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TAX SHIFT 2024: UNDERSTANDING THE NEW TAXATION RULES

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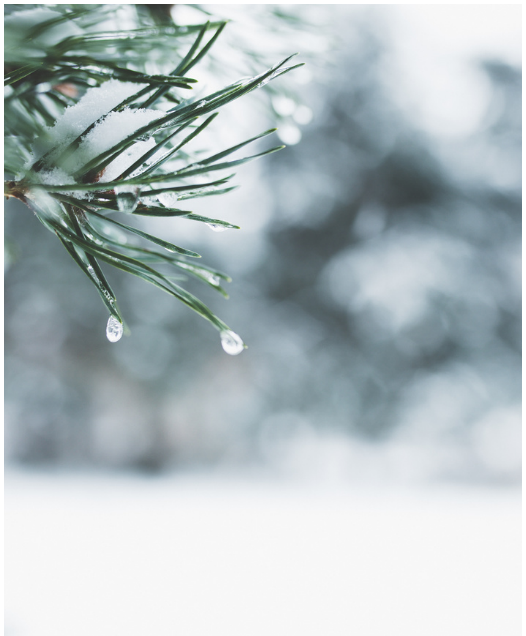
Are you familiar with how our federal tax code originated?

In 1909, progressives in Congress attached a provision for an income tax to a tariff bill. Hoping to kill the idea for good, conservatives proposed enacting such a tax as they believed 75% of states would never ratify a constitutional amendment, according to the National Archives.

Much to their surprise, the 16th Amendment was ratified in 1913, establishing Congress's right to impose a federal income tax. Initially, fewer than 1% of the population paid income taxes. The rate was only 1% of net income due to generous exemptions and deductions.

Clearly, the tax code has changed dramatically over the years, and it will continue to change.



Diving into the details

The Internal Revenue Service announced last year the annual inflation adjustments for more than 60 tax provisions (63 to be exact) for the tax year 2024, including the tax rate schedules. As incorporated into law, the IRS adjusts various categories to account for inflation.

It's not a perfect measure, but the adjustments help mitigate the impact of inflation on income. Without indexing, a cost-of-living raise, for example, could automatically push you into a higher tax bracket or reduce the value of your standard deduction.

Annual inflation adjustments, however, do not cover all tax provisions. We won't cover each of the 63 changes. We will touch on the high points.

We won't cover each of the 63 changes. We will touch on the high points. If you have questions, please reach out to us. As always, if you have specific tax questions, feel free to check with your tax advisor.

1. Tax brackets and tax rates have changed. Table 1 highlights the seven separate tax brackets for 2024 for single, married, head-of-household, and married filing separately.

Table 1: 2024 Tax Rate Schedule

Taxable income ($)	Base amount of tax ($)	Plus	Marginal tax rate	Of the amount over ($)
Single				
0 to 11,600		+	10.0	
11,601 to 47,150	1,160.00	+	12.0	11,600.00
47,151 to 100,525	5,426.00	+	22.0	47,150.00
100,526 to 191,950	17,186.50	+	24.0	100,525.00
191,951 to 243,725	39,110.50	+	32.0	191,950.00
243,726 to 609,350	55,678.50	+	35.0	243,725.00
Over 609,350	183,647.25	+	37.0	609,350.00

Married filing jointly and surviving spouses				
0 to 23,200		+	10.0	
23,201 to 94,300	2,320.00	+	12.0	23,200.00
94,301 to 201,050	10,852.00	+	22.0	94,300.00
201,051 to 383,900	34,337.00	+	24.0	201,050.00
383,901 to 487,450	78,221.00	+	32.0	383,900.00
487,451 to 731,200	111,357.00	+	35.0	487,450.00
Over 731,200	196,669.50	+	37.0	731,200.00

Head of household				
0 to 16,550		+	10.0	
16,551 to 63,100	1,655.00	+	12.0	16,550.00
63,101 to 100,500	7,241.00	+	22.0	63,100.00
100,501 to 191,950	15,469.00	+	24.0	100,500.00
191,951 to 243,700	37,417.00	+	32.0	191,950.00
243,701 to 609,350	53,977.00	+	35.0	243,700.00

Married filing separately				
0 to 11,600		+	10.0	
11,601 to 47,150	1,160.00	+	12.0	11,600.00
47,151 to 100,525	5,426.00	+	22.0	47,150.00
100,526 to 191,950	17,168.50	+	24.0	100,525.00
191,951 to 243,725	39,110.50	+	32.0	191,950.00
243,726 to 365,600	55,678.50	+	35.0	243,725.00
Over 365,600	98,334.75	+	37.0	365,600.00

Source: IRS

For example, if you are married, filing a joint return, and your taxable income is $50,000, you would pay 10% to the federal government on income up to $23,200. You would pay 12% on the remainder of your income up to $50,000.

Table 2: 2024 Estates and Trusts	
Taxable Income	**Marginal Tax Rate**
$0 to $3,100	10%
$3,101 to $11,150	24%
$11,151 to $15,200	35%
Over $15,200	37%

Source: IRS

2. The standard deduction in tax year 2024 rises to $29,200 from $27,700 for those who are married and filing jointly. The standard deduction for single filers and married and filing separately rises to $14,600 from $13,850. For head of household, the standard deduction rises to $21,900 from $20,800.

