HW Hot Topics Article 2018-04 Capital Gain Tax Rates

HW Hot Topics articles are brief summaries of a topic, for clients to gain a general understanding. We intend for the information to answer the "quick questions" and to advance the dialog when we provide further analysis and planning.

One FAQ – What is my capital gain tax rate?

This is a simple question with a complex answer. The federal income tax rates are summarized below. Some states have special rates for capital gains. Others tax gains at the same rates as other income.

To start, it is important to understand that long-term capital gains get a favorable tax rate, and short-term gains do not. A long-term gain results when the asset has been held a full year before sale.

The "NIIT", 3.8% net investment income tax, may or may not apply. Some gains are not subject to NIIT regardless of income level. For example, gains from sales of business property within a business in which you "materially participate".

Sales of business property are not technically "capital gains", but are taxed like capital gains in some cases. Sales of depreciated personal property assets are usually fully taxed as ordinary income. Sales of depreciated real estate are usually taxed like capital gains, except for the depreciation part of the gain. To the extent of depreciation taken, the gain is "unrecaptured Section 1250 gain". That may be subject to a 25% tax rate, depending on other factors in the particular tax scenario.

To understand the rates, visualize filling brackets with taxable income, and adding the capital gains last. Following are the 2018 rates and brackets of taxable income for long-term capital gains.

Tax rate		Single Person	Joint Return
0.0%	Taxable income	$ 38,600	$ 77,200
15.0%	Taxable income	$ 425,800	$ 479,000
20.0%	Taxable income	Beyond the 15% bracket	
3.8%	"MAGI" threshold	$ 200,000	$ 250,000
	Modified adjusted gross income;		
	NIIT applies beyond this threshold.		
18.8%	Income tax plus NIIT		
23.8%	Income tax plus NIIT		

For example, the married couple with taxable income of $57,200 before gains could add a $20,000 long-term capital gain and have it be taxed at 0.0%.

As another example, if they have taxable income of $400,000 before gains (of course, "MAGI" is over $250,000), they could add $79,000 of long-term capital gain and have it be taxed at 18.8%. Beyond the $479,000 "breakpoint", the rate is 23.8% (20% plus 3.8%).