

# A TALE OF TWO INVESTORS

A REVIEW OF THEIR 1099 TAX FORMS



Taking a closer look at your Form 1099-DIV can be eye-opening. Your financial professional or CPA can help you connect the dots between your December 31 investment statement and your April 15 tax bill. Form 1099-DIV is one of many IRS tax forms and is used to record investment-related income. This simple guide walks you through what to look for along with insights, implications, and actions you may want to take to improve the tax efficiency of your investments.

## How much might the IRS take from Joe & Joan Traditional Taxpayer?

Their year-end investment statement stood at **\$1,000,000**, BUT after paying taxes to the IRS, it went down to **\$983,315**.

Taxes reduced their investment return by **1.7%** and this assumes no active trading during the year. Remember capital gains distributions may occur even if markets were down and the portfolio value has declined.

Take a closer look at their 1099-DIV to see how this can happen.



## Joe & Joan Traditional Taxpayer

**Household Taxable Income: \$400,000**

**Marginal Tax Rate on Unearned Income: 35.8%** (32% + 3.8% NIIT\*)

**Long-Term Capital Gain/Qualified**

**Dividend Tax Rate: 18.8%** (15% + 3.8% NIIT\*)

**Filing Status: Married filing jointly**

**Investments:**

- **Equity Mutual Fund**  
\$500,000 Balance  
1.8% Yield / 7% Capital gains distribution† (average % for U.S. equity in 2022)
- **Taxable Bond Mutual Fund**  
\$500,000 Balance  
4.7% Yield

PAYER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.		1a Total ordinary dividends		OMB No. 1545-0110	
Mutual Fund Company		\$ 32,500		Form 1099-DIV	
		1b Qualified dividends		(Rev. January 2022)	
PAYER'S TIN		\$ 9,000		For calendar year	
		2a Total capital gain distr.		20	
RECIPIENT'S TIN		\$ 35,000		2b Unrecap. Sec. 1250 gain	
RECIPIENT'S name		2c Section 1202 gain		2d Collectibles (28%) gain	
		2e Section 897 ordinary dividends		2f Section 897 capital gain	
Joe & Joan Traditional Taxpayer		\$		3 Nondividend distributions	
		4 Federal income tax withheld		6 Investment expenses	
Street address (including apt. no.)		\$		7 Foreign tax paid	
		8 Foreign country or U.S. possession		9 Cash liquidation distributions	
City or town, state or province, country, and ZIP or foreign postal code		\$		10 Noncash liquidation distributions	
		11 FATCA filing requirement		12 Exempt-interest dividends	
Account number (see instructions)		13 Specified private activity bond interest dividends		14 State	
		15 State identification no.		16 State tax withheld	
		\$		\$	

Form 1099-DIV (Rev. 1-2022) (keep for your records) www.irs.gov/Form1099DIV Department of the Treasury - Internal Revenue Service

**Box 1a: Total Ordinary Dividends:**  
Dividend from mutual fund: \$9,000  
Interest income from mutual fund: \$23,500  
Total Ordinary Dividends: \$32,500

**Box 1b: Qualified Dividends**  
\$9,000 X 18.8% = \$1,692 in federal taxes (A)

**Box 1a - Box 1b = Non-Qualified Dividends\*\***  
\$32,500 - \$9,000 = \$23,500  
\$23,500 X 35.8% = \$8,413 in federal taxes (B)

**Box 2a: Total Capital Gains Distribution**  
\$35,000 X 18.8% = \$6,580 in federal taxes (C)

**Box 12: Exempt-Interest Dividends**  
Interest income from municipal bond funds. Generally, tax-free at the federal level. Joe & Joan had \$0 in municipal bonds.

### Four boxes to review

#### Box 1a: Total Ordinary Dividends

- Includes qualified dividends
- Includes non-qualified dividends
- Includes net short-term capital gains distribution from mutual funds and/or real estate investment trusts (REITs)
- Includes taxable interest income from mutual funds (not just dividends)

- Not all foreign dividends are qualified
- Generally, lower tax rate for qualified dividends

#### Box 1a - Box 1b = Non-Qualified Dividends

- Includes interest income
- Includes dividends from REITs
- Taxed as ordinary income and often a higher corresponding tax rate

#### Box 1b: Qualified Dividends

- Dividends paid by a U.S. company or qualifying foreign company

#### Box 2a: Total Capital Gains Distribution

- Net long-term capital gains distribution from mutual funds or REITs

### Summary of taxes

- (A) Tax on dividends: \$1,692
- (B) Tax on interest income: \$8,413
- (C) Tax on capital gains: \$6,580

**Total Federal Tax Due: \$16,685**  
**Percent lost to taxes: -1.7%**

A hypothetical illustration.

\*Net Investment Income Tax of 3.8%.

\*\*Any non-qualified dividends are taxed as ordinary income at 35.8%.

† Using 2022 average capital gains distribution % of Morningstar broad category 'US Equity' which includes mutual funds and ETFs.

