Approaching Zero Taxes

Investment Tax Tools to Maximize After-Tax Wealth
This position paper was written and edited as part of a collaborative effort between Savant Capital Management, Inc. of Rockford, Illinois and BHCO Capital Management, Inc. of Dallas, Texas. Savant and BHCO collectively manage nearly $700 million in client assets. Additionally, the two firms have provided fee-only financial planning advice on unmanaged assets well in excess of a billion dollars. Savant and BHCO are also founding members of Zero Alpha Group, LLC, a national organization of independent advisory firms that collectively manage nearly $3.0 billion in client assets and share a common investment and planning philosophy. Both Savant and BHCO were recently recognized among the top wealth managers in the United States by Bloomberg, one of the most respected firms in finance. Savant has further been recognized as one of the nation’s top 250 financial advisors by Worth magazine each year since 1997. We would like to extend a special thanks to our many team members for their significant contributions to this project. The resulting intellectual capital contained within is truly borne from the unique teamwork exhibited within and between our firms.
Approaching Zero Taxes

GOAL: COMPLETELY ELIMINATE TAX

Albert Einstein once noted, “The hardest thing in the world to understand is the income tax.” We concur.

Since Congress fatefuly ratified the sixteenth amendment in 1913 legalizing the income tax, entire industries and professions have been born to eliminate and defer tax. This is reasonable and fair. As Judge Learned Hand so eloquently put it, “Over and over again, courts have said there is nothing sinister in arranging one’s affairs to keep taxes as low as possible. Everyone does, rich or poor, and all do right, for nobody owes any public duty to pay more than the law demands.” While these words resound with common sense, the investment industry largely ignores the idea. Even worse, most conventional wisdom regarding tax-efficient investing is misdirected, antiquated, or simply wrong!

In their seminal paper on the impact of taxes on investing, Arnott and Jeffery said, “Taxes matter a lot.” They demonstrated that taxes are one of the single largest and most controllable costs of investing. While ignoring taxes was easy in the double-digit return era of the 1990s, reducing taxes in today’s lower return environment is more important than ever. A recent study1 confirmed this. Amazingly, over 30 years, the average mutual fund investor lost a whopping 58% of their cumulative return to taxes. While a $1 investment grew to $21.89 for a tax-free investor, the taxable investor with identical holdings accumulated only $9.87.

While the goal of completely eliminating taxes is worth striving for, its pursuit leads many astray. Driven by this goal, too many people make ill-conceived decisions that result in poor returns, or even worse, loss of principal. The more optimal goal is to maximize your after-tax rate of return. In other words, “Having the tax tail wag the dog is not a good thing, but neither is ignoring the tail.”

This paper explores a relatively new approach to investing known as “Tax-efficient investing.” In the past, the investment industry and academia have largely ignored tax implications and instead focused strictly on risk and return. Tax-efficient investing adds tax ramifications as the critical third leg to the investment management stool (risk/return/taxes). This is a complex concept. Tax-efficient investing deals with constantly changing tax laws, multiple types and rates of tax, the continual battle between tax strategists and fickle politicians, and the added complexity of state and local taxes. We suspect it is both this complexity and inherent conflicts of interest that have led the industry to largely ignore taxes. We will introduce a suite of investment tools that can be used to form a Tax-efficient investment approach, with the ultimate goal of increasing after-tax returns. We can’t overstate the importance of after-tax returns. As legendary investor Sir John Templeton said, “For all long-term investors, there is only one objective—maximum total return after taxes.” We couldn’t agree more!

The scope of this paper is limited to tax tools and strategies applicable to existing portfolios. We do not cover tax strategies for accumulating and saving money, consuming portfolio assets or avoiding estate taxes. “We also make some important simplifying assumptions (see references and methodology).” Of critical importance, this paper incorporates the tax law changes legislated in the recent Jobs and Growth Tax Relief Reconciliation Act of 2003.
In his classic book, *A Random Walk Down Wall Street*, Burton G. Malkiel suggested, "Investors should be wary of any scheme that promises unusually large returns based on past patterns. Relative to a buy-and-hold strategy, the only beneficiaries are likely to be your broker and tax collector." This statement fairly summarizes the challenges that active managers face in taxable investing. As difficult as it is to outperform the market before taxes, it’s nearly impossible after taxes. Even the SEC recognizes this. They now require mutual funds to report after-tax returns. Unfortunately, this disclosure is made in the fund prospectus, which is usually so complex that few investors even attempt to read it.

In their quest to "beat the market" via speculation and superior stock picking, active managers face an uphill battle. In practice, active investors and traders need to overcome three burdens compared to passive investors: higher expenses, higher trading costs, and a higher tax burden. Trading costs include commissions as well as the potentially more significant bid-ask spread and market impact. While the challenges of high costs are well documented, few people in the money management business understand that the tax cost of trading is just as important. In fact, it may be the single most important expense item.

The problem is that routine securities trading by the active manager makes it almost impossible for investors to defer taxes. It triggers the recognition of expensive short-term capital gains (taxed at up to 35%). Unfortunately, this problem cannot be eliminated. Active managers are in the business of selling alpha—a measure of above market performance—which is then reduced by taxes. Brokers are compensated by commissions on the trades that generate the taxes, so there is little incentive on the "sell side" of Wall Street to highlight tax considerations.

Figure 1 illustrates the tax and expense drag imposed by active management. Jeffery and Arnott noted, "Passive indexing is a very difficult strategy to beat on an after-tax basis, and therefore, active taxable strategies should always be benchmarked against the after-tax performance of an indexed alternative." Accordingly, our analysis compares after-tax expected returns for actively managed investment strategies—ranging from low turnover to high turnover—to a buy-and-hold, tax-efficient index strategy. Based on estimated (gross) equity returns of 10.2% per year for actively managed and index funds alike, and based on current dividend yields, tax rates and expenses, the index investor is expected to lose 1.06% per year (10.20% – 9.14%) to mostly "unavoidable" tax and expense. In contrast, actively managed strategies are expected to lose up to 5.8% of their return to tax and expense. Even low turnover active strategies add considerable "avoidable cost."

To be fair, the above analysis assumes that active managers earn market returns before expense. In the aggregate, this must be true. Still, some managers actually "beat the market." The problem is, after tax and expenses, even skilled managers must beat the market by huge margins to add value. Figure 2 illustrates this challenge. Average and high turnover managers must beat the market by 3.72% and 7.29% annually just to match the after-tax return of a tax-efficient index fund.

