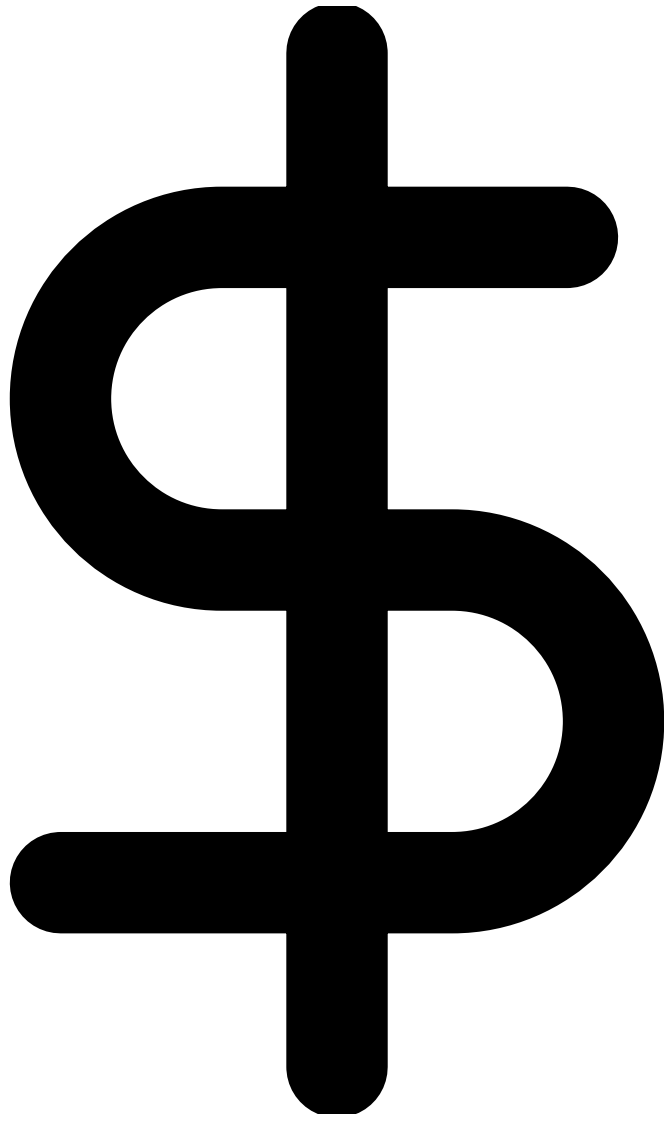
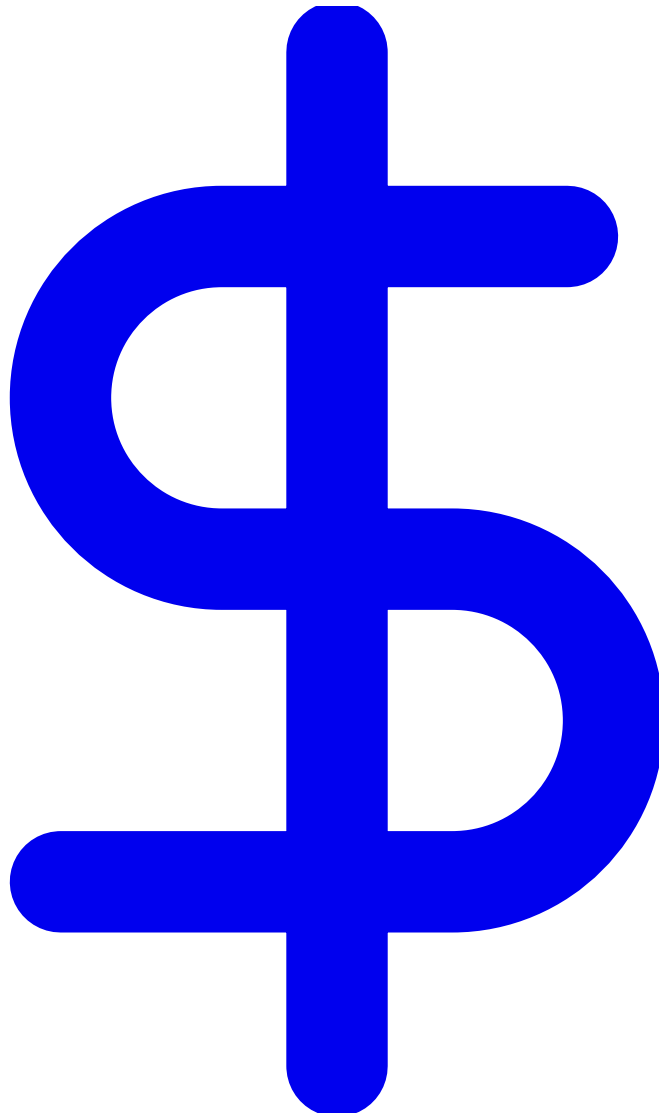






