

SPECIAL REPORT

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50 Years of the Federal Capital Gains Tax Burden

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During each of the 50 tax years from 1942 through 1992, almost every income group has borne some share of the federal capital gains tax burden. *Figure 1* reveals that, on an average annual basis, taxpayers making under \$100,000 annually (in constant 1992 dollars) have paid almost one-third of all capital gains taxes. The remaining two-thirds of the capital gains tax burden has been split almost equally between the \$100,000-to-\$500,000 and the over-\$500,000 income groups.

Figure 2 depicts the tax base for the capital gains tax burden in *Figure 1* — that is, each income group's share of the 50-year cumulative

dollar amount of capital gains subject to the federal income tax. It shows that taxpayers with under \$100,000 in annual income have reported more than one-third of the taxable capital gains over the 1942-to-1992 time period. The remaining share is, again, split almost equally between the \$100,000-to-\$500,000 and the over-\$500,000 income groups.

To some degree, the distribution of taxable gains reported in *Figure 2*, and, therefore, the tax burden reported in *Figure 1*, are biased toward the upper-income groups. This bias results from the use of current-year

Figure 1
Income Groups' Shares of Total Capital Gains Taxes
1942-1992

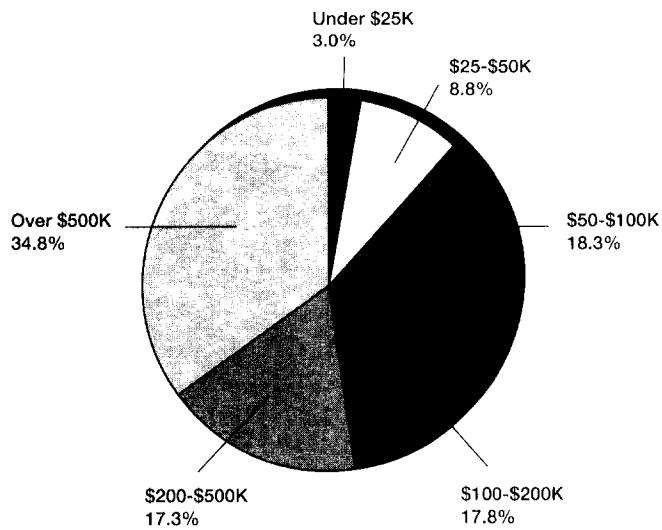


Figure 2
Income Groups' Shares of Total Taxable Capital Gains
1942-1992

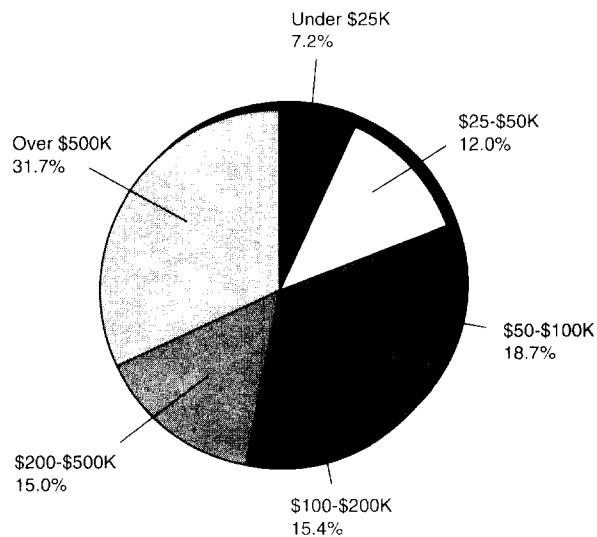


Table 1
Distribution of Total Estimated Capital Gains Taxes Paid (Constant 1992 Dollars)

