

INTRODUCTION TO CAPITAL GAINS TAX

For many investors, capital gains tax is one of the more confusing financial topics. Yet a basic understanding of capital gains is key to building a financial plan that reflects your goals and needs. It's important to be aware of the tax consequences of selling your personal assets, as doing so may significantly impact your tax return—and your financial picture as a whole.

What is a capital asset?

Almost anything you own for personal or investment purposes may be considered a capital asset. This applies to a range of assets, including investment vehicles such as stocks and bonds, real estate, and collectibles. Any capital gain resulting from the sale of these assets may be subject to capital gains tax.

What is a capital gain?

When a capital asset is sold, the difference between the purchase price of the asset and the amount it is sold for is a capital gain or a capital loss. You have a capital gain if you sell the asset for more than its original purchase price (basis). A capital gain is classified as *short-term* if you held the asset for a year or less before selling it; it is considered *long-term* if you held the asset for more than a year. Net long-term capital gains are often taxed at a lower rate than the ordinary income tax rate. For IRS reporting purposes, all capital gains or losses must be claimed on Schedule D and then transferred to Form 1040, line 13.

Special tax considerations

Keep in mind that different types of capital gains are taxed at different rates. Tax rates for capital gains tend to vary based on the asset class:

- **Collectibles.** Long-term collectibles are taxed at a maximum 28-percent rate, and short-term collectibles are taxed as ordinary income. Items such as coins, stamps, gems, antiques, and fine art are considered collectibles.
- **Real estate.** Special exceptions apply to capital gains on real estate. If you are considering selling your primary home, you may qualify for a tax exclusion if you meet certain criteria.
- **Business assets.** Fixed assets that are used for your business, such as furniture and machinery, are taxed as ordinary gains.

Your tax planning

Remember, your capital gains tax rate depends on a variety of factors, including your income level, when you bought and sold the asset, and changes to the tax code. Your financial advisor can assist you and your tax advisor in creating and implementing a comprehensive tax plan that is consistent with your financial goals and personal situation.

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