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Tax-Loss Harvesting Explained: How Offsetting Losses Can Lower Your Tax Bill

By the [IncomeTaxCentre Editorial Team](#) · Reviewed against our [editorial standards](#) · 8 min read · Last reviewed 2026

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Tax-Loss Harvesting Explained: How Offsetting Losses Can Lower Your Tax Bill

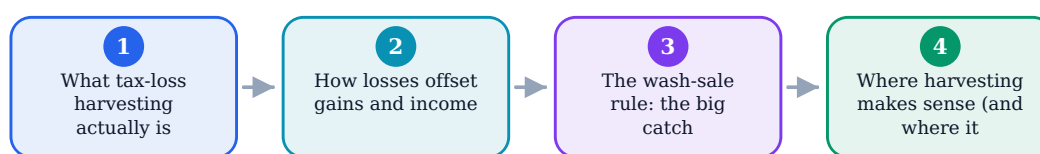


Figure: Tax-Loss Harvesting Explained: How Offsetting Losses Can Lower Your Tax Bill

When an investment falls below what you paid for it, that paper loss can feel like nothing but bad news. Tax-loss harvesting is a strategy that tries to make something useful out of it: by selling the losing investment, you realise a capital loss that can offset capital gains elsewhere and, in many systems, a limited amount of ordinary income.

This guide explains how tax-loss harvesting works in plain terms, the important rules that stop it from being abused, who tends to benefit, and the practical mistakes to avoid. It is general education rather than personalised advice.

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What tax-loss harvesting actually is

Tax-loss harvesting is the practice of selling an investment that has dropped in value so that the loss becomes **realised** rather than just a number on a screen. A realised loss is one the tax system recognises, and it can be used to reduce the tax you owe on realised gains from other investments.

The core idea is simple. If you sold one investment for a \$5,000 gain and another for a \$5,000 loss in the same year, the two can cancel out, leaving no net gain to be taxed. Without the loss, you might have owed tax on the full \$5,000 gain.

How losses offset gains and income

In most systems, losses first offset gains of the same type (for example, long-term losses against long-term gains), then across types, and finally a capped amount against

ordinary income. Any losses left over after that are usually **carried forward** to future tax years indefinitely.

The exact limits, categories and carry-forward rules vary by country, so treat the numbers here as illustrative. What is broadly consistent is the order: gains first, then a limited slice of income, then carry the rest forward.

The wash-sale rule: the big catch

The rule most likely to trip you up is the **wash-sale rule**. It disallows the tax loss if you buy the same, or a 'substantially identical', investment within a defined window around the sale (commonly a period before and after). The goal is to stop people from selling purely for the tax break and immediately rebuying to keep the same position.

To stay compliant, investors often wait out the window before repurchasing, or buy a similar-but-not-identical investment that keeps their overall exposure roughly the same. Definitions of 'substantially identical' can be nuanced, which is one reason professional guidance helps here.

Where harvesting makes sense (and where it doesn't)

Harvesting only matters in **taxable accounts**. Inside tax-sheltered retirement accounts, gains and losses are not taxed year to year, so there is nothing to harvest. It tends to add the most value when you have significant realised gains to offset and when your losses are meaningful rather than trivial.

It adds little value if you have no gains to offset and only the small income offset applies, or if trading costs and complexity outweigh the saving.

Common mistakes to avoid

The biggest mistake is letting the tax tail wag the investment dog — selling a good long-term holding just to bank a loss. Another is accidentally triggering the wash-sale rule by rebuying too soon, including through automatic dividend reinvestment or a similar fund in another account. A third is ignoring transaction costs that erode the benefit.

Keeping clear records of purchase prices, sale dates and the reason for each trade makes the whole process far less error-prone.

Is it worth it for you?

For investors with taxable accounts and real gains to offset, disciplined harvesting can be a genuine, legitimate way to reduce tax and keep more capital invested. For someone with a simple portfolio, few gains, and little turnover, the effort may not be worthwhile.

Because rules on wash sales, carry-forwards and income offsets differ by jurisdiction and change over time, it is wise to confirm the current specifics for your situation with a qualified tax professional before acting.

