History of Capital Gain Tax Rates

Understanding Capital Gain Taxes

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Different types of income are taxed differently under the United States tax system. There are significant distinctions between ordinary income tax and capital gains tax. Ordinary income tax applies to income earned from regular activities such as wages, salaries, and commissions. It also applies to interest earned on bank deposits.

The capital gains tax applies when an investor sells a capital asset such as stocks, bond, real estate, or other investments when the sale price exceeds the adjusted cost basis. Individual investors and corporations pay tax on the net total of all capital gains. The tax rate depends on both (1) the investor's tax bracket and (2) the length of time the investment was held.

Short-term capital gains are taxed at the investor's ordinary income tax rate and are defined as investments held for a year or less before being sold.

Long-term capital gains, on dispositions of assets held for more than one year, are taxed at a lower rate.

HISTORY OF CAPITAL GAIN TAX RATES

1913 – 1921: Capital gains were taxed at ordinary rates, initially up to a maximum rate of 7%.

1921 – 1993: The Revenue Act of 1921 allowed a tax rate of 12.5% on gains for assets held at least two years. 1031 exchanges were introduced into the tax code.

1934 – 1941: Taxpayers could exclude from taxation up to 70% of gains on assets held for 1, 2, 5, and 10 years.

1942 – 1954: Taxpayers could exclude 50% of capital gains on assets held at least six months or elect a 25% alternative tax rate if their ordinary tax rate exceeded 50%.

1954 – 1967: The maximum capital gains tax rate was 25%.

1969 – 1975: Imposed a 10% minimum tax, excluded gains, and limited the alternative tax to $50,000 of gain.

1976 – 1977: The 1976 Tax Reform Act increased the minimum tax rate to 15%.

1978 – 1985: Congress eliminated the minimum tax on excluded gains and increased the exclusion to 60%, reducing the maximum rate to 28%.

1986 – 1989: The Tax Reform Act of 1986 repealed the exclusion of long-term gains, raising the maximum rate to 28% (33% for taxpayers subject to phaseouts).

1990 – 1993: Budget acts increased ordinary tax rates but re-established a lower rate of 28% for long-term gains, though effective tax rates sometimes exceeded 28% because of other tax provisions.

1997: The Taxpayer Relief Act of 1997 reduced capital gains tax rates to 10% and 20% and created the $250,000/$500,000 exclusion for the sale of a primary residence.

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1998 – 2017: Tax law keyed the tax rate for long-term capital gains to the taxpayer's tax bracket for ordinary income, and set forth a lower rate for capital gains. (Short-term capital gains were taxed at the same rate as ordinary income throughout this period.) From 1998 through 2017, tax law keyed the tax rate for long-term capital gains to the taxpayer's tax bracket for ordinary income, and set forth a lower rate for the capital gains. (Short-term capital gains have been taxed at the same rate as ordinary income throughout this period.)

2001: The Economic Growth and Tax Relief Reconciliation Act of 2001 reduced tax rates to 8% and 18%, for assets held for five years or more.

2003: The Jobs and Growth Tax Relief Reconciliation Act of 2003 reduced tax rates to 5% and 15%, and extended the preferential treatment to qualified dividends.

2005: The 15% tax rate was extended through 2010 as a result of the Tax Increase Prevention and Reconciliation Act of 2005.

2010: The Small Business Jobs Act of 2010 exempted taxes on capital gains for angel and venture capital investors on small business stock investments if held for five years. This was a temporary measure but was extended through 2011 by the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 as a jobs stimulus.

2012: Extension of the 15% tax rate through 2012. The American Taxpayer Relief Act of 2012 made qualified dividends a permanent part of the tax code - but added a 20% rate on income in the new highest tax bracket.

2013: Provisions of the Patient Protection and Affordable Care Act took effect that imposing a new Medicare tax of 3.8% (formerly a payroll tax) on capital gains of high-income taxpayers. Any net investment income over $200,000 for single filers and over $250,000 for married filing jointly faced this additional 3.8% net investment income tax.

2018 – 2025: Tax Cuts and Jobs Act of 2017 (TCJA) lowered tax rates across all tax brackets, starting with tax year 2018. Most tax provisions in the TCJA are set to expire at the end of 2025.

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