Taxable Returns AGI Class (\$000s)	1940s	1950s	1960s	1970s	1980s	1990s
Under \$25	9.78%	5.59%	3.27%	2.88%	1.98%	2.18%
\$25-50	12.26	9.98	7.58	9.94	8.32	8.06
\$50-100	15.35	16.33	15.06	22.85	18.60	16.13
\$100-200	14.26	23.69	20.01	18.33	16.01	15.72
\$200-500	18.33	14.91	16.80	19.47	17.04	15.67
Over \$500	30.02	29.51	37.27	26.53	38.05	42.25
Subtotal	100	100	100	100	100	100
Nontaxable Returns	NA	NA	NA	NA	NA	NA
Share Total	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%
Dollar Total (Millions)	\$34,974.90	\$79,777.70	\$189,183.10	\$220,919.60	\$388,460.50	\$95,162.90

Table 2
Distribution of Capital Gains Included in Adjusted Gross Income (Constant 1992 Dollars)

Taxable Returns AGI Class (\$000s)	1940s	1950s	1960s	1970s	1980s	1990s
Under \$25	16.06%	10.04%	6.62%	7.39%	5.47%	4.78%
\$25-50	18.20	14.88	12.12	14.54	9.08	7.81
\$50-100	16.37	16.02	16.52	22.27	16.99	13.98
\$100-200	10.56	17.34	15.42	15.11	13.59	13.61
\$200-500	13.12	10.81	12.69	15.03	14.54	14.39
Over \$500	19.81	21.63	28.55	17.81	34.47	38.81
Subtotal	94.12	90.72	91.91	92.16	94.14	93.37
Nontaxable Returns	5.88	9.28	8.09	7.84	5.86	6.63
Share Total	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%
Dollar Total (Millions)	\$103,320.60	\$213,852.10	\$475,851.70	\$513,733.10	\$1,123,906.60	\$369,935.00

Table 3
Distribution of Returns Reporting Capital Gains in Adjusted Gross Income

Taxable Returns AGI Class (\$000s)	1940s	1950s	1960s	1970s	1980s	1990s
Under \$25	38.28%	26.91%	21.10%	16.91%	21.05%	21.37%
\$25-50	26.93	27.41	29.43	29.25	29.14	25.85
\$50-100	13.39	15.66	23.28	28.29	29.46	27.17
\$100-200	5.34	7.71	7.96	7.88	6.59	10.81
\$200-500	2.95	1.70	2.15	2.78	2.34	4.16
Over \$500	0.97	0.56	0.56	0.42	0.67	1.45
Subtotal	87.87	79.96	84.49	85.53	89.25	90.80
Nontaxable Returns	12.13	20.04	15.51	14.47	10.75	9.20
Share Total	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%
Numerical Total	11,150,750	26,915,563	56,580,848	60,639,209	83,593,231	24,035,549

Table 4
Average Annual Capital Gains Tax Burden per Filer with Gains (Constant 1992 Dollars)

Taxable Returns AGI Class (\$000s)	1940s	1950s	1960s	1970s	1980s	1990s
Under \$25	\$739	\$620	\$518	\$635	\$448	\$407
\$25-50	1,317	1,118	831	1,243	1,226	1,245
\$50-100	3,233	3,219	2,200	2,904	3,026	2,380
\$100-200	7,918	9,146	8,379	8,674	12,057	5,949
\$200-500	18,866	25,719	25,911	26,649	38,160	15,170
Over \$500	125,722	152,212	244,803	276,990	319,965	116,397
Subtotal	3,445	3,707	3,865	4,223	5,091	4,417
Nontaxable Returns	NA	NA	NA	NA	NA	NA
Total	\$3,445	\$3,707	\$3,865	\$4,223	\$5,091	\$4,417

