Tax Planning for the Mass Affluent Investor:

Adding value through Tax Bracket Management

Presented by

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Agenda

1. The Multi-Dimensional Tax System
2. Tax Rates and Brackets
3. The Net Investment Income Tax
4. The Section 199A Deduction
5. Tax-Efficient Investing
6. “Flying Below the Radar”
7. Capital Gain & Loss Harvesting

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Mutli-Dimensional Tax System

- Ordinary Tax Rates
- Capital Gains Tax Rates
- The AMT
- Section 199A Deduction
- 3.8% Net Investment Income Tax (NIIT)
- Various other phase-outs and limitations

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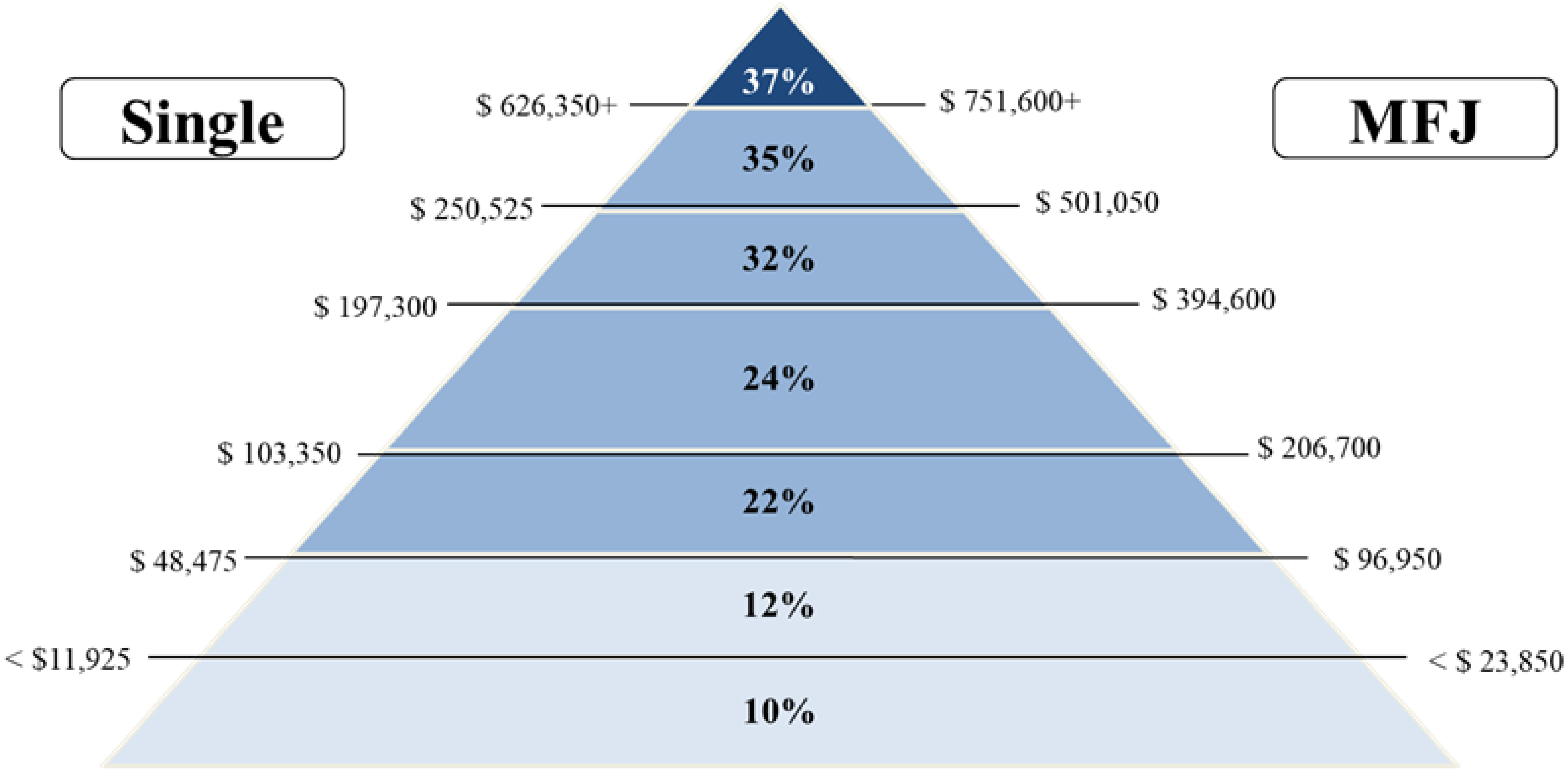
2025 Federal Income Tax Rates and Brackets



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2025 Ordinary Income Rates

TOP OF EACH BRACKET

	S	MFJ/QW	MFS	HOH	T&E
10%	$ 11,925	$ 23,850	$ 11,925	$ 17,000	$ 3,150
12%	$ 48,475	$ 96,950	$ 48,475	$ 64,850	-
22%	$ 103,350	$ 206,700	$ 103,350	$ 103,350	-
24%	$ 197,300	$ 394,600	$ 197,300	$ 197,300	$ 11,450
32%	$ 250,525	$ 501,050	$ 250,525	$ 250,500	-
35%	$ 626,350	$ 751,600	$ 375,800	$ 626,350	$ 15,650
37%					

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2025 Capital Gain Rates

TOP OF EACH CAPITAL GAINS BRACKET

	S	MFJ/QW	MFS	HOH	T&E
0%	$ 48,350	$ 96,700	$ 48,350	$ 64,750	$ 3,250
15%	$ 533,400	$ 600,050	$ 300,000	$ 533,400	$ 15,900
20%					

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Alternative Minimum Tax

AMT

	S	MFJ/QW	MFS	HOH	T&E
Exemption	$88,100	$137,000	$68,500	$88,100	$30,700
Phaseout Threshold	$626,350	$1,252,700	$626,350	$626,350	$102,500
Complete Phaseout	$978,750	$1,800,700	$900,350	$952,150	$225,300
28% Bracket	$239,100	$239,100	$119,550	$239,100	$239,100

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The Net Investment Income Tax

3.8% X
the lesser of

1. Net Investment Income

   OR

2. The excess (if any) of—
   - "Modified Adjusted Gross Income (MAGI) over the "Threshold Amount"

See IRC Section 1411(a)(1) and Reg. Section 1.1411-2(b)(1)

3.8% NIIT THRESHOLDS

S	MFJ/QW	MFS	HOH
$ 200,000	$ 250,000	$ 125,000	$ 200,000

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3.8% NIIT Overview – Net Investment Income

Includes:

- Interest
- Dividends
- Non-qualified annuity distributions (taxable portion)
- Rents
- Royalties
- Income derived from passive activity
- Net gain derived from the disposition of property (capital gains)

Does NOT Include:

- Salary, wages, or bonuses
- Distributions from IRAs or qualified plans
- Any income taken into account for self-employment tax purposes
- Gain on the sale of an active interest in a partnership or S corporation (generally)
- Items which are otherwise excluded or exempt from income under the income tax law, such as interest from tax-exempt bonds, capital gain excluded under IRC 121, and veterans benefits

Four Business Classifications

And the Limitations

TYPES OF TAXPAYERS	2025 THRESHOLD AMOUNT
Married filing jointly	$ 394,600
Married filing separately	$ 197,300
All others (Single, Head of Household, Trusts & Estates)	$ 197,300

	Most Trades or Businesses	Specified Service Trade or Business (SSTB)
Taxable income less than the Threshold Amount	**20% deduction**	**20% deduction**
Taxable income above the Threshold Amount, but within the phase-in range	Limitation phased-in	Deduction phased-out
Taxable income greater than the Threshold Amount, Plus $50,000 ($100,000 for MFJ)	**Wage/Capital Testing**	**No deduction**

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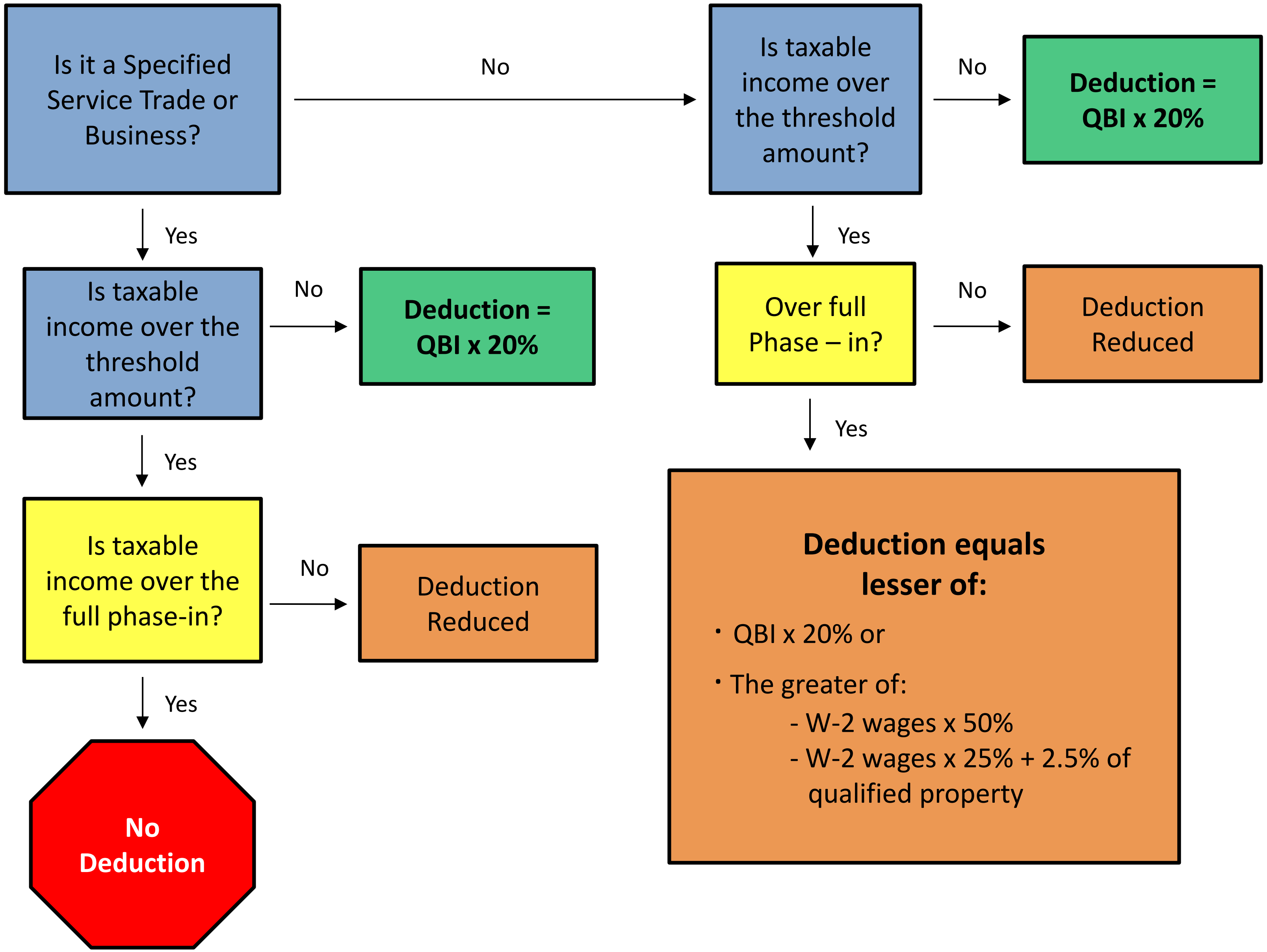
Is it a Specified Service Trade or Business?
No
Is taxable income over the threshold amount?
No
Deduction = QBI x 20%
Yes
Over full Phase – in?
No
Deduction Reduced
Yes
Deduction equals lesser of:
• QBI x 20% or
• The greater of:
- W-2 wages x 50%
- W-2 wages x 25% + 2.5% of qualified property
Yes
Is taxable income over the threshold amount?
No
Deduction = QBI x 20%
Yes
Is taxable income over the full phase-in?
No
Deduction Reduced
Yes
No Deduction

Calculation of the Deduction

Simplified

- W-2 Wages
  - Equal to wage expense
  - Does not include guaranteed payments or payments to independent contractors
- Qualified Property
  - Tangible property being depreciated (e.g. does not include land)
  - Depreciation period is the later of the regular depreciation period or 10-years
- Unadjusted Basis
  - Equal to basis immediately after acquisition
  - Not adjusted for depreciation (including bonus depreciation)
  - Not adjusted for § 179
  - The final regulations liberalize the use of § 754 for UBIA purposes