The implications are obvious. One study showed that while 21% of active managers beat the market, fewer than 7% did so after taxes. Another study found the top 8% of managers beat the market by an average of 1.4% per year, after taxes. However, the worst 8% of managers failed by 9.7% per year. Active management hardly seems worth the risk!
Expected Annualized After-Tax Returns of Various Equity Fund Strategies

(Assumes a 20-year holding period with liquidation at end.)

Pre-Tax Active Management Returns Required to Beat a Buy-and-Hold Index Fund Strategy

(Assumes a 20-year holding period with liquidation at end.)
The High Costs & Negative Tax Implications of Variable Annuities Consumes Investor’s Wealth
(Assumes a 20-year holding period with liquidation at end.)

Figure 3

State Sponsored Section 529 College Savings Plans are Not Always the Best Way to Save for College
(Assumes a 20-year holding period with liquidation at end.)

Figure 4

*12.20% Pre-tax estimated equity return based on S&P 500 from 1/1/80 – 2/02.
Having already referenced the admonition, “Don’t let the tax tail wag the dog,” let’s explore how investors fall prey to this possibility in the real world. Sadly, it is the investors’ disdain for paying taxes that frequently leads them astray. Too often, they pursue high-risk schemes or purchase marginal products from opportunistic salespeople who happily prey on their contempt for paying tax. The products they peddle are often misdirected, based on antiquated laws, fail to survive IRS scrutiny or are simply inappropriate. While the investor may pay less tax, it often comes at the cost of lower returns.

The seventeenth century French politician Jean Baptiste Colbert once said, “The art of taxation consists in so plucking the goose as to get the most feathers with the least hissing.” Likewise, the art of designing tax-avoidance products is to opportunistically press a prospective investor’s tax “hot-buttons” to justify inordinate fees without notice. History offers many examples. They include oil and real estate limited partnerships, life insurance schemes, principal-protected funds and exotic derivatives strategies. The dollars lost in these flawed products often end up serving as expensive “tuition.”

For example, popular variable annuity contracts issued by insurance companies are often flawed from a tax perspective, yet they are sold on the premise of being tax favorable. Money is invested in mutual fund-like “separate accounts” which are owned inside of annuity wrappers. Salespeople aggressively promote the fact that annuity contracts defer tax on interest, dividends and capital gains. As always, the devil is in the details.

Variable annuities come with a number of fatal flaws. First, they are expensive. In addition to the typical trading costs incurred by most stock mutual funds, annuities are often accompanied by very high internal fees. Likewise, annuity commissions and surrender fees are often quite large. Second, in the long-term, annuities are “tax-nasty.” Though they feel good along the way, annuities effectively convert long-term capital gains (taxed at rates of up to 15%) into ordinary income (taxed at higher rates of up to 35%).

Figure 3 illustrates the 20-year impact of taxes and costs on variable annuities. Each example assumes estimated (gross) equity returns of 10.2% per year and current dividend yields, tax rates and expenses. Note that the index fund owned outside of a variable annuity performs better than the same fund that’s owned inside of the more costly variable annuity wrapper. In fact, in light of the recent tax-law changes, it is now mathematically impossible for investors to overcome the high costs and negative long-term tax implications of a typical variable annuity.

State-sponsored 529 college savings plans are another popular tax-avoidance product. As Figure 4 shows, these plans lost much of their appeal with the recent tax-law changes of 2003. While optimal use of low cost 529 plans may deliver slightly more return than outright index investing, gifting strategies using traditional index funds may offer even higher returns. Also, if 529s are used for non-educational purposes (non-qualified distribution), their after-tax returns plummet. Section 529 plans were previously too good to be true. Now they are merely interesting.

The bottom line: investors should avoid investment products whose advantage or investment merit is contingent on an effective lobby (i.e. by the insurance companies). Investors usually fare best by following sound investment strategies that are not easily sabotaged by politicians.
Many or even most conventional "tax-avoidance" products and strategies are not conducive to one’s financial health. With that being the case, what is the best way to protect yourself from tax-hungry politicians who want to get their hands on your money? First, you need to concede that tax laws continually change. Fickle politicians are influenced by public opinion, which is fluid and constantly changing. They react by constantly passing new tax laws. Art Buchwald, the newspaper columnist, wittily wrote, “Tax reform is when you take taxes off things that have been taxed in the past and put taxes on things that haven’t been taxed before.”

To appreciate the ever-changing tax law, simply glance at history. Prior to 1913, the Federal income tax was unconstitutional. When politicians fixed that, the floodgates burst open! Figure 5 illustrates the, until recently, mostly upward “tax rate roller coaster.” Initially, the highest tax rate was only 7%, but by 1944, high-income earners were losing 94% to tax. Years later, while making his case for tax reform, then President Ronald Reagan explained how, during his Hollywood days, he refused to make more than one movie per year. If he worked any harder, he kept only 10% of the profits.

The good news is that tax rates have returned to rational levels. The recent 2003 tax cuts reduced ordinary income tax rates to a maximum of 35%. This applies to earned income as well as interest income. Capital gains and dividends now face a top rate of 15%—their lowest rates since 1933 and 1916, respectively. Where will rates go next? The answer probably depends on our next president.

The secret to tax-efficient investing is having a dynamic and systematic process to structure your portfolio for maximum tax efficiency. It must recognize that today’s tax situation will probably be different tomorrow. You must constantly adjust your tactics to new realities. The process involves optimizing a suite of tax tools to take advantage of current and future tax benefits.

In developing this process and suite of tax tools, investors need to understand that there are three primary investment strategies to reduce or eliminate tax. They include 1) permanent elimination of taxes, 2) deferral of taxes into future years, and 3) deliberately timing the recognition of income to low rate years. As Figure 6 illustrates, all tax reduction strategies leverage these three methods. For example, the primary strategy used by tax-managed index funds and exchange traded funds (“ETFs”) is deferring tax. This also allows investors to convert short-term capital gains into lower rate long-term capital gains. In addition, tax deferral creates the opportunity to time the recognition of income into lower tax rate years. In the event that an investor died prior to the recognition of any unrealized gains, there is also a distinct possibility of permanently eliminating capital gains tax (see the step-up in basis discussion on pages 20-21).