## How about a tax-managed investor such as Uncle Sam & Aunt Betsy?

Contrasting with Joe & Joan on the prior page, let's look at tax-aware investors in two distinct mutual funds; their \$500,000 U.S. large cap fund has a full-year focus on tax-management and their \$500,000 in fixed income is invested in a municipal bond fund. So, while Joe & Joan received the average taxable distribution from their investments, Uncle Sam & Aunt Betsy took advantage of an investment approach with a full-year focus on tax-management and their results were quite different:

Their year-end investment statement stood at **\$1,000,000** and after paying taxes to the IRS, it's only down to **\$999,436**.

They lost just **0.1%** of their investment return to the payment of taxes.

Take a closer look at their 1099-DIV to see how this can happen.

PAYER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.		1a Total ordinary dividends		OMB No. 1545-0110	
<b>Mutual Fund Company</b>		\$ <b>3,000</b>		Form <b>1099-DIV</b> (Rev. January 2022) For calendar year 2022	
		\$ <b>3,000</b>			
PAYER'S TIN		2a Total capital gain distr.		2b Unrecap. Sec. 1250 gain	
RECIPIENT'S TIN		\$ <b>0</b>		\$	
RECIPIENT'S name		2c Section 1202 gain		2d Collectibles (28%) gain	
<b>Uncle Sam &amp; Aunt Betsy</b>		\$		\$	
		2e Section 897 ordinary dividends		2f Section 897 capital gain	
Street address (including apt. no.)		3 Nondividend distributions		4 Federal income tax withheld	
City or town, state or province, country, and ZIP or foreign postal code		\$		\$	
Account number (see instructions)		5 Section 199A dividends		6 Investment expenses	
		\$		\$	
11 FATCA filing requirement		7 Foreign tax paid		8 Foreign country or U.S. possession	
<input type="checkbox"/>		\$		\$	
		9 Cash liquidation distributions		10 Noncash liquidation distributions	
		\$		\$	
		12 Exempt-interest dividends		13 Specified private activity bond interest dividends	
		\$ <b>18,000</b>		\$	
		14 State		15 State identification no.	
		\$		\$	
		16 State tax withheld		\$	
		\$		\$	

**Dividends and Distributions**

**Copy B For Recipient**

This is important tax information and is being furnished to the IRS. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.



## Uncle Sam & Aunt Betsy Tax-Aware Taxpayer

**Household Taxable Income:** \$400,000  
**Marginal Tax Rate on Unearned Income:** 35.8% (32% + 3.8% NIIT\*)

**Long-Term Capital Gain/Qualified Dividend Tax Rate:** 18.8% (15% + 3.8% NIIT\*)  
**Filing Status:** Married filing jointly

### Investments:

- **Tax-Managed Equity Mutual Fund**  
\$500,000 Balance  
0.6% Yield / No capital gains distribution
- **Municipal Bond Mutual Fund**  
\$500,000 Balance  
3.6% Yield (generally tax-free at federal level)

**Box 1a: Total Ordinary Dividends:**  
Dividend from mutual fund: **\$3,000**  
Taxable int. income from mutual fund: **\$0**  
Total Ordinary Dividends: **\$3,000**

**Box 1b: Qualified Dividends**  
**\$3,000 X 18.8% = \$564 in federal taxes (A)**

**Box 1a - Box 1b = Non-Qualified Dividends\*\***  
**\$3,000 - \$3,000 = \$0**  
**\$0 X 35.8% = \$0 in federal taxes (B)**

**Box 2a: Total Capital Gains Distribution**  
**\$0 X 18.8% = \$0 in federal taxes (C)**

**Box 12: Exempt-Interest Dividends**  
Interest income from municipal bond funds  
Generally, tax-free at the federal level.  
**\$18,000 X 0% = \$0 in federal taxes**

A hypothetical illustration. \*Net Investment Income Tax of 3.8%. \*\*Any non-qualified dividends are taxed as ordinary income at 35.8%.

### Summary of taxes

(A) Tax on dividends:	<b>\$564</b>
(B) Tax on interest income:	<b>\$0</b>
(C) Tax on capital gains:	<b>\$0</b>
<b>Total Federal Tax Due:</b>	<b>\$564</b>
<b>Percent lost to taxes:</b>	<b>-0.1%</b>

## How low can you go?

A quick comparison of two hypothetical cases:

As you see here, two taxpayers with the same portfolio value can potentially end up with very different outcomes on an after-tax basis. Note that these two couples had same investment amount and materially different federal tax bills. Details matter as no one wants to pay more than they have to the IRS. Remember, you DON'T need to be in the top tax bracket to feel the pinch from taxes.