§ 199A, § 11011

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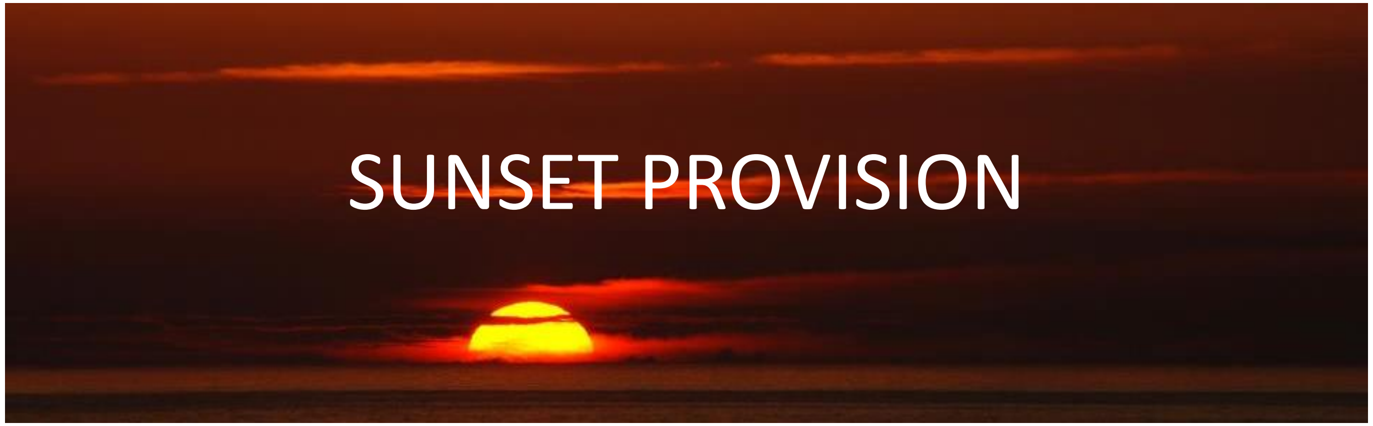
Termination

The Statute

(i) Termination.

This section shall not apply to taxable years beginning after December 31, 2025.



Congress seems likely to further extend or make permanent the deduction beyond 2025.

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Tax Alpha

Tax Bracket		Account Type
37%	35%	**Tax-Free**: Roth IRAs; Life Insurance; Tax-Exempt Interest Income
32%	24%	22%	**Tax-Deferred**: IRAs, 401(k)s, 403(b)s; Non-qualified Deferred Annuities
12%	10%	**Taxable**: Interest Income; Capital Gains; Qualified Dividends

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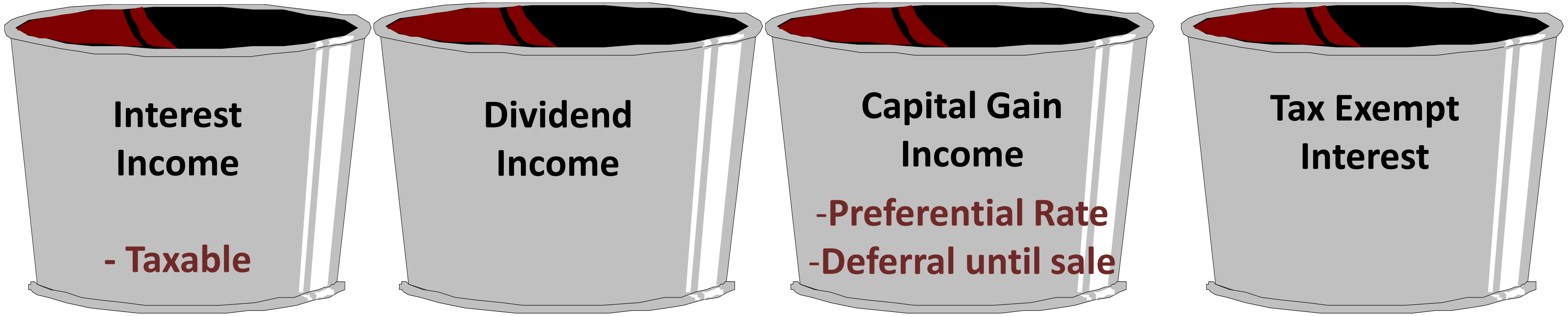
Tax Asset Classes



Interest Income

- ✓Money market
- ✓Corporate bonds
- ✓US Treasury bonds (exempt from state and local income taxes)

Attributes

- ✓Annual income tax on interest
- ✓Taxed at highest marginal rates

Dividend Income

- ✓Equity securities
- ✓Mutual Funds

Attributes

- ✓Qualified dividends at LTCG rate
- ✓Return of capital dividend
- ✓Capital gain dividends (for mutual funds)

Capital Gain Income

- ✓Equity Securities
- ✓Bonds, Mutual Funds, etc.

Attributes

- ✓Deferral until sale
- ✓Reduced capital gains rate for long term gains
- ✓Step-up basis at death

Tax Exempt Interest

- ✓Bonds issued by State and local Governmental entities

Attributes

- ✓Federal tax exempt
- ✓State tax exempt (Depends on state of issue and residence of holder)

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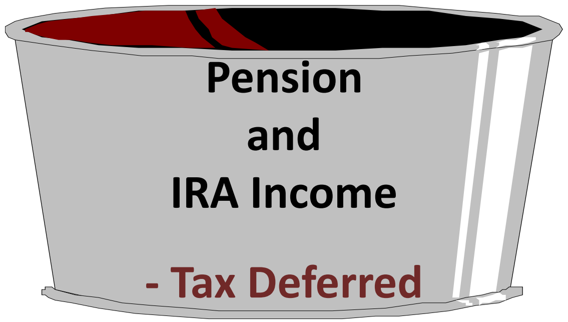
Tax Asset Classes (continued)



✓Pension plans
✓Profit sharing plans
✓Annuities
✓IRAs

Attributes

✓Tax-deferred growth during lifetime
✓RMD for IRA and qualified plans
✓No step-up

Real Estate

✓Depreciation tax shield
✓1031 exchanges
✓Deferral on growth until sale (depreciation recapture)
✓199A Deduction

Oil & Gas

✓Large up front IDC deductions
✓Depletion allowances

Roth IRA

✓Tax-free growth during lifetime*
✓No 70½ RMD
✓Tax-free distributions out to beneficiaries' life expectancy*

Life Insurance

✓Tax-deferred growth
✓Tax-exempt payout at death

* If certain conditions are met

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Taxation of Retirement Distributions

	Basis	Tax-Free Loans	Earnings
IRA[(1)]	Pro rata Method	N/A	Pro rata Method
ERISA Plan	Pro rata Method	N/A	Pro rata Method
Roth IRA[(2)]	Basis First	N/A	Earnings Follow
Non-qualified Annuity	Basis Follows	N/A	Earnings First
Life Insurance[(3)] Non-Modified Endowment Contract	Basis First	Available	Earnings Follow
Life Insurance[(4)] Modified Endowment Contract	Earnings First	N/A	Basis Follows

