

2026 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	\$ 16,000*

* 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 **\$16,000 in 2026**. 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 **\$16,000 for 2026**).
- 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.



CALIFORNIA
RETIREMENT
ADVISORS

1419 Highland Avenue, Manhattan Beach, CA 90266 ☎ 310.643.7472 🌐 www.CRAAdvisors.com

Investment advisory services offered through Mutual Advisors, LLC DBA California Retirement Advisors, a SEC registered investment adviser. Securities offered through Mutual Securities, Inc., member FINRA/SIPC. Mutual Securities, Inc. and Mutual Advisors, LLC are affiliated companies. CA Insurance license #0B09076. Mutual Advisors, LLC and California Retirement Advisors takes no responsibility for the current accuracy of this information. Ed Slott and Company LLC is not affiliated with Mutual Advisors.

© 2026 Ed Slott and Company LLC. Reprinted with permission. Ed Slott and Company LLC takes no responsibility for the current accuracy of this information.

This is being provided for informational purposes only and should not be construed as a recommendation to buy or sell any specific securities. Past performance is no guarantee of future results, and all investing involves risk. The views expressed are those of California Retirement Advisors (CRA) and do not necessarily reflect the views of Mutual Advisors, LLC or any of its affiliates. CRA, nor any of its members, are tax accountants or legal attorneys, and do not provide tax or legal advice.

For tax or legal advice, you should consult your tax or legal professional.