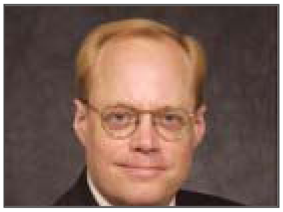
Forbes



Robert W. Wood

THE TAX LAWYER

TAXES | 3/02/2013

Killing Golden Goose, California Taxes Capital Gains As Ordinary Income

(Image credit: AFP/Getty Images via @daylife)

Living in California has many perks, but tax rates are not among them. As the Phil Mickelson brouhaha underscored, poor economics and rising tax rates can cause a perfect storm. See Moving To Beat High State Taxes? Watch Out. Everyone gets upset, regardless of income levels. And while views differ, complaining about taxes may be part of the human condition.

In November 2012, California ramped up its already high state tax rates retroactively to January 1, 2012. That meant a whopping rate increase of 30% for some high income taxpayers. Those earning $250,000 to $300,000 a year now pay 10.3%, up from 9.3%. For $1 million-plus-earners, California's rate is 13.3%, up from 10.3%.

In some cases, California taxes are causing migrations out of state. See FTB Publication 1031. But as the federal tax debate reveals, it isn't only top

ordinary rates that are debated, but capital gain rates as well. At the federal level, the capital gain rate remains 15% for some, but rose to 20% for higher income taxpayers. Add the 3.8% investment tax that results from the new healthcare law known as Obamacare, and you have 23.8% for many. That's a far cry from the 15% applicable in 2012.

What about Californians? Although we may understandably focus primarily on federal taxes, most states have an income tax too. But exactly how they tax capital gain is another matter and can be surprising. Some states–and California is one of them–tax capital gains as high as 13.3%. It's one thing to compare states, but the comparisons can be even more depressing when one looks around the world.

In fact, if you are paying up to a 33% combined federal and state tax on capital gains as you may be in California, you are paying more than virtually anyone else in the ***world***. That will hit you in your pocketbook. Plus, experts say the impact is bigger than that. Such a high tax rate has long-term negative implications for the economy, for people save and invest less.

Meanwhile, they say, capital seeks higher returns in other countries. See The High Burden of State and Federal Capital Gains Taxes. Take a look at how we stack up:

Long-term Capital Gains Rate		
Rank	Country/State	Capital Gains Rate
1	Denmark	42.0%
2	California	33.0%
3	France	32.5%
4	Finland	32.0%
5	New York	31.4%
6	Oregon	31.0%
7	Delaware	30.4%
8	New Jersey	30.4%
9	Vermont	30.4%
10	Maryland	30.3%

11	Maine	30.1%
12	Ireland	30.0%
13	Sweden	30.0%
14	Idaho	29.7%
15	Minnesota	29.7%
16	North Carolina	29.7%
17	Iowa	29.6%
18	Hawaii	29.4%
19	District of Columbia	29.1%
20	Nebraska	29.1%
21	Connecticut	29.0%
22	West Virginia	28.9%
23	Ohio	28.7%
24	Georgia	28.6%
25	Kentucky	28.6%

Robert W. Wood practices law with Wood LLP, in San Francisco. The author of more than 30 books, including Taxation of Damage Awards & Settlement Payments (4th Ed. 2009 with 2012 Supplement, Tax Institute), he can be reached at Wood@WoodLLP.com. This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.