An effective, tax-efficient investment process requires continual monitoring of one’s portfolio strategy to maximize after-tax returns. The suite of investment tax tools must continually evolve. While it is challenging to predict which politician will win the next tax battle, you are best served by using current tax rules—knowing that you may have to re-engineer and update your process every time Congress meets.
Politicians Are Fickle:
Tax Rates and Rules Change Continually

Figure 5

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<td>30%</td>
<td>40%</td>
<td>50%</td>
<td>60%</td>
<td>70%</td>
<td>80%</td>
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Current Maximum 2003 Tax Rates
35% Ordinary Income and Interest
15% Long-Term Capital Gain and Dividends

*2003 is first year dividends and interest income rates were different. Prior to the recent 2003 tax legislation dividends were taxed at the same rate as income and interest.

Legitimate Investment Tax Tools
Leverage 3 Key Tax Reduction Strategies

Figure 6

<table>
<thead>
<tr>
<th>TAX STRATEGY</th>
<th>Tax-Managed Index ETF</th>
<th>Cow and Structured Solutions</th>
<th>IRA’s Annuity and 401(k)</th>
<th>Section 529 Plans</th>
<th>Roth IRAs</th>
<th>Tax Engineering</th>
<th>Tax Loss Harvesting</th>
<th>Tax-Free Municipal Bonds</th>
<th>Step-Up in Basis</th>
<th>HFA Accounting</th>
<th>Charitable Strategies</th>
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<td>1 Permanently Eliminate Tax</td>
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</tr>
<tr>
<td>2 Defend Taxes</td>
<td>✓ ✓ ✓ ✓ ✓</td>
<td>✓ ✓ ✓ ✓ ✓</td>
<td>✓ ✓ ✓ ✓ ✓</td>
<td>✓ ✓ ✓ ✓ ✓</td>
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</tr>
<tr>
<td>3 Time Tax in Low Rate Years</td>
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</tbody>
</table>

✓✓ PRIMARY STRATEGY ✓ SECONDARY STRATEGY NOT APPLICABLE
Large Growth Stocks are Inherently Tax-Efficient for Buy-and-Hold Investors

“Core and Structured Satellite™” Approach
If traditional active management is tax-nasty and if traditional tax avoidance products are ineffective, how do you minimize taxes? Tax-efficient investing focuses on portfolio structure as well as low turnover, broad diversification and adherence to a long-term buy and hold strategy.

Previously we compared active management to index funds. As discussed, index funds provide the optimal way of maximizing after-tax asset growth. Jonathan Clements, the popular Wall Street Journal columnist, wrote: “If index funds look great before taxes, their performance is almost unbeatable after taxes, thanks to their low turnover and thus slow realization of capital gains.”

What is an index fund? It is a mutual fund that buys all or most of the securities in a given asset class. For example, a large stock index fund might purchase all the stocks traded on domestic stock exchanges with a market capitalization above a certain size. Index funds are available for every asset class imaginable. Examples include large, small, growth, value, foreign, bond, and REIT funds.

While index funds are inherently tax efficient, some index strategies are more efficient than others. Figure 7 depicts different levels of tax efficiency for a variety of stock index funds. Small value stocks tend to be the least tax-efficient. As small value stocks “graduate,” they become either large company stocks or growth stocks and are sold from the small value index fund, thus causing the recognition of capital gains. Furthermore, value stocks pay higher taxable dividends than growth stocks. In contrast, large growth stocks are very tax efficient. Since it is impossible to graduate from being a large growth stock, they are rarely sold (and taxable gains go unrealized). They also pay low dividends. Most of their return comes in the form of unrealized appreciation in value, which is tax-deferred until the shares are sold.

Figure 8 depicts the “core and Structured Satellite” approach to investing. This is a proprietary term that is used to describe our diversified asset class investing. Tax wise, the “ideal” core fund is a market-wide index fund such as the Wilshire 5000, Russell 3000 or Dow Jones Total Stock Market index. Capitalization weighted index funds based on these indices are core holdings that invest in most publicly traded stocks. This “core” holding offers three inherent advantages: First, it is simple, broadly diverse and reflects the consensus view of most market participants. Second, the funds automatically remain in perfect alignment with the market and require little or no rebalancing. Third, the buy and indefinite hold strategy avoids realizing most gains—even on small and value stocks.

Some people assume that investing in such a broad market index is sufficient. However, the market’s extreme bias toward large growth (the largest and most expensive stocks dominate the market) exposes such investors to a high degree of speculative risk. For example, from the market peak in March of 2000 until the market bottom in 2003, market wide funds lost approximately 50% of their value.

The “Structured Satellite” investments (small, value, international, etc.) provide a high degree of diversification from the large growth bias that is present in the core. Around the tax-efficient core, these “Structured Satellite” funds provide exposure to under-represented asset classes such as micro cap stocks, small value stocks and large value stocks.22
Many investors mistakenly assume that owning mutual funds results in higher taxes. This is a myth. While it is true that most actively managed funds, and even some index funds, frequently trigger unnecessary tax, most index and exchange traded funds (ETFs) are extremely tax efficient. In particular, tax-managed index funds avoid many of the common tax traps associated with traditional funds while taking advantage of the established tax law to accomplish optimal tax efficiency.

While tax-managed index funds avoid stock picking and speculation, they differ from traditional index funds that invest in exact alignment with an underlying benchmark. In contrast, tax-managed funds only attempt to approximate a benchmark—occasionally breaking the rules. Though this means the fund will not perfectly track an index (it will vary slightly plus or minus over time), this approach increases after-tax returns. Furthermore, it does so with high certainty and minimal cost. Unlike “active” stock picking, where the odds of failure are high, “active tax-management” offers very high odds for increasing returns. Ironically, for taxable investors, ignoring tax-management may be just as irresponsible as “active” stock picking.

Figure 9 illustrates six techniques that tax-managed index funds use to maximize tax efficiency. An example illustrates the concept. Without tax management, micro cap indexes tend to be relatively tax-nasty. Since they represent only about 5% of the entire value of the stock market, each year the most successful micro cap stocks “graduate” to become small or mid cap stocks. Without tax management, these stocks are sold and the investors must realize capital gains.

