Summary

For over 100 years, with one brief exception (1987-1990), the U.S. has taxed long-term capital gain at a lower rate than ordinary income. Previous administrations have proposed raising capital gains tax rates and taxing unrealized gains.

RER encourages Congress to continue to support investment and job creation with a meaningful capital gains incentive.

Key Takeaways

- The reduced capital gains rate partially offsets the higher risk that comes with illiquid, capital-intensive real estate projects, as well as the economic effects of inflation. The current structure decreases the cost of capital, drives long-term investment, encourages productive entrepreneurial activity, draws investment from around the world, and increases U.S. workforce productivity and competitiveness.
- Unlike other tax policies, such as immediate expensing, the capital gains preference only rewards smart, productive investments that generate profits.
- High taxes on capital income make it harder to attract the investment needed to rebuild our urban centers. Opportunity Zone capital gains incentives facilitated $75 billion in new investment in low-income communities in the first two years after enactment.
- Current law on capital gains encourages taxpayers to put capital to work on projects that won't pay off for many years. By taxing business assets and investments annually, a tax on unrealized gains would remove one of the major incentives for patient, productive capital investment.
- Risk capital differs from wage compensation. The entrepreneur who forgoes a traditional job in favor of starting a business forfeits many protections and benefits offered to employees, such as a pre-negotiated salary.
- A proposed tax on unrealized gains is quite possibly unconstitutional. Supreme Court jurisprudence has applied a realization requirement to determine whether gains or profits constitute income taxable under the 16th Amendment.
- In addition, taxing unrealized gains would trigger wasteful disputes and litigation, detracting from productive economic activity. Annual valuation requirements will require costly appraisals. Valuation disagreements will be a constant source of audits and administrative appeals.