If you are 65 or older and single or head of household, you may take an additional deduction of $1,950. If married and filing jointly or separately, you may take an additional $1,550.

Changes on the horizon

The Tax Cuts and Jobs Act (TCJA) of 2017 significantly increased the standard deduction, simplifying the filing process, as it eliminated the need for many taxpayers to itemize. But it also scrapped the personal exemption.

Unless extended, please be aware that many provisions of the TCJA will expire at the end of 2025. Among the expected changes:

- Individual income tax rates will revert to their 2017 levels.
- The standard deduction will be cut roughly in half, the personal exemption will return, and the child tax credit will be reduced.
- The estate tax exemption will be reduced.
- The special 20% tax deduction for pass-through businesses will disappear.
- The cap of $10,000 on state and local income taxes, which is not adjusted for inflation, will disappear. Those who are married but file separately may deduct up to $5,000 if they itemize.

3. Favorable treatment for long-term capital gains is a cherished tax break for investors. Long-term capital gains, such as the profit on the sale of a stock held for more than one year, are taxed at a more favorable rate than short-term gains. A short-term gain is taxed as if it were ordinary income.

Table 3: Long-Term Capital Gains Rates and Qualified Dividends

Tax Brackets	Single, Taxable Income Over	Married Filing Joint Return, Taxable Income Over	Head of Household, Taxable Income Over	Married Filing Separately, Taxable Income Over	Estates and Trusts, Taxable Income Over
0%	$0	$0	$0	$0	$0
15%	$47,025	$94,050	$63,000	$47,025	$3,150
20%	$518,900	$583,750	$551,350	$291,850	$15,450

Source: Tax Foundation, IRS

4. The TCJA includes a **20% deduction for pass-through businesses.** Limits on the deduction begin phasing in for taxpayers with income above $191,950 and $383,900 for joint filers in 2024.

5. Other taxes you may be subject to or credits you may capture.

- High-income taxpayers are subject to the **net investment income tax** of 3.8%, levied on the lesser of net investment income or modified adjusted gross income over $200,000 for single filers and $250,000 for married filing jointly. These amounts have never been indexed to inflation. In general, net investment income includes but is not limited to interest, dividends, capital gains, rental and royalty income, and non-qualified annuities, according to the IRS. Net investment income generally does not include wages, unemployment compensation, Social Security Benefits, alimony, and most self-employment income.

- Congress enacted the **AMT**, or the **alternative minimum tax**, in 1969 following testimony by the Secretary of the Treasury that 155 people with adjusted gross income above $200,000 had paid no federal income tax on their 1967 tax returns. Limits were never adjusted for inflation and, in time, threatened tens of millions with a parallel tax system. More recently, annual patches were put into lace until the TCJA was passed, dramatically increasing the thresholds for avoiding the AMT. The AMT exemption amount for 2024 is $85,700 for singles and $133,300 for married couples filing jointly.

- Exclusions for the estate, gift, and generation-skipping transfer will increase from $12,920,000 in 2023 to $13,610,000 in 2024. **Higher lifetime-exemption amounts** are set to expire at the end of 2025. Unless Congress makes these changes permanent, after 2025 the exemption will revert to the $5.49 million exemption (adjusted for inflation).

- The **kiddie tax** applies to unearned income, such as dividends or interest, for kids under the age of 19 and college students under 24. Your child will be required to pay taxes on their unearned income in 2024, but if that amount is more than $1,300 but less than $13,000, you may be able to elect to include that income on your return rather than file a separate return for your child.

- The **child tax credit** is $2,000 for each child that qualifies. The child must be under 17 years old at the end of the year. The refundable amount rises to $1,700 for tax year 2024, up from $1,600 in 2023. A refundable credit means that you can take advantage of the credit above your tax liability, in this case, up to $1,700.

- For the tax year 2024, you can have a modified adjusted gross income (MAGI) of up to $252,150 and may qualify for **the adoption credit** of $16,810 if you incur adoption-related expenses. The amount of the credit is reduced for taxpayers with a MAGI of more than $252,150 and is eliminated when your MAGI tops $292,150. The credit is nonrefundable, so the amount cannot exceed your tax liability. However, you may apply any excess credit amount to future years, up to five years.

IRA Contributions

The **IRA contribution limit for 2024** is $7,000 for those under age 50, and $8,000 for those age 50 or older.

You can make 2024 IRA contributions until the federal tax filing deadline for income earned in 2024.

This is up from 2023's limits of $6,500 for those under age 50, and $7,500 for those age 50 or older. You can make 2023 IRA contributions until your April 15th federal tax deadline for income earned in 2023.

SEP-IRA Limits

You can **contribute up to 25%** of the employee's total compensation or a maximum of $69,000 for the 2024 tax year, whichever is less. That's up from $66,000 in 2023. If you're self-employed, your contributions are generally limited to 20% of your net income.
We are mindful that the tax code is quite complex. We are happy to answer any questions you may have. Feel free to consult with your tax advisor.

