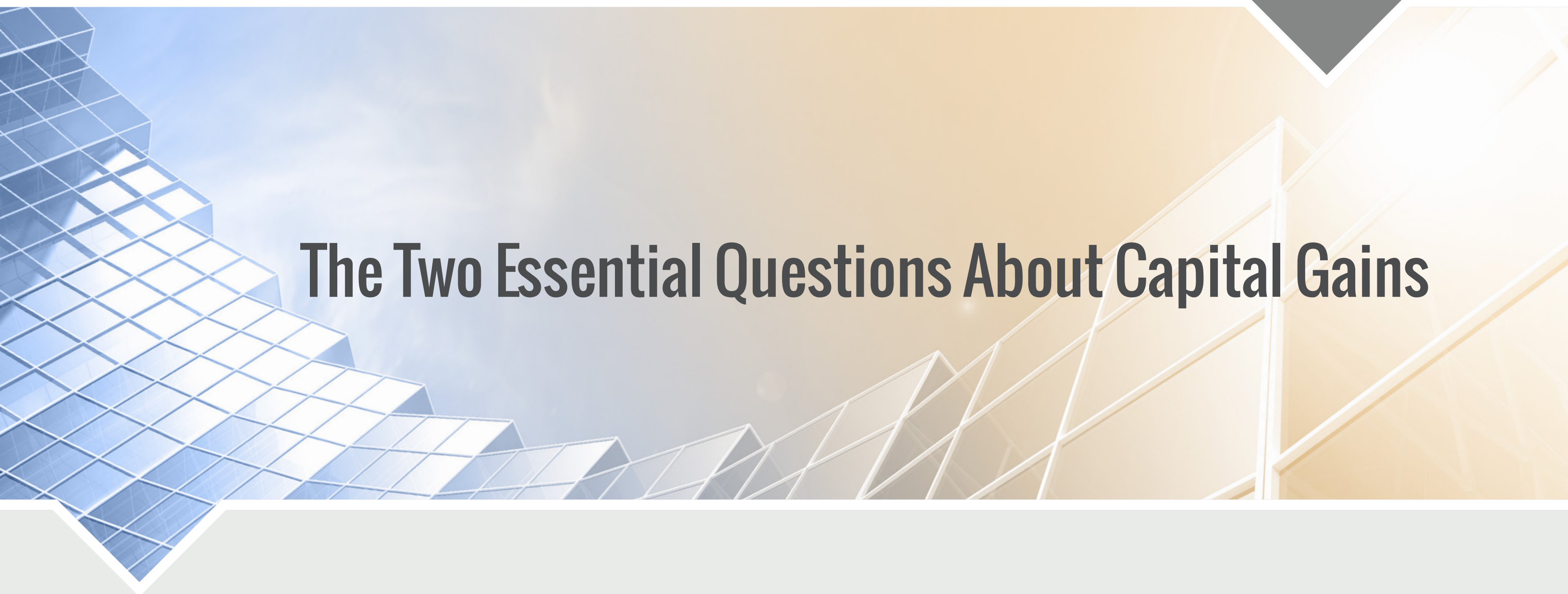

The Two Essential Questions About Capital Gains

In 2016, more than 11 million federal tax returns were filed that included over $700 billion in taxable capital gains.[1] These represent financial gains reaped from **capital assets**, a broad category that encompasses nearly anything held for personal and/or investment purposes.

Like many parts of the federal tax code, capital gains taxes can be difficult to digest. However, much of what investors need to know is captured by two simple questions:

What gets taxed? and How much will I pay?

What Gets Taxed?

THE BASICS

It's easy to think of capital gains as falling into two categories. The first is **gain on intangible assets**, such as securities, held in an investment account, which may include stocks, bonds, mutual funds and ETFs. In general, selling investments at a profit, or receiving distributions/ interest from them, will result in a capital gains tax if the asset is held in a taxable account.

The second category is **gain on other capital assets**, such as real estate, gold, wine, and baseball cards. Again, if you sell such an asset for a profit, capital gains taxes may apply.

WHAT ELSE TO KNOW

Within the two categories of capital gains lie two important rules, among others:

- Interest income is not considered a capital gain. Interest derived from **qualified municipal bonds** is always tax-free.
- Gains from the **sale of your home**[2] are potentially excludable if you:
  - Owned it and used it as your primary residence for at least two of the previous five years
  - Have not excluded gains from the sale of another home in the past two years

[1] https://www.irs.gov/pub/irs-soi/15in14acg.xls

[2] Up to $250,000 for an individual taxpayer or $500,000 for a married couple filing jointly.

How Much Will I Pay?

The answer here is defined by two variables: income level and how long you've owned the asset. The latter matters as there are different tax rates for short-term gains, where the underlying asset has been held for less than one year, and long-term gains, where the asset has been held for more than one year.

Based on the tax law as of the date of publication (November 2017) short-term capital gains are taxed at the same rate as ordinary income; the rates for long-term gains range from 0% up to 20%.

Head of Household Brackets and Rates			
Income	Ordinary Income Tax Bracket	Short-term Capital Gains Rate	Long-term Capital Gains Rate
Up to $13,350	10%	10%	0%
$13,351 to $50,800	15%	15%	0%
$50,801 to $131,200	25%	25%	15%
$131,201 to $212,500	28%	28%	15%
$212,501 to $416,700	33%	33%	15%
$416,701 to $444,550	35%	35%	15%
$444,551 and over	39.6%	19.6%	20%

As with the first question, there are a variety of exceptions that can apply. Capital gains tax rates on collectibles, such as wine or baseball cards, differ from those in the above table. And for certain high income earners[3] the Net Investment Income Tax can add an additional amount to what is owed.

Furthermore, investors have methods at their disposal to minimize capital gains taxes. The easiest is to simply hold assets in tax-advantaged accounts. Investors can also deploy a strategy of tax loss harvesting, in which gains are potentially offset by selling other securities investments at a loss.[4]

The rules surrounding many aspects of the tax system are notoriously complex, and capital gains are no exception. Even so, by having a sound grasp of the essentials investors will be well-positioned to understand how capital gains taxes can impact them year in and year out.

Please consult with your Financial Advisor to help ready yourself for the impact of capital gains. Or visit our Readiness Building Blocks website at **AMGFunds.com/readiness**.

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[3] $200,000 or more in modified adjusted gross income for individual taxpayers and $250,000 or more for married couples filing jointly. Via: https://www.irs.gov/newsroom/net-investment-income-tax-faqs

[4] To the extent that capital losses exceed capital gains, deductions for capital losses are capped at $1,500 annually for a married individual taxpayer filing a separate return and $3,000 for other taxpayers, including married couples filing jointly. However, additional losses can be carried over to subsequent years.

The information contained herein is based on the Internal Revenue Code of 1986, as amended (the "Code"), and other applicable authorities, in each case as of the date of publication, [November, 2017], and does not take into account the potential effect of any future changes to the Code or such other authorities, some of which may be of retroactive effect.

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