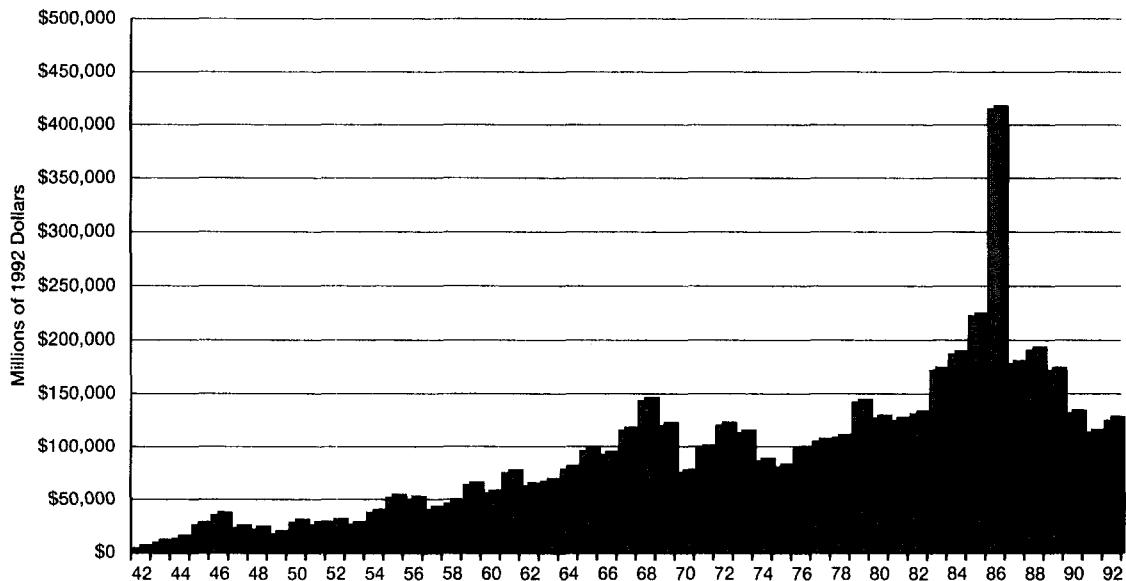
Table 5
Average Annual Capital Gains Included in Adjusted Gross Income per Filer with Gains (Constant 1992 Dollars)

Taxable Returns AGI Class (\$000s)	1940s	1950s	1960s	1970s	1980s	1990s
Under \$25	\$3,584	\$2,984	\$2,639	\$3,752	\$3,522	\$3,474
\$25-50	5,786	4,451	3,400	4,221	3,937	4,679
\$50-100	10,331	8,397	6,028	6,617	7,905	7,974
\$100-200	17,433	17,905	16,344	16,675	27,936	19,795
\$200-500	43,497	49,933	49,934	48,391	85,801	54,179
Over \$500	246,232	299,002	470,888	436,597	688,629	415,704
Subtotal	9,463	9,033	9,012	9,079	13,658	15,996
Nontaxable Returns	4,493	3,678	4,384	5,335	9,119	12,773
Total	\$9,129	\$7,945	\$8,410	\$8,472	\$13,445	\$15,391

Table 6
Average Annual Share of Returns Reporting Capital Gains in Adjusted Gross Income Relative to All Taxable Returns

Taxable Returns AGI Class (\$000s)	1940s	1950s	1960s	1970s	1980s	1990s
Under \$25	2.01%	2.64%	4.51%	4.20%	4.50%	4.18%
\$25-50	5.47	5.39	7.99	6.86	8.58	7.20
\$50-100	18.38	20.12	20.27	14.31	19.34	14.52
\$100-200	26.97	40.00	45.64	34.80	47.09	33.47
\$200-500	37.15	57.02	61.21	47.46	62.03	48.32
Over \$500	50.01	71.48	77.14	65.12	77.10	61.02
Subtotal	3.50	4.82	8.68	8.09	9.09	8.24
Nontaxable Returns	NA	NA	NA	NA	NA	NA
Total	3.50%	4.82%	8.68%	8.09%	9.09%	8.24%

Figure 3
Inflation-Adjusted Capital Gains Realizations, 1942-1992



Source: Tax Foundation.

statistics on the distribution of taxpayers by adjusted gross income. The realization of capital gains can propel a taxpayer to an abnormally high income level — and, possibly, an abnormally high tax bracket. (During various tax years between 1942 and 1987, the federal tax code categorized taxpayers into as many as 27 tax brackets.) The U.S. Treasury Department has established that when specific taxpayers' incomes are averaged over five-year periods, so as to mitigate the influence of a capital gain on taxpayers' income levels, the distribution of capital gains becomes more concentrated in the low-to-middle income groups.

