Franklin|Madison
PRIVATE WEALTH

How Forward-Looking Tax Planning

Kept Several Financial Decisions Within a $20,000 Tax Budget

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The issue wasn't whether the tax return would be prepared correctly

Based on what we've just calculated, it looks like you may have been overpaying—not necessarily because your accountant prepared an inaccurate return, but because no one was evaluating your financial decisions before the tax year ended.

Here's what that looked like for a client whose accountant, like yours, was primarily reporting what had already happened.

The client had accumulated substantial unrealized gains inside a taxable investment account. He wanted to begin reducing a concentrated position and repositioning the portfolio.

At the same time, we were evaluating a Roth conversion and reviewing a Roth IRA contribution he'd already completed earlier in the year.

Each decision made sense by itself.

Selling investments could reduce concentration risk and improve the portfolio.

Completing a Roth conversion could shift money from a tax-deferred retirement account into a Roth account.

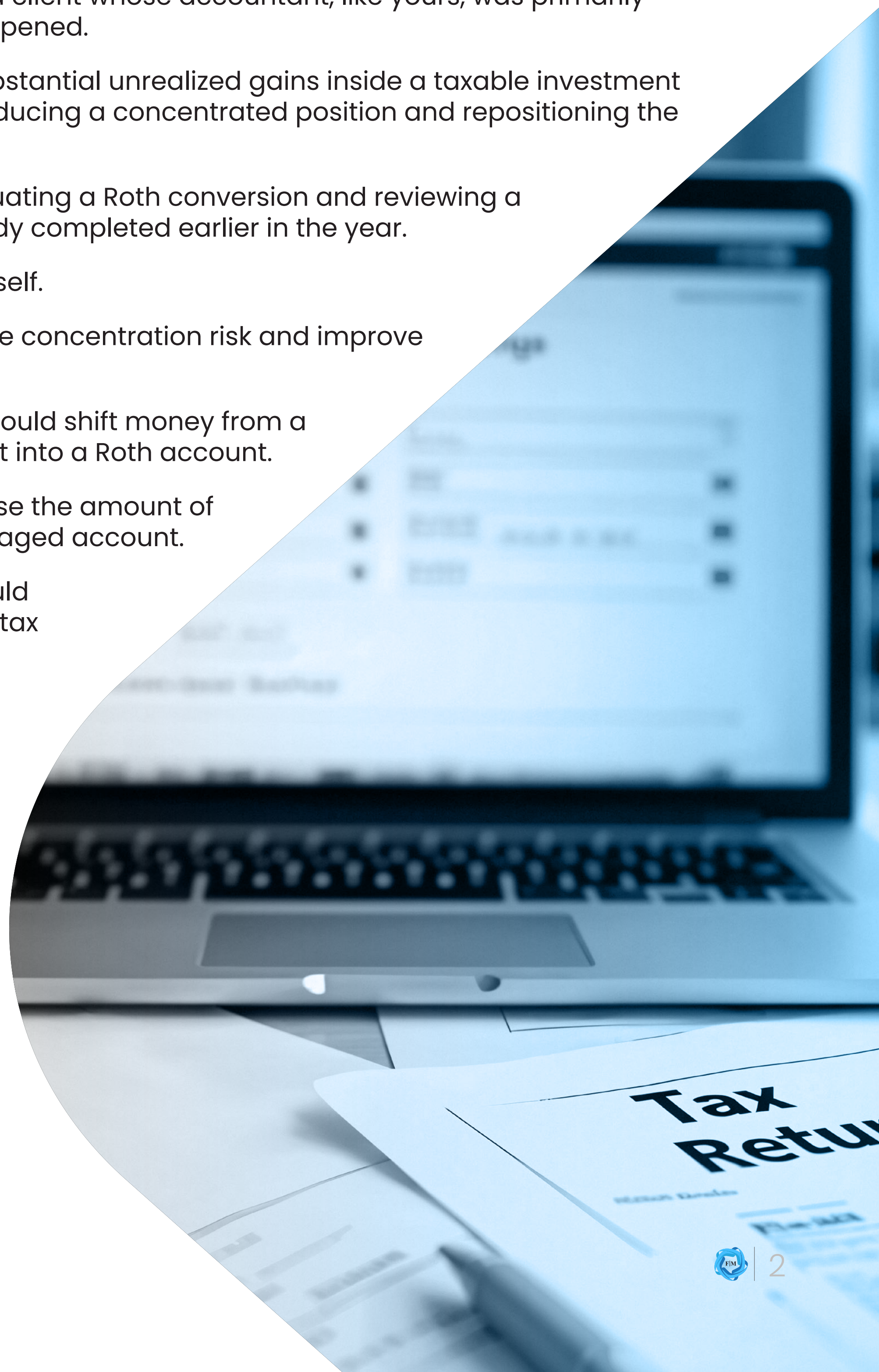
Funding a Roth IRA could increase the amount of money growing in a tax-advantaged account.

