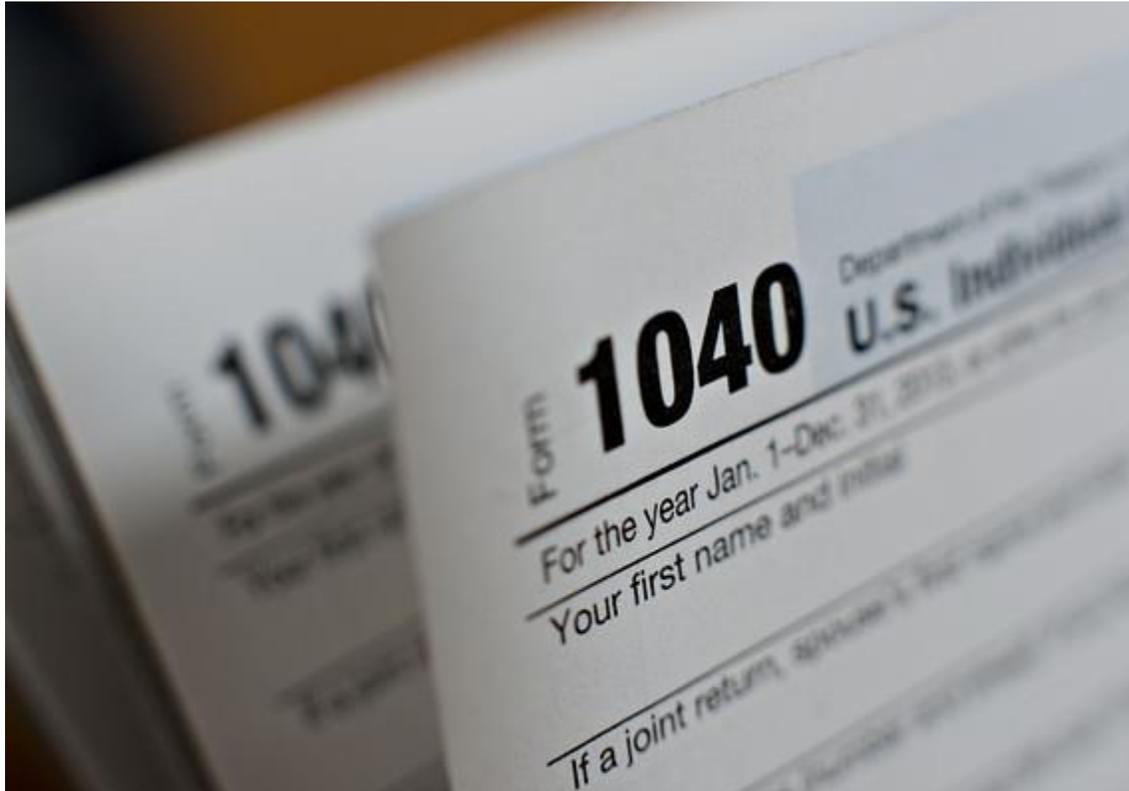


# Capital gains: At what rate will your long-term sales be taxed?

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Contrary to popular opinion, not all of your long-term capital gains are taxed at 15%. No, that would be far too simple. So in addition to the 15% rate, there is a 20% rate for upper-income investors and there are several additional long-term capital-gains rates, which can range from 0% to 28%. Last but not least, there's potentially a 3.8% Medicare surtax on capital gains reaped by upper-income investors. Which category your profit will fall into depends on your income-tax bracket, the type of asset you sold, how long you held it and when you sold it. Keep in mind, short-term gains (on assets held for one year or less) are taxed at your ordinary income rate, which can range from 10% to 39.6%.

Here's the breakdown of the long-term capital gains rates under the current federal income tax rules.

## **Investment securities**

### **The 0% rate**

**Who's Eligible:** Individuals in the 10% and 15% federal income tax brackets with net long-term capital gains from selling investment securities held for more than one year.

