Tax-Loss Harvesting FAQs

Frequently asked questions about tax-loss harvesting through Vanguard Personal Advisor Services®

Tax-loss harvesting goes to work to bring you more value at a time you least expect—when markets are volatile. It's part of Vanguard Personal Advisor's suite of tax strategies that can help you optimize your overall financial wellness.

Who could benefit

How do I know if tax-loss harvesting makes sense for me?

Your advisor can talk with you about how much tax-loss harvesting could benefit you. Generally, you'll see the most positive impact from tax-loss harvesting if you:

- Have a substantial portion of your money invested in taxable accounts.
- Are in a higher tax bracket than you'll likely be in the future.
- Have purchased your investments at a variety of prices over time and have capital gains to offset using losses harvested by the service.
- Have a substantial portion of your investments advised by Vanguard Personal Advisor Services.

Does tax-loss harvesting involve risk?

Yes. As with all aspects of investing, tax-loss harvesting comes with some risk.

- There's a risk you may not see any benefit (or you may experience a loss) if:
  - » The Vanguard surrogate funds bought with proceeds from tax-loss harvesting sales underperform the Vanguard funds sold.
  - » You're in a higher tax bracket in the future.
  - » You don't reinvest your tax savings, or the return on reinvestments is negative over the long term.
- There's also the risk that your tax-loss harvesting sales may violate the IRS wash-sale rule. If you buy the same or a "substantially identical" investment within 30 days before or after you sold at a loss, you won't be able to claim the loss. We'll attempt to use investments that won't be considered substantially identical by the IRS when we're tax-loss harvesting.* However, it's possible that transactions outside your advised accounts could cause wash sales.

When will you start tax-loss harvesting in my Vanguard Personal Advisor® portfolio?

Generally, you'll see the majority of tax-loss harvesting activity when there's a high level of market volatility. This could happen almost immediately, or not for months or years.

How much could it help me save?

You can offset all of your capital gains with losses during the same tax year, plus up to $3,000 of ordinary income. If there are remaining losses, you can carry forward those losses indefinitely to offset future gains. The bottom line is that you need to have realized capital gains to offset in order to truly benefit from tax-loss harvesting.

What happens if I don't sign up for tax-loss harvesting?

Your advisor will recommend tax-loss harvesting if they believe it'll likely result in better outcomes for you in the form of lower taxes. You can reinvest the money saved from lower taxes to grow your money faster. While we can't guarantee results, deciding not to sign up could mean you'll miss potential opportunities for additional growth.

How it works

What's tax-loss harvesting?

Tax-loss harvesting involves selling an investment that has experienced a loss and replacing that investment with a different holding designed to maintain your asset allocation. It can primarily add value in the form of reduced income taxes when realized ("harvested") losses are used to lower a tax bill by offsetting realized capital gains and up to $3,000 of ordinary income (based on current tax provisions). Additionally, tax-loss harvesting may increase after-tax returns if those tax savings are reinvested, assuming the additional investments experience compounded growth in the markets over time.

How do you decide what and when to sell?

We've done extensive research and analysis to determine an optimal methodology for tax-loss harvesting. We'll scan your portfolio every day the market is open to find opportunities for tax-loss harvesting in certain Vanguard funds, and we'll recommend selling investment lots of those funds that meet our research-based criteria. Details on which Vanguard funds can be harvested will be available in the Tax-Loss Harvesting Addendum to Your Service Agreement for Vanguard Personal Advisor Services that you'll discuss with your advisor.

How do you decide what to buy with proceeds from a harvesting transaction?

We'll first check if your portfolio needs rebalancing. For example, before we replace a stock fund investment with another stock fund, we'll make sure your overall portfolio isn't overweighted in stocks. If it is, we'll use the proceeds from the sale to buy more of the underweighted asset class. If there's no need to rebalance, we'll buy a surrogate Vanguard fund that's similar to the sold investment but not substantially identical. Details on which Vanguard funds can be used as surrogates will be available in the Tax-Loss Harvesting Addendum to Your Service Agreement for Vanguard Personal Advisor Services that you'll discuss with your advisor.

When it comes to wash sales, what does "substantially identical" mean? How will Vanguard Personal Advisor avoid wash sales?

The IRS hasn't defined "substantially identical," but an example could be replacing a fund that tracks the S&P 500 Index with another fund that also tracks that index.

The surrogate funds Vanguard Personal Advisor uses to replace any investments harvested for losses are intended to provide similar exposures—but not so similar that we think they'd cause a wash sale.

What are surrogate funds?

Surrogate funds are the ETFs (exchange-traded funds) Vanguard Personal Advisor uses to replace investments sold to harvest losses. They are Vanguard ETFs® with similar asset and sub-asset allocations to the funds we're replacing. Details on which Vanguard funds can be used as surrogates will be available in the Tax-Loss Harvesting Addendum to Your Service Agreement for Vanguard Personal Advisor Services that you'll discuss with your advisor.

Will my Vanguard Personal Advisor fee increase if I sign up for tax-loss harvesting?

No. Tax-loss harvesting is included in your Vanguard Personal Advisor fee.

How it fits with your strategy

Is this a new investment strategy? Will it change my current investments?

Tax-loss harvesting is a tax strategy—not an investment strategy. Your overall portfolio will still align with your goals, timeline, and risk tolerance. Tax-loss harvesting allows you the ability to reduce your taxes while still adhering to your investment strategy.

Your investments will fluctuate during periods of volatility as lots are sold and replaced with surrogate funds. As new money comes into your accounts (whether it's the result of new investments or sales of existing investments), we'll invest that money in your "core" Vanguard funds as long as it won't trigger a wash sale. That way, the majority of your money will return to your core funds over time.

How does tax-loss harvesting fit with Vanguard's core philosophy?

Vanguard's investment philosophy and the Vanguard Personal Advisor methodology have a clear focus on investing for the long term. It's very important to note that tax-loss harvesting trades aren't intended to change the allocation of a portfolio or make investment decisions based on what's performing best at a given moment. Instead, surrogate Vanguard funds are specifically chosen so that your portfolio's overall asset allocation and suballocation should remain close to your target, while still allowing you to get a potential tax benefit.

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*Note that when making other non-tax-loss-harvesting trades in your portfolio in order to align with our investment methodology, we may choose to cause a wash sale in certain circumstances.

We recommend that you carefully review the terms of the Tax Loss Harvesting Addendum to Your Service Agreement for Vanguard Personal Advisor Services and consult a tax advisor before enrolling in tax-loss harvesting in your advised accounts. We do not provide legal or tax advice, and none of the information provided on this webpage is intended as tax or legal advice. All investing is subject to risk, including the possible loss of the money you invest.

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