# NIIT's alive!  NIIT's alive!  How the net investment income tax can affect your estate plan

Published on October 31, 2019

The Tax Cuts and Jobs Act reduced individual income tax rates, but it left the 3.8% net investment income tax ("NIIT") in place.  It's important to address the NIIT in your estate plan, because it can erode your earnings from interest, dividends, capital gains and other investments, leaving less for your heirs.

**How it works**

The NIIT applies to individuals with modified adjusted gross income ("MAGI") over $200,000. The threshold is $250,000 for joint filers and qualifying widows or widowers and $125,000 for married taxpayers filing separately.  The tax is equal to 3.8% of (1) your net investment income, or (2) the amount by which your MAGI exceeds the threshold, whichever is less.

Suppose, for example, that you're married filing jointly and you have $350,000 in MAGI. Presuming $125,000 in net investment income, your NIIT is 3.8% of $100,000 (the excess of your MAGI over the threshold, which is less than your net investment income), or $3,800.

Nongrantor trusts — with limited exceptions — are also subject to the NIIT, and at a much lower threshold:  For 2019, the tax applies to the lesser of (1) the trust's undistributed net investment income, or (2) the amount by which the trust's AGI exceeds $12,750.

**Reducing the tax**

You can reduce or eliminate the NIIT by lowering your MAGI, lowering your net investment income, or both. Techniques for doing so include:

- Reducing this year's MAGI by deferring income, accelerating expenses or maxing out contributions to retirement accounts;
- Selling poor-performing investments to offset the losses against investment gains you've realized during the year; or
- Reducing net investment income by investing in tax-exempt municipal bonds or in growth stocks that generate little or no current income.

If you own an interest in a business, you may be able to reduce NIIT by increasing your level of participation.  Income from a business in which you "materially participate" isn't considered net investment income.  (However, increasing your participation may, in certain cases, trigger self-employment tax liability.)

For trusts, you can reduce or eliminate the NIIT by:

- Structuring them as grantor trusts;
- Distributing the trust's income to its beneficiaries (remember that the NIIT applies only to *undistributed* income); or
- Shifting the trust's investments into tax-exempt municipal bonds, growth stocks or tax-deferred investments (e.g., life insurance).

If you use a grantor trust, its income will be passed through to *you* as grantor, potentially increasing your personal liability for NIIT.

**Review your plan**

The NIIT can affect the financial performance of your personal investments as well as your trusts. To maximize the amount of wealth available for your heirs, be sure to consider strategies for reducing the impact of this tax. Please contact us with any questions.



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