If you're planning to sell capital assets at a loss to offset gains you realized during the year, beware of the "wash sale" rule. Under this tax rule, selling stock or securities for a loss and buying back substantially identical stock shares or securities **within 30 days** before or after the sale date means the loss can't be claimed for tax purposes.

The Rule

The wash sale rule is designed to prevent taxpayers from benefiting from a loss without actually parting with ownership. Note that the rule applies to a 30-day period before or after the sale date to prevent "buying the stock back" before it's even sold. (If you participate in dividend reinvestment plans, the wash sale rule may be inadvertently triggered when dividends are reinvested under the plan if you've separately sold some of the same stock at a loss within the 30-day period.)

Although the loss can't be claimed on a wash sale, the disallowed amount is added to the cost of the new stock to increase its tax basis for future disposition. So, the disallowed amount can be claimed when the new stock is finally disposed of (other than in a wash sale).

An Example

Assume you buy 500 shares of XYZ Inc. for $10,000 and sell them on November 5 for $3,000. On November 29, you buy 500 shares of XYZ again for $3,200. Since the shares were "bought back" within 30 days of the sale, the wash sale rule applies. Therefore, you can't claim a $7,000 loss. Your basis in the new 500 shares is $10,200: the actual cost plus the $7,000 disallowed loss.

If only a portion of the stock sold is repurchased, only that portion of the loss is disallowed. In the example above, if 60% of the shares sold were bought back, you'd be able to claim 40% of the loss on the sale. The remaining loss would be disallowed and added to your cost of the repurchased shares.

No Surprises

The wash sale rule can deliver a nasty surprise at tax time. Contact us with questions.