	Joe & Joan Traditional Taxpayer	Uncle Sam & Aunt Betsy Tax-Aware Taxpayer
Year-end investment statement showed:	\$1,000,000	\$1,000,000
Federal tax due from:		
Dividends	\$1,692	\$564
Interest Income	\$8,413	\$0
Capital Gains	\$6,580	\$0
<b>Total Federal Tax</b>	<b>\$16,685</b>	<b>\$564</b>
After-tax value:	\$983,315	\$999,436
<b>Percent of investments lost to taxes:</b>	<b>-1.7%</b>	<b>-0.1%</b>

## Between a Rock and Hard Place?

Here are some ideas on changes to consider:

### CAPITAL GAINS DISTRIBUTIONS (BOX 2A)

**Q:** Are these distributions high for your investment amount? Are the capital gains being reinvested?

**A:** If these distributions are being reinvested, look into turning off that reinvestment, and migrate that cash into a tax-managed approach that may work to minimize capital gains.

### DIVIDENDS (BOX 1A/1B)

**Q:** Is there a need for the dividend income? Are the dividends being reinvested?

**A:** If these dividends are being reinvested, look into turning off that reinvestment, and migrate that cash into a tax-managed approach that may work to balance dividends with capital appreciation.

### INTEREST INCOME (BOX 1A)

**Q:** Is there a need for this current income? Is interest income being reinvested?

**A:** Consider municipal bonds for tax-free income or a lower tax bill.

### TRANSITION PLAN

**Q:** Do you have a similarly frustrating tax bill year after year after year? When was the last time you rebalanced your portfolio? Are you letting the potential tax bill influence your decision-making?

**A:** It may make sense to transition all (or part) of the portfolio to a more tax-managed approach. Understand the tax impact of a transition, if any, and what the payback period might be. Russell Investments can work with your financial advisor to help analyze potential taxes and the payback period for portfolio transitions.

### REALLOCATIONS, TACTICAL TRADING AND FUND REPLACEMENTS

**Q:** Does the portfolio trade frequently due to reallocations, tactical adjustments or fund replacements?

**A:** Frequent trading within a taxable portfolio can result in unnecessary taxes when positions with unrealized gains are constantly and/or systematically sold. When making changes to a taxable portfolio always be sure to consider the tax consequences. Smaller and less frequent allocation changes may be better for tax-sensitive investors so that benefits from portfolio improvements are not outweighed by tax costs.

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**“WHEN YOU FIND  
YOURSELF IN A HOLE,  
THE FIRST THING TO  
DO IS STOP DIGGING.”**

—WILL ROGERS

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## 2023 Federal Income Tax Brackets (Short-term capital gains are taxed as ordinary income.)

Tax Rate	Married Filing Jointly	Single	Married Filing Separately	Head of Household
10%	\$0 - \$22,000	\$0 - \$11,000	\$0 - \$11,000	\$0 - \$15,700
12%	\$22,001 - \$89,450	\$11,001 - \$44,725	\$11,001 - \$44,725	\$15,701 - 59,850
22%	\$89,451 - \$190,750	\$44,726 - \$95,375	\$44,726 - \$95,375	\$59,851 - \$95,350
24%	\$190,751 - \$364,200	\$95,376 - \$182,100	\$95,376 - \$182,100	\$95,351 - \$182,100
32%	\$364,201 - \$462,500	\$182,101 - \$231,250	\$182,101 - \$231,250	\$182,101 - \$231,250
35%	\$462,501 - \$693,750	\$231,251 - \$578,125	\$231,251 - \$346,875	\$231,251 - \$578,100
37%	Over \$693,750	Over \$578,125	Over \$346,875	Over \$578,100

## 2023 Long-Term Capital Gain/Qualified Dividend Tax Rates

Tax Rate	Married Filing Jointly	Single	Married Filing Separately	Head of Household
0%	\$0 - \$89,250	\$0 - \$44,625	\$0 - \$44,625	\$0 - \$59,750
15%	\$89,251 - \$553,850	\$44,626 - \$492,300	\$44,626 - \$276,900	\$59,751 - \$523,050
20%	Over \$553,850	Over \$492,300	Over \$276,900	Over \$523,050

## 2023 Standard Deduction<sup>1</sup>, NIIT<sup>2</sup> Threshold, Capital Loss Limit<sup>3</sup>

	Married Filing Jointly	Single	Married Filing Separately	Head of Household
<b>Standard Deduction</b>	\$27,700	\$13,850	\$13,850	\$20,800
<b>3.8% NIIT Thresholds</b>	\$250,000	\$200,000	\$125,000	\$200,000
<b>Capital Loss Limit</b>	\$3,000	\$3,000	\$1,500	\$3,000

Source: Internal Revenue Service

<sup>1</sup> Blind, or age 65 or older: +\$1,500 (Married); +\$1,850 (Single or Head of Household).

<sup>2</sup> Net investment income tax.

<sup>3</sup> If your capital losses exceed your capital gains.

**Talk to your financial professional and/or tax accountant to see what steps can be taken to potentially minimize your tax burden.**

Or visit [russellinvestments.com](https://russellinvestments.com) to discover the potential benefits of tax-managed investing.

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