==

Should you change your tax strategy this year-end?

==

As year-end approaches, investors typically consider a tax strategy called "harvesting" capital losses. There's an added wrinkle to this tax move this year. Due to pending tax law changes, you might try instead to reap more capital gains than losses in 2012. Thus, the usual strategy of harvesting losses could be turned upside down.

Here's a recap of the basic rules. The capital gains and capital losses you realize during the year are "netted" under complex rules when you file your tax return. A gain or loss is treated as being long-term if you've held the securities for more than one year. For 2012, net long-term capital gain is taxed at a maximum tax rate of 15% (0% for investors in the regular 10% and 15% tax brackets).

If you're showing a net capital gain on paper as year-end approaches, any capital losses you realize will reduce the amount of the taxable gain or offset it completely. An excess loss can then offset up to $3,000 of highly taxed ordinary income before any remainder is carried over to next year. However, the usual strategy of harvesting losses is complicated this year by three key tax law changes scheduled for 2013.

* The maximum tax rate for net long-term capital gain will increase to 20% (10% for investors in the lower tax brackets).

* Ordinary tax rates are going up. For example, the top rates of 33% and 35% will increase to 36% and 39.6%, respectively.

* A special 3.8% Medicare surtax will apply to the lesser of net investment income for the year or the amount by which modified adjusted gross income (MAGI) exceeds $250,000 ($200,000 for single filers).

Barring any late legislation by Congress, investors may be inclined to harvest capital gains instead of losses at year-end. As a result, you can benefit from the favorable tax rates in effect for 2012. If you've already realized short-term gains in 2012, you might want to realize short-term losses to offset those gains. But don't use short-term losses to offset long-term gains, if you can help it, because long-term gains are taxed at a maximum rate of only 15% in 2012.

Other considerations may come into play. The best approach is to do what's best for your situation. See us for a review of your year-end investment tax strategy.