However, all three decisions would eventually appear on the same tax return.

The investment gains could affect the cost of the Roth conversion. Together, the gains and conversion could also increase the client's income enough to make the Roth IRA contribution ineligible.

The problem wasn't that any one decision was obviously wrong.

The problem was that several reasonable decisions were competing for the same tax capacity.



What the investment statement didn't show

The client's taxable account contained approximately $357,000 of unrealized long-term capital gains.

That number represented appreciation that hadn't yet been recognized for tax purposes.

As long as the investments remained unsold, those gains generally wouldn't appear on the client's tax return. However, the tax consequences would become real once the positions were sold.

The client didn't need to liquidate the entire portfolio.

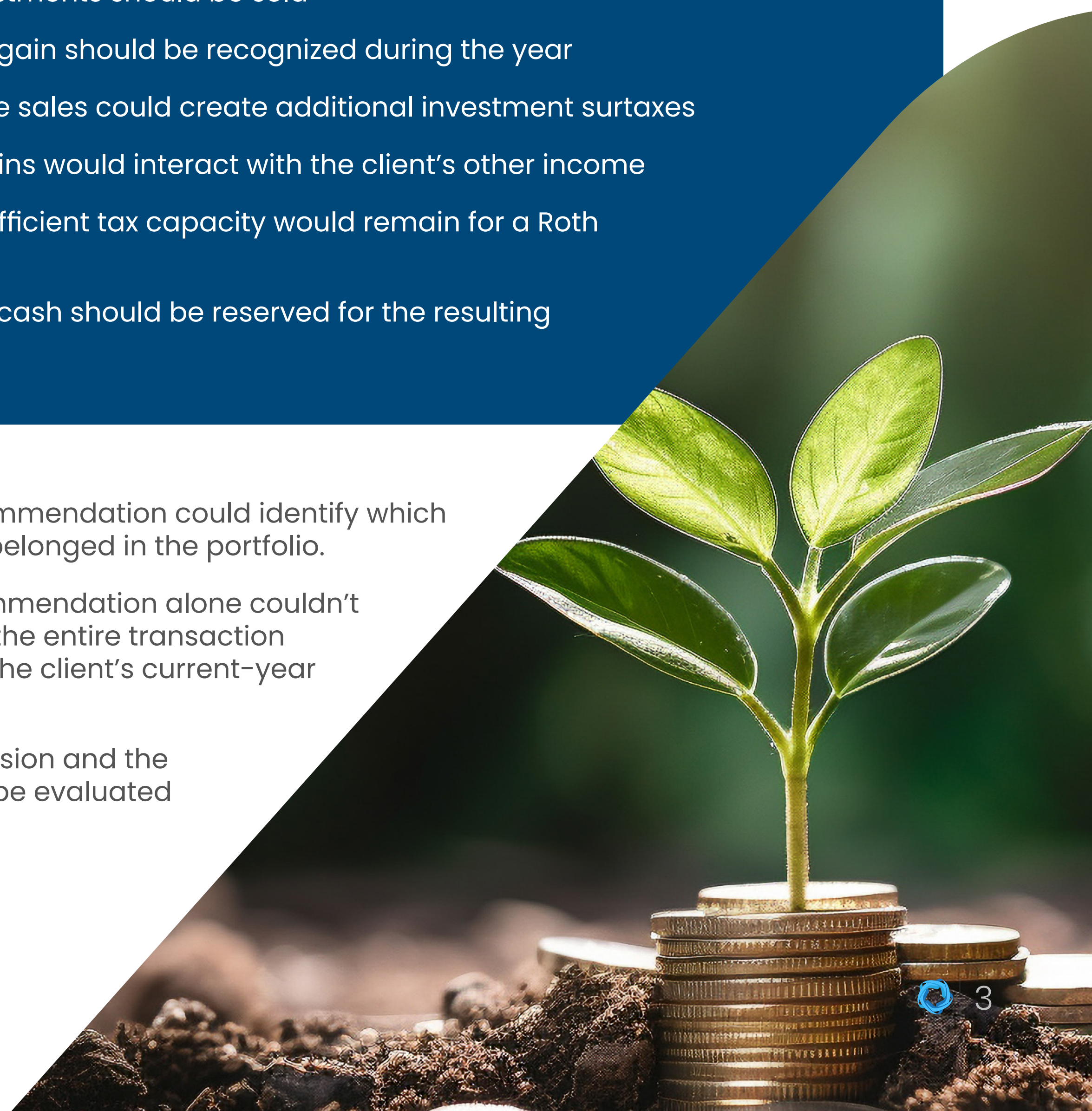
Nevertheless, repositioning the account would require deciding:

- Which investments should be sold
- How much gain should be recognized during the year
- Whether the sales could create additional investment surtaxes
- How the gains would interact with the client's other income
- Whether sufficient tax capacity would remain for a Roth conversion
- How much cash should be reserved for the resulting liability

An investment recommendation could identify which holdings no longer belonged in the portfolio.

However, that recommendation alone couldn't determine whether the entire transaction made sense within the client's current-year tax picture.

The investment decision and the tax decision had to be evaluated together.



Why tax preparation couldn't answer the question in time

Tax preparation is generally backward-looking.

After the year ends, tax documents show which investments were sold, how much gain was realized, how much was converted from an IRA, and which retirement contributions were completed.

The accountant can then report the transactions and calculate the resulting liability.

That work is important.

However, accurate reporting after the year ends doesn't answer the planning questions that existed before the transactions occurred.

By the time the tax return was prepared:

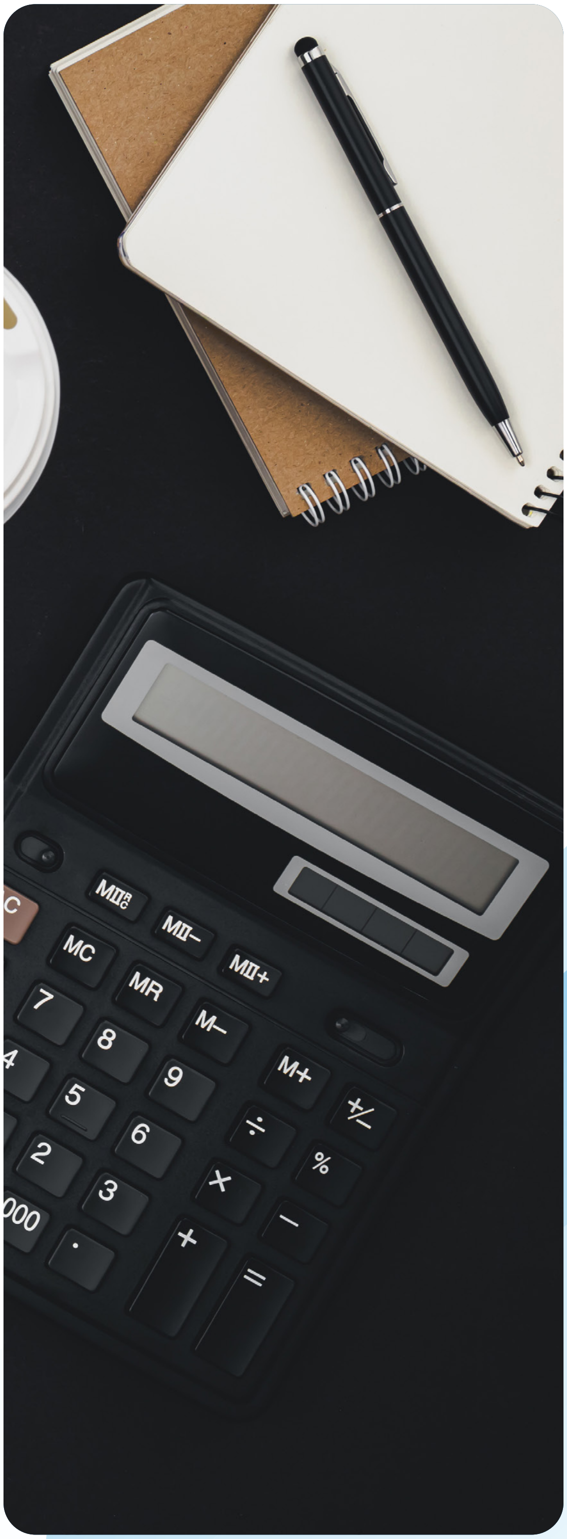
- The investment gains would already have been realized
- The Roth conversion generally couldn't be reversed
- The client's income for the year would already be established
- The Roth IRA contribution might already require a correction
- The opportunity to select a different combination of transactions could have passed

The tax return could explain what the client owed.

It couldn't go back and change the decisions that created the liability.

What would it mean to discover during tax season that several individually reasonable decisions had combined to create a result you never intended?

That was the outcome we wanted to prevent.



We started with the amount of tax the client was willing to accept

The goal wasn't to avoid realizing every capital gain.

Doing nothing would have allowed the client to defer the tax. However, it also would have left the concentrated investment position unchanged.

Similarly, the goal wasn't to complete the largest possible Roth conversion.

A larger conversion might move more money into a Roth account, but it could also increase the tax rate applied to the conversion, reduce flexibility for the investment sales, or create a larger current-year liability than the client wanted.

There wasn't one transaction that automatically maximized every outcome.

Therefore, we began by establishing a planning constraint.

