WELLS FARGO Wealth & Investment Management

Tax treatment of capital gains and dividends

Capital gains and capital losses

A capital gain or loss results from the sale of a capital asset. Examples of capital assets are stocks, bonds, mutual funds, and real estate. The amount of the capital gain or loss equals the net sales proceeds minus the adjusted cost basis.

Capital gains do not include ordinary income, such as interest or dividend income. Although qualified dividends are taxed at long-term capital gains rates under current tax law, you cannot use capital losses to directly offset qualified dividends.

How you manage your capital gains and losses and the type of dividends generated by your portfolio can play a major role in determining your after-tax return. To help get the greatest benefit from current tax law, there's important information you need to understand.

Capital gains holding periods

Your holding period and taxable income (discussed below) determine your capital gains tax rate. Assets you hold long-term — longer than one year — receive a preferential rate. Assets held short-term are those held for one year or less. To determine if you held property longer than one year, start counting on the date following the day you acquired the property.

For example, if you purchased an investment on Feb. 4, begin counting on Feb. 5. The short-term holding period would end on Feb. 4 of the next year. To establish a long-term holding period, you would have to sell the asset on or after Feb. 5 of the next year. (Note that dates of acquisition and disposition are determined by the trade date, not the settlement date. Exceptions may apply to short sales.)

Special holding-period rules for assets acquired by gift or inheritance

Your holding period for an appreciated asset received as a gift includes the length of time you held the asset plus the time the donor held it. Any property you inherit related to a death occurring in a year other than 2010 has an automatic long-term holding period — no matter how long you or the deceased held the asset.

For deaths that occurred in 2010 the basis and holding period rules are complex. Discuss the rules with your tax or legal advisor to determine the treatment of each specific security inherited.

Long-term capital gains and qualified dividend tax rates[1]

Generally, long-term capital gains and qualified dividends fall into one of three tax brackets: 0%, 15%, or 20%. The thresholds for determining which bracket applies are illustrated in the federal tax rate summary that follows below. The 0% long-term capital gains rate only applies to the amount of gain and qualified dividends equal to or below the threshold of $96,700 (married filing jointly) or $48,350 (single) for 2025. While long-term capital gains and qualified dividends may be eligible for 0% rates for lower income individuals, the gain itself is still considered income, potentially impacting certain deductions, tax credits, and the taxation of Social Security.

The following example shows the amount of gain and qualified dividends taxed at the 0% rate for a married couple with $100,000 taxable income; $80,000 from wages and $20,000 from long-term capital gains and qualified dividends. Although their total taxable income exceeds the $96,700 limit, they pay no tax on $16,700 of capital gains and qualified dividends. The excess $3,300 would be taxed at 15%.[2]

Taxable income	=	$100,000
Maximum threshold for 0% rate	=	$96,700
Amount exceeding threshold	=	$3,300 (15% long-term capital gain rate applies)
Amount under threshold	=	$16,700 (0% long-term capital gain rate applies)
Total gain and qualified dividends	=	$20,000

Capital gains and qualified dividends

Long-term capital gain rate (held longer than one year)			
Filing Status	**0%**	**15%**	**20%**
Married filing jointly and surviving spouse	$0 – $96,700	$96,701 – $600,050	$600,051 +
Single	$0 – $48,350	$48,351 – $533,400	$533,401 +
Head of household	$0 – $64,750	$64,751 – $566,700	$566,701 +
Married filing separately	$0 – $48,350	$48,351 – $300,000	$300,001 +
Trusts and estates	$0 – $3,250	$3,251 – $15,900	$15,901 +

Exceptions to these rates include gains from sales of collectibles and certain depreciable property. Capital gains on those items may be taxed at a higher capital gains rate. For more information, consult your tax advisor.

[1] Stated rates are for federal income tax purposes only. Consult your tax advisor for state income tax rates.
[2] Although this example is conceptually accurate, the actual tax calculation would involve a separate worksheet to determine the amount of the capital gains and dividends that would be categorized and taxed at various rates.

Think about taxes all year

Although many investors wait until year-end or the approach of the tax-filing deadline to begin thinking about taxes, it may be wiser to periodically assess your tax situation — especially those issues surrounding your portfolio — throughout the year. Talk with your financial professional and tax advisor regularly to review how well your investments are helping you work toward your goals in a tax-efficient manner.

Short-term capital gains and nonqualified dividend rates

Like ordinary income, short-term capital gains and nonqualified dividends are taxed at an individual's marginal tax rate, which can currently be as high as 37%.

What is a "qualified dividend"?

Qualified dividends are paid by U.S. corporations or by entities incorporated in a U.S. possession to their preferred or common shareholders. Dividends passed through by mutual funds or other regulated investment companies can be qualified or nonqualified, depending on the underlying securities held by the fund. If a fund receives a qualified dividend, that dividend will maintain its qualified status when passed through to shareholders. Dividends paid by certain foreign corporations may also be qualified. *Keep in mind that the foreign corporate dividend may remain subject to foreign tax withholding.*

Distributions from partnerships and real estate investment trusts typically are not characterized as qualified dividends. Also, qualified dividends do not include distributions from preferred debt. Individuals, estates, and trusts may be able to deduct 20% of qualifying dividends from Real Estate Investment Trusts (REITs). Eligible dividends are REIT dividends which are not characterized as a capital gain distribution or qualified dividend. It is critical to obtain proper tax classification of an investment to determine whether the dividend is qualified.