The first strategy expands the fund’s target capitalization range to include both micro and small cap stocks. This allows the fund to avoid taxable sales as micro cap stocks graduate into the small cap range. Imagine, however, that the stocks keep growing. Employing a “hold” range to allow some “graduation” into mid cap stocks further defers recognition of gains. If stocks later graduate from the “hold” range, the tax-managed fund then sells such stocks, but only after they have been held for 12 months, thus qualifying for long-term rates (15%) instead of short-term rates (35%). Recent tax law changes make this particularly important. At the same time this gain is realized, the fund may harvest other losses (see pages 16-17) while carefully avoiding the 30-day wash sale rule. The losses conveniently offset the gains. Tax-managed funds also employ tax-smart techniques like HIFO accounting (see pages 16-17) and imposing surrender fees on short-term traders.

While the technical nature of exchange traded funds (ETFs) is well beyond the scope of this paper, these index funds, which trade like stocks, are inherently tax efficient. Investors buy ETFs through intermediary market makers. A creation/redemption process* allows the ETF fund company to wash out low basis stock to the market maker without causing detriment to fund owners. This helps avoid realizing gains. Figure 10 illustrates this complex process.

Tax-management techniques defer taxes to the future. Deferring tax is like getting an interest-free loan from the government to be repaid at your option—generally when you are in a lower tax bracket. Though tax-management techniques may slightly increase costs and portfolio turnover, and introduce tracking error, they increase after-tax returns by significantly more than they increase costs.
Tax-Managed Index Fund

Figure 9

Universe of 8,499
Publicly Traded Stocks

LARGE STOCKS
(Sell Range)

MID-CAP STOCKS

SMALL STOCKS

MICRO CAP STOCKS

Hold Range

Expand capitalization range
2) Employ "hold" range
3) Convert short-term gains to long-term by holding more than 12 months
4) Harvest losses to offset Capital Gains
5) FIFO Accounting Method
6) Penalty/transaction fees to discourage short-term trading

Exchange Traded Index Fund (ETF)
Tax-Efficient Creation/Redemption Process

Figure 10

INVESTOR
(Buyer)

Exchange

ETF MARKET MAKER
(Absorbs Most Capital Gain)

ETF FUND COMPANY
(Passes Most Capital Gains to Market Maker)

CASH

ETF SHARES

HIGH BASIS SECURITIES

ETF SHARES CREATED

LOW BASIS SECURITIES

ETF SHARES REDEEMED

CASH

CASH

CAPITAL MARKETS
Investor Tax Buckets are Taxed at Multiple Tax Rates, Currently and in the Future

**Figure 11**

<table>
<thead>
<tr>
<th>TYPE OF GAIN</th>
<th>Maximum Current Tax Rate</th>
<th>Maximum Future Tax Rate</th>
<th>Retirement Rate (if below max)</th>
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<tbody>
<tr>
<td>Interest and NQ Dividend</td>
<td>N/A</td>
<td>35 %</td>
<td>10 – 33 %</td>
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<tr>
<td>Short-Term Capital Gain</td>
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<td>10 – 33</td>
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<td>Qualified Dividend</td>
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<td>10 – 33</td>
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<tr>
<td>Long-Term Capital Gain</td>
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<td>10 – 33</td>
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<tr>
<td>IRD (Income Tax at Death)</td>
<td>N/A</td>
<td>35</td>
<td>10 – 33</td>
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</table>

<table>
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</thead>
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<td>N/A</td>
</tr>
<tr>
<td>Short-Term Capital Gain</td>
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<td>35 %</td>
<td>10 – 33</td>
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<tr>
<td>Qualified Dividend</td>
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<td>N/A</td>
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<td>Long-Term Capital Gain</td>
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<td>IRD (Income Tax at Death)</td>
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<table>
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<tr>
<th>TYPE OF INVESTMENT</th>
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<th>Taxable Accounts</th>
<th>Roth IRA Accounts</th>
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<tr>
<td>TAX-NASTY STOCKS (High Dividend, High Realized Gain)</td>
<td>BETTER&quot;</td>
<td>BAD</td>
<td>BEST&quot;</td>
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<tr>
<td>TAX-EFFICIENT STOCKS (Low Dividend, Low Realized Gain)</td>
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<td>BEST</td>
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<td>TAXABLE BONDS (Government, Agency, Corporate)</td>
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<td>BAD</td>
<td>FAIR</td>
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<tr>
<td>TAX-FREE BONDS (Municipal)</td>
<td>VERY BAD</td>
<td>BETTER</td>
<td>VERY BAD</td>
</tr>
<tr>
<td>CASH (Money Market, T-Bills, Savings, CDs)</td>
<td>BETTER</td>
<td>BAD</td>
<td></td>
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Note: Ideal asset locations are in bold.
In the quest for maximum tax-efficiency, asset location is nearly as important as the actual investments you make.

To understand, imagine that you hold your portfolio in three different tax buckets (which are discussed below). The buckets catch and hold your growth. Still, some gains evaporate due to taxes, depending upon which bucket your money is in. This “tax bucket” analogy simplifies the myriad of tax rates, regulations, rules and types of income.

The three most common tax buckets include 1) tax-deferred accounts (i.e. traditional IRA, 401k, 403b, annuity and pension assets), 2) taxable accounts and 3) Roth IRA accounts. By happenstance, some people have all their assets in one bucket, although most investors have them spread over two or more buckets. The Roth IRA bucket is often the smallest (since this is a newer type account) while taxable and tax-deferred buckets are typically largest.

Understanding how, when and at what rates your investments are taxed is essential in deciding which investment you should hold in which bucket. The implications of investing in various “tax buckets” are illustrated on the previous page.

Investors love the Roth IRA bucket and the tax-deferred bucket. The Roth investor generally avoids all taxes—currently and in the future. Tax-deferred investors defer all taxes to the future. However, this deferral comes at a cost. When the money is withdrawn, all gains—even capital gains—are taxed as ordinary income at rates up to 35%. Lower capital gains rates do not apply. Tax-deferred investors likewise miss an opportunity to receive a step-up in basis (see pages 20-21). At death, the investors’ estate or heirs always get taxed on the accumulated gains inside of tax deferred accounts.

