The End Is Near: Plan or Be Damned

Kathleen Hartman | 11-08-00 |

A year ago, financial-service professionals were focused on getting through Y2K with their clients' portfolios intact. This year, although it's business as usual, advisors still have their hands full. For some, in fact, it is the busiest time of the year, as many services they provide will make a big difference come April 15.

A call to advisors brought forth a wealth of year-end planning ideas. So many, in fact, that we'll highlight them in two parts. Some advisors offered classic strategies that are easy to forget in the holiday shuffle. Others provided more complex strategies that will take the remainder of the year to wrap up. Overall, it's hard to imagine a client who can't benefit from one or more of these suggestions.

Gifting with Stock

Although the wobbly stock market may have clients feeling somewhat less generous, that consideration is typically still offset by the need for tax relief and the client's abiding interest in making charitable gifts. Consequently, Sheri Robinson, of Haines Financial Advisors in Birmingham, Ala., recommends that advisors make gifts of appreciated stock by late November in order to give brokerage firms time to execute the transfer.

Robinson notes that low-basis stock is, regardless of the market, always an asset to consider gifting with. Such stock has often been inherited by, or gifted to, clients. If it was a gift, the client may have been hesitant to sell the stock, so this method may provide a psychological benefit as well as a tax benefit. Nowadays, Robinson says, most major charities have multiple brokerage accounts so that the transfer process is relatively painless. Indeed, as charities make their year-end appeals, it is important for clients to be reminded of this strategy, rather than allowing them to write a check.

Perhaps clients are charitably inclined, but they haven't had the time to decide on a recipient. In this case, establish an account and give the stock to a donor-advised fund, such as

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Gifting with Mutual Funds

Mark Wilson of Tarbox Equity, Inc., in Newport Beach, Calif., makes a pitch for charitable giving with mutual funds. While a bit trickier, perhaps, than working with individual stocks, Wilson notes that funds that are going to make large capital-gains distributions, especially short-term gains, are terrific assets to give to a charity.

Wilson acknowledges that capital-gains distribution information is rarely easy to come by. He praises some fund families, such as Alger, for providing estimates on their Web site. Other fund groups provide this information during conference calls or in correspondence with advisors. Still, in many instances, Wilson's firm will simply make persistent phone calls, hoping to get wind of the distribution before it takes place.

Like many advisors, Robinson also reminds clients to make annual exclusion gifts. Rather than suggest this in isolation, though, she makes it part of an estate planning process, so that clients have the ability to see estate tax projections and understand the reasons for giving--or not.

Steve Wightman of Lexington Financial Management in Lexington, Mass., is fond of establishing charitable remainder trusts with appreciated assets as a year-end planning technique. He suggests that high-net-worth clients use CRTs for education funding, in which case the donor not only avoids capital gains tax, but also enjoys a substantial charitable tax deduction. The income stream is taxed at the beneficiaries' rate, in this case the clients' children, and looking forward, the asset has been removed from the estate, so there is no taxable event upon death.

Turning a Bad Market into a Good Opportunity

Almost every year, some segments of the stock and bond markets suffer declines. Last year it was real estate and long bonds. This year, almost every international fund category has declined, with Asia and the Pacific Rim taking the biggest hits. Telecommunications and technology stocks have also been experiencing large losses. Advisors such as Steve Wightman are fond of techniques that use stock or fund losses to offset the year's gains.

Wightman notes that long-term losses must first be applied against long-term gains. After that, $3,000 of excess loss can be applied to the year's short-term gains. If a client has neither long-term nor short-term gains, then $3,000 can be applied A'as an ordinary income deduction.A☐

Wightman cautions against triggering wash rules by repurchasing the same security within 30 days. He suggests that advisors A'weigh the tax savings against the risk of the stock rebounding.A☐ In today's volatile market, clients may be more worried than ever about missing a market spike. For such clients, Wightman suggests purchasing call options. If the stock spikes, the client can still reap some profits.

Advisor Gayle Buff, of Buff Capital Management in Newton, Mass., agrees that stock sales are a major year-end planning technique. She says if the downtrodden stock is in an industry she favors for a comeback, then she will recommend buying another stock in the same industry. For example, Buff points to Home Depot HD, which is currently down more than 40% for the year. Instead of crossing her fingers for 31 days, Buff recommends that clients who sell Home Depot for tax purposes buy Lowe's Companies LOW, which, like many stocks in the home-supply industry, is well off its yearly highs.

Losses, Gains, and Mutual Funds

Robert Zimberg, of Financial Mountain Inc., in Boulder, Colo., applies the same planning technique to mutual funds. While he says that A'there are no strict rules,A☐ he looks for funds with year-to-date losses greater than 20% combined with large unrealized capital gains. Prime candidates for this category are manager departures after a disappointing year. Oftentimes, a new fund manager will clean out the portfolio, thus booking unrealized capital gains. Of course, fund holdings with unrealized losses can also be good candidates for selling.

Zimberg notes that this process can help him rebalance his allocation mixes. In such cases, the client carries a higher tax basis into retirement. Careful planning can accomplish a dual purpose.

Much like his charitable-giving technique, Mark Wilson closely watches clients' mutual funds for impending capital-gains distributions. In this case, however, he is looking to sell the fund before the gain is distributed. Admittedly, this is not an easy strategy and it is sometimes discouraged by fund companies. But, it can make a world of difference, especially if Wilson's client purchased the fund recently or if the expected distribution is a sizable percentage of the fund's NAV.

Wilson warns advisors, however, to be alert to possible redemption fees with this strategy. He also recommends that when undertaking partial fund sales, advisors should specify share lots in order to further control the tax event. Lastly, Wilson points out that the wash sale rule applies only when the security is being sold at a loss. If the sale is a gain, you can buy the fund back after the distribution with no penalties.

Part two will cover many additional ideas, including those concerned with retirement plans.

Your Thoughts

Do you have a charitable-giving or investment-related strategy to share? Let us know in our Retirement Planning forum.

Questions and comments about this article should be directed to site manager Jerry Kerns.