BRIEF MARKET UPDATE

A blockbuster year that wasn't supposed to happen

Last month, we discussed some of the hazards that Wall Street analysts may encounter when forecasting market returns.

On average, strategists predicted roughly a 2% decline for the S&P 500 Index in 2023, according to Bloomberg. When those who are given such a task encounter difficulties, we are hesitant to provide any predictions regarding the stock market.

When the final returns were tallied, 2023 turned out to be a banner year, surprising nearly everyone.

Key Index Returns		
Index	**MTD %**	**YTD %**
Dow Jones Industrial Average	4.8	13.8
Nasdaq Composite	5.5	43.4
S&P 500 Index	4.4	24.2
Russell 2000 Index	12.1	15.1
MSCI World ex-U.S.A*	5.4	14.8
MSCI Emerging Markets*	3.7	7.0
Bloomberg Barclays U.S. Aggregate Bond TR USD	3.8	5.5

Source: Wall Street Journal, MSCI.com, Bloomberg, MarketWatch
MTD returns: November 30, 2023–December 29, 2023
YTD returns: December 30, 2022–December 29, 2023
*U.S.D.

Disciplined investors 1, Analysts 0

Strategists came up short, allowing the patient, disciplined, and long-term approach to take top honors. Why did the market have a strong year? Let's discuss three factors.

- As 2023 got underway, the prevalent view on Wall Street and many economists was that a recession was inevitable.

  Economists have always struggled to pinpoint turning points in an economic cycle. In most cases, recessions sneak up on us. Last year, we observed the opposite. The loud din of recession calls failed to hit the mark. The miss was probably the biggest economic story of the year, especially for the millions of Americans who would have been thrown out of work.

- As the rate of inflation began to slow, the Federal Reserve, which had slammed on the monetary brakes in 2022, eased up.

  In 2022, the Fed raised the fed funds rate by 4.25 percentage points, according to St. Louis Federal Reserve data. It was the fastest pace of rate hikes since 1980.

  The pace slowed to one percentage point in 2023, reducing a stiff headwind for stocks.

By December, the Federal Reserve had effectively shifted its stance and is now openly discussing potential interest rate cuts in the coming year. Of course, forecasts can change, but the shift fueled the market's advance into the end of the year.

While the S&P 500 Index ended 2023 just shy of its all-time early 2022 high, the smaller but better-known Dow Jones Industrials eclipsed its all-time high in December.

- One other variable helped fuel last year's rise: the emergence of artificial intelligence, which is putting advanced programs into the hands of Main Street.

The technology is in its infancy, but the potential is enormous, and cash began pouring into investments that could someday yield big dividends. Bottom line, the tech-heavy Nasdaq Composite posted a gain of over 40%.

The **same winners on the Nasdaq** also powered gains in the S&P 500 Index.

Peering into 2024

Expect surprises. No one can accurately see into the future. As we saw in 2023, expect the unexpected.

We believe that having a diversified portfolio is the best way to protect yourself against market volatility and achieve your financial objectives. While it won't completely shelter you from market pullbacks, it has historically proven to be a strong strategy that can help you reach your financial goals.

Although volatility can be unsettling, it is often temporary, as demonstrated by the failure of Silicon Valley Bank last year and, so far, the ongoing war in the Middle East.

If we were to take a stab at issues on the front burner, we'd start with the economy.

If inflation continues to slow down, it will take pressure off the Federal Reserve, and rate cuts could come sooner rather than later.

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While the Fed didn't reduce rates in 2023, the year followed a similar pattern to 1985, 1995, and 2019, when the Fed was able to engineer a soft landing, and stocks performed quite well.

But, if economic growth slows too much, stalls, or a recession ensues, i.e., the hard-landing scenario, any tailwinds from a faster pace of rate cuts might easily be offset by weak corporate profits, as we have seen in the past.

Rate cuts in 1974, 1990, 2001, and 2008 failed to prevent a slide in stocks until investors anticipated an economic upturn.

In other words, rate cuts that occur because the Fed "can," not because they "must," is the more preferred path, in our view.

I trust you have found this review to be informative. If you have any inquiries or wish to discuss any other matters, please don't hesitate to contact me or any team member. Thank you for choosing us as your financial advisor. We are honored and humbled by your trust.

As we bid farewell to 2023, may the New Year bring you excitement, adventure, and fulfillment. May the year create cherished memories and be filled with joy. Happy New Year from all of us!

Final thoughts...

Finally, here's to 2023! Boy, was it a humdinger. Talk about ROLLERCOASTER... But we more than survived, and I am so excited for 2024.

It's been amazing diving into discussions about your financial goals and seeing the lightbulb moments during our workshops. Your commitment toward shaping your financial future is super inspiring.

Every conversation has been a step forward in making your financial dreams a reality. A huge thank you for bringing your energy and smarts to the table. We're here to navigate this financial journey with you, keeping things fun and focused.

As we continue navigating the world of finance together, let's keep the momentum going, making finance fun and approachable. Here's to a year of empowering you to hit those financial targets and having a great time along the way!

Happiest of New Years to all of you!

Kelly

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