Many inter-related factors influence when a taxpayer will choose to realize a capital gain. Thus, one-year snapshots of the tax burden can prove misleading. The 50-year time span analyzed here, on a decade-by-decade basis, endeavors to provide a more consistent picture of the taxpayers that pay capital gains taxes.

The capital gains tax burden reported here assumes that capital gains are each taxpayer's marginal source of income and are, therefore, subject to each taxpayer's marginal income tax rate (as opposed to some type of average tax rate measure). This assumption is justified because in most cases taxpayers subject themselves to capital gains taxation only if they choose to realize capital gains. Although

the capital gains tax burden was calculated each year using current-year income measures, each table and chart reflects the conversion of all income measures (including income groups) and tax-burden measures into constant 1992 dollars, using the consumer price index. (The only exception is *Table 8*.)

Capital Gains Realizations vs. Taxable Capital Gains

Figure 3 maps the inflation-adjusted trend in capital gains realizations between 1942 and 1992. The trend in both taxable capital gains and capital gains taxes paid closely mirrors the trend in total realizations. The current-year data on each of these series is reported in *Table 8*.

Before the Tax Reform Act of 1986 passed, the amount of long-term capital gains subject to federal income taxation differed from the amount of capital gains realized by taxpayers. From 1942 to 1977, taxpayers could exclude 50 percent of their net long-term capital gains from their adjusted gross income (see *Table 7*). Between 1978 and 1986 they could exclude 60 percent. Between 1942 and 1986, only the included portion was taxable. The 1986 Act eliminated the exclusion, which made realizations and taxable gains equal beginning in the 1987 tax year. However, short-term capital gains, historically defined as gains

Table 7
Tax Rules for Capital Gains

Years	Percent of Long-Term Capital Gains Excluded from Taxation	Definition of Long-Term Capital Gain: Assets Held in Excess of (Years):
1942-1976	50%	0.50
1977	50	0.75
1978-1983	60*	1.00
1984-1986	60	0.50
1987-current	0	NA

* The 60-percent exclusion became effective on October 31, 1978.

Note on Capital Gains Tax Rate: From 1942 to 1971, the statutory marginal tax rate on the taxable portion of long-term capital gains was the lesser of the taxpayer's marginal tax rate or 50 percent (excluding surtaxes). After 1971, the taxable portion of long-term gains were generally taxed at the taxpayer's marginal tax rate. Since 1987, the maximum tax rate on long-term capital gains has been 28 percent, except during the tax years 1988-1990, when some taxpayers were subject to a 33 percent tax rate. Short-term gains were always subjected to the taxpayer's marginal tax rate.

Source: Internal Revenue Code.

realized on capital assets held for one year or some fraction thereof (see *Table 7*), have always been fully included in taxable income.

Because the emphasis here is on the capital gains tax burden, only data on taxable capital gains are reported by income group. The overall distribution of realizations and the taxable portion of the realizations are similar, but not identical. For example, although similar to *Figure 2*, the distribution of capital gains realizations is more concentrated in the lower income groups. Beginning with the lowest income group in *Figure 2* (under \$25,000) and moving up the income scale, the distribution of total realizations is 7.6 percent, 12.5 percent, 19.5 percent, 15.5 percent, 14.9 percent, and 30 percent for the highest income group (over \$500,000).

Decade-by-Decade Trends in the Capital Gains Tax Burden

The most notable aspect of the data reported in *Table 1* is how stable the distribution of the capital gains tax burden has remained across all income groups over the decades. This stability is closely linked with the stability of the distribution of taxable gains reported in *Table 2*.

Notice, in general, that over time the distribution of both the tax burden and the gains have drifted upwards throughout the income groups. In large measure this upward drift is attributable to the rising real

income of the average taxpayer. From 1942 to 1992, in 1992 constant dollars, the average income per taxable income tax return almost doubled, rising from \$22,746 to \$40,182.

Despite the relative stability of the capital gains tax burden, some decades show a notable degree of variation. Because taxpayers subject themselves to the capital gains tax only by choosing to realize capital gains, three key reasons underlie the decade-by-decade variations in the capital gains tax burden: the overall economy's influence on capital asset values; the financial circumstances of individual taxpayers; and changes in the tax law.

