Year-end strategies for Investors.

The volatile securities markets make year-end planning for investors especially challenging this year. As year-end approaches, you should consider the following moves to make the best tax use of paper losses and actual losses from your stock market investments.

Sell at a loss to offset earlier gains. If you have realized gains earlier in the year from sales of stock held for held for more than one year (long-term capital gains) or from sales of stock held for one year or less (short-term capital gains), take a close look at your portfolio with a view to selling some of the losers -- those shares that now show a paper loss. The best tax strategy is to sell enough of the losers to shelter your earlier gains and generate a $3,000 loss. Selling to yield this amount of loss is a good idea from the tax viewpoint because a $3,000 capital loss (but no more) can offset a like amount of ordinary income each year.

For example, let's suppose you have $10,000 of capital gain from the sale of stocks earlier this year. You also have several losing positions, including shares in ABC Corp., in which you are showing a $15,000 loss. Strictly from the tax viewpoint, you should consider selling enough of your ABC shares to recognize a $13,000 loss. Your capital gains will be offset entirely, and you will have a $3,000 loss to offset against a like amount of ordinary income.

Suppose that you believe that the shares showing a paper loss (in our example, the ABC shares) still have the potential to turn around and eventually generate a profit. You can sell and then repurchase the shares without forfeiting the loss deduction only if you avoid the wash-sale rules. This means that you must buy the new shares outside of the period that begins 30 days before and ends 30 days after the sale of the loss stock. However, note that if you expect the price of the shares showing a paper loss to rise quickly, your tax savings from taking the loss may not be worth the potential investment gain you may lose by waiting more than 30 days to repurchase the shares.

Use earlier year losses to offset gains you would benefit from taking. If you have capital losses on sales earlier in the year, consider whether you should take capital gains on some stocks that you still hold. For example, if you have appreciated stocks that you would like to sell, but don't want to sell if it will cause you to have taxable gain this year, consider selling just enough shares to offset your earlier-in-the-year capital losses (except for $3,000 of those which can be used to offset ordinary income). You should consider selling appreciated stocks now if you believe those stocks have reached (or are close to) the peak price and you also believe that you can invest the proceeds from the sale in other property that will give you a better rate of return in the future.

For example, suppose you have $20,000 of long-term capital losses from 2005 stock transactions, and $4,000 of short-term capital gains. If you don't have other transactions involving securities or other capital assets for 2005, you'll wind up the year with a $16,000 long-term capital loss, of which only $3,000 can be used to shelter ordinary income. The $13,000 balance of the loss could be used to offset gain on appreciated stock that you wish to sell but which you would not sell now if you had to pay tax on the gain recognized on the sale.

If this strategy applies to you, and your holdings showing a paper gain consist of stocks you haven't held for more than one year, as well as stocks you have held for more than one year, you should consider selling those stocks on which you will have short-term gain first, and then stocks that would yield long-term gain. This way, you'll be in a better position to wind up with gain taxed at favorable rates when you sell other stocks with paper gains. To the extent possible, you should also try to use long-term capital losses to offset short-term capital gains. This can be done, however, only if the total of your long-term capital losses is more than your long-term capital gains. Deferring long-term capital gains until next year is one way of achieving this goal.

Since individual taxpayers may carry over capital losses indefinitely, there is no reason to sell appreciated stocks just to have offsetting gains. If you don't have a better investment for the proceeds of a sale of these stocks, don't sell them. You can carry over your capital losses to next year when you may have a better opportunity to make use of those losses. You can even offset another $3,000 of the carried over losses against ordinary income next year (and in succeeding years if the full amount of the capital loss carryover is not used next year).

When gain on sale of stock this year should be taken this year even if you don't have offsetting losses. A 2005 sale of paper-gain stocks you have held for more than one year may make sense (even if you haven't recognized losses) if you will be in the 10% or 15% bracket in 2005, for example, due to large business net operating losses that will offset most of your ordinary income, but expect to be in a 25% or higher bracket in 2006. By selling in 2005 rather than 2006, part or all of the gain will be taxed at a maximum rate of only 5% (instead of 15%).

These are just a few of the year-end strategies that can make a big dollar difference to you and your family.