Income taxes and their impact on your investments.

Taking a closer look at taxes.

Investing wisely, with the intent on having your invested dollars grow, is the basis of a sound financial plan. Knowing all the facts about what you are investing in, and what can potentially affect those investments, is critical, but often ignored.

One key element affecting your return on investment (ROI) that is often overlooked and misunderstood is taxes. Exactly how can taxes impact your investments? Have you ever wondered how much you would have to earn on a taxable investment to get the same accumulation as on a non-taxable investment?

Before we look at an example, let's first find where you fall within the 2019 Federal Tax Bracket:

Married taxable income	Single taxable income	Marginal income tax rate
$0-$19,400	$0–$9,525	10.00%
$19,401-$78,950	$9,526–$38,700	12.00%
$78,951-$168,400	$38,701–$82,500	22.00%
$168,401-$321,450	$82,501–$157,500	24.00%
$321,451-$408,200	$157,501–$200,000	32.00%
$408,201-$612,350	$200,201–$500,000	35.00%
Over $612,350	Over $500,000	37.00%

Long-term capital gains and dividends rate.

Married taxable income	Single taxable income	Long-term capital gains and dividends rate
$0–$19,050	$0–$9,525	0.00%
$19,051–$77,400	$9,526–$38,700	0.00%
$77,401–$165,000	$38,701–$82,500	15.00%
$165,001–$315,000	$82,501–$157,500	15.00%
$315,001–$400,000	$157,501–$200,000	15.00%
$400,001–$600,000	$200,201–$500,000	15.00%
Over $600,000	Over $500,000	20.00%

In 2019, individuals with more than $200,000 in income ($250,000 for a married couple filing jointly), who also have investment income (the sum of gross income from items such as interest, dividends, and royalties), will pay an additional tax of 3.8% on met investment income or the excess of modified adjusted gross income over the threshold amount (whichever amount is less). Net investment income includes dividends, interest, passive rental income, income from passive activities, royalties, capital gains, and taxable nonqualified annuity distributions.

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Now that you know where you fall, let's take a look at an example of how income taxes affect your investment returns:

If your federal income tax bracket is:*	10%	12%	22%	24%	32%	35%	37%
And the return on your currently non-taxable investment is:	**You would have to earn the return below on a taxable investment** To calculate your own after-tax return, use the formula: Rate of Return ÷ (1 – Tax Bracket)						
10.00%	11.11%	11.36%	12.82%	13.18%	14.70%	15.38%	15.87%
9.50%	10.55%	10.79%	12.18%	12.50%	13.97%	14.61%	15.08%
9.00%	10.00%	10.23%	11.54%	11.84%	13.23%	13.85%	14.28%
8.50%	9.44%	9.66%	10.89%	11.18%	12.50%	13.08%	13.49%
8.00%	8.88%	9.09%	10.26%	10.53%	11.76%	12.31%	12.70%
7.50%	8.33%	8.52%	9.61%	9.87%	11.03%	11.54%	11.90%
7.00%	7.78%	7.95%	8.97%	9.21%	10.29%	10.77%	11.11%
6.50%	7.22%	7.39%	8.33%	8.55%	9.56%	10.00%	10.32%
6.00%	6.67%	6.82%	7.69%	7.89%	8.82%	9.23%	9.52%
5.50%	6.11%	6.25%	7.05%	7.24%	8.09%	8.46%	8.73%
5.00%	5.55%	5.68%	6.41%	6.58%	7.35%	7.69%	7.94%
4.50%	5.00%	5.11%	5.77%	5.92%	6.62%	6.92%	7.14%
4.00%	4.44%	4.54%	5.13%	5.26%	5.89%	6.15%	6.35%
3.50%	3.89%	3.98%	4.49%	4.60%	5.15%	5.38%	5.55%
3.00%	3.33%	3.41%	3.85%	3.95%	4.41%	4.61%	4.76%
2.50%	2.78%	2.84%	3.20%	3.29%	3.68%	3.85%	3.97%
2.00%	2.22%	2.27%	2.56%	2.63%	2.94%	3.08%	3.17%
1.50%	1.67%	1.70%	1.92%	1.97%	2.20%	2.31%	2.38%
1.00%	1.11%	1.14%	1.28%	1.31%	1.47%	1.54%	1.59%

What does this mean?

This table is illustrating that if, for example, you earn 10.00% on a non-taxable investment, in oder to get the SAME net return on your investment from a taxable vehicle, you would have to earn 13.18% before taxes. Similarly, in order to get the SAME net return from a non-taxable investment earning 4.00%, your taxable investment would need a return of 5.26% before taxes. Examples assume a 24% tax bracket.