1. All IRAs are combined for the distribution computation
2. All Roth IRAs are combined for the distribution computation
3. Loans available, with interest to the extent of cash surrender
4. Each contract is treated separately for distribution purposes

“Flying Below the Radar”

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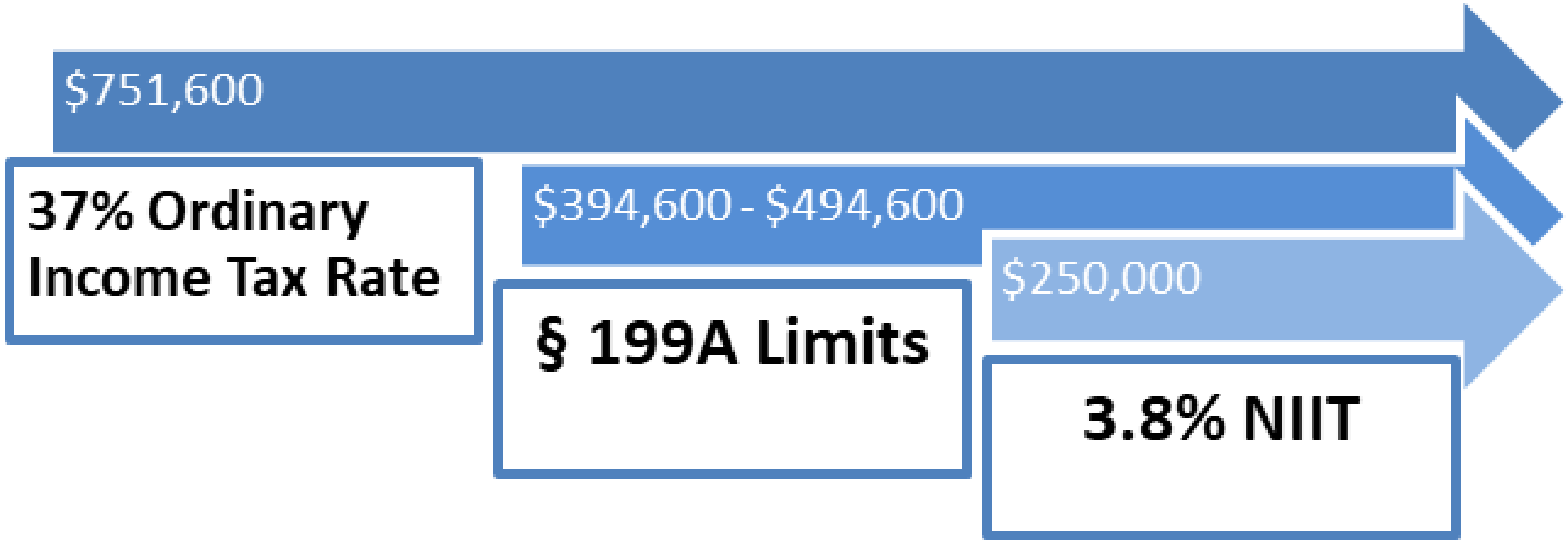
“Flying below the radar”



Thresholds for married filing jointly.

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Strategies

- Strategies:
  - Capital Gain Harvesting
  - Harvesting Capital Losses
  - Income smoothing strategies
  - Tax deferral strategies

- Maximize the benefit of tax rate arbitrage

- Remember: “Fly below the radar”

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Capital Gain Harvesting – Overview

- Capital Gain Harvesting Strategy:
  - Taxpayer expects to be in a higher tax bracket in the future
  - Sell assets this year, pays tax on the gains at the lower current tax rate and steps-up the basis on the assets to the sale price
  - Shortly thereafter, repurchases the assets and sells them whenever they would have been sold had the taxpayer not harvested gains
- Effect: Shifts recognition of part of the capital gain from the higher bracket future tax year to the lower bracket current tax year
  - Could save the taxpayer substantial amounts of CGs tax

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Capital Gain Harvesting – Tradeoffs

- On the surface, it appears that taxpayers should always harvest gains
- However, harvesting gains introduces a tradeoff between lower tax rates versus the loss of tax deferral
  - Tax is paid at a lower rate, but it is paid sooner
  - Need to determine a crossover point at which selling sooner makes more sense

    A way to conceptualize this would be to use a return on investment (ROI) approach

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Capital Gain Harvesting – Key Variables to Consider

- Time period between sales
- Difference in tax rates
- Growth rate of the asset
- Taxpayer's opportunity cost of capital
- Volatility of the investment

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Capital Gain Harvesting – Example

- Tom owns ABC company growth stock
  - Basis: $50,000
  - FMV: $150,00
- Tom is thinking ABC won't appreciate much more in value and expects to sell no later than Spring 2026
- Tom expects his income to increase in 2026 and therefore computes his capital gains tax rate will be lower in 2025:
  - 2025: 18.8%
  - 2026: 23.8%

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Capital Gain Harvesting – Example: Scenario 1

Scenario 1: No Gain Harvesting – Sells stock in 2026

	2025	2026
Stock Value	$ 150,000	$ 150,000
Less Basis		$ 50,000
Gain		$ 100,000
Tax @ 23.8%		$ 23,800
After-Tax Gain		$ 76,200
Total Value (gain + basis)	$ 150,000	$ 126,200

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Capital Gain Harvesting – Example: Scenario 2

Scenario 2: Gain Harvesting – Sells stock in 2022

	2025	2026
Stock Value	$ 150,000	$ 0
Less Basis	$ 50,000	
Gain	$ 100,000	
Tax @ 18.8%	$ 18,800	
After-Tax Gain	$ 81,200	
Total Value (gain + basis)	$ 131,200	

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Capital Gain Harvesting – Example

- Tom ends up with $5,000 more in the gain harvesting scenario ($131,200 - $126,200).
- Tom's rate of return on the tax paid in 2025 is 26.60% ($5,000 / $18,800).
- This is presumably far above Tom's opportunity cost of capital
  - Thus, Tom should harvest gains in 2025
  - However, the opportunity cost is key as it erodes the return on the "tax investment" made over time; i.e. this works well for Tom because he already planned to sell relatively soon

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Harvesting Capital Losses – Overview

- Harvesting Capital Losses: Selling assets at a loss and using those losses to offset capital gains realized on other assets
- Basic Strategy:
  - It reduces or eliminates tax on current capital gain
  - If the asset is repurchased, it gives the taxpayer a lower basis in the repurchased asset
  - Thus, it increases the amount of gain (current fair market value) that is recognized when the asset is later sold
  - Therefore, total gain/loss recognized is the same, but loss harvesting creates a kind of tax deferral (only a timing benefit)

