

Capital Asset Defined:

In general, everything owned for personal or investment purposes is a capital asset. For example, stocks and bonds, a house, real estate, household furnishings, a car used for pleasure or commuting, coin or stamp collections, gems and jewelry, gold, silver or any other metal.

Capital Gain or Loss:

In general, a taxpayer recognizes a capital gain or loss when a capital asset is sold or exchanged. A noncapital asset produces ordinary income or loss when sold. Gain or loss is the difference between the sales price and the taxpayer's adjusted basis in the asset.

Holding Period:

Capital gains and losses must be separated according to how long the property was held.

Short-term – The holding period for short-term capital gains and losses is one year or less.

Long-term – The holding period for long-term capital gains and losses is more than one year.

Capital Gain Rates:

In general, the long-term capital gain rate is 15% on certain asset sales. Short term capital gains are taxed as ordinary income according to ordinary income tax rates.

Like-Kind Exchanges (IRC 1031 Exchanges):

No gain or loss is recognized if property held for use in a trade or business or for investment is exchanged solely for property of a like kind to be held either for use in trade or business or for investment. Any gain or loss realized, but not recognized, adjusts the basis of like-kind property received in the exchange.

Like-kind property means property of the same nature or character, not necessarily of the same grade or quality. For example, improved real estate can be exchanged for unimproved real estate. Stocks, bonds, notes and other securities do not qualify for like-kind exchange.

The property to be received in a nonsimultaneous exchange must be identified in a written agreement within 45 days after the transferred property is surrendered.

The property in the nonsimultaneous exchange must be received on or before the earlier of:

. 180 days after the transfer of the property given up or

. The due date (including extensions) for the tax return year in which the transfer of the property given up occurs.

If property is transferred through a qualified intermediary, the transfer of the property given up and receipt of like-kind property is treated as an exchange. This rule applies even if the taxpayer receives money or other property directly from a party to the transaction other than the qualified intermediary.

Property that is not like-kind property (including cash) is “boot”. The receipt of boot will cause a realized gain on an exchange to be recognized. Gain is realized if the FMV of the property received exceeds the tax basis of the property given. The amount of gain to recognize is the lesser of the boot received or the realized gain.

Sale of Residence Exclusion Rules:

A taxpayer can exclude from income up to \$250,000 (\$500,000 jointly) of gain from the sale of a personal residence if the following tests are met:

. Ownership and Use – The individual must have owned and used the home as a principal residence for a least two out of the five years prior to the sale (the two years do not have to be consecutive).

. Frequency Limitation – The exclusion applies to only one sale every two years.

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