

## Harvesting Strategy

### Anticipating Tax Changes

With the election front and center, many investors are focused on the investment, and investment tax strategy, implications post-November. [Last week](#) we discussed stock returns and the impact a candidate or party might have.<sup>1</sup> Now let's shift to taxation, the determinant of how much of those returns investors can actually keep.<sup>2</sup>

Our focus this week: candidate Joe Biden's tax proposal to raise the long term capital gains rate to the ordinary income tax rate of 39.6 percent on income above \$1 million.<sup>3</sup> Note that even if Mr. Biden wins, there is no assurance that any of his proposals will come to pass. That said, over the capital gains tax's 107-year history, there have been nearly 20 meaningful changes, so it's worth keeping in mind that change is possible if not probable.<sup>4</sup> We'd like to offer three inferences related to Tax Benefit Capture (TBC) strategies to help investors and advisors as they begin planning for any such potential changes.<sup>5</sup>

1. **Flexibility and Control:** The ability to control the specific timing of gains may become even more important. For instance, investors with income close to the \$1M threshold may find themselves pushed over the threshold by mutual fund or hedge fund distributions or individual equity buyouts. In contrast, tax efficient indexed Exchange Traded Funds (ETFs) can be held long-term as core holdings and so could become even more attractive as they offer liquidity as well as a record of [limited capital gains distributions](#).
2. **More TBC.** Should higher rates go into effect, TBC strategies could be even more valuable in mitigating higher tax cost. Investors consistently over the \$1M income threshold may want to implement or enhance TBC to offset the higher tax cost of any realized long-term gains. Investors at or near the \$1M income threshold may want to implement or enhance TBC to stay below it. In some instances, it may make sense to accelerate TBC now to accumulate loss carryforwards to offset potential realized gains in future years.
3. **Capture Capital Gains in 2020?** Typically, high-income investors look to benefit from TBC by realizing capital losses. But investors anticipating that their specific tax rates may increase to the 39.6% rate may wish to consider capturing (realizing) long-term gains as early as this year, i.e. before higher rates potentially go into effect. This can be seen as a form of TBC but be aware there are risks. For instance, in the event personal circumstances change or tax rates do not rise, the gains may have been realized at a greater cost.

As taxes are the largest cost many investors pay, TBC is an important part of the investment process, particularly for high-income investors. TBC may become even more important should tax rates increase, especially if applied at specified income thresholds. While there's much uncertainty at this stage of the election, the most critical step now is for advisors to learn about different strategy options, prepare their clients, and plan accordingly.

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#### [Download Our White Paper: Future Value of Tax Benefits](#)

<sup>1</sup>For anyone interested in further exploration of the party's impact on stocks and the economy, check out this comprehensive and insightful analysis published last week:

<https://wallethub.com/edu/which-party-is-better-for-the-economy/24468/>

<sup>2</sup>We should be clear that Green Harvest Asset Management does not provide tax or political advice to its clients. We focus on providing efficient exposure in investment strategies to both manage risk and after-tax returns. Also, individual circumstances vary and consideration should be given to the totality of investors' situations.

<sup>3</sup>See: <https://taxfoundation.org/joe-biden-tax-plan-2020/> and <https://www.taxpolicycenter.org/>

<sup>4</sup>[https://en.wikipedia.org/wiki/Capital\\_gains\\_tax\\_in\\_the\\_United\\_States#History](https://en.wikipedia.org/wiki/Capital_gains_tax_in_the_United_States#History)

<sup>5</sup>Tax Benefit Capture (TBC) typically refers to the practice of purposely selling positions with unrealized losses to minimize taxes by offsetting realized gains. In this context however, it may include the potential benefit of purposely selling positions with unrealized gains so as to pay taxes at a lower rate than if those gains were realized in the future at a higher rate.



**Tax Benefit Capture Heat Map for period spanning October 5 – October 9, 2020:**

Market Exposure	Sectors/Regions with GHAM Tax Benefit Capture	Total Return (%)	Weekly Max Drawdown	
			(%)	Day of Low
<b>Broad Market Index (e.g. S&amp;P500)</b>	<b>X</b>	<b>3.9%</b>	<b>-1.6%</b>	<b>Tuesday</b>
Materials		5.1%	-1.4%	Tuesday
Energy	<b>X</b>	5.0%	-3.3%	Thursday
Financials		3.8%	-1.4%	Tuesday
Industrials		4.0%	-1.3%	Tuesday
Consumer Staples		2.6%	-0.9%	Tuesday
Utilities		4.6%	-1.6%	Monday
Health Care	<b>X</b>	4.0%	-1.4%	Tuesday
Real Estate		1.4%	-2.0%	Monday
Info Tech		4.6%	-1.9%	Tuesday
Consumer Discretionary		3.5%	-2.0%	Tuesday
Communication Services	<b>X</b>	2.2%	-2.3%	Wednesday
<b>MSCI ACWI Ex-US</b>		<b>3.1%</b>	<b>-1.0%</b>	<b>Tuesday</b>
Asia Ex-Japan		3.8%	-0.3%	Wednesday
Japan		1.0%	-0.4%	Thursday
Australia		1.8%	-2.0%	Tuesday
Switzerland		2.4%	-1.8%	Tuesday
EuroZone		3.4%	-1.4%	Tuesday
United Kingdom		2.8%	-1.6%	Tuesday
Lat America		7.3%	-3.2%	Thursday
Canada		3.4%	-1.0%	Monday

Areas with Tax Benefit Captures (TBCs) indicates where individual tax-loss harvest trades were executed in each market exposure across all eligible accounts for period specified. Darker shaded areas contained more TBCs.  
Broad Market Index (e.g. S&P500) reflects TBC in hedged positions.

Max Drawdown calculated as max decline from interim peak to Intra-Day Low.

Market Data Source: Bloomberg  
Market statistics calculated using representative ETFs.



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Performance quoted represents past performance, which is no guarantee of future results. Investment return and principal value will fluctuate, so you may have a gain or loss when the portfolio is liquidated. Current performance may be higher or lower than that quoted. Performance of an index is not illustrative of any particular investment. It is not possible to invest directly in an index.

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The availability of tax alpha is highly dependent upon the initial date and time of investment as well as market direction and security volatility during the investment period. Tax loss harvesting outcomes may vary greatly for clients who invest on different days, weeks, months and all other time periods.

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