



IMPROVE INVESTMENT RETURNS: AVOID HARMFUL INCOME TAX SURPRISES WHEN INVESTING IN EXCHANGE-TRADED PRODUCTS AND MUTUAL FUNDS

**Presented By
James J. Holtzman, CFP®
Wealth Advisor and Shareholder
Legend Financial Advisors, Inc.®**

JAMES J. HOLTZMAN, CFP®



James J. Holtzman, CFP®, is a Wealth Advisor and Shareholder with Legend Financial Advisors, Inc.® and Emerging Wealth Investment Management, Inc.®

Jim has been selected nine consecutive times by *Medical Economics* as one of “The 150 Best Financial Advisors for Doctors in America.”

Mr. Holtzman has been selected five times by *Dental Products Report* as one of “The Best Financial Advisors for Dentists in America”.

Jim has also been previously selected three times by *Pittsburgh Magazine* as one of the Pittsburgh area’s FIVE STAR Wealth Managers, a list that represents the most elite financial advisors in Pittsburgh.

With over 20 years of experience, Jim assists all types of clients with their financial planning and investment needs. Jim’s extensive skill set includes providing financial advice to retirement-focused clients, medical and dental practices, and businesses.

Jim serves as the firm’s Income Tax and Education Funding and Planning Specialist.

Jim’s previous professional experience includes employment with various CPA and Financial Advisory organizations where he provided tax, accounting, auditing and financial consulting services to individuals and businesses. Jim has also provided financial advice to various Fortune 500 and public company executives.

Jim’s areas of concentration include income tax planning, estate planning, stock option exercise planning, insurance, retirement planning and Section 529 Plans.

Mr. Holtzman was selected by *Pittsburgh Business Times* as one of the 2013 Fast Tracker's, which honors leaders in the Pittsburgh area's business community who've had a significant impact on the growth of their organization.

INTRODUCTION

TAXABLE INCOME CALCULATION

- 1. Gross Income**
- 2. Less: Above Adjusted Gross Income Deductions**
- 3. Less: Greater Of Itemized Deductions Or Standard Deduction**
- 4. Equals: Taxable Income**

TAX RATE SCHEDULE-SINGLE FILERS

2017 Tax Rate	2017 Single Filers – Taxable Income	2018 Tax Rate	2018 Single Filers – Taxable Income
10%	\$0 to \$9,325	10%	\$0 to \$9,525
15%	\$9,326 To \$37,950	12%	\$9,526 To \$38,700
25%	\$37,951 To \$91,900	22%	\$38,701 To \$82,500
28%	\$91,901 To \$191,650	24%	\$82,501 To \$157,500
33%	\$191,651 To \$416,700	32%	\$157,501 To \$200,000
35%	\$416,701 To \$418,400	35%	\$200,001 To \$500,000
39.6%	More Than \$418,400	37%	More Than \$501,001

TAX RATE SCHEDULE-MARRIED

2017 Tax Rate	2017 Married Filing Jointly Taxable Income	2018 Tax Rate	2018 Married Filing Jointly Taxable Income
10%	\$0 To \$18,650	10%	\$0 To \$19,050
15%	\$18,651 To \$75,900	12%	\$19,051 To \$77,400
25%	\$75,901 To \$153,100	22%	\$77,401 To \$165,000
28%	\$153,101 To \$233,350	24%	\$165,001 To \$315,000
33%	\$233,351 To \$416,700	32%	\$315,001 To \$400,000
35%	\$416,701 To \$470,700	35%	\$400,001 To \$600,000
39.6%	More Than \$470,700	37%	More Than \$600,001

TRUSTS AND ESTATES

2017 Tax Rate	Trust And Estate Filers	2018 Tax Rate	Trust And Estate Filers
15%	\$0 to \$2,550	10%	\$0 to \$2,550
25%	\$2,551 To \$6,000	24%	\$2,551 To \$9,150
28%	\$6,001 To \$9,150	35%	\$9,151 To \$12,500
33%	\$9,151 To \$12,500	37%	More Than \$12,501
39.6%	More Than \$12,501		

RECOGNIZING CAPITAL GAINS

	10% And 12% Tax Brackets	22% Up To 35% Tax Brackets	37.0% Tax Bracket
Short-Term (One Year Or Less)	Ordinary Income Tax Rate		
Long-Term (Longer Than One Year)	0%	15%	20%
Dividends	* Qualified - Long-Term Capital Gains Rates. * Non-Qualified - Ordinary Income Tax Rates.		

