



# CARDINAL ADVISORS

## 2025 Tax Planning-Investment Income-3.8% Surtax

Hans and Tom use Ed Slott's charts to discuss taxes in the video entitled "2025 Tax Planning-Investment Income-3.8% Surtax".

2025 TAX PLANNING-INVESTMENT INCOME-3.8% SURTAX											
S.S	NET INVESTMENT INCOME TAX (NIIT) -EFFECTIVE JAN 1, 2013 -3.8% OF INVESTMENT INCOME -THRESHOLDS = MARRIED JOINT \$250,000 SINGLE \$200,000 ESTATES/TRUSTS \$15,650	MARRIED FILING JOINT			SINGLE			INCOME	<input type="checkbox"/>		
		MARGINAL	TAX	EFFECTIVE	MARGINAL	TAX	EFFECTIVE				
MED	- INVESTMENT INCOME - INTEREST, DIVIDENDS, CAPITAL GAINS (LONG+SHORT), TAXABLE ANNUITY INCOME (EXCLUDES IRAS), ROYALTY INCOME, PASSIVE RENTAL INCOME, - NOT INVESTMENT INCOME - WAGES + SELF EMPLOY, ACTIVE TRADE OR BUSINESS, DISTRIBUTIONS FROM IRAS, ROTH IRAS, COMPANY PLANS, EXCLUDED GAIN FROM THE SALE OF PRINCIPAL RESIDENCE, MUNICIPAL BOND INTEREST PROCEEDS FROM LIFE INSURANCE, SOCIAL SECURITY AND VETERANS BENEFITS, GAINS ON THE SALE OF ACTIVE INTEREST IN A PARTNERSHIP OR S CORP	10%	0-23,850	2.385	10%	10%	0-11,295	1,192	10%	ESTATE	<input type="checkbox"/>
LTC		12%	23,850-96,950	11,157	11.5%	12%	11,295-48,475	5,578	11.5%		
401K/IRA		22%	96,950-206,700	35,302	17.1%	22%	48,475-103,350	17,651	17.1%	TAXES	<input type="checkbox"/>
		24%	206,700-399,600	80,398	20%	24%	103,350-197,300	40,199	20%		
		32%	399,600-501,050	114,462	22.9%	32%	197,300-250,525	57,231	22.9%		
		35%	501,050-751,600	202,154	26.9%	35%	250,525-626,350	188,769	30.1%		
		37%	751,600+			37%	626,350+				
		CAPITAL GAINS			ESTATES + TRUSTS						
		MARRIED	0-96,700	0%	10%	0-3,150	315	10%			
			96,700-600,050	15%	24%	3,150-11,450	2,307	20%			
			600,000+	20%	35%	11,450-15,560	3,777	24.2%			
		SINGLE	0-48,350	0%	37%	15,560+					
			48,350-533,400	15%							
			533,400+	20%							

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# 2025 Tax Planning for Investment Income

## 3.8% Surtax on Net Investment Income

### What Will Be Considered Investment Income?

#### Investment Income

Interest, Dividends, Capital Gains (long and short - including the gain on the sale of investment real estate and second homes)  
Annuities (but not annuities in IRAs or company plans)  
Royalty Income  
Passive Rental Income and Other Passive Activity Income

#### NOT Investment Income

Wages and Self-Employment Income  
**Active** Trade or Business Income (including interest, dividends, capital gains)  
Distributions from IRAs, Roth IRAs, and Company Plans – Including Net Unrealized Appreciation  
Excluded Gain from the Sale of a Principal Residence  
Municipal Bond Interest  
Proceeds of Life Insurance Policies  
Social Security and Veterans' Benefits  
Gains on the Sale of an Active Interest in a Partnership or S Corporation

Taxable income from items that are **NOT** investment income can push taxpayers over the income threshold and cause investment income to be subject to the 3.8% surtax.

### MAGI Thresholds for 3.8% Surtax

Married Filing Joint	\$ 250,000
Individuals	\$ 200,000
Married Filing Separate	\$ 125,000
Trusts and Estates	\$ 15,650*

\* Trusts are hit hard – The 3.8% surtax kicks in at much lower income levels for trusts. The threshold for trusts and estates is the amount at which the top trust tax bracket takes effect. This amount is **\$15,650** in **2025**. All other threshold amounts are NOT indexed for inflation.

### MAGI (Modified Adjusted Gross Income)

The 3.8% surtax applies to net investment income when MAGI exceeds these threshold amounts.

For this purpose, MAGI is a taxpayer's regular AGI, plus any foreign income excluded from AGI.

The 3.8% Medicare tax is imposed on the lesser of (1) net investment income or (2) the amount of MAGI over the threshold amount.

Taxpayers with income below these MAGI levels will not be subject to the tax.