Taxable accounts are more complex. Dividends are now taxed (in the year received) at rates up to 15%. Non-qualified dividends and interest currently get taxed at rates up to 35%. By design, capital gains—both short-term (held less than 12 months) and long-term (held 12 months or more)—are taxed in the future, when shares are sold. Short-term gains are taxed at up to 35% while long-term capital gains can be deferred for a long time and are ultimately taxed at rates no higher than 15%. As discussed on pages 20-21, the step-up in basis that occurs at death may result in the permanent elimination of capital gains.

One big advantage of deferring tax (tax-deferred and taxable buckets) is that rates often decline in retirement. A top bracket taxpayer (35%) may see their tax rate decline to 25% or less during retirement years. This can greatly reduce taxes!

Conventional wisdom is often wrong with respect to tax bucket management (asset location). Historically, many investors have errantly held long-term investments (stocks) in tax-deferred accounts. Unfortunately, this eliminates the opportunity to benefit from preferential long-term capital gains and dividend tax rates (of only 15%). In addition, holding stocks in tax-deferred accounts prevents the investor from engaging in loss harvesting (see pages 16-17). As Figure 11 illustrates, it makes more sense to hold most stocks in taxable accounts. Certain “tax-nasty” stocks are better off in Roth IRAs while corporate and government bonds are ideally placed in tax-deferred accounts.

Most investors ignore tax consequences or don’t properly divide their investments among their accounts. Though effective tax bucket management is counter-intuitive and complex, the benefit of getting it right is significant. Effective asset location does not increase your gross return but reduces how much tax you pay on April 15th. You earn more by saving tax.
Tax-Engineering may be the most Effective Way to Reduce Tax

Tax-Engineering is an effective method of coordinating and assembling your assets to eliminate and/or defer unnecessary taxes. It focuses on getting the right investments, within your asset allocation strategy, positioned in the right tax buckets (see previous page). This does not change your actual gross return, it just systematically reduces your tax bill and increases your after-tax return.

Tax-engineering is neither simple nor intuitive. It requires making investment decisions on a portfolio-wide basis and is a two-step process. First, investors must determine their overall asset allocation. This is based on risk and return preferences. The allocation decision determines the optimal combination of asset classes including large stocks, small stocks, bonds, etc. Step two then focuses on proper asset location—it determines which investments belong in which tax buckets.

The benefit of tax-engineering is illustrated by the example in Figure 12. We illustrate three different scenarios in which we compare a tax-engineered portfolio to two others in which tax assumptions were either incorrect or ignored (which we refer to as “tax-backwards investing”). Each example assumes an investment of 60% equity and 40% fixed income, which is a typical retirement allocation. We assume 2/3 of the equities are invested in a “core” market portfolio with the remaining 1/3 in small stocks. The investor also has three buckets—40% each in tax-deferred and taxable accounts and 20% in a Roth IRA. In all three examples, the gross expected return before costs and taxes is 9.3%.16

In the first scenario, the tax-engineered index portfolio optimally positions the market-wide fund in the taxable bucket, small stocks (a “Structured Satellite” fund) in the Roth bucket and bonds in the tax-deferred bucket. This tax-efficient investor loses only 1.0%16 annually to taxes. The second scenario shows an investor with the same exact holdings, but located in exactly the wrong buckets. This simple “location error” causes the investor to pay an additional 1.1%16 in extra tax (7.2% net return after taxes instead of 8.3%). The third investor is most typical. Instead of investing in index funds with core and Structured Satellite investments, they own tax-naïve, actively managed funds in a “tax-backwards” manner (using the wrong buckets). Even before tax, the high costs of active management cause a significant reduction in return for this investor (7.1% net return after costs vs. 8.9% for the index and Structured Satellite investor).17 After taxes and costs, the tax-backwards, actively managed portfolio sees its gross return of 9.3% shrink to a mere 5.6%—a total shrinkage of almost 40%.

If anything, the above examples underestimate the true benefits of optimal tax-engineering. In the first scenario, losses in the taxable bucket could be harvested to offset gains (see pages 16-17). In contrast, the “tax-backwards” investor loses the ability to harvest and recognize losses since you cannot deduct losses in tax-deferred accounts.

Tax-engineering provides significant opportunities for investors. Though effective asset location is often ignored by many financial advisors and is contrary to conventional financial advice, it can empower investors to proactively organize their portfolios and earn far more than those who ignore taxes.
Tax-Engineering and Low Costs Increase Returns Over Time
60/40 stock/bond portfolio, liquidation after 20 yr. holding period, no rebalancing
40% tax-deferred, 40% taxable, 20% Roth IRA assets

Figure 12

TAX-ENGINEERED 60/40 USING CORE TAX-NAGED INDEX AND STRUCTURED SATELLITE

TAX-BACKWARDS 60/40 USING CORE INDEX FUND AND STRUCTURED SATELLITE

TAX-BACKWARDS 60/40 USING ACTIVE CORE AND ACTIVE SATELLITE STRATEGIES

Source: Savant Analysis
The Arithmetic of Tax Loss Harvesting

Three-year tax savings from harvesting a $25,000 loss.

![Figure 13](image)

Comparing HIFO (Highest-in, First-out) to Alternative Tax Accounting Methods

![Figure 14](image)
Recognizing capital losses is never fun. While we would prefer to never lose money, as in contests and sporting events, you can’t win all the time. Growth oriented investors occasionally suffer the agony of defeat. Happily, the investment world does offer taxable investors a consolation prize. Tax loss harvesting allows us to recapture some of the loss from Uncle Sam.

Loss harvesting is not complex. Investors have the ability to control the timing and recognition of gains and losses. Successful investments can be held indefinitely—allowing long-term deferral of gains. In contrast, it is prudent to sell losing investments in order to get current year tax write-offs. Importantly, this can only be done in taxable accounts (not in tax-deferred accounts, i.e. IRAs).

Ideally, losses are harvested in a disciplined and systematic manner that continually captures tax benefits and preserves them for current and future use. Any unused losses can be carried forward indefinitely to offset future gains. This counter-intuitive process is mentally difficult in that it requires investors to admit their losses by selling losers.

A typical loss harvesting transaction might involve selling an investment with a $25,000 capital loss and concurrently buying back a similar, but not identical investment. To avoid IRS “wash sale rules,” you cannot repurchase the identical security for 31 days. Nothing really changes aside from realizing a valuable tax benefit. Figure 13 illustrates that this mostly risk free and cost free transaction results in a $6,750 tax reduction over three years. Without loss harvesting, other gains result in $3,600 of additional tax. In contrast, the investor that harvests $25,000 in losses receives a net tax reduction (refund) of $3,150. This $6,750 difference effectively recaptures 27% of the original $25,000 loss incurred.