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Harvesting Capital Losses – Key Issues

- “Wash sale” rule (IRC §1091)
- Diminishing value of capital losses
- Inefficiency of capital loss offsetting

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Harvesting Capital Losses –
Inefficiency of Harvesting Capital Losses

- In general, capital losses are more tax effective if they can be used to offset income taxed at higher tax rates (e.g. short-term capital gains and ordinary income allowed to a limited extent)
  – Thus, long-term losses used against short-term gains are more tax-efficient than short-term losses being used against long-term capital gains

	Short-Term Gain	Long-Term Gain
Short-Term Loss	NEUTRAL	INEFFECTIVE
Long-Term Loss	EFFECTIVE	NEUTRAL

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Harvesting Capital Losses – Strategies

- Buy stock of similar company
- Double-up “loss stock” – wait 31 days
- Double-up “loss stock” – enter into “cashless collar”
- Buy call option at-the-money

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Harvesting Capital Losses

- Jill is in the 23.8% long-term capital gains (LTCG) tax bracket
- Jill recognizes $100,000 of LTCG on Blackacre in 2025
- Jill harvests capital losses to net out the gain
  - She sells 1,000 shares of ABC stock with a basis of $300,000 for $200,000 (current fair market value).
- This $100,000 loss eliminates her LTCGs and saves her $23,800 of tax (0.238 x $100,000).

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Harvesting Capital Losses – Example

- Jill waits 31 days and repurchases the 1,000 shares of ABC stock at $200/share (current fair market value).
  - – Basis: $200,000
- In 2030, the FMV of the stock is $500,000
  - – She sells it and recognizes a gain of $300,000
  - – Pays tax of $71,400 ($300,000 x 0.238)

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Harvesting Capital Losses – Example

- If Jill had not harvested the loss and sold the original shares in 2030, she would have recognized gain of:
  - $100,000 on Blackacre, and
  - $200,000 on ABC stock in 2030 (her basis was $300,000 on the original shares)
- Assume Jill has a 7% opportunity cost of capital (before tax)

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Harvesting Capital Losses – Example

No Loss Harvesting:

Year	Gain Recognized	Tax Payable	FV @ 7%
2025	$100,000	$23,800	$33,381
2030	$200,000	$47,600	$47,600
Total	$300,000	$71,400	$80,981

Loss Harvesting:

Year	Gain Recognized	Tax Payable	FV @ 7%
2025	$0	$0	0$
2030	$300,000	$71,400	$71,400
Total	$300,000	$71,400	$71,400

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Harvesting Capital Losses – Example

- By harvesting losses, Jill pays $9,581 less tax in future value terms than she would have paid without loss harvesting ($80,981-$71,400).
- Key Factors:
  - Time period between the two sales (the longer the better the economic benefit of loss harvesting)
  - Taxpayer's opportunity cost of capital (the higher the better the economic benefit of loss harvesting)
  - The tax rates that apply to the two sales
  - The market price of the asset whether the assets appreciate or depreciate (particularly when out of the market)

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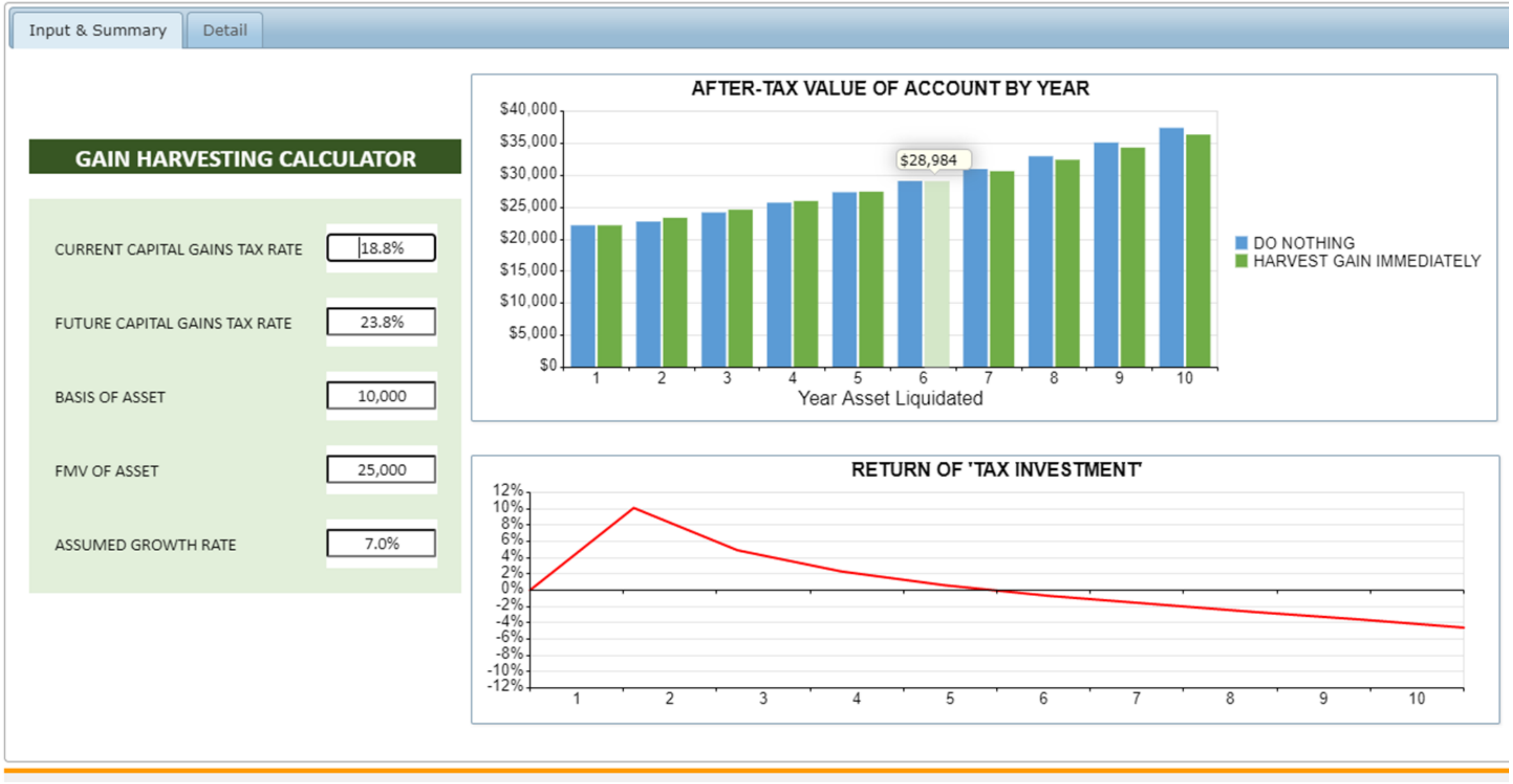
Gain Harvesting