A simple illustration

A basic example makes the idea concrete. The figures below are illustrative only and not tax advice:

Situation	Illustrative effect
Realised a gain on one investment	That gain may be taxable
Sold another at a loss	The loss may offset the gain
Net position	Only the net gain, if any, may be taxed
Losses exceed gains	Rules may allow limited use against other income

Exactly how this works depends on your jurisdiction and personal circumstances, so treat this only as a general illustration and consult a qualified tax professional.

Pitfalls to be aware of

Tax-loss harvesting has rules and traps that make professional guidance valuable:

- Rules often prevent claiming a loss if you quickly rebuy the same or a very similar asset.
- Chasing a tax benefit can distort otherwise sound investment decisions.
- Transaction costs can erode the benefit of selling.
- The rules vary by country and change over time.
- What helps one person's tax situation may not help another's.

These are general cautions, not advice; a professional can tell you what applies to you.

Why the strategy must fit the bigger picture

Tax-loss harvesting is often presented as a clever trick for reducing a tax bill, and while the underlying idea — using investment losses to offset gains — is legitimate and can be useful, it is important to understand that it should never be pursued in isolation from your overall financial and investment picture, which is exactly why generic explanations, including this one, cannot tell you whether it makes sense for you. The core appeal is straightforward: if you have realised taxable gains, deliberately realising losses elsewhere may reduce the net amount subject to tax, and in some jurisdictions losses beyond your gains can be used in limited ways against other income or carried forward. However, the strategy carries real complications. Rules frequently restrict claiming a loss if you repurchase the same or a substantially identical investment within a certain window, so a poorly timed rebuy can disqualify the very benefit you sought. More subtly, letting tax considerations drive investment decisions can lead you to sell holdings you should have kept, or to distort a sound long-term plan for a short-term tax saving that may be smaller than it appears once transaction costs are considered. The rules also differ significantly between countries and can change, meaning that guidance that fits one person may be wrong for another. All of this points to the same conclusion: tax-loss harvesting can be a sensible tool when it fits within a well-considered investment and tax strategy, but deciding whether and how to use it requires understanding your specific situation, goals and local rules. Because this is a matter with real financial and tax consequences, nothing here is financial or tax advice, and

the appropriate step before acting is to consult a qualified professional who can evaluate your circumstances and tell you what is suitable for you.

Printable checklist

Print this page or save the PDF to keep these steps handy.

- ☐ What tax-loss harvesting actually is
- ☐ How losses offset gains and income
- ☐ The wash-sale rule: the big catch
- ☐ Where harvesting makes sense (and where it doesn't)
- ☐ Common mistakes to avoid
- ☐ Is it worth it for you?
- ☐ A simple illustration
- ☐ Pitfalls to be aware of

Summary

Tax-loss harvesting means deliberately selling investments at a loss to offset taxable gains and, in some cases, a limited amount of income. Done carefully it can reduce your tax bill and let you reinvest, but the wash-sale rule prevents you from immediately rebuying the same asset. It suits taxable accounts, adds most value at higher gains, and should never drive you into a poor investment decision just to save tax.

Key Takeaways

- A realised capital loss can offset realised capital gains, reducing the tax owed on those gains.
- Many tax systems let you offset a limited amount of ordinary income with net losses, and carry the rest forward.
- The wash-sale rule disallows the loss if you rebuy the same or a substantially identical asset within a set window.
- Harvesting only matters in taxable accounts, not tax-sheltered retirement accounts.
- Never let a tax saving push you into a bad investment decision — the investment case comes first.

Frequently Asked Questions

Does tax-loss harvesting eliminate tax or just delay it?

Often it delays rather than eliminates tax, because selling at a loss and rebuying lowers your cost basis, which can mean a larger gain later. The benefit comes from deferring tax and offsetting gains now, which has real value even when it is partly a timing effect.

Can I harvest losses in my retirement account?

No. Gains and losses inside tax-sheltered retirement accounts are not taxed each year, so there is nothing to harvest. The strategy only applies to taxable investment accounts.

What counts as a 'substantially identical' investment?

It generally means an asset so similar that repurchasing it recreates essentially the same position. The precise definition can be nuanced and varies by jurisdiction, so professional guidance is valuable when you are unsure.

Related Guides

- [Capital Gains Tax Guide](#)
- [Capital Gains vs Ordinary Income](#)
- [Tax Deductions vs Credits](#)
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