While this transaction lowers tax basis (possibly creating future gains), it also maximizes tax savings by potentially offsetting short-term capital gains and ordinary income of up to $3,000 per year.

At tax time, many investors err in their selection of an accounting method for tax purposes. After selling a partial position, the IRS offers multiple methods to determine your tax basis in the shares sold. Most investors accumulate shares over time and at varying prices. Thus, the wrong accounting method may cause the investor to realize gains on highly appreciated shares (tax lots) while holding shares with smaller gains or possibly even losses.

To illustrate this concept, Figure 14 shows an investor who is selling $30,000 from what was originally a $70,000 holding. The total position was accumulated in three transactions—15 months, 10 months and one month ago. All three purchases or lots have appreciated in value. The first purchase or position should qualify for long-term gain while the latter two lots would produce short-term gains. At the far right, we provide the tax calculation for FIFO (first-in, first-out), average cost (most typical method) and HIFO (highest-in, first-out) accounting methods. HIFO is also at times referred to as “specific lot” accounting.

As is nearly always the case, HIFO accounting results in much lower taxes. Importantly, there is no additional cost or risk in choosing HIFO—it is merely an accounting election. HIFO elections can be instrumental in maximizing loss harvesting opportunities.
When the constitution was changed in 1913 to legalize income taxes, the prohibition against the federal government’s taxing of state and local governments remained intact. This provides high bracket investors with a valuable tax savings opportunity. While Treasury, government agency, corporate and foreign bonds are all taxed at ordinary rates of up to 35%; bond interest paid by most state and local governments (municipalities) is exempt from federal taxation.

There are many varieties of tax-free municipal bonds. General obligation bonds are backed by an issuer’s general taxing authority and revenue bonds are backed by revenues generated by specific projects. Insured municipal bonds have insurance companies who contractually assure their repayment, while pre-refunded bonds are collateralized by U.S. Treasury bonds.

While the tax-free nature of municipal bonds is appealing, like everything in life, it comes with a price. Because of their tax-free status, issuers of municipal bonds have a leg up on issuers of taxable bonds. Thus, the tax-free yield they offer is generally lower than that paid by corporations or the U.S. Treasury. While the reduction in yield has varied over time, on average, municipal bonds historically pay 74% to 81% of the corresponding yield offered by U.S. Treasuries. Large tax bracket investors should generally avoid municipal bonds—irrespective of the tax-free advantage. Even after paying taxes, low bracket investors are usually better off buying taxable bonds. In contrast, the yield reduction is generally well worth it for high bracket investors (i.e. 30% tax bracket or higher).

To better understand municipal bonds, and to compare apples to apples, the yield on tax-free muni-bonds must be converted into a “taxable-equivalent” yield. Figure 15 calculates the break-even rate for taxable versus municipal bonds. This point depends on your marginal tax bracket. For example, a 3.5% tax-free municipal bond investor in the 35% bracket would need to earn more than 5.38% in taxable bonds to be better off. In contrast, a low bracket (10%) taxpayer needs to earn only 5.89% to be better off in taxable bonds. You can reference Figure 16 to determine your marginal tax bracket.

For investors in high tax states, municipal bonds issued in your home state often make great sense because most states do not tax municipal bond interest paid on their own bonds. California, New York, Massachusetts, and Iowa are good examples.

Though municipal bonds offer advantages, they are often misused. While municipal bonds are most appropriate for high bracket investors, low bracket investors often use them inappropriately and when taxable bonds would make more sense. Investors also forget that, unlike Treasury bonds, municipal bond issuers occasionally default. Tax-free municipal bonds never make sense in IRA accounts, even for high bracket taxpayers, since they are eventually taxed in such accounts. High bracket investors are better served by holding taxable bonds inside their tax-deferred accounts (IRA, 401k, etc.) when possible. Finally, since the Alternative Minimum Tax (AMT) can sneak up on municipal bond investors, professional tax advice may be warranted.

While municipal bonds offer opportunity, they need to be handled with caution. They require continual monitoring of tax brackets, yield curves and personal tax circumstances.
Municipal Bond Taxable Equivalent Yields

Taxable Equivalent Yield = Tax-Free Yield/(1–Marginal Tax Rate)

Tables incorporate revised 2003 tax rates.

**Figure 15**

<table>
<thead>
<tr>
<th>MUNICIPAL TAX-FREE YIELD</th>
<th>MARGINAL TAX BRACKETS 10%</th>
<th>MARGINAL TAX BRACKETS 15%</th>
<th>MARGINAL TAX BRACKETS 25%</th>
<th>MARGINAL TAX BRACKETS 33%</th>
<th>MARGINAL TAX BRACKETS 35%</th>
</tr>
</thead>
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<tr>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>1.0</td>
<td>1.11 %</td>
<td>1.18 %</td>
<td>1.33 %</td>
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<td>1.49 %</td>
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<td>2.00</td>
<td>2.08</td>
<td>2.24</td>
</tr>
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<td>2.0</td>
<td>2.22</td>
<td>2.35</td>
<td>2.67</td>
<td>2.78</td>
<td>2.99</td>
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<td>2.78</td>
<td>2.94</td>
<td>3.33</td>
<td>3.47</td>
<td>3.73</td>
</tr>
<tr>
<td>3.0</td>
<td>3.33</td>
<td>3.53</td>
<td>4.00</td>
<td>4.17</td>
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<td>3.89</td>
<td>4.12</td>
<td>4.67</td>
<td>4.86</td>
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</tr>
<tr>
<td>4.0</td>
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<td>4.71</td>
<td>5.33</td>
<td>5.56</td>
<td>5.97</td>
</tr>
<tr>
<td>4.5</td>
<td>5.00</td>
<td>5.29</td>
<td>6.00</td>
<td>6.25</td>
<td>6.72</td>
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<td>5.56</td>
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<td>6.67</td>
<td>6.94</td>
<td>7.46</td>
</tr>
<tr>
<td>5.5</td>
<td>6.11</td>
<td>6.47</td>
<td>7.33</td>
<td>7.64</td>
<td>8.21</td>
</tr>
<tr>
<td>6.0</td>
<td>6.67</td>
<td>7.08</td>
<td>8.00</td>
<td>8.33</td>
<td>8.96</td>
</tr>
</tbody>
</table>