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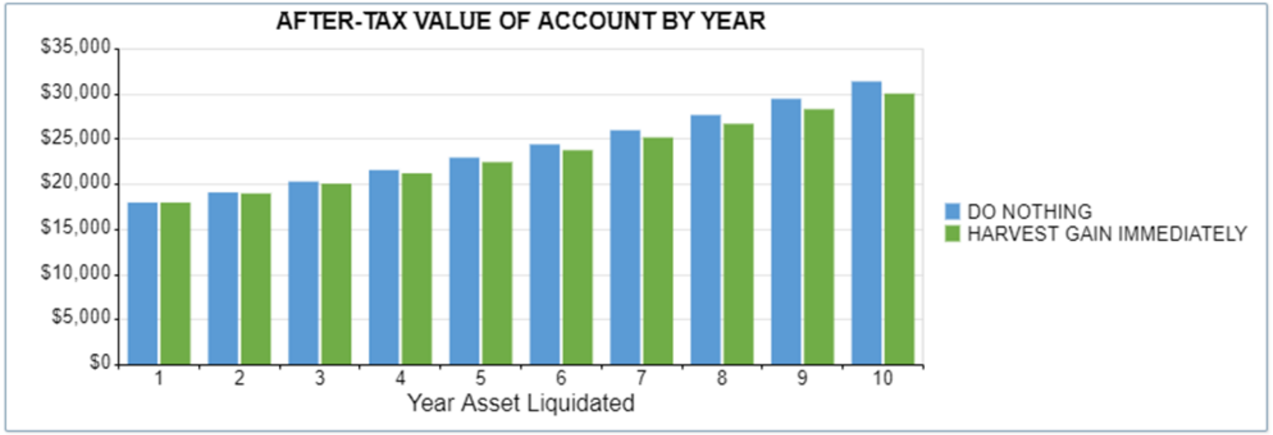
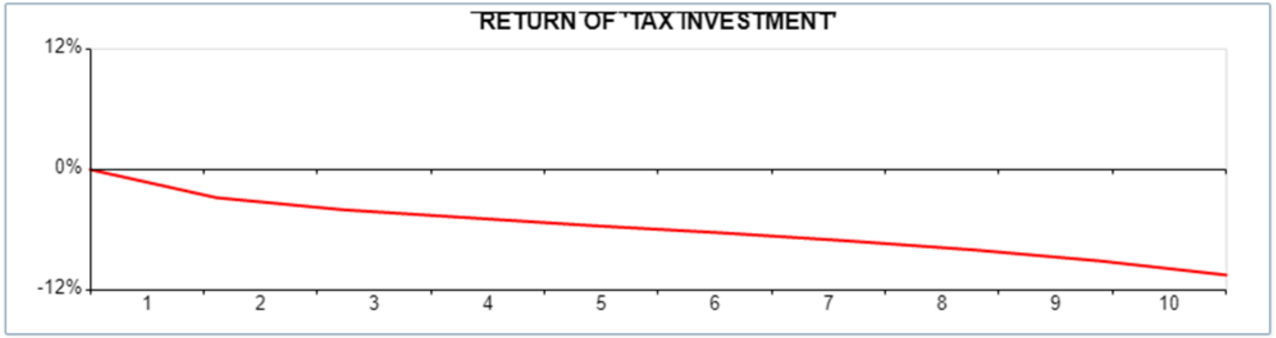
Gain Harvesting

Input & Summary | Detail

GAIN HARVESTING CALCULATOR

CURRENT CAPITAL GAINS TAX RATE	20.0%
FUTURE CAPITAL GAINS TAX RATE	20.0%
BASIS OF ASSET	10,000
FMV OF ASSET	20,000
ASSUMED GROWTH RATE	7.0%





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Medicare Premiums – Part B

If your yearly income in 2023 was:			
File individual tax return	**File joint tax return**	**File married & separate tax return**	**You pay each month (in 2025):**
$106,000 or less	$212,000 or less	$106,000 or less	$185.00
above $106,000 up to $133,000	above $212,000 up to $266,000	not applicable	$259.00
above $133,000 up to $167,000	above $266,000 up to $334,000	not applicable	$370.00
above $167,000 up to $200,000	above $334,000 up to $400,000	not applicable	$480.90
above $200,000 and less than $500,000	above $400,000 and less than $750,000	above $106,000 and less than $394,000	$591.90
$500,000 or above	$750,000 or above	$394,000 or above	$628.90

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Medicare Premiums – Part D

If your filing status and yearly income in 2023 was		
File individual tax return	**File joint tax return**	**You pay each month (in 2025)**
$106,000 or less	$212,000 or less	your plan premium
above $106,000 up to $133,000	above $212,000 up to $266,000	$13.70 + your plan premium
above $133,000 up to $167,000	above $266,000 up to $334,000	$35.30 + your plan premium
above $167,000 up to $200,000	above $334,000 up to $400,000	$57.00 + your plan premium
above $200,000 and less than $500,000	above $400,000 and less than $750,000	$78.60 + your plan premium
$500,000 or above	$750,000 and above	$85.80 + your plan premium