### – Tax Planning Points –

- 1 - The 3.8% tax is **in addition** to the tax rates for high income individuals. Those at the top brackets can have long-term capital gains and dividends taxed at 23.8% and other investment income taxed at 40.8%.
- 2 - There is an additional 0.9% Medicare tax on wages and self-employment income over the threshold amounts.
- 3 - IRA and plan distributions (including sales of employer securities with net unrealized appreciation) are exempt from the 3.8% surtax on net investment income, but taxable distributions from these accounts can push income over the threshold amounts causing other investment income to be subject to the tax.
- 4 - Roth conversions will increase current income, but future tax-free Roth distributions will be more valuable as a means to eliminate taxable income and required minimum distributions from traditional IRAs.
- 5 - The 3.8% surtax is subject to the estimated tax provisions.
- 6 - Taxpayers who have named a discretionary (accumulation) trust as their IRA beneficiary should consider Roth conversions to avoid potential harsh trust tax rates at low trust income levels. After the SECURE Act, the 10-year payout rule will apply to most trusts named as the IRA beneficiary. The inherited IRA funds will have to be paid out to the trust within the 10 years. Any funds retained in the trust will be subject to the high trust tax rates, including the 3.8% tax on trust net investment income that applies above the MAGI threshold (only **\$15,650 for 2025**).
- 7 - Salary deferrals (401(k), 403(b), etc.) can reduce MAGI for the 3.8% surtax but cannot reduce earned income for the 0.9% additional Medicare tax.

# 2025 Tax Planning

## Taxable Income Brackets for 2025 Ordinary Income Tax Rates

Marginal Tax Rate	Married Filing Joint	Single
10%	\$0 - \$23,850	\$0 - \$11,925
12%	\$23,851 - \$96,950	\$11,926 - \$48,475
22%	\$96,951 - \$206,700	\$48,476 - \$103,350
24%	\$206,701 - \$394,600	\$103,351 - \$197,300
32%	\$394,601 - \$501,050	\$197,301 - \$250,525
35%	\$501,051 - \$751,600	\$250,526 - \$626,350
37%*	Over \$751,600	Over \$626,350

\* The top rate is effectively 40.8% for those subject to the 3.8% Medicare surtax on net investment income (those with MAGI over the thresholds of \$250,000 joint filers/\$200,000 single filers).

## 2025 Trust Tax Rates

Ordinary Income Tax		Capital Gain Rates	
10%	\$0 - \$3,150	0%	\$0 - \$3,250
24%	\$3,151 - \$11,450	15%	\$3,251 - \$15,900
35%	\$11,451 - \$15,650	20%	Over \$15,900
37%	Over \$15,650		

**Trust Tax Rates** – Distributions from inherited IRAs that exceed **\$15,650** and are made to and retained in discretionary trusts will be subject to the top 37% rate. After the SECURE Act, inherited IRA funds will have to be paid out to most of these trusts under the 10-year rule, accelerating trust taxes. Roth conversions during the IRA owner's life become more valuable if the IRA beneficiary is a trust.

## Qualified Business Income (QBI) Deduction

### 20% Deduction Phase-Out Ranges

\$394,600 - \$494,600 - Married Joint  
 \$197,300 - \$247,300 - Single

## Taxable Income Brackets for 2025 Long Term Capital Gains and Qualified Dividends Tax

Long Term Capital Gains Rate	Married Filing Joint	Single
0%	\$0 - \$96,700	\$0 - \$48,350
15%*	\$96,701 - \$600,050	\$48,351 - \$533,400
20%**	Over \$600,050	Over \$533,400

\*The 15% rate is effectively 18.8% for those subject to the 3.8% Medicare surtax on net investment income.

\*\*The top rate is effectively 23.8% for those subject to the 3.8% Medicare surtax on net investment income.

## 2025 Transfer Taxes

Transfer Tax	Exemption*	Maximum Rate
Estate, Gift, GST Tax	\$13,990,000	40%

\*The estate and gift exemptions are portable. The unused amount can be transferred to a surviving spouse. The GST exemption is NOT portable.

**Annual Gift Tax Exclusion \$19,000**

## Standard Deductions

Married-Joint	\$30,000
Single	\$15,000
Head of Household	\$22,500
<b>Extra Standard Deduction for Age 65 or Blind</b>	
\$1,600 (married-joint)	
\$2,000 (single)	

## Qualified Charitable Distributions

Available only to IRA owners and IRA beneficiaries who are 70½ or older. The annual QCD limit for 2025 is \$108,000 per IRA owner, **not** per IRA account. For 2025, the limit for a QCD to a split interest entity is \$54,000. QCDs are more valuable due to the larger number of taxpayers that are using the increased standard deduction.

## Roth Conversion Planning Ideas

Roth conversions are permanent and work best for those who believe they will be subject to higher marginal tax rates in the future. Roth conversions are not all or nothing. Consider a series of smaller annual conversions over time to spread out the income tax.

Timing Roth conversions for maximum tax efficiency:

Convert before RMDs begin. RMDs cannot be converted, so no conversion can be done until the RMD is withdrawn.

Avoid the impact of Roth conversions on Medicare IRMAA charges for Parts B and D based on income. Since Medicare has a 2-year lookback provision, consider conversions before age 63.

If a spouse died during the year, consider a Roth conversion for the surviving spouse since this may be the last year to take advantage of married-joint tax return rates. Include the conversion income on the final joint tax return.