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After-Tax Advisor

Harvest Tax Losses Midyear to Help Grow Returns

By: Eaton Vance | June 3, 2024

Your clients likely think of year-end when they hear the term tax-loss harvesting, the practice of strategically selling assets that have experienced a decline in value to offset capital gains or taxable income. As an After-Tax Advisor, you know the importance of a year-round tax-loss harvesting strategy. Midyear is a great time to check in and remind clients of the ways they can minimize their tax liabilities and help maximize returns with tax-loss harvesting.

Start the conversation by asking clients if they are open to discussing how different types of investment vehicles are treated for tax purposes and which are best suited for tax-loss harvesting. Let's review a few of them:

Mutual Funds

Mutual fund portfolio managers make investment decisions on behalf of all the shareholders. Individual investors have no control over the timing and magnitude of capital gains within the fund. Mutual funds are required by law to distribute capital gains to their shareholders. If the manager sells securities at a profit, shareholders may be subject to capital gains taxes even if they didn't personally benefit from the gains. These capital gains distributions are taxable to the shareholders even if they reinvest the distributions back into the fund. This can result in an unexpected tax liability for investors, thereby reducing their after-tax returns.

Exchange Traded Funds (ETFs)

ETFs can be more tax efficient than mutual funds because they are expected to have fewer taxable events. ETFs tend to have lower portfolio turnover than actively managed mutual funds, which helps to reduce capital gain recognition. ETFs also offer in-kind creation and redemption, meaning that when an ETF needs to meet redemptions or create new shares, it can do so by exchanging a basket of underlying securities instead of selling those securities and potentially triggering a gain recognition event.

Separately Managed Accounts (SMAs)

Unlike mutual funds and ETFs, investors hold individual stocks in a SMA. This gives them the flexibility to time the recognition of gains and to selectively sell underperforming stocks to realize losses. This approach allows for precise control over the timing and magnitude of tax events.

Bottom Line: Remind clients that tax-loss harvesting is a year-round strategy for those investors looking to reduce tax liabilities and enhance after-tax returns. Start the conversation by discussing the common types of investment vehicles, their tax implications, and whether they can actively harvest losses at midyear.

The Firm does not provide tax advice. The tax information contained herein is general and is not exhaustive by nature. Tax laws are complex and subject to change. Investors should always consult their own legal or tax professional for information concerning their individual situation.

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