Other Strategies

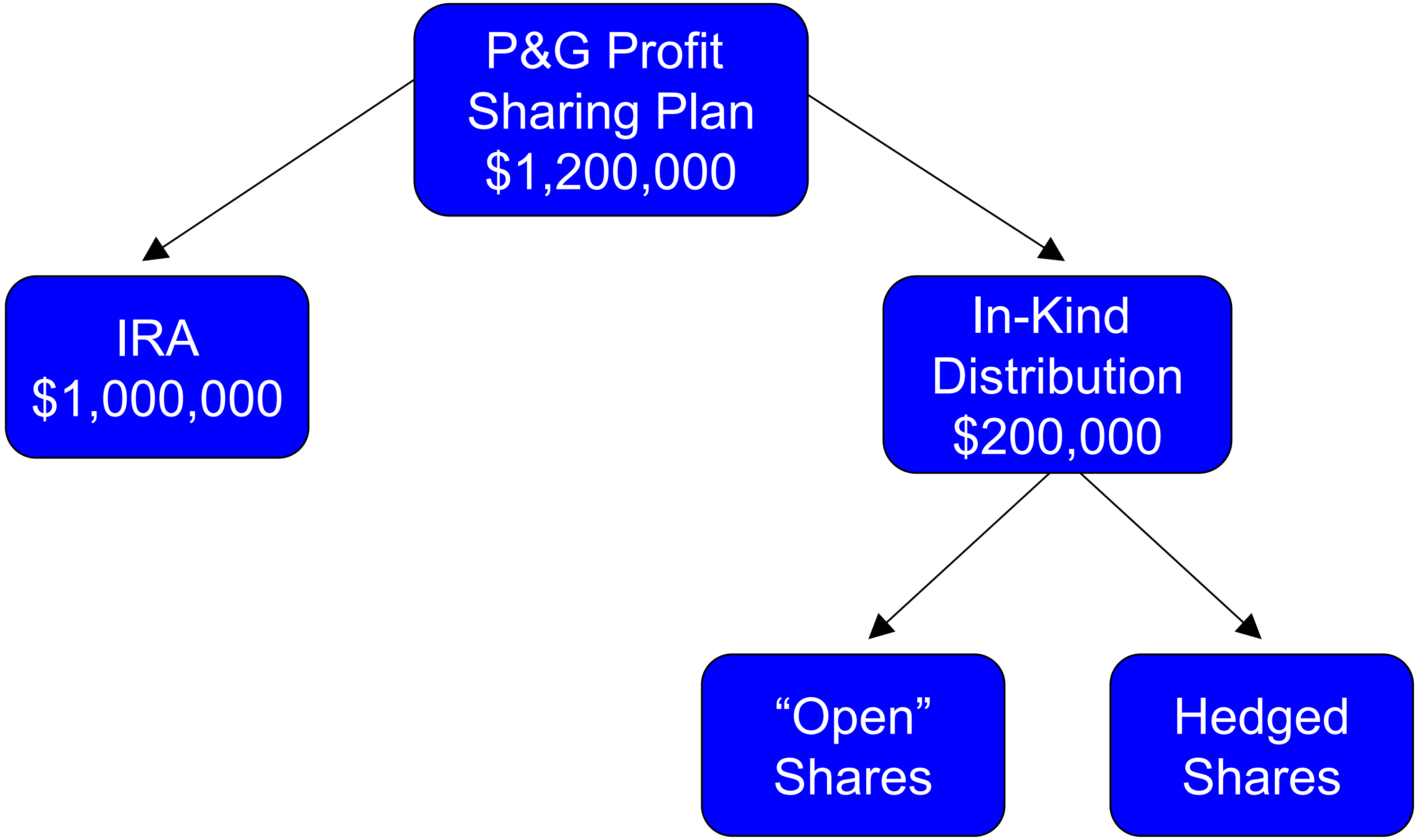
- Roth Conversions
- NUA Opportunities
- Annuities
- Life Insurance
- Estate Planning Techniques (Bypass Trust)

Net Unrealized Appreciation (NUA)

Net Unrealized Appreciation

- Key issues
  - Triggering events
    - ➢On account of employee's death
    - ➢After the employee attains age 59½
    - ➢On account of employee's separation from service
    - ➢After the employee has become disabled (within the meaning of section 72(m)(7)
  - Taxation of rollout
    - ➢Ordinary income recognized on basis
    - ➢Difference between Fair Market Value (FMV) at rollout and basis is Net Unrealized Appreciation (NUA)
    - ➢NUA is taxed long-term capital gain tax rates (0%/15%/20%)

Net Unrealized Appreciation



Annuities

Nonqualified Tax Deferred Annuities

- Strategy
  - A taxpayer, during higher tax bracket years, invests in deferred annuities
    - Thereby reducing taxable income, and thus, income taxes and NIIT
  - Later, when the taxpayer is in lower tax bracket years, the payments from the deferred annuities begin
    - Thus, smoothing out income and subjecting the taxpayer to lower taxes

Nonqualified Tax Deferred Annuities

- Benefits
  - Earnings accumulate tax-free and are not taxed until withdrawn
  - “Flying below the radar”

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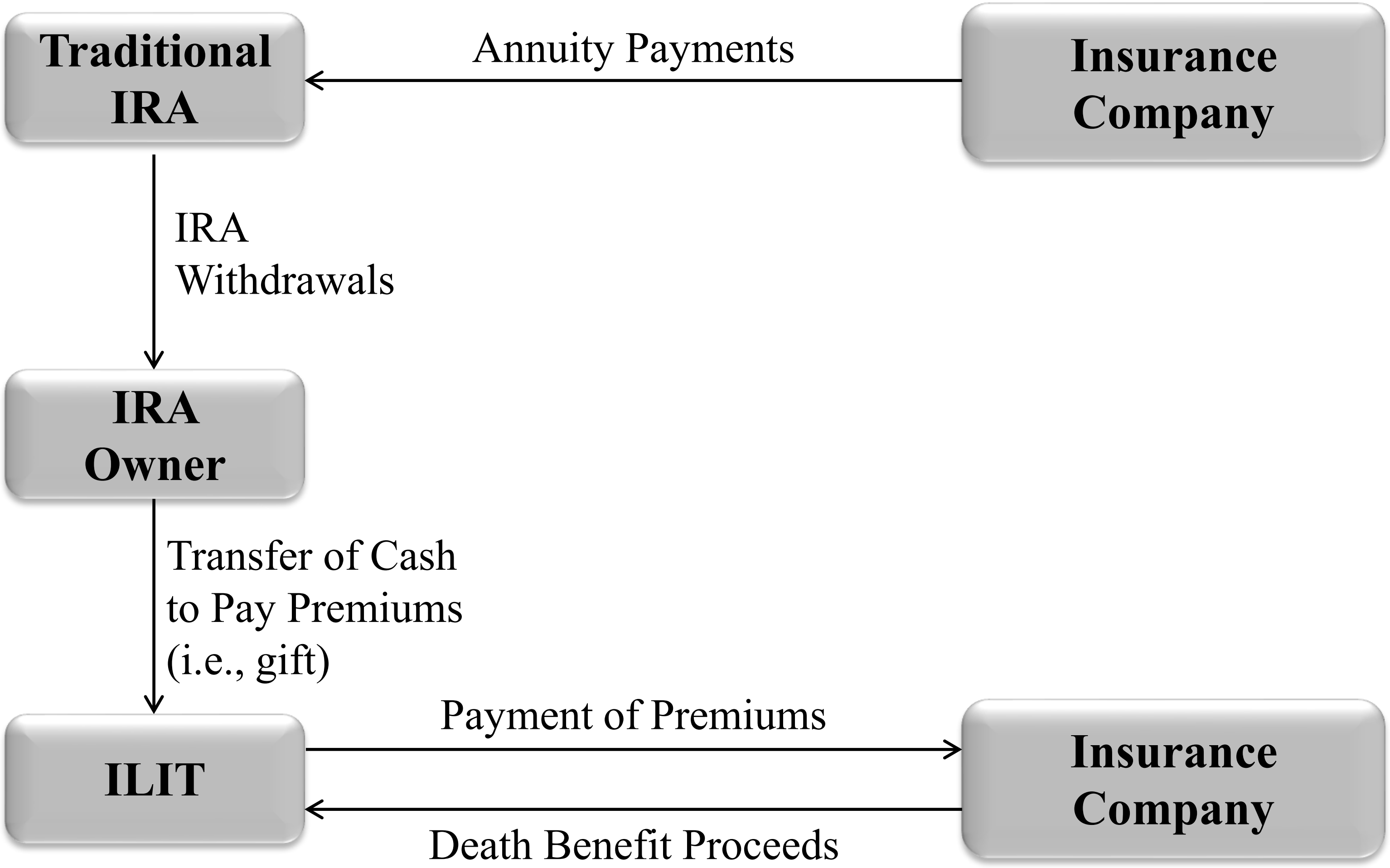
The IRA-Annuity Strategy