RECOGNIZING CAPITAL LOSSES

- 1. Tax-Loss harvesting**
- 2. Fully Deductible Against Capital Gains**
- 3. Deduct Up To \$3,000.00 Against Ordinary
Income**

REGULATED INVESTMENT COMPANY (RIC)

1. RIC Can Be The Following:

- a. Mutual Fund**
- b. Exchange-traded Fund**
- c. Unit Investment Trust (UIT)**
- d. Real Estate Investment Trust (REIT).**

2. Distribute To Shareholders At Least 90% Of The Following:

- a. Interest**
- b. Dividends**
- c. Capital Gains.**

MUTUAL FUNDS

MUTUAL FUND TAXATION

1. Dividends And/Or Capital Gain Distributions Can Be:

1. Received As Cash

2. Reinvested Back Into Investment

2. Distributions Are Income Taxed

CAPITAL GAIN DISTRIBUTIONS FROM MUTUAL FUNDS

- 1. Long-Term Is Taxed At Long-Term Capital Gain Rates.**
- 2. Short-Term Is Reported As Non-Qualified Dividends On IRS Form 1099-DIV.**

YEAR-END CAPITAL GAIN DISTRIBUTIONS

Buying Mutual Fund Before Year-End Capital Gain Distribution.

WHAT ARE QUALIFIED DIVIDENDS

- 1. Dividend Must Be Paid By U.S. Company Or Qualifying Foreign Company.**
- 2. Real Estate Investment Trusts, Foreign Stocks And Bond Funds That Pay Dividends Are Non-Qualified.**
- 3. Taxed At Long-term Capital Gain Rates**
- 4. Holding Period: Common Stockholders**
 - a. Hold Shares For More Than 60 Days**
 - b. During The 121-Day Period That Starts 60 Day Before The Ex-Dividend Date (Date That Security Trades Without Dividend)**

NONTAXABLE DISTRIBUTIONS FROM MUTUAL FUNDS

- 1. Return Of Capital – Pays Out More Than Income**
- 2. Reported On Form 1099-DIV As A Nontaxable Distribution.**
- 3. Subtract From The Cost Basis Of Your Shares.**
- 4. Any Amounts Paid Above Your Cost Basis Are Treated As Capital Gains.**

FORCED SELL BY A MUTUAL FUND IN A DOWN MARKET

- 1. Liquidate Securities In A Rapidly Deteriorating Market Decline**
- 2. Sell Securities With Unrealized Capital Gains In Order To Meet Redemptions.**
- 3. Could Pay Taxes On Capital Gain Distributions For Investment That Lost Value.**

REVIEW BEFORE PURCHASING A MUTUAL FUND

- 1. Distribution Date**
- 2. What Is The Mutual Fund's Unrealized Capital Gain Or Loss?**
- 3. Does The Mutual Fund Have A Capital Loss Carryover?**
- 4. Review The Mutual Fund's Turnover Ratio.**

MUTUAL FUND SHARE EXCHANGES

- 1. An Exchange Of Shares From One Mutual Fund To Another Fund**
 - a. Taxable Event.**

- 2. An Exchange Of Share Classes Within The Same Mutual Fund**
 - a. Not A Taxable Event.**

DIVIDENDS RECEIVED IN JANUARY

Dividends Declared Before Year-End But Paid In January Are Considered Received Prior To December 31.

COST BASIS METHODS FOR MUTUAL FUNDS

1. Specific Identification

- a. Choose To Sell Specific Shares**
- b. Minimize Or Maximize Capital Gains Or Losses**

2. First-in/First-out (FIFO)

- a. IRS Presumes FIFO Is Used**
- b. Most Brokerage Firms/Custodians Assume This**

3. Average Share Cost

- a. Average Cost Of All Shares Purchased In The Fund.**
- b. Once Chosen, Must Continue To Use For That Investment
Until It Is Completely Sold**

