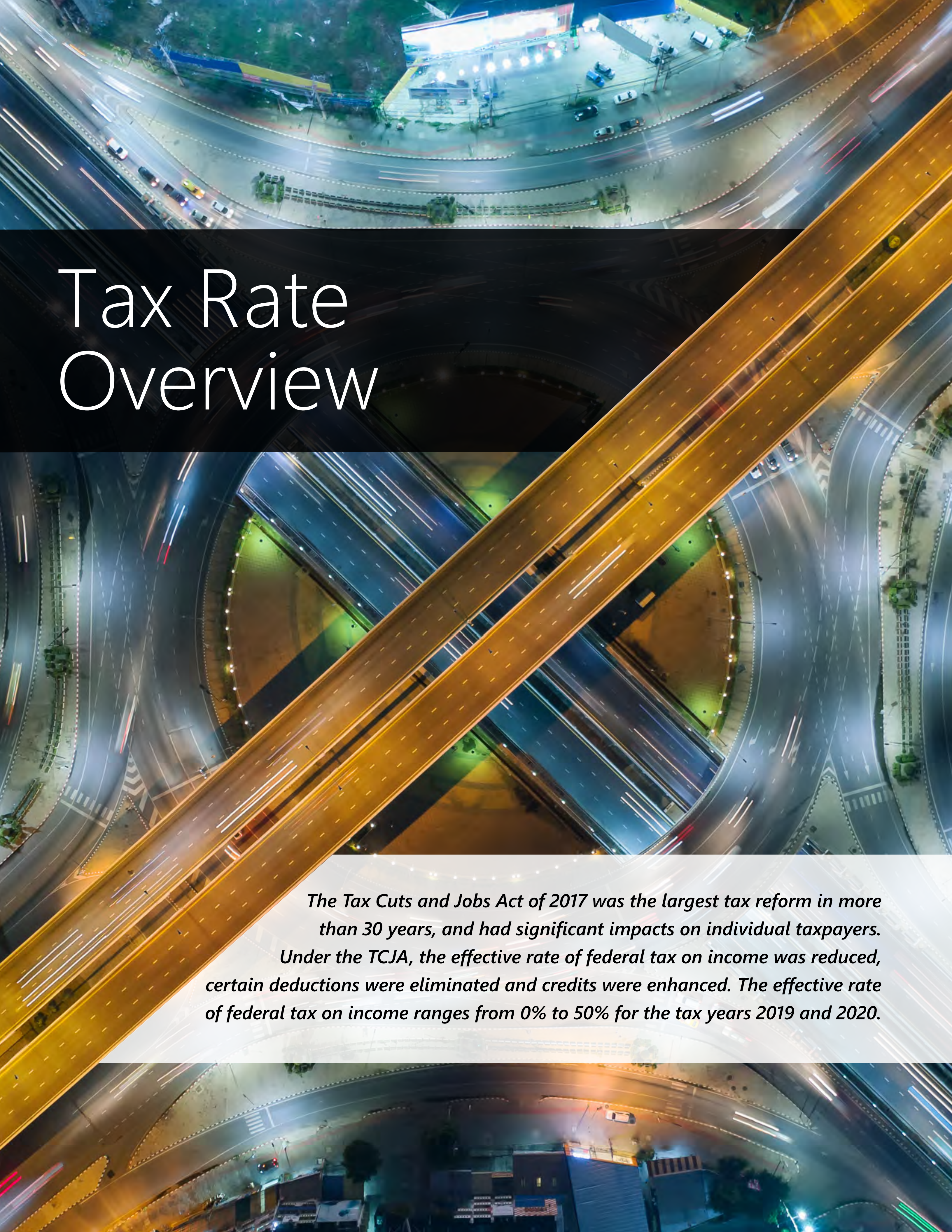

Tax Rate Overview

The Tax Cuts and Jobs Act of 2017 was the largest tax reform in more than 30 years, and had significant impacts on individual taxpayers. Under the TCJA, the effective rate of federal tax on income was reduced, certain deductions were eliminated and credits were enhanced. The effective rate of federal tax on income ranges from 0% to 50% for the tax years 2019 and 2020.

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 50% in 2019 and 2020 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?
- Are you taking the itemized deductions or the standard deduction?
- Should you accelerate your charitable contributions and certain deductions in a particular year to meet the itemized deduction threshold?
- Is any of your income eligible to be excluded from your taxable base?
- Are credits available to offset your tax?
- Is your income considered qualified business income (QBI) and subject to QBI deduction?

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

- For 2019, the 20% tax rate for net long-term gains and qualified dividends is applicable to taxpayers with taxable income over $488,850 ($496,600 in 2020) for married filing joint and $434,550 ($441,450 in 2020) for single individual taxpayers. Under the TCJA, the preferential tax rates for the net long-term capital gains and qualified dividends are based on their own tax bracket and they are no longer tied to the ordinary income tax rates.
- 28% for ordinary income subject to the AMT.
- For 2019, the highest rate for ordinary income, such as short-term capital gains for married filers with taxable income over $612,350 ($622,050 in 2020) and for single taxpayers with taxable income over $510,300 ($518,400 in 2020) is 37%.
- For 2019, the top rate for the first $132,900 ($137,700 for 2020) of wages is approximately 46% and 50% 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 2019 and 2020, 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 40.80%, inclusive of the Medicare Contribution Tax on net investment income. Chart 1 shows the different tax brackets that apply to ordinary income in 2019 and 2020 for married filing jointly and single taxpayers.