- IRA assets are used to purchase lifetime annuity contract
- Every year as annuity payments are credited to the IRA and then distributed to the account owner, the IRA distributions are used to pay premiums on a life insurance policy held in an Irrevocable Life Insurance Trust (ILIT)
- At the account owner’s death, neither the IRA (due to the cancellation-at-death feature of the annuity) nor the ILIT will be included in the account owner’s taxable estate

The IRA-Annuity Strategy



The IRA-Annuity Strategy

Inside Taxable Estate

Traditional IRA $0

Because the annuity cancels at death, the IRA does not have any value for estate tax purposes

Outside Taxable Estate

ILIT $2,000,000

Because the trust is irrevocable and the gifts are "complete gifts" for gift tax purposes, none of the policy proceeds will be included in the taxable estate (provided the transferor has no "incidents of ownership" over the policy)

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The IRA-Annuity Strategy

IRA Only

Yr	IRA	Estate Tax	Trust (Brokerage Account)	**Net Wealth to Family**
1	$ 970,000	$ (485,000)	$ -	**$ 485,000**
5	$ 827,478	$ (413,739)	$ 305,431	**$ 719,170**
10	$ 585,507	$ (292,753)	$ 699,910	**$ 992,663**
15	$ 246,129	$ (123,065)	$ 1,209,399	**$ 1,332,463**
20	$ -	$ -	$ 1,731,151	**$ 1,731,151**
25	$ -	$ -	$ 2,235,864	**$ 2,235,864**
30	$ -	$ -	$ 2,887,726	**$ 2,887,726**

IRA-Annuity Strategy

Yr	IRA	Estate Tax	Trust (Life Insurance)	**Net Wealth to Family**
1	$ -	$ -	$ 2,000,000	**$ 2,000,000**
5	$ -	$ -	$ 2,000,000	**$ 2,000,000**
10	$ -	$ -	$ 2,000,000	**$ 2,000,000**
15	$ -	$ -	$ 2,000,000	**$ 2,000,000**
20	$ -	$ -	$ 2,000,000	**$ 2,000,000**
25	$ -	$ -	$ 2,000,000	**$ 2,000,000**
30	$ -	$ -	$ 2,000,000	**$ 2,000,000**

ASSUMPTIONS:
Pre-Tax Growth Rate on IRA = 7.00%
After-Tax Growth Rate on Brokerage Account = 5.25%
Combined Income Tax Rate = 45.00%
Beginning IRA balance = $1,000,000
Annual Pre-Tax Withdrawal From IRA = $100,000
Annual Life Insurance Premium = $55,000

Oil & Gas Investments

Oil & Gas Investments

- Key Tax Concepts
  - Intangible Drilling Costs (IDCs) – IRC § 263(c)
  - Exception to the Passive Loss Rules – IRC § 469(c)(3)
  - IRC § 179 Deduction
  - Bonus Deprecation
  - Depletion

Oil & Gas Investments

- Intangible drilling costs (IDCs) provide a large immediate income tax deduction (up to 85% of the initial investment)
  - Losses, if any, created as a result of IDCs will be ordinary (thus lowering a taxpayer's AGI)
    - Must be a general partner in the first year
  - Possible AMT add-back issues if IDCs exceed 40% of AMTI

Oil & Gas Investments

- Example
  - George, a single taxpayer, recently invested $100,000 in a working interest in an oil well.
  - According to the oil well driller's accountants, 80% of the initial investment can be deducted in the first year as an "intangible drilling cost" ("IDC").
  - Assuming that George has $80,000 of net investment income subject to the 3.8% NIIT and is in the 37% marginal income tax bracket, below is a summary of the total tax savings from the oil well investment

Income tax savings from IDC deduction	$29,600	$100,000 x 80% x 37%
NIIT savings from the IDC deduction	$3,040	$100,000 x 80% x 3.8%
Total tax savings	$32,640	

Life Insurance

Retirement Asset & Tax Comparison: With vs. Without Insurance

Scenario Assumptions:

- John & Susan retire at age 65
- Total retirement assets:

  $3M in IRA, $1M in brokerage, $1M in life insurance (cash value)

Annual income need: $250,000

- RMDs begin at 73, taxed as ordinary income
- Assume 5% growth and 25% marginal tax rate

10-Year Retirement Projection: Taxable Income and Net Spendable Yearly Averages (Ages 65–74):

Without Life Insurance:

- IRA withdrawals: $250,000/year
- Taxes paid: $62,500/year
- Net spendable income: $187,500

With Life Insurance Strategy:

- IRA withdrawals: $125,000/year
- Policy loans: $125,000/year (tax-free)
- Taxes paid: $31,250/year
- Net spendable income: $218,750

Loan Strategy from $1M Life Insurance Cash Value

Illustrative Logic Behind $125K Annual Loans:

- Starting cash value at retirement: $1,000,000
- Annual loan target: $125,000 for 10 years ($1.25M total)
- Max loan-to-value typically 85%–90% (~$900,000 accessible)
- Strategy depends on policy growth offsetting loan interest
- Assumes net crediting rate ≥ loan rate (e.g., both ~5%)
- Loans structured as participating or offset loans
- Death benefit provides cushion to prevent policy lapse
- Requires in-force management and appropriate design
- No tax due if policy stays in force (IRC §72, §7702)

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