What you earn versus what you keep:

We just saw from the above table what type of pre-tax return you would have to receive from a taxable investment in order to get the same return back as a non-taxable investment. What about after you invest? The after-tax yield? As you might imagine, there is a difference between what the return on your investment is and what you actually "take home" when using taxable investments.

*Tax rates illustrated in chart are for 2018. IRS estimated 2019 Federal Tax Rate Schedules based on federal inflation index. The calculations in this chart are used solely for illustrative purposes only. The returns shown are hypothetical and do not indicate the performance of any individual investment. They do not include any fees or expenses associated with the investments or impact of state income taxes, if any. Inclusion of these items would increase the returns needed. Under the assumptions in the table, return on a taxable investment is taxed 100% as ordinary income at the income tax rate specified. Capital gains tax and the net investment income tax are not applied.

Let's take a look at how your returns look prior to taxes and after taxes when using taxable investment vehicles:

If your federal income tax bracket is:*	10%	12%	22%	24%	32%	35%	37%
And the return on your currently non-taxable investment is:	**You would have to earn the return below on a taxable investment** To calculate your own after-tax return, use the formula: Rate of Return X (1 – Tax Bracket)						
10.00%	9.00%	8.80%	7.80%	7.60%	6.80%	6.50%	6.30%
9.50%	8.55%	8.36%	7.41%	7.22%	6.46%	6.17%	5.98%
9.00%	8.10%	7.92%	7.02%	6.84%	6.12%	5.85%	5.67%
8.50%	7.65%	7.48%	6.63%	6.46%	5.78%	5.52%	5.35%
8.00%	7.20%	7.04%	6.24%	6.08%	5.44%	5.20%	5.04%
7.50%	6.75%	6.60%	5.85%	5.70%	5.10%	4.87%	4.72%
7.00%	6.30%	6.16%	5.46%	5.32%	4.76%	4.55%	4.41%
6.50%	5.85%	5.72%	5.07%	4.94%	4.42%	4.22%	4.09%
6.00%	5.40%	5.28%	4.68%	4.56%	4.08%	3.90%	3.78%
5.50%	4.95%	4.84%	4.29%	4.18%	3.74%	3.57%	3.46%
5.00%	4.50%	4.40%	3.90%	3.80%	3.40%	3.25%	3.15%
4.50%	4.05%	3.96%	3.51%	3.42%	3.06%	2.92%	2.83%
4.00%	3.60%	3.52%	3.12%	3.04%	2.72%	2.60%	2.52%
3.50%	3.15%	3.08%	2.73%	2.66%	2.38%	2.27%	2.20%
3.00%	2.70%	2.64%	2.34%	2.28%	2.04%	1.95%	1.89%
2.50%	2.25%	2.20%	1.95%	1.90%	1.70%	1.62%	1.57%
2.00%	1.80%	1.76%	1.56%	1.52%	1.36%	1.30%	1.26%
1.50%	1.35%	1.32%	1.17%	1.14%	1.02%	0.97%	0.94%
1.00%	0.90%	0.88%	0.78%	0.76%	0.68%	0.65%	0.63%

What does this mean?

This table is illustrating that if, for example, your pre-tax return on your taxable investment is 10.00%, your after-tax return, the money you actually keep, is only 7.60%. Similarly, if your return was 5.00%, you keep 3.80% as your after-tax yield. Examples assume a 24% tax bracket.

*Tax rates illustrated in chart are for 2018. IRS estimated 2019 Federal Tax Rate Schedules based on federal inflation index. This chart is for illustrative purposes only and does not represent the performance of any specific product. The hypothetical returns do not include any fees or expenses associated with investments or any other taxes that inclusion of these items would lower the returns shown. Under the assumptions in the table, return on a taxable investment is taxed 100% as ordinary income at the income tax rate specified. Capital gains tax and the net investment income tax are not applied.

Additional considerations:

Actual taxes may vary from those shown. Please consult your own tax advisor for the specific tax implications of any particular investment. The rates of return are hypothetical. In reality, the returns of most types of investments fluctuate, and investment losses are possible. Although this material does not portray any specific type of investment or financial product, please keep in mind that with many types of retirement accounts, withdrawals are taxable and may also be subject to penalty taxes. "Currently non-taxable investments" are hypothetical investments and are not taxed. These assumptions were made for simplicity, but keep in mind that depending on the type of product or strategy, the assumptions may understate the impact of taxes and may not be accurate as an indicator of how any specific portfolio or product would be impacted.

The material is provided for the limited purpose of illustrating the possible effect of taxes on investment returns and accumulations in circumstances in which a hypothetical investor is both seeding the initial investment and then later making withdrawals. The material does not account for other factors which can influence an investor's investment results.

Depending on where you live, you may be subject to state and city taxes.

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