social Security and Medicare taxes. The amount of income subject to the Social Security tax is limited (see Chart 2), but all earned income is subject to the Medicare Contribution Tax.

If you are self-employed, your share of Social Security and Medicare taxes almost doubles because you pay both the employer's and employee's portions of these taxes. As a result, for 2017, the federal effective tax rate on self-employment income can be as high as 56% (53% for 2018) on the first $127,200 ($128,400 for 2018) of such income, compared to about 48% (43% for 2018) for income from wages (after including your employee share of Social Security and Medicare taxes). The reason there is not a greater spread is primarily because you receive a deduction against AGI for 50% of the self-employment tax you pay.

MEDICARE WAGE SURTAX

An additional 0.9% Hospital Insurance Tax applies to earned income. This tax applies to wages and/or self-employment income in excess of $250,000 for married couples filing joint returns, $125,000 for married filing separate returns and $200,000 for all other taxpayers. The threshold amounts are not indexed for inflation.

MEDICARE CONTRIBUTION TAX ON NET INVESTMENT INCOME

The Health Care and Education Reconciliation Act of 2010 provided for a 3.8% tax on net investment income of higher income taxpayers for years beginning in 2013.

The additional 3.8% tax will apply if your AGI (with certain modifications) is in excess of $250,000 for a joint return (and qualifying widow(er) with dependent child), $200,000 if single, and $125,000 if married filing separate. The tax will apply to the lesser of your net investment income or your AGI in excess of the applicable threshold amounts stated above. Net investment income includes interest, dividends, capital gains, annuities, royalties, rents, income from passive business activities and income from trading in financial instruments or commodities. The amount of gross investment income may be reduced by expenses associated with earning that income. Such expenses include directly allocable state and local taxes, investment advisory fees (over 2% of AGI), and investment interest expenses.

The maximum federal tax rate on long-term capital gains and qualified dividends will be 23.8% (20% plus 3.8% additional Medicare Contribution Tax on net investment income). The threshold amounts are not indexed for inflation.

ITEMIZED DEDUCTIONS AND PERSONAL EXEMPTIONS

Reduction of miscellaneous itemized deductions

For 2017, you must reduce certain miscellaneous itemized deductions by 2% of your AGI. The deductions subject to the 2% disallowance include investment advisory fees, unreimbursed employee business expenses, professional dues and subscriptions, tax return preparation fees and deductible legal expenses. Miscellaneous itemized deductions subject to the 2% "haircut" are suspended from January 1, 2018 through December 31, 2025.

Reduction of itemized deductions

For 2017, the reduction of itemized deductions affects married taxpayers with AGI over $313,800 and single taxpayers with AGI over $261,500. Certain itemized deductions are to be reduced by the lesser of 3% of the amount by which AGI exceeds a certain limit or 80% of the itemized deductions subject to the reduction rules. This provision is suspended from January 1, 2018 through December 31, 2025.

Personal exemptions

The personal exemption amount ("PEP") for 2017 is $4,050 for each of your qualifying dependents. The 2017 PEP begins to phase out for married taxpayers with AGI over $313,800 and single taxpayers with AGI over $261,500. It completely phases out for married taxpayers at $436,300 and for single taxpayers at $384,000 for 2017. However, the personal exemption is eliminated from 2018 through 2025 as a result of the Tax Cuts and Jobs Act.

FOR 2018 AND BEYOND

The Tax Cuts and Jobs Act has made modifications to itemized deductions for tax years from 2018 through 2025, such as limiting the nonbusiness state/local taxes and property taxes to a maximum of $10,000 for married or single filers and $5,000 for married filing separately. The taxpayers have the option to deduct either the actual state and local sales tax paid or the state and local income taxes paid. It also temporarily eliminates all miscellaneous itemized deductions that are subject to 2% AGI floor limitations. In addition, the itemized deductions are not subject to phase out for any tax year after December 31, 2017 and before January 1, 2026.

As a result of the changes in itemized deductions and the increased standard deduction amounts, more taxpayers may be claiming the standard deduction instead of itemized deduction.