The Number of Taxpayers that Report Capital Gains

Discerning which taxpayers report capital gains in a given time period provides insight into the fluctuations in the capital gains tax burden. *Tables 3* and *6* show the relative fluctuation in the number of taxpayers that reported taxable capital gains. *Table 3* shows the distribution of tax returns, by income group and tax status, that reported capital gains as part of their adjusted gross income. *Table 6* reports, by income group, the share of taxable returns that reported capital gains as part of their adjusted gross income relative to all taxable returns filed.

As the "Total" line in *Table 6* shows, an average of between 8 and 9 percent of all taxpayers have reported capital gains each year since 1960. The reason for the smaller percentage of taxpayers reporting capital gains before 1960 is not immediately apparent, except for the influence of World War II on the pattern of capital gains realizations in the 1940s. In the 1980s, the protracted economic expansion, in conjunction with the period of tax rate reductions, helps explain the above-average share of taxpayers that reported capital gains.

Despite the data in *Table 6*, which shows that a relatively low percentage of lower-income taxpayers reported capital gains, *Table 3* indicates that these low-income groups represented a relatively large share of the total number of taxpayers that reported gains. The group of taxpayers with under \$100,000 in annual income represent about 90 percent of all the taxable returns that reported gains in each decade, except for the three years which represent the 1990s. This percentage grows even larger when one considers that the vast majority, if not all, of the nontaxable returns belong to the under-\$100,000 income group.

Variation in the Distribution of Capital Gains Taxes Paid

As a result of the large share of low-to-middle income taxpayers that reported capital gains, small fluctuations in the realization patterns of these taxpayers had a substantial influence on the overall distribution of the tax burden reported in *Table 1*. Fluctuations in the realization patterns of the top income group, because of the large average taxable gains reported in *Table 4*, also had a perceptible influence in the overall distribution. The most noteworthy decades in this regard are the 1940s, 1970s, 1980s, and the 1990s.

Notice that in the 1940s, unlike other decades, the two lowest income groups bore about 22 percent of the capital gains tax burden, an atypically large share. The under-\$25,000 group had a particularly large surge in capital gains realizations from 1942 through 1946. This surge accounts for the high share of returns reporting gains shown in *Table 3* and the high share of taxable gains shown in *Table 2*.

World War II and its aftermath offer the most cogent explanation for taxpayer behavior with regard to capital gains realizations. Relative to all other reported decades, the percentage of taxpayers realizing capital gains in the 1940s was inordinately low, especially in the income range of \$100,000 or more, as an inspection of *Table 6* will show. Moreover, *Table 4* shows that the average annual capital gains tax burden for each of the income groups under \$100,000 was large relative to other decades. This situation resulted not from the tax law, but from the relatively large average level of taxable gains realized by these three groups, as revealed in *Table 5*. One explanation for this scenario is that many taxpayers were motivated to sell some of their capital assets in order to secure themselves financially as a result of the war. Such a motivation may not have impressed itself upon the top income groups, which will always have a greater amount of discretion about when to liquidate their capital assets.

Unlike the 1940s, the 1970s shift in the distribution of the capital gains tax burden toward the middle income groups listed in *Table 1* can be explained, in part, by a change in tax policy. With the exception of a war-time surtax imposed from 1968 through 1970, the Tax Reform Act of 1969 disrupted the stability of capital gains tax law that had existed since 1942.

The 1969 Act created an individual alternative minimum tax and a maximum tax. Moreover, the Revenue Act of 1971 (1972 tax year)

eliminated the long-time cap of 50 percent (excluding surtaxes) placed on the tax rate applicable to taxable long-term capital gains. As a consequence, it changed the maximum rate to 70 percent for all taxable long-term gains in excess of \$50,000.

In brief, the alternative minimum tax placed a levy on the excluded portion of long-term capital gains realizations. The maximum tax created a lower tax rate for "earned," as opposed to "unearned," income. Capital gains did not qualify for the lower ("maximum") rate. But more importantly, so-called tax preferences — of which the excluded portion of capital gains realizations was one — reduced the amount of earned income that could reap the advantages of the maximum tax. Thus, each dollar of long-term capital gains realized, because of the 50 percent exclusion, reduced the amount of earned income subject to the maximum tax by 50 cents, thereby increasing a taxpayer's effective marginal income tax rate.