UNREALIZED GAINS AND LOSSES

<u>Description</u>	<u>Trade Date</u>	<u>Quantity</u>	<u>Unit Cost</u>	<u>Cost Basis</u>	<u>Current Value</u>	<u>Unrealized Gain (Loss)</u>	<u>% G/L</u>
Mutual Funds							
Caldwell & Orkin Mkt Oppt	3/5/2004	499.238	17.272	8,622.81	10,593.83	1,971.02	22.90%
Caldwell & Orkin Mkt Oppt	2/8/2007	786.937	17.79	14,000.00	16,698.80	2,698.80	19.30%
Caldwell & Orkin Mkt Oppt	3/11/2011	520.94	19.196	10,000.00	11,054.35	1,054.35	10.50%
		1,807.12		32,622.81	38,346.98	5,724.17	17.50%
First Eagle Sogen Global Inst'	4/10/2008	1,236.99	45.004	55,669.31	62,604.06	6,934.75	12.50%
First Eagle Sogen Global Inst'	4/8/2009	256.876	31.143	8,000.00	13,000.49	5,000.49	62.50%
First Eagle Sogen Global Inst'	4/27/2012	390.935	48.601	19,000.00	19,785.22	785.22	4.10%
		1,884.80		82,669.31	95,389.78	12,720.47	15.40%
IVA Worldwide - Inst'l	3/22/2011	2,934.59	17.038	50,000.00	48,332.63	-1,667.37	-3.30%
JP Morgan MBS - Select	10/19/2011	1,660.19	11.444	19,000.00	19,291.43	291.43	1.50%
Marketfield	3/21/2011	3,397.34	13.54	46,000.00	54,629.24	8,629.24	18.80%
Marketfield	4/27/2012	2,101.12	15.23	32,000.00	33,785.95	1,785.95	5.60%
		5,498.46		78,000.00	88,415.19	10,415.19	13.40%
PIMCO All Asset All Authority	6/6/2011	8,233.12	11.053	91,000.00	93,528.27	2,528.27	2.80%
Princeton Futures Strategy - I	3/11/2011	3,458.97	10.575	36,579.60	34,174.62	-2,404.98	-6.60%
				389,871.72	417,478.90	27,607.18	7.10%

COST BASIS REPORTING FROM BROKERAGE FIRMS

- 1. Stocks Bought On Or After January 1, 2011**
- 2. Mutual Funds Bought On Or After January 1, 2012**
- 3. Options And Fixed Income Bought On Or After January 1, 2013**
- 4. IRS Form 1099-B Will Report Cost Basis**

EXCHANGE-TRADED PRODUCTS

EXCHANGE-TRADED FUNDS

- 1. Generally, More Favorable Income Tax Treatment Than Mutual Funds**
- 2. Mutual Funds Have To Sell Securities Within The Portfolio To Meet Redemptions.**
- 3. ETFs Will Designate Authorized Participants To The Fund**
 - 1. Authorized Participants Create And Redeem Shares With In-Kind Transactions**
 - 2. Investors Purchase Or Redeem With Authorized Participants**

EXCHANGE-TRADED FUNDS: TAXATION

- 1. ETFs Structured As Limited Partnerships (L.P.)**
 - a. ETFs That Hold Futures Contracts Must Be Structured As L.P.'S**
 - b. 60% Of Gains - Long-Term**
 - c. 40% Of Gains - Short-Term**
 - d. K-1**
- 2. ETFs That Invest In Foreign Currencies – Grantor Trusts**
 - a. Taxed As Ordinary Income.**
- 3. ETFs That Own Physical Precious Metals Are Structured As Trusts**
 - a. Example: SPDR Gold Shares (GLD)**
 - b. Long-Term Capital Gains At 28%.**

EXCHANGE-TRADED FUNDS CONTINUED: TAXATION

- 1. ETFs That Utilize Leverage (Including Shorting)**
 - a. Utilize Index Swaps And Other Derivatives**
 - b. Taxed At The Short-Term Capital Gains Rate, Regardless Of Holding Period.**
 - c. Interest On The Cash Pool Is Taxed As Ordinary Income.**
 - d. Potential For Significant Capital Gains If There Are Substantial Redemptions.**

EXCHANGE-TRADED NOTES

- 1. Senior, Unsecured, Unsubordinated Debt Security**
- 2. Pays The Holder Based Upon The Performance Of An Index.**
- 3. There Are No Holdings Within An ETN**
- 4. Credit Risk Of Issuer Must Be Evaluated**

EXCHANGE-TRADED NOTES CONTINUED: TAXATION

- 1. Exchange-Traded Notes Are Typically Very Tax-Efficient**
 - a. Capital Gains Taxes Are Applied To The Holding Period**
 - b. No Capital Gains Distributions, Etc....**

- 2. Exception: Currency ETNs**
 - a. Always Taxed As Ordinary Income Upon Sale**

BONDS

MUNICIPAL BONDS

- 1. Federal Income Tax-Tree**
- 2. Exempt From State Income Tax In The State That They Were Issued.**
- 3. Lack Of Liquidity.**
- 4. Interest Rate Risk.**
- 5. Credit Risk - Example Detroit General Obligation Bonds**

U.S. TREASURY BOND INCOME TAXATION

- 1. Interest Income Taxable At Federal Level.**
- 2. Not Taxed At State Or Local Level.**