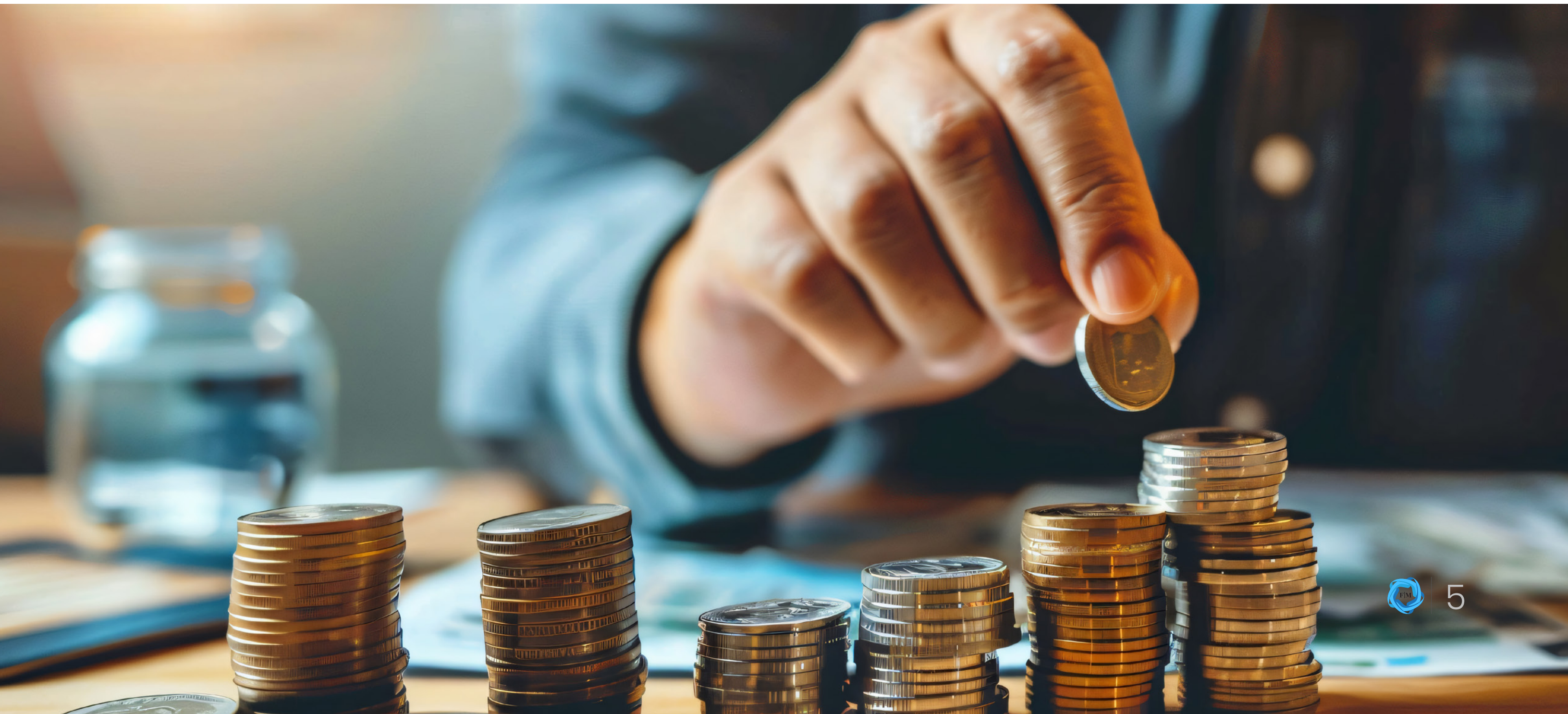
The client wanted the additional taxes associated with the proposed investment sales and Roth conversion to remain below approximately $20,000.

That amount became the client's tax budget for the strategy.

The tax budget didn't mean the final liability could be predicted perfectly. Investment prices, realized gains, income, deductions, and other activity could still change.

Nevertheless, it gave us a framework for comparing the available choices.

Instead of asking how much stock the client could sell or how much he could convert in isolation, we could determine which combination of transactions best supported the broader plan.



How we evaluated the opportunity

We built a forward-looking tax projection using the information available at the time.

The analysis considered:

- The client's projected ordinary income
- The cost basis of the investments being considered for sale
- The amount of long-term capital gain each sale could create
- The federal tax rate applied to those gains
- Potential net investment income tax exposure
- Pennsylvania income taxes
- The client's current and projected marginal tax brackets
- The amount being considered for a Roth conversion
- The income limitations affecting the Roth IRA contribution
- Available cash for federal and state tax payments

Most importantly, the proposed transactions weren't modeled separately.

