

10 Things You Should Know About Capital Gains

Selling stocks, bonds, or fund shares at a profit could have implications for your wallet beyond simply increasing its contents.

- 1. There are capital gains and capital gains distributions.** If you sell an investment for more than its cost basis (its purchase price adjusted for dividends and distributions), that's a capital gain. Fund managers buy and sell holdings throughout the year and are legally required to pass profits from those sales on to shareholders—those are capital-gains distributions.
- 2. Capital-gains distributions aren't a response to action on your part.** You can receive a capital-gains distribution from a fund you own even if you haven't sold any shares. Funds are required to distribute nearly all the capital gains they accrue at least once a year.
- 3. You could see distributions even if your fund is in the red.** You can receive capital-gains distributions even if the fund you own posted negative returns for the year. This happens when a fund manager sells underlying shares for a profit even though the fund itself experienced a loss.
- 4. The tax man won't cometh (in a retirement account).** Capital-gains distributions aren't taxable if they're from a fund you own in a tax-deferred account such as a 401(k), 403(b), or IRA—unless you make a withdrawal from those accounts instead of allowing them to be reinvested.
- 5. A gift that could keep on giving.** In a tax-deferred account, if you reinvest your capital-gains distribution to purchase additional shares, it's not a taxable event.
- 6. For non-retirement accounts, how much you owe Uncle Sam depends on length of ownership.** If an asset is sold within a year or less of its purchase, it's considered a short-term capital gain and is taxed at the same rate as your ordinary income. Investments sold after more than one year are considered long-term capital gains and are generally taxed at a lower rate than your ordinary income (see tables on page 2).
- 7. Dividends are different than capital gains.** Dividends are a share of earnings paid to current shareholders, typically at regular intervals. If you own individual stocks, the companies you own shares of may pay dividends directly to you. If you own a fund, it could distribute dividends to you, too. Conversely, capital gains are only created when an asset is sold, either by you or by your fund manager.
- 8. Look for IRS Forms 1099.** If you still own your investments, you'll likely receive a Form 1099-DIV. It lists all your dividend or capital-gains distributions for the previous tax year. If you sold an investment, Form 1099-B shows your capital gains (or capital losses if you sell an investment for less than its cost basis).
- 9. If you win some but lose more, it changes the situation.** In taxable accounts, if all your capital losses are greater than your capital gains after netting them out on Form 1099-B, it could negate your tax liability. You may also be able to deduct up to \$3,000 of your losses on your tax return each year if they exceed your gains, and you can carry those losses forward in future years.
- 10. Some funds distribute more than others.** Exchange-traded funds (ETFs), for example, tend to have relatively low turnover (e.g., they buy and sell securities less frequently), so they may have lower capital-gains distributions than many other investments.

Tax Rates for Capital Gains Vary by Income Level

2023 Capital Gains Tax Brackets

Single Filers

Income Level	Long-Term Tax Rate	Short-Term Tax Rate*
<\$44,625	0%	10-12%
≥\$44,625 and <\$492,300	15%	22-35%
≥\$492,300	20%	37%

Married Filing Jointly

Income Level	Long-Term Tax Rate	Short-Term Tax Rate*
<\$89,250	0%	10-12%
≥\$89,250 and <\$553,850	15%	22-35%
≥\$553,850	20%	37%

Head of Household

Income Level	Long-Term Tax Rate	Short-Term Tax Rate*
<\$59,750	0%	10-12%
≥\$59,750 and <\$523,050	15%	22-35%
≥\$523,050	20%	37%

Data Sources: TaxFoundation.org and IRS, as of 10/23. *Range shown because the actual rate depends on an investor's tax bracket.

If you have questions about capital gains and capital-gains distributions, talk to your financial professional or tax professional.

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