ORIGINAL ISSUE DISCOUNT (OID)

- 1. Difference Between Issue Price And Amount Payable At Maturity**
- 2. Pay Income Taxes Each Year For Part Of Discount That Accrues.**
- 3. 3 Types Of Tax Consequences:**
 - a. Interest Attributable To Discount**
 - b. Coupon Payment**
 - c. Capital Gain Or Loss When Bond Is Sold**
- 4. OID Does Not Apply To:**
 - a. Tax-Exempt Obligations**
 - b. U.S. Savings Bonds**
 - c. Short-Term Debt Instruments**
- 5. OID Is Reported On IRS Form 1099-OID**

MARKET DISCOUNT BONDS

- 1. Occurs When The Value Of The Debt Decreases After Issue Date.**
- 2. Difference Between A Bond's Stated Redemption Price And Its Purchase Price On The Secondary Market, If Purchased Below Par.**
- 3. Likely To Occur More Often Due To Increasing Interest Rate Environment.**
- 4. How To Report Income On Tax Return:**
 - a. Accrue The Market Discount Over The Period And Include That Amount In Income Each Year, Or**
 - b. Treat Any Gain As Interest Income At The Time Of Sell**

MARKET PREMIUM BONDS

- 1. Prorated Portion Of Premium Can Be Deducted Each Year Until Maturity (And Reduce Cost Basis In The Same Amount).**
- 2. A Bond Purchased At A Premium Can Elect To Deduct Nothing Each Year And Claim A Capital Loss At Maturity.**
- 3. A Bond Premium Can Occur When Interest Rates Have Dropped And The Price Of The Bond Increases.**

ZERO COUPON BONDS

- 1. Issued At A Discount.**
- 2. No Stated Coupon Rate.**
- 3. Report A Pro-Rated Portion Of Discount Each Year**
- 4. No Interest Income I Paid.**
- 5. Significant Interest Rate Risk Because There Are No Coupons.**
- 6. Credit Risk Is Very Important.**
- 7. Difference Between Discount And Par Is Reported Each Year – Interest Income**

TREASURY INFLATION LINKED BONDS (TIPS)

- 1. Federal Taxable**
- 2. State And Local Tax Exempt**
- 3. Increase In The Inflation-Adjusted Principal Is Income Taxed As Original Issue Discount.**
- 4. Interest Payments Are Income Taxed**
- 5. Yield Equals The Treasury Bond Yield Minus Rate Of Expected Inflation.**

COLLATERALIZED DEBT OBLIGATION

1. Debt Instrument Secured By A Pool Of

- a. Mortgages**
- b. Automobile Loans**
- c. Equipment Leases**
- d. Credit Card Receivables.**

2. OID, Market Discount And Other Income Reporting Rules Apply.

BANK LOAN FUNDS

- 1. Loans Made By Banks Or Other Financial Institutional To Companies.**
- 2. Below Investment Grade But Are Senior Secured With Collateral.**
- 3. Coupon Payments Are Ordinary Income Taxable.**
- 4. Could Be Capital Gains Or Losses.**
- 5. Interest Rates Are Adjustable Typically Based Upon London Interbank Offering Rate (LIBOR).**
- 6. Typically 75.0%-80.0% Recovery Rate If Loan Defaults.**

OTHER INVESTMENTS

GOLD TAXATION

- 1. Gold Is Considered A Collectible (Art, Antiques, Etc.).**
- 2. Collectible Tax Rate Is 28.0% If Held More Than 12 Months.**
- 3. No Tax Until Gold Is Sold.**
- 4. Gold Mining Stocks**
 - a. Provides Equity Exposure**
 - b. Not Direct Exposure To Gold And**
 - c. Long-term Capital Gains Taxes**
- 5. ETFs That Invest In Gold Could Cause Investors To Pay Tax Each Year (SPDR Gold Trust).**

LIMITED PARTNERSHIPS

- 1. Partners Are Liable Only To The Extent Of Their Investment.**
- 2. Passive Activity Rules.**
- 3. Income Is Usually Apportioned According To Their Ownership Interests.**
- 4. Taxed Every Year Even If Profits Are Reinvested And No Distributions**
- 5. General Partners Are Subject To Self-employment Tax.**
- 6. Concerns: Illiquidity, Lock-Up Periods**
- 7. K-1 Tax Reporting**

