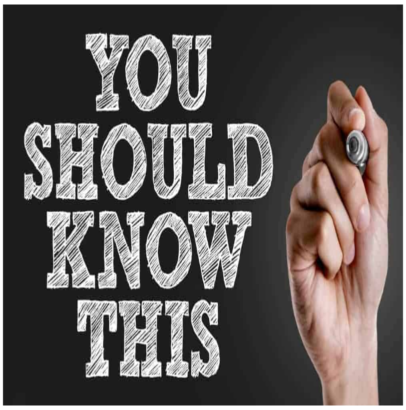

CRA: Avoid These 3 Big Mistakes in Tax-Loss Selling

Description

Believe it or not, but the Canada Revenue Agency (CRA) provides a legal way for investors to save taxes — through tax-loss selling, which often occurs at year end (i.e., this month), when stock investors rebalance their portfolios and sell losers.

Tax-loss selling is a tax strategy that uses your capital losses to help you reduce taxes of capital gains. This tax-saving strategy applies to more than just stocks.

You can use it for ETFs and mutual funds, too. But all these investments must reside in your non-registered accounts. To rephrase it, tax-loss selling does not apply in tax-advantaged accounts like TFSAs, RRSPs, RESPs, and RDSPs.

Capital losses can be used to offset capital gains from up to three years ago or carried forward indefinitely. You can also offset capital gains from investment properties like rental properties or family cottages.

For example, if you made tonnes of money from selling a family cottage last year, and you have some losers in your stock portfolio that you want to sell, you can offset the capital gains of your family cottage sale by selling the losing stocks.

Of course, you might be sitting on super-large gains on stocks bought during the March market crash this year. You can also sell any losers you may have to offset the capital gains for this year.

The idea of saving taxes from tax-loss selling is enticing — just avoid these three big mistakes.

Don’t book losses in registered accounts

We already discussed this point earlier. Don’t accidentally book losses in registered accounts such as TFSAs, RRSPs, RESPs, or RDSPs. The tax-loss selling strategy doesn’t apply there. It only applies to non-registered accounts.

Don’t sell for the sake of saving taxes

Don’t go selling all your stocks that are in the red after you read this article just because it’s tax-loss selling season. Not all temporary losers are permanent losers. (In fact, some turn out to be big winners if you give them more time.)

In other words, don’t sell for the sake of saving taxes.

Only sell a loser if you think the fundamentals of its underlying business are broken and you don’t think the business is going to recover.

Avoid superficial losses

Essentially, when you sell a stock at a loss, you cannot buy the stock 30 calendar days before or after the stock. Otherwise, the tax-loss selling is nullified.

As TaxTips.ca describes, a company controlled by you, your spouse/common-law partner, or a trust for which you or someone affiliated with you is a beneficiary also can’t buy it back in that duration.

This also means you cannot transfer in kind a stock that’s underwater into a registered account.

You can however sell a stock at a loss and buy another stock in the same industry. For example, if you sell **BCE** stock at a loss now, you can buy **TELUS** immediately.

The Foolish takeaway

Tax-loss selling is a neat strategy to help you save taxes in capital gains by offsetting them with capital losses. The key point is to never book losses for the sake of saving taxes. Before that, the sale should make sense for your broader investment portfolio strategy.

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