

Tax Tips You Can Use



Capital Gains- A Primer
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Many people are confused about reporting Capital Gains on their tax return. A Capital Gain is a type of income (or loss) and must be reported on your tax return just like all other types of income. This article will talk about the types of capital gains that exist and how they are reported.

A capital gain is the net profit or loss after the sale of a capital asset. A capital asset can be stocks, bonds, rental property, a debt owed to you, your home, equipment, a car or personal property like a stamp collection. When an asset is sold, money is made or lost at sale and it should be accounted for on one's tax return. If it is property used in a business, it is reported as a "sale of business property" form. If it is not business property, it is reported as a sale on a Schedule D form.

The type of capital gain differs by the length of time the property was held. "Long term" capital gains are generated when an asset was sold after being owned for more than one year, that is, at least one year plus one day. If you bought an asset on June 1 2005, then you must wait until June 2, 2006 to sell the asset to get long term capital gain treatment of the sale. The reason this is important is that long term capital gains are taxed at a lower rate than regular, ordinary income. Long term capital gains are taxed at a maximum of 15%, where ordinary income can be taxed up to 35%. The dates are critical. If you are buying or selling a stock, the purchase or sale date is trade date, not the order or settlement date.

If an asset is held one year or less, then the gains are "short term" and are treated as ordinary income like wages, bank interest, or self-employment income. This means that the gains are taxed at normal rates of 10% to 35% depending on your total income.

If an asset is sold at a loss, then the loss is treated as a long term loss or short term loss by the same rules as gains. Short losses are used to reduce short term gains and long term losses are used to reduce long term gains. If you still have a loss, then you reduce any type of gains by any remaining losses. If you still have a loss, you can take up \$3000 per year of the loss to reduce your other income, like wages. Any losses not used can be carried into subsequent years. The losses can be carried forward indefinitely.

If you have a carry-forward loss and change tax preparers, you should make sure the new preparer has your carry forward information from the last years tax return, so your loss is not lost.

Next month's article will discuss the "basis" of an asset and how to determine if you have a gain or loss.

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The fine print: This article is for information only. Please see your tax professional for questions about your individual tax situation.