PREFERRED STOCKS

- 1. Income Taxed At Ordinary Income Tax Rate.**
- 2. Shareholders Receive Priority Before Common Stockholder**
- 3. Cumulative Or Non-cumulative.**
- 4. Interest Rate Risk Is Still A Concern.**
- 5. Pay Fixed Dividends (Like Bonds).**
- 6. Shares Can Be Called.**
- 7. Minimal Benefit In Price From Common Stock Increase.**
- 8. Convertible Preferred Stocks Can Be Converted To Common Stock.**
 - a. After Conversion To Common Stock, More Favorable Tax Treatment.**

MASTER LIMITED PARTNERSHIPS (MLP)

- 1. K-1 Tax Reporting.**
- 2. Cash Distributions Can Partially Be A Return Of Capital, Which Reduces Cost Basis.**
- 3. Unrelated Business Taxable Income Concerns**
- 4. Gain From Sale Of MLP**
 - 1. Ordinary Income That Is Attributable To Depreciation And Capital Gain For The Rest.**
- 5. MLPs Can Use Depreciation (A Noncash Expense) To Reduce Reported Net Income Below The Level Of Cash That Is Actually Available To Be Paid Out As Distributions.**
- 6. Can Have Multiple States To File Tax Returns In.**

MARK TO MARKET – SECTION 1256 CONTRACT

1. Examples:

- a. Regulated Futures Contracts**
- b. Non Equity Option**
- c. Foreign Currency Contracts.**

2. Treated As If They Are Sold At Year-End For Fair Market Value.

3. Default

- a. 60.0% Are Taxed As Long-Term Capital Gains**
- b. 40.0% Are Taxed As Short-Term Capital Gain.**

ADDITIONAL WAYS TO REDUCE TAXES

WAYS TO MINIMIZE TAXES BY USING TAX DEFERRED ACCOUNTS

- 1. IRA Contributions.**
- 2. Work-Sponsored Retirement Plans**
 - 1. 401(k)**
 - 2. 403(b)**
 - 3. 457(b)**
- 3. Invest Tax-Inefficient Funds In Retirement Accounts**
- 4. Invest Tax-Efficient Funds In Taxable Accounts**
- 5. Section 529 Plans And Coverdell Education Savings Accounts.**
- 6. Health Savings Accounts.**
- 7. Annuities Can Be A Costly Way To Achieve Tax Deferral**
- 8. No-Load Variable Annuities**

GIFTING APPRECIATED SHARES OF AN INVESTMENT

- 1. Avoid Capital Gains On Significant Appreciated Investments.**
- 2. To Charities**
- 3. To Family Members, Especially Children**
- 4. Kiddie Tax Concerns For Children**
 - a. Under The Age Of 19 Or**
 - b. Under The Age Of 24 If A Full-Time Student.**
- 5. Annual Gifting Limits To An Individual (\$15,000.00 In 2018).**

WASH SALE RULES

- 1. Disallowed Loss:**
 - a. If Security Is Sold At A Loss And**
 - b. Substantially Identical Security Is Purchased Within 30 Days**
 - c. Before Or After The Sale**
- 2. Replace Security With Another Security In Same Industry**
- 3. Replace With Mutual Fund Or ETF In Same Industry**

MEDICARE TAX ON UNEARNED INCOME

- 1. Tax Rate: 3.8%.**

- 2. Tax Applies To Whichever Is Less:**
 - a. Net Investment Income Or,**
 - b. Amount That Your Modified AGI Exceeds The Threshold.**

- 3. Unearned Income Defined:**
 - a. Capital Gains**
 - b. Interest**
 - c. Dividends**
 - d. Rental Income**
 - e. Passive Investor**

MEDICARE TAX ON UNEARNED INCOME

Beginning Modified Adjusted Gross Income Subject To Tax		
Single Filers	Married Filing Jointly	Married Filing Separately
\$200,000.00	\$250,000.00	\$125,000.00

INVESTMENTS SUBJECT TO PHANTOM INCOME

1. **Earnings Are Taxed And Sometimes Not Received**
 - a. **Limited Partnerships**
 - b. **Zero-Coupon Bonds**
 - c. **Treasury Inflation-Protected Securities (TIPS):**
 - i. **Investors Are Taxed On Annual Income And**
 - ii. **The Amount Of The Adjusted Principal (A.K.A. As Phantom Income)**

QUESTIONS AND ANSWERS





**Call Us With Any Questions
At (412) 635-9210**



**Legend Financial Advisors, Inc.®
5700 Corporate Drive, Suite 350
Pittsburgh, PA 15237-5829
Phone: (412) 635-9210
E-mail: legend@legend-financial.com
www.legend-financial.com**