The high-income taxpayers subject to all elements of the new tax laws experienced an increase in their effective marginal tax rate on capital gains by more than 40 percent in certain years from 1970 through 1978. For those subject to both the alternative minimum and maximum tax provisions, the effective top rate on taxable long-term gains reached 98.2 percent.

Unfortunately for the sake of analysis, this change in the top capital gains tax rate coincided with the onset of the 1973-1975 recession. Since real realizations for every income group declined over this period, it is unclear how much the change in tax law influenced the realizations of high-income taxpayers and, therefore, capital gains tax collections.

However, *Table 5* reveals that, relative to the 1960s, the average level of taxable gains dropped for the top two income groups, those affected by the change in tax law. Furthermore, from 1972 to 1975, real realizations declined an average of 33.5 percent for the groups unaffected by the tax rate increase, whereas real realizations declined an average of 51.5 percent for the affected top two income groups. In addition, the real realizations for the top two groups increased much less quickly than the middle-income groups during the post-1975 recovery period (prior to the Tax Reform Act of 1978). And, finally, unlike the other income groups, real realizations increased for the top two groups during the severe 1981-1982 recession, which overlapped with the 1981 tax rate reduction.

Unlike the top two income groups, each group in the \$25,000- to-\$200,000 income range showed a substantial acceleration in their real

Table 8

Capital Gains Realizations, Taxable Capital Gains, and Capital Gains Taxes Paid, 1942-1992
(\$Millions, except average tax burden)

