Pro Spotlight: A Champion for Tax-Smart Investing

Holly Swan, Head of Wealth Solutions

As head of Wealth Solutions for the Global Client Strategy team, **Holly Swan** is Allspring's expert on tax-aware investing. Her series of articles, Income Insights and Swan Songs, help advisors and investors better understand tax- and estate-related concepts like systematic tax-loss harvesting.

Q: HOW DID YOU COME TO FOCUS ON THE WEALTH AND TAX SIDE OF ASSET MANAGEMENT?

A: I actually went to a performing arts high school for musical theater. Unfortunately, my singing voice leaves something to be desired. When it was time to decide what was next, my family asked if I would please pursue something a little more conventional. So I went to college, majored in economics, continued on to law school, and thought I would practice entertainment law. Entertainment law turned out to be less about entertainment and more about reviewing documents. My favorite professor pointed out that I already had an economics degree and that I loved her trust and estates class—which was true. I also love meeting people and problem-solving. Trust and estates is one of the most personable areas of the law, so that's where I focused. I practiced law for a decade and discovered it was partially about people, but it was also a lot about generating forms. So, I moved into financial services where it's much more about the human side of planning, and my practice expanded beyond estate planning to include taxes.

My world has really come full circle, combining my arts background with taxes, estate planning, and economics, helping advisors deliver on the personal planning side for their clients. Now I spend my time educating advisors on taxes and planning in a way that I hope is engaging and entertaining. Shockingly, a lot of people don't find taxes to be entertaining, but I think we can all agree that they're an important part of our clients' overall investment outcomes.

Q: WHAT IS TAX-AWARE INVESTING, AND WHAT IS TAX ALPHA?

A: Tax-aware investing is really about making a series of small changes to asset location and to investment strategies that allow investors to keep more of what they earn after paying income tax.

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That might be a tiny change like switching from a mutual fund to an exchange-traded fund (ETF) in a taxable account, because ETFs are more tax efficient. Or it could mean holding high-turnover strategies and other tax-inefficient assets in tax-deferred accounts while keeping stocks that generate qualified dividends, municipal bonds, and other tax-efficient assets in your taxable accounts. It also means taking advantage of tax-loss harvesting throughout the year instead of waiting until December, which has typically been a very good month for the market. Tweaks like that can make a huge difference over time. We call it tax alpha.

Q: WHAT DO INVESTORS AND ADVISORS MISUNDERSTAND ABOUT TAX-AWARE INVESTING?

A: A lot of people think tax-smart investing is only for high-net-worth or even ultra-high-net-worth investors and that it's out of reach for other segments. But all investors should minimize taxes due on their investments. Technology has also made that easier. Certain investment options that used to be available only for ultra-high-net-worth investors are now more broadly accessible.

Take separately managed accounts (SMAs), for instance. They were created specifically for family offices. But with technology and automation, the benefits of SMAs are now broadly available to many investors. Investors can really customize their holdings and control the timing of their capital gains and harvest losses in a systematic way. Technology allows them to do that cost-effectively.

Q: MARKET VOLATILITY COULD BE WITH US FOR A WHILE. HOW SHOULD INVESTORS THINK ABOUT IT FROM A TAX PERSPECTIVE?

A: Market volatility actually offers a lot of opportunity, even beyond tax-loss harvesting. First, it provides buying opportunities, and some of these opportunities we haven't talked about in years because of high valuations. A lot of advisors talk about net unrealized appreciation (NUA) with clients for their retirement accounts. There's also a counterpoint to NUA called NUD, or net unrealized depreciation, where employees who own shares of company stock in their 401(k)s who might take advantage of NUA down the road can actually sell those shares when the valuation is lower. That means they can potentially lower their cost basis in those shares, and then if they choose to use NUA down the road, the basis on which they're going to be taxed at ordinary income levels can be lowered. Any advisor who's ever had an NUA conversation with a client should be talking with them about NUD right now to help them take advantage of market volatility.

Also from an estate planning perspective, lower valuations present a great opportunity to do planning. Of course, with gifting you have carryover basis, so you want to be careful about the asset types you're planning with. But if you're expecting to have a large federally taxable estate, there can be big benefits to making certain gifts while valuations are low.

Q: WHAT WOULD YOU LIKE TO SEE ADVISORS STARTING TO DO NOW THAT TAX SEASON HAS ENDED TO HELP INVESTORS PREPARE FOR NEXT YEAR?

A: I would love for advisors to stop thinking of taxes as a seasonal event. Investors file income tax seasonally, but they should be planning for taxes on a year-round basis. Once tax season is here, there's very little that can be done to help clients reduce their taxes.

From a best practice perspective, advisors should discuss tax-related issues with clients every single time they talk. Maybe one month it's about the client's incentive compensation. The next month could be about systematic tax-loss harvesting, estate planning, or charitable giving. The key is making sure you're having these conversations early enough in the year so they can take action well before tax season.

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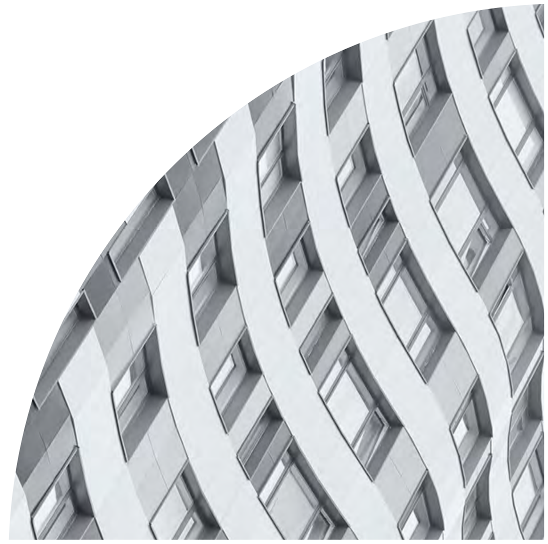

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