Revised Tax Tables Pursuant to Jobs and Growth

Tax Relief Reconciliation Act of 2003

**Figure 16**

<table>
<thead>
<tr>
<th>MARGINAL FEDERAL TAX RATE</th>
<th>Single</th>
<th>Married Filing Jointly*</th>
<th>Married Filing Separate</th>
<th>Head of Household</th>
<th>Trusts &amp; Estates</th>
</tr>
</thead>
<tbody>
<tr>
<td>10%</td>
<td>$ 7,000</td>
<td>$ 14,000</td>
<td>$ 7,000</td>
<td>$ 10,000</td>
<td>N/A</td>
</tr>
<tr>
<td>15%</td>
<td>$ 7,001 – 28,490</td>
<td>$ 14,001 – 56,800</td>
<td>$ 7,001 – 28,490</td>
<td>$ 10,001 – 38,050</td>
<td>M$1,900</td>
</tr>
<tr>
<td>33%**</td>
<td>143,501 – 311,950</td>
<td>174,701 – 311,950</td>
<td>87,351 – 155,975</td>
<td>159,101 – 311,950</td>
<td>6,851 – 9,350</td>
</tr>
<tr>
<td>35%**</td>
<td>311,950 +</td>
<td>311,951 +</td>
<td>155,876 +</td>
<td>311,951 +</td>
<td>9,351 +</td>
</tr>
</tbody>
</table>

* Includes surviving spouses. Marriage Penalty Relief scheduled to sunset 12/31/04.
** Marginal effective tax rates may be higher due to phaseouts of personal exemptions, itemized deductions and imposition of Alternative Minimum Tax (AMT).
Index and Tax-Engineered Balanced Investment Strategies Benefit from Forgiveness of Capital Gains Taxes Upon Death

(Assumes 20-year holding period comparing returns at death vs. liquidation at end.)

Annual Gifting with Cash

<table>
<thead>
<tr>
<th>YEAR</th>
<th>MARGINAL TAX RATE</th>
<th>DESCRIPTION</th>
<th>CASH DISBURSED</th>
<th>TAX SAVINGS</th>
<th>NET COST</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>35%</td>
<td>Cash to Charity</td>
<td>$5,000</td>
<td>$1,750</td>
<td>$3,250</td>
</tr>
<tr>
<td>3</td>
<td>15%</td>
<td>Cash to Charity</td>
<td>$5,000</td>
<td>$750</td>
<td>$4,250</td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong></td>
<td></td>
<td><strong>$15,000</strong></td>
<td><strong>$3,250</strong></td>
<td><strong>$11,750</strong></td>
</tr>
</tbody>
</table>

Alternative Gifting Strategy: Gift Appreciated Securities to a Donor Advised Fund (DAF)

<table>
<thead>
<tr>
<th>YEAR</th>
<th>MARGINAL TAX RATE</th>
<th>DESCRIPTION</th>
<th>CASH DISBURSED</th>
<th>TAX SAVINGS</th>
<th>NET COST</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>35%</td>
<td>Gift $15,000 in Stock to DAF</td>
<td>$0</td>
<td>$6,375</td>
<td>$8,625</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Cost Basis of $7,500)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Direct $5,000 from DAF to Charity</td>
<td>5,000</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>2</td>
<td>15%</td>
<td>Direct $5,000 from DAF to Charity</td>
<td>5,000</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>3</td>
<td>15%</td>
<td>Direct $5,000 from DAF to Charity</td>
<td>5,000</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong></td>
<td></td>
<td><strong>$15,000</strong></td>
<td><strong>$6,375</strong></td>
<td><strong>$8,625</strong></td>
</tr>
</tbody>
</table>

Tax-Advantage of DAF Strategy $11,750 – $8,625 = $3,125
Effective tax-engineering combines the strategies of tax elimination, tax reduction and tax deferral to achieve optimal tax efficiency. As such, long-term planning opportunities are available that benefit investors, their families and frequently charities. Investors can utilize a number of different gifting and charitable strategies to reduce or eliminate deferred gains that build up over time. Only Uncle Sam loses out.

Most people don’t know that unrealized capital gains are completely forgiven at death. While long-term capital gains during life are taxed at rates of up to 15%, even the wealthiest Americans escape tax on unrealized capital gains at death. If Bill Gates sold his Microsoft stock tomorrow, he would pay 15% in capital gains tax on the sale. However, if Mr. Gates were to die and his family was to sell the stock after his death, the taxable gain would vanish. They would save the 15% capital gains tax—permanently! This permanent elimination of capital gains tax at death is referred to as the “step-up in basis” and is available to almost every investor.

Benjamin Franklin once observed, “In this world nothing is certain but death and taxes.” For once, here’s a case where death at least eliminates one layer of tax!

Figure 17 illustrates potential tax savings from the step-up in basis. On page 20, we noted that equity investors have historically earned 10.2%. Assuming that trend continues, after expense and taxes, a tax-managed index fund should earn 9.14%. This assumes liquidation and payment of tax on deferred gains after 20 years. However, if the same investor passes away after 20 years, the step-up in basis increases the return to heirs by 0.63% annually, from 9.14 to 9.77%. In contrast, IRAs, variable annuities and other tax-deferred accounts are not eligible for this “step-up in basis.”

Gifting strategies (to family or charity) can provide an earlier opportunity to achieve the same result as the step-up in basis. High bracket taxpayers often gift highly appreciated stock to family members in lower tax brackets. Upon sale, capital gain rates can decline from 15% to 5%, or possibly even less. Charitable gifts of appreciated stocks offer even larger tax benefits. The donor gets a charitable deduction for the full value of the stock at rates of up to 35% and permanently eliminates any unrealized capital gains. As such, a 35% tax bracket investor making a $15,000 gift of appreciated stock (with a basis of $7,500) would enjoy total tax savings of $6,375. Thus, the net cost of the gift is only $8,625.