Dividend required holding period

To qualify for the special tax treatment, shareholders must satisfy a certain holding period[3] based on the type of stock held:

- For common stock, shareholders must own the stock for more than a 60-day period containing the ex-dividend date.
- For preferred stock, the owner must hold the shares for more than a 90-day period including the ex-dividend date. Active traders should monitor their holding periods carefully to benefit from the qualified-dividend tax treatment.

Offsetting capital gains and losses

Capital losses you incur may be tax-deductible; however, there are limitations on the deductible amount in any given year. Here are the steps to follow to deduct a capital loss:

1. Offset short-term capital gains against short-term capital losses to determine the net short-term capital gain or loss.
2. Offset long-term capital gains against long-term capital losses to determine the net long-term capital gain or loss.
3. Combine the net short-term result with the net long-term result if one result is a net gain and the other a net loss.
4. If a net capital loss remains after completing steps 1 through 3, you may use it to offset up to $3,000 in ordinary income in the current tax year.

[3] When a stock trades ex-dividend, the dividend, when paid, goes to the seller. In general, the exchange designates a stock's ex-dividend a few days before the record date. Certain hedge positions may suspend the holding period for this purpose.

You can count on us

Your financial professional can work with you and your tax advisor to help manage your capital gains and losses whenever you sell an investment.

Although there are tax advantages to owning a qualified-dividend-paying stock, that in itself does not make that stock appropriate for your portfolio. Before you make an investment, your financial professional will work with you to consider a variety of factors, such as your long-term goals, time horizon and risk tolerance, in addition to the tax implications.

Note: Although qualified dividends and long-term capital gains are taxed at the same rates, this does not mean that capital losses can be used to offset qualified dividends directly. However, if you have a net capital loss after offsetting all capital gains, up to $3,000 per year of capital loss may offset regular taxable income which may include dividends.

5. If there's still a remaining capital loss, you may carry it forward to offset future years' capital gains and/or ordinary income (in accordance with steps 1 through 4).

For example, an investor has a:

- $6,000 short-term gain
- $4,000 short-term loss
- $5,000 long-term gain
- $12,000 long-term loss

He or she should:

1. Calculate the net short-term capital gain or loss:

Short-term gain:	$6,000
Short-term loss:	(4,000)
Net short-term capital gain:	$2,000

2. Calculate the net long-term capital gain or loss:

Long-term gain:	$5,000
Long-term loss:	(12,000)
Net long-term capital loss:	($7,000)

3. Calculate the net capital loss:

Net long-term capital loss:	($7,000)
Net short-term capital gain:	2,000
Net long-term capital loss:	($5,000)

4. Use $3,000 of the net long-term capital loss to offset ordinary income in the current year.[4]

5. Carry over the remaining $2,000 long-term capital loss to offset future years' capital gains and/or ordinary income.

Capital loss carryover

Losses carried over to future years retain their long-term or short-term character. For example, if a taxpayer reported a net short-term loss carryover from a prior year, then in the current year that loss would first be applied against short-term gains.

Unused net capital losses can be carried over until they are fully used or until the taxpayer's death. Carryover losses may be used on a deceased individual's final income tax return in the same manner as described above. Surviving spouses can carry forward only half of a joint loss, if applicable. Any remaining losses cannot be passed on to the deceased's spouse or heirs.

[4] When calculating the Medicare surtax, the $3,000 capital loss cannot offset dividend income.

Watch out for wash sales

When you sell stocks at a loss, the IRS lets you offset the loss against capital gains or take up to $3,000 of your capital losses against your taxable income. The exception to this is a “wash sale.” If you buy the same stock within 30 days before or after the sale for a loss, the IRS will disallow the loss. This prevents you from selling the stock, including the loss on your return and then buying the stock back immediately to capture any future gains.

If the wash sale rule applies, the disallowed loss in the current year is added to the cost basis of the new security purchased within the wash sale window. When you sell that stock, the gain or loss is determined by utilizing the adjusted cost basis which was increased by the previous loss amount. This may result in a loss or less of a capital gain due to the higher cost basis. The date of the new purchase also changes to include the holding period of the original shares.

One strategy to avoid a wash sale is to "double up" your position in a security at least 31 days before you sell your original position for a loss. If you utilize this strategy near year end be sure to purchase your double up position early enough to allow the sale of your original security on or before the last trading day of the year.

These rules are complex so be sure to work closely with your financial professional and your tax advisor.

Medicare surtax

Higher income taxpayers may be subject to an additional Medicare tax of 3.8% on net investment income. The tax affects taxpayers with modified adjusted gross income in excess of $200,000 for single individuals and $250,000 for married couples filing jointly. This surtax is in addition to any capital gain or ordinary income taxes that apply.

Talk with your tax advisor

It’s important that you understand how capital gains and dividends are taxed, and this is only a brief summary. For more detailed information, contact your tax advisor.

However, keep in mind that although taxes certainly affect investment returns, the effects of taxes should be only one of many factors you consider when making investment decisions.

Talk to a Wells Fargo Professional

We welcome the opportunity to work with you to help you achieve your financial goals. Let us know if there are any topics or services of interest to you.