Year	Capital Gains Realizations			Capital Gains Included in Adjusted Gross Income*			Estimated Total Capital Gains Taxes	Est. Avg. Tax Burden Per Filer with Gains
	Taxable Returns	Nontaxable Returns	Total	Taxable Returns	Nontaxable Returns	Total		
1942	\$442.9	\$28.2	\$471.0	\$303.7	\$19.6	\$323.3	\$120.9	\$259
1943	1,119.3	34.7	1,154.0	770.1	24.1	794.2	300.7	472
1944	1,608.3	47.6	1,655.9	1,109.3	32.7	1,142.0	417.2	424
1945	3,231.2	91.2	3,322.5	2,245.6	62.5	2,308.0	861.8	544
1946	4,622.5	232.4	4,854.8	3,157.8	160.8	3,318.6	1,093.1	553
1947	3,369.0	226.7	3,595.6	2,290.7	161.6	2,452.3	789.8	486
1948	3,350.0	345.9	3,695.9	2,262.9	236.8	2,499.7	842.4	617
1949	2,543.5	358.0	2,901.6	1,714.3	241.2	1,955.5	637.9	562
1950	4,453.0	425.8	4,878.8	3,000.4	258.1	3,258.6	1,215.6	781
1951	4,353.9	506.5	4,860.4	2,938.7	343.5	3,282.2	1,186.9	685
1952	4,946.1	539.7	5,485.9	2,558.9	277.0	2,835.9	1,043.9	633
1953	4,422.7	518.2	4,940.9	2,265.6	271.0	2,536.6	916.9	569
1954	6,435.7	718.5	7,154.2	3,359.5	370.8	3,730.3	1,383.7	712
1955	9,077.9	803.5	9,881.4	4,712.3	414.1	5,126.4	1,978.2	866
1956	8,853.1	830.4	9,683.5	4,556.0	435.1	4,991.1	1,891.2	767
1957	7,312.0	797.7	8,109.7	3,721.3	407.0	4,128.2	1,516.8	665
1958	8,520.8	918.5	9,439.3	4,406.0	473.2	4,879.1	1,794.0	643
1959	11,969.4	1,167.2	13,136.6	6,185.3	611.3	6,796.6	2,581.3	805
1960	10,486.8	1,259.8	11,746.7	5,362.0	641.8	6,003.9	2,213.8	723
1961	14,829.1	1,173.0	16,002.1	7,689.9	601.0	8,290.9	3,248.6	830
1962	12,060.4	1,390.9	13,451.4	6,114.7	706.7	6,821.4	2,544.0	728
1963	13,087.8	1,490.6	14,578.5	6,704.5	763.8	7,468.3	2,799.0	694
1964	15,860.9	1,568.2	17,429.2	9,751.4	804.6	10,556.0	4,185.4	963
1965	19,738.5	1,746.1	21,484.6	10,172.2	897.2	11,069.5	4,179.4	842
1966	19,264.0	2,083.8	21,347.8	9,893.8	1,066.5	10,960.3	4,037.8	794
1967	25,476.8	2,056.2	27,532.9	13,532.0	1,061.7	14,593.7	5,732.7	952
1968	33,303.6	2,301.5	35,605.0	17,659.4	1,187.4	18,846.9	8,209.9	1,226
1969	29,200.7	2,236.6	31,437.3	14,930.1	1,148.1	16,078.2	7,025.0	1,136
1970	19,252.5	1,593.8	20,846.3	9,839.5	816.1	10,655.6	4,545.9	961
1971	26,464.4	1,875.9	28,340.3	13,597.6	961.0	14,558.6	6,508.9	1,273
1972	33,676.8	2,193.2	35,869.9	17,258.1	1,138.6	18,396.7	7,840.1	1,332
1973	33,090.8	2,666.6	35,757.4	16,828.2	1,372.5	18,200.7	7,435.3	1,329
1974	27,155.8	3,061.0	30,216.8	13,803.4	1,574.5	15,377.9	6,008.5	1,334
1975	27,513.9	3,389.3	30,903.2	14,048.5	1,750.7	15,799.2	6,146.1	1,458
1976	35,945.9	3,546.0	39,491.9	18,385.2	1,821.9	20,207.1	8,189.7	1,602
1977	41,852.5	3,484.3	45,336.7	21,567.4	1,796.0	23,363.3	10,384.2	1,966
1978	47,058.3	3,467.7	50,526.0	24,389.6	1,842.8	26,232.4	11,310.9	1,988
1979	68,399.2	5,044.3	73,443.5	29,146.6	2,184.4	31,331.0	15,824.0	2,759
1980	69,521.1	5,061.4	74,582.5	30,455.0	2,268.3	32,723.3	16,773.4	2,742
1981	75,070.0	5,868.1	80,938.0	32,141.5	2,571.6	34,713.1	18,173.0	2,946
1982	83,601.0	6,552.6	90,153.6	35,700.5	2,813.9	38,514.4	16,459.2	2,647
1983	112,243.2	9,761.7	122,004.9	48,162.2	4,235.5	52,397.7	12,098.2	1,904
1984	129,444.8	9,212.9	138,657.7	54,203.9	3,994.2	58,198.0	23,925.2	3,434
1985	159,080.0	11,490.2	170,570.2	66,632.6	4,967.0	71,599.5	29,891.4	4,002
1986	310,410.0	14,038.1	324,448.1	129,110.1	5,933.2	135,043.2	59,141.0	6,169
1987	136,278.3	7,894.5	144,172.8	136,278.3	7,894.5	144,172.8	37,087.8	3,456
1988	153,658.2	7,289.6	160,947.8	153,658.2	7,289.6	160,947.8	43,917.6	6,113
1989	142,958.3	8,930.8	151,889.0	142,958.3	8,930.8	151,889.0	40,901.5	5,235
1990	115,374.9	7,336.1	122,711.0	115,374.9	7,336.1	122,711.0	32,980.6	5,097
1991	101,662.0	8,564.1	110,226.2	101,662.0	8,564.1	110,226.2	27,331.3	3,734
1992	117,007.1	7,834.3	124,841.4	117,007.1	7,834.3	124,841.4	31,651.0	3,939

* The concept of adjusted gross income began in the 1944 tax year. Before that, a "total" and "net" income concept was used.
Source: Tax Foundation.

realizations during the post-1975 recovery period, posting a cumulative increase of 68.3 percent prior to the Tax Reform Act of 1978. The under-\$25,000 group showed only a 9 percent increase in real realizations. Relative to the 1960s, the surge in low-to-middle income group realizations shows up in *Table 2* as a greater share of taxable gains; in *Table 5* as an increased average level of taxable gains; and, consequently, in *Table 1* as an increased share of the tax burden.