More people than you might think qualify for the 0% rate. Why? Because the 15% bracket covers 2014 taxable income of up to \$36,900 for singles, \$73,800 for joint filers, \$49,400 for heads of households, and \$36,900 for married individuals who file separately. Here's how this rule works in real life. Say you're a joint filer and have \$65,000 of "regular" taxable income in 2014 and a net long-term gain of \$10,000 from stock sales. The first \$8,800 of gain (\$73,800 - \$65,000) will be taxed at 0%. The remaining \$1,200 (\$10,000 - \$8,800) will get taxed at the standard 15% rate you hear so much about. Now let's say your net long-term gain is \$8,800 or less. In this case, you'll pay 0% on the entire gain. You get the idea.

### **The 15% rate**

Who's Eligible: Individuals in the 25% federal income tax bracket or higher with net long-term capital gains from selling investment securities held for more than one year.

### **The 20% rate**

Who's Eligible: Everyone, including billionaires. Specifically, for 2014, this rate only applies if your taxable income is above \$406,750 for singles or \$457,600 for married joint-filing couples. For 2015, the 20% rate thresholds are \$413,200 and \$464,850 respectively.

#### **Investment real estate**

### **The 25% rate**

Who's Eligible: Property owners and real-estate investment trust (REIT) investors in the 25% income-tax bracket or higher who hold property for more than one year.

Investment real estate gains are tricky since they can be taxed in two different ways. If you claim depreciation deductions, at least some of those gains (so-called unrecaptured Section 1250 gains) are taxed at a maximum federal rate of 25%.

For example, say you own a rental duplex and have deducted \$32,000 of depreciation over the years. That depreciation reduces your basis in the property and results in a bigger taxable gain (or smaller loss) when you sell. Now you sell for a \$100,000 gain. The first \$32,000 (the unrecaptured Section 1250 gain) is taxed at a maximum federal rate of 25%. The remaining \$68,000 of gain is taxed at the "general rule" maximum federal rate of no more than 20%.

If you own shares in a REIT, you can receive capital-gains distributions subject to the 25% maximum rate. This happens when the REIT sells a piece of depreciable property and distributes the profit to its shareholders.

To the extent an unrecaptured Section 1250 gain falls into the 10% or 15% bracket, it gets taxed at that rate.

#### **Collectibles and small-business stock**

### **The 28% rate**

Who's Eligible: Any collector in the 28% tax bracket or higher; some small-business stock shareholders.

Net long-term gains from collectibles (stamps, coins, baseball cards and the like) are subject to a 28% maximum federal rate rather than the usual 20%. To the extent a long-term collectibles gain falls into the 10%, 15% or 25% bracket, it's taxed at that rate.

The 28% maximum rate also applies to the taxable part of a gain from selling certain small-business stock that qualifies for a special 50% or 75% gain exclusion rule (under the tax code). Basically, these are shares in relatively small corporations that were originally issued to you and that you've owned more than five years. Consult your tax adviser if you think you have any shares fitting this description.

### **The 3.8% Medicare surtax rate**

Who's Affected: Upper-income folks with adjusted gross income above \$200,000 or \$250,000 for married joint-filing couples. Under complicated rules, all or part of your capital gains could be hit. Or not!

#### **Homes and small-business stock**

### **The 0% rate**

Who's Eligible: Homeowners who owned and used their home as a main residence for at least two years before selling; some shareholders of small-business stock.

Believe it or not there are a couple of ways you can lock in a gain without paying Uncle Sam a dime. The first is if you sell a home you've owned and used as your main residence for at least two years out of the five-year period ending on the sale date. You are allowed to exclude (pay zero federal tax on) up to \$250,000 of gain. If you are married, you can potentially exclude up to \$500,000.

Even if you don't meet the two-out-of-five-years rule, you may still qualify for a reduced gain exclusion privilege. If your gain exceeds the amount you can exclude, the difference is treated as a long-term capital gain eligible for the 15% or 20% federal rate (or 0% if your taxable income is low enough).

Up to 50% or 75% or even 100% of the gain from selling certain small-business stock can be excluded from your federal tax return. Again, consult a tax pro if you think you might qualify for this break. (Relatively few people do, but you could be one of the lucky ones.)