No sales tax on home sales, BUT ...

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Does the 2010 healthcare law (the PPACA) actually impose a 3.8% sales tax on home sales? Despite the scary email zipping around the Internet, this claim isn't entirely true. It is an exaggeration based on one of a troubling pair of new Medicare taxes.

The viral email says, in part: *"Did you know that if you sell your house after 2012 you will pay a 3.8% sales tax on it? ... That's $3,800 on a $100,000 home etc. ... When did this happen? It's in the healthcare bill. Just thought you should know."*

To repeat - this claim is not true (at least not entirely). However, the law does contain a 3.8% tax, and an accompanying 0.9% tax.

- **Medicare Payroll Tax:** There is currently a 1.45% payroll tax that funds a portion of Medicare. The PPACA adds a 0.9% surtax on wage/salary income that exceeds $200,000 for single filers and $250,000 for joint filers. This tax has several troubling features. It hits both personal and business income for entrepreneurs - job creators - who report both on their Form 1040s. It applies not only to the individual's income, but also to that of spouses and other household members. (Yet another marriage penalty.) And despite the name, the funds will be used the pay for the new healthcare law and not Medicare.
- **Medicare Net Investment Tax:** This is the 3.8% tax, and it applies to a *portion* of investment income according to a complex formula (explained below). Someone who sells a primary residence will only pay the 3.8% on the profits of the sale *above and beyond a threshold of $250,000 for a single filer or $500,000 for joint filers.* (Actually, the formula is more complex than that.) The $250,000/$500,000 thresholds only apply to the sale of a primary residence, so the tax will hit other property sales harder. This tax provides a sizable disincentive for businesses to grow It marks the first time that non-wage income is designated to fund Medicare; but again, despite the designation, these funds will not actually go to Medicare.

For those who dislike math, you can stop here. For those who want to understand the mechanics of these taxes, there's a fuller explanation below. One caveat: we believe the following explanation is correct, but the wording in the law is confusing, and you can find conflicting interpretations on the Internet. And of course, businesses need to check the facts with their own accountants to be sure. ... The math follows here, and you may wish to listen to this recording while working through the equations:

STEP ONE: Collect the raw data. We'll look at the example of a couple, filing jointly. They have:

- $270,000 in wage/salary income,
- $27,000 in investment income (rents, dividends, interest, royalties, capital gains on property sales other than primary residence, etc.), and
- $305,000 in capital gains on the sale of their primary residence.

STEP TWO: Calculate Modified Adjusted Gross Income (MAGI).

- A single filer can exclude $250,000 from the sale of a primary residence, and joint filers can exclude $500,000. In this case, since $305,000 is less than $500,000, the capital gains on their home sale is completely exempt. No "sales tax" at all on this sale.
- With the home sale proceeds excluded, MAGI is simply $270,000+$27,000=$297,000.

STEP THREE: Decide whether these taxes are applicable.

- These two taxes are only applicable if MAGI is greater than $200,000 for a single filer or $250,000 for joint filers. Since MAGI=$297,000 and these are joint filers, the taxes are applicable in this case.

STEP FOUR: Calculate the taxes.

- The new payroll tax equals 0.9% of the amount of **household** wage/salary income above the threshold described in Step Three. So, here, it's 0.9% x ($270,000 - $250,000) = $180.
- The new investment tax equals 3.8% times the LESSER of net investment income ($27,000 in this case) OR the difference between MAGI and the Step-Three threshold ($55,000 here). So in this case, it would equal 3.8% of $27,000 - which is $1,026.
- So the two new taxes add $1,206 (= $1,026 + $180) on top of the old Medicare payroll tax.

STEP FIVE: Calculate how much of this tax will actually go to Medicare.

- $0. Remember? Though the law refers to these two new taxes as "Medicare" taxes, none of the proceeds actually go to Medicare. Instead, these new funds mostly go toward health insurance for people who are NOT on Medicare.

Summing up: Contrary to the claims in the viral email, the sale of your home will not automatically face this new tax. But there is a new tax. It might hit part of the gains on your home sale. It's even more likely to hit the sale of property other than your primary residence. And, like much else in the PPACA, it is all very, very confusing.