There are many tax-efficient charitable gifting strategies available (e.g. CRUTs, CLATs and CRATs). Their benefits vary with your tax rate, charitable intent, and estate planning needs. A little known example is the Donor Advised Fund (“DAF”). These are particularly effective for high bracket taxpayers who are expecting a drop in their tax rates over the next few years. Figures 18 and 19 compare outright gifts of cash to using a DAF to leverage identical gifts. We assume an investor donates $5,000 to their designated charity for three consecutive years. In year one, they are in the 35% tax bracket. In years two and three, they expect to be in the 15% tax bracket. Figure 18 shows the three-year, after-tax cost of a $15,000 cash gift as being $11,750. In contrast, using a DAF to make identical gifts (Figure 19) has an after-tax cost of $8,625—a $3,125 tax savings!

In the example, the investor contributes $15,000 of appreciated stock in year one to the DAF (when their tax rate is high). This charitable deduction eliminates the $7,500 in unrealized capital gains on the $15,000 of appreciated stock. The investor gets an immediate tax deduction for what would have been three years of contributions. However, the DAF still enables the donor to control the timing of the actual disbursements of DAF assets. Thus, they can make the same $5,000 per year gift from the DAF to their designated charity.
Tax-Efficient Investing is a Disciplined and Systematic Process—Not a Product or Event

The power to tax is the power to destroy,” John Marshall once proclaimed. While we can begrudge the politicians for their propensity to tax, we are probably better off conceding, like Ben Franklin, that “taxes are one of the certainties of life.” We also believe that an investor’s desire to reduce taxes is fairly certain. Thus, tax-efficient investing involves arranging one’s financial affairs in such a way as to avoid paying any more tax than the law requires.

Making investment decisions in light of tax consequences is both an art and a science. While many tax management techniques are small, collectively they add up to real value. Some decisions are straightforward and clear while others require difficult judgment calls. These decisions require the investor to quantify the tax benefits and be aware of currently available strategies. Our primary objective with this paper was to provide information regarding the practical application, modeling and quantification of several different tax strategies that exist after the 2003 tax act.

Tax-efficient investors should remember several key rules, including:

- Be open to education about tax matters
- Active management is inherently tax-nesy
- Most traditional tax-advantaged products are gimmicky and should be avoided
- Tax laws are dynamic and continually changing
- Think about and evaluate your portfolio as a whole
- Proper asset location and tax efficiency are synonymous
- Harvest losses by selling your losers, even if it hurts
- Be wary of conventional wisdom and outdated beliefs
- Weigh tax benefits against marginal risk and cost
- Only after-tax returns matter

Taxes should be an important consideration for all investors, maybe the most important. The bad news is that taxable investing is both counter-intuitive and difficult. While tax-smart investing does offer intellectual challenges, it also offers the most basic of tangible rewards—more money in your pocket. It’s an effort worth pursuing.

We believe that tax-efficient investing requires a knowledgeable coach. Tax management may be the single most valuable contribution offered by an effective financial advisor. To add value, an advisor needs to use a disciplined, systematic and integrated process.

Though tax-efficient investing might be easy to ignore in the short-term, it is hugely beneficial over the long-term. Getting it right may be the difference between success and failure in a long-term financial plan. We relate well with the late entertainer Arthur Godfrey, who said, “I’m proud to be paying taxes in the United States...the only thing is, I could be just as proud for half the money!”
In Figure 2, we calculate the mean return (thick line) required to conform a tax-managed fund to ETFs allowing for switching. We used the same methodology as described in Section 1 and FV above. However, instead of assuming 15% long-term capital gains, the activity-based approach suggests that the activity-based tax return of a tax-managed index is greater than that of ETF. The activity-based strategies need to be used by investors who are likely to make long-term gains with an index strategy over time. The ETF approach results in higher gains than that of ETFs, and is therefore recommended for such investors.
23. As of October 31, 2007, the Wilshire 5000, Russell 3000 and Dow Jones Total Stock Market indexes include a smaller percentage of the overall market at the end of the year than any of the indexes in the Vanguard Index family. We assumed that the Vanguard Index family includes a substantially larger percentage of the overall market at the end of the year than the indexes in the Vanguard Index family.

24. These claims are often better held in IRAs, pension or Roth accounts because they generally have more favorable tax characteristics. To estimate the savings, we assumed that all deferred capital gains are taxed at ordinary rates, including tax-exempt municipal bonds and REITs.

25. In addition, the Vanguard Tax Manager Index Funds and the Vanguard Long-Term Tax-Managed Equity Fund do not currently exclude capital gains. If they were to implement such an exclusion in the future, the savings, as shown above, would be lower.

26. When computing tax, we first offset short-term gains and losses. Bonds are realized when an investment is sold for less than 30 days. Short-term capital gains or losses are subject to tax at the rate of 35% or 28%. Dividends from domestic and international income taxed annually are ordinary income and taxed at the ordinary income rate. When computing tax, we first offset short-term gains and losses. Bonds are realized when an investment is sold for less than 30 days. Short-term capital gains or losses are subject to tax at the rate of 35% or 28%. Dividends from domestic and international income taxed annually are ordinary income and taxed at the ordinary income rate. When computing tax, we first offset short-term gains and losses. Bonds are realized when an investment is sold for less than 30 days. Short-term capital gains or losses are subject to tax at the rate of 35% or 28%. 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Our clients are not speculative, high-risk investors. All are concerned with preserving capital, growing assets, and avoiding the myriad of risks that abound in today’s investment environment. To meet these objectives, we help clients use the same Nobel Prize winning strategies traditionally reserved for the nation’s largest institutional investors.

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Each client account is tailored to the individual client’s needs, yet all clients share the goal of maximizing after-tax return at a controlled level of risk. Global diversification, based on sound asset allocation principles, is one of the most effective means toward this end. Therefore, we advocate the maintenance of portfolios using a wide variety of the world’s capital markets.

Using sophisticated investment planning tools, we assist clients in determining the mix of financial assets best suited to their investment objectives, risk tolerance, and financial goals. For individual investors, we consider income tax status and we attempt to identify the most advantageous apportionment of investment assets among personal and tax-deferred retirement accounts. Our services also help individuals minimize the confiscatory effects of estate taxes.

BHCO follows highly structured, systematic, and disciplined investment strategies designed to maximize wealth in a conservative and well-thought-out manner. BHCO’s investment process intuitively makes sense because it is based on investment theory that has stood the test of time in both theory and practice.

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Our planning oriented approach allows our clients to more effectively maximize their assets, enhance the quality of their lives, and realize personal and financial goals.