The stage was set for the 1980s boom in real realizations (illustrated in *Figure 3*) by the Tax Reform Act of 1978. This Act increased from 50 to 60 percent the amount of long-term capital gains that taxpayers could exclude from taxation. It also removed the influence on capital gains of the minimum and maximum tax. This change in the law had an immediate effect on the real realizations of those taxpayers with annual incomes over \$200,000.

However, it was not until 1983, following the 1981-1982 recession, that the across-the-board tax rate reduction of 1981 combined with the 60-percent exclusion to produce a boom in real realizations in every income group. This boom culminated in 1986 with a record level of realizations for all but the lowest income group. Furthermore, as *Table 5* shows, a record level of annual average taxable gains was realized by each of the groups with over \$100,000 in annual income. These record realizations resulted in a record level of annual average capital gains tax burdens.

The boom in capital gains realizations culminated in 1986 because the Tax Reform Act of 1986 eliminated the exclusion on long-term capital gains. That provision effectively increased the tax rate on long-term capital gains, despite the fact that the 1986 Act legislated a phased-in decrease in marginal income tax rates.

Notice on *Table 8*, however, that in terms of both nominal and real taxable gains, the 1980s boom peaked in 1988. After 1988, as *Figure 3* shows, realizations/taxable gains declined continuously (for each income group) until the end of the 1990-1991 recession.

Because two of the three years that define the "decade" of the 1990s were marked by a recession, the 1990's distribution of the capital gains tax burden shown in *Table 1* may not be representative. The top income group bore an atypically large share of the tax burden. This large share resulted from the relatively small percentage of high-income taxpayers that represented an unusually large share of the total returns that reported capital gains. Over the remainder of the decade, if past trends hold,

the distribution of the capital gains tax burden will shift downward to taxpayers in the low-to-middle income groups.

Conclusion

Over the 50 tax years from 1942 to 1992, the capital gains tax burden has been split almost equally between three income groups — those with annual incomes (in constant 1992 dollars) of under \$100,000, \$100,000 to \$500,000, and over \$500,000. This distribution, along with a similar distribution of capital gains realizations, has remained remarkably stable over time. Although a greater percentage of taxpayers in the upper-income groups realize capital gains on an annual basis, taxpayers in every income group realize capital gains. Taxpayers in virtually every income group, therefore, bear the burden of the capital gains tax.

In most cases, taxpayers subject themselves to capital gains taxation only if they choose to realize capital gains. Therefore, the distribution of capital gains realizations and the resulting tax burden are dictated by three key factors: (1) The overall economy's influence on capital asset values; (2) the financial circumstances of individual taxpayers; and (3) changes in the tax law.

Explaining the decade-to-decade variation in the distribution of capital gains and the capital gains tax burden requires evaluating the interaction of the above three factors on taxpayer realization patterns. Because the vast majority of all taxpayers that report capital gains reside in the low-to-middle income groups, small fluctuations in their realization behavior can have a perceptible influence on the distribution of the tax burden. However, fluctuations in the realization patterns of high-income taxpayers, because of the relatively large dollar value of their capital gains, also influence the distribution of the tax burden.

Of the three factors, one can generally discern only the distributional influence of fluctuations in capital asset values and tax changes. The decades of the 1970s and 1980s stand out in this regard. The early 1970s capital gains tax rate increase worked to depress the realizations of the top two income groups following the 1973-1975 recession, thereby shifting the distribution of the capital gains tax burden toward the low-to-middle income groups. In contrast, the interaction of the capital gains tax reductions of 1978 and 1981, combined with the general increase of capital asset values during the mid-1980s, worked to accelerate the realizations of the upper-income groups, thereby shifting the capital gains tax burden onto these groups.

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