Chart

1. 2019 and 2020 Federal Tax Rate Schedules

2019 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%
19,400	1,940.00	12%
78,950	9,086.00	22%
168,400	28,765.00	24%
321,450	65,497.00	32%
408,200	93,257.00	35%
612,330	164,709.50	37%
Single		
$ 0	$ 0	10%
9,700	970.00	12%
39,475	4,543.00	22%
84,200	14,382.50	24%
160,725	32,748.50	32%
204,100	46,628.50	35%
510,300	153,798.50	37%

2020 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%
19,750	1,975.00	12%
80,250	9,235.00	22%
171,050	29,211.00	24%
326,600	66,543.00	32%
414,700	94,735.00	35%
622,050	167,307.50	37%
Single		
$ 0	$ 0	10%
9,875	987.50	12%
40,125	4,617.50	22%
85,525	14,605.50	24%
163,300	33,271.50	32%
207,350	47,367.50	35%
518,400	156,235.00	37%

Note: *See Appendix B for detailed 2019 tax rate schedules, including tax rates for married taxpayers filing separately and taxpayers filing as head of household. See Appendix C for detailed 2020 tax rate schedules, including tax rates for married taxpayers filing separately and taxpayers filing as head of household.*

RETURN TO TOC

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 0%, 15% or 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 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 2019, 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 $488,850 ($496,600 in 2020) and $434,550 ($441,450 in 2020) 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.

Note: *See Appendix B for detailed 2019 tax rate schedules, including tax rates for married taxpayers filing separately and taxpayers filing as head of household. See Appendix C for detailed 2020 tax rate schedules, including tax rates for married taxpayers filing separately and taxpayers filing as head of household.*

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

Chart

2. Social Security and Medicare Taxes for 2019 and 2020

Maximum Income Subject to Tax			Tax Rates/Maximum Tax Cost	
			Employer and Employee Portion	Self-Employed
Social Security	2019	$132,900	6.2%/$8,239.80 each	12.4%/$16,479.60
	2020	$137,700	6.2%/$8,537.40 each	12.4%/$17,074.80
Medicare	2019	No limit	1.45%/No limit 2.35%/No limit**	2.678%/No limit* 3.578%/No limit**
	2020	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 AMT rate on ordinary income is lower than the highest regular tax rate of 37%, if it applies to a higher taxable income base, it should result in a greater tax. For tax years beginning 2018 through 2025, the AMT exemption and exemption phase out threshold amounts have increased significantly, which means less taxpayers will be subject to AMT. See the chapter on the AMT for a more detailed discussion.

Kiddie Tax

On December 20, 2019, President Trump signed into law the Setting Every Community Up for Retirement Enhancement Act ("SECURE"). In effect, SECURE retroactively repeals the provisions of the kiddie tax imposed by the TCJA and reinstates the pre-TCJA kiddie tax calculations so that it's once again based on the parents' marginal rate. SECURE is effective for 2020 and beyond. However, there is an option to apply any kiddie tax savings to the 2019 tax returns and amended 2018 returns.

For 2020, and beyond, the portion of the taxable income that consists of net unearned income and that exceeds the unearned income threshold ($2,200 for 2019 and 2020) is subject to the kiddie tax and is taxed at the parents' marginal federal income tax rate. That rate can be as high as 37% for ordinary income and short-term gains and 20% for long-term gains and dividends. The child may also be subject to the Medicare Contribution Tax on net investment income (see below).

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 2019 and 2020, the federal effective tax rate on self-employment income can be as high as 50% on the first $132,900 ($137,700 for 2020) of such income, compared to about 46% for income from wages (after including the 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, and investment interest expenses. For 2018 through 2025, the miscellaneous itemized deductions are suspended due to the TCJA.

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

The TCJA has made modifications to itemized deductions for tax years from 2018 through 2025, such as limiting the non-business state/local income 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.

Suspension of miscellaneous itemized deductions

One of the major changes due to the TCJA is the miscellaneous itemized deductions subject to the 2% "haircut" are suspended from January 1, 2018 through December 31, 2025. The deductions subject to the 2% disallowance such as investment advisory fees, unreimbursed employee business expenses, professional dues and subscriptions, tax return preparation fees and deductible legal expenses are temporarily eliminated for tax years beginning after December 31, 2017 and before January 1, 2026.

Personal exemptions

The personal exemption is eliminated from 2018 through 2025 as a result of the TCJA.

Standard deductions

The standard deduction amounts for individual taxpayers have increased for tax years from 2018 through 2025. In 2019, the standard deductions amount for married filing joint taxpayers (or surviving spouse) is $24,400 ($24,800 for 2020), for single taxpayer (or married filing separately) is $12,200 ($12,400 for 2020) for single taxpayers (or married filing separately) and $18,350 ($18,650 for 2020) for head of household taxpayers.

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 deductions.