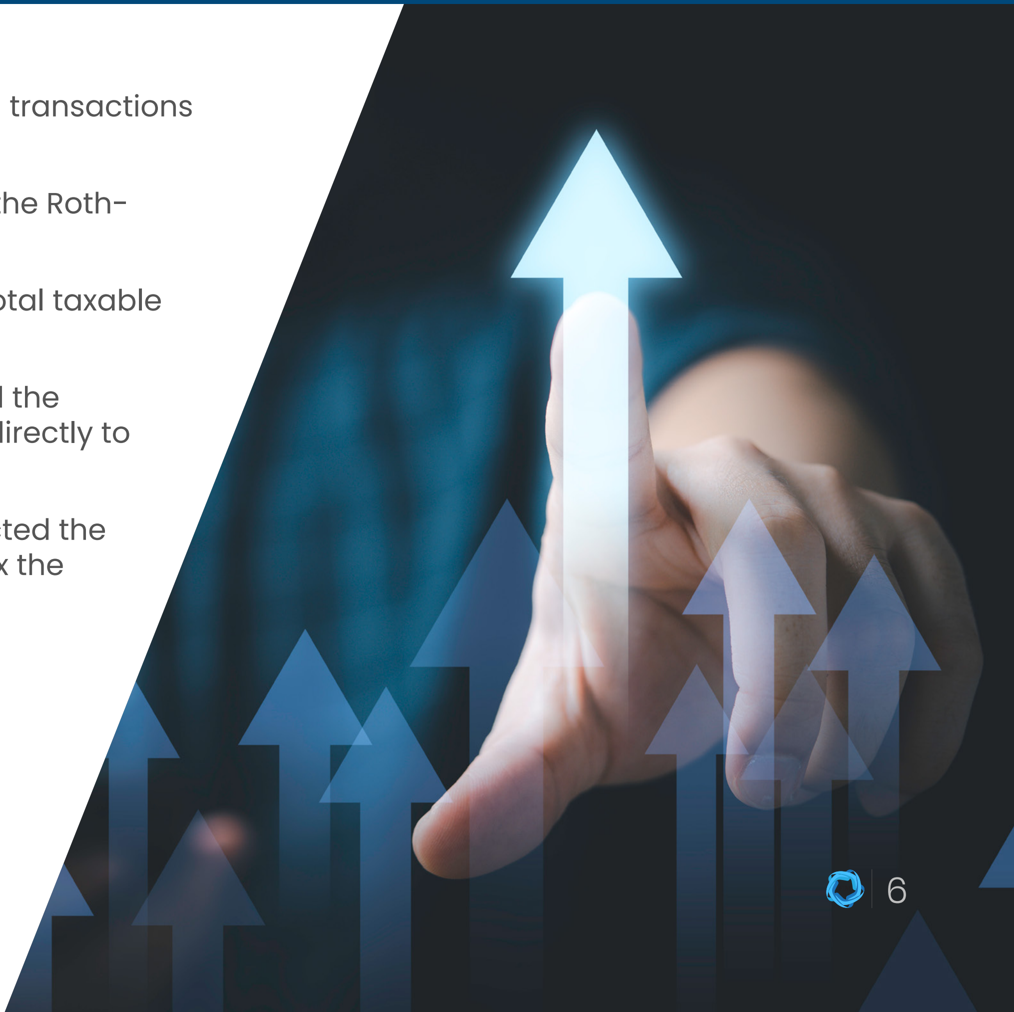
The investment sales affected the Roth-conversion opportunity.

The Roth conversion affected total taxable income.

The combined income affected the client's eligibility to contribute directly to a Roth IRA.

Meanwhile, each decision affected the amount of federal and state tax the client needed to reserve.

The projection allowed us to see those relationships before implementation.



The initial strategy

Based on the first projection, we developed a coordinated strategy that included approximately:

- $47,000 of realized long-term capital gains
- A $30,000 Roth conversion
- The recharacterization of an $8,000 Roth IRA contribution
- $15,800 of projected additional federal and state taxes

The projected liability remained within the client's approximately $20,000 tax budget.

This allowed the client to begin repositioning the taxable portfolio while also using some of the remaining tax capacity for a Roth conversion.

The analysis also identified a separate issue.

The client had previously contributed $8,000 to a Roth IRA. However, the additional income generated by the planned investment sales and conversion was expected to make him ineligible to complete the direct Roth contribution.

The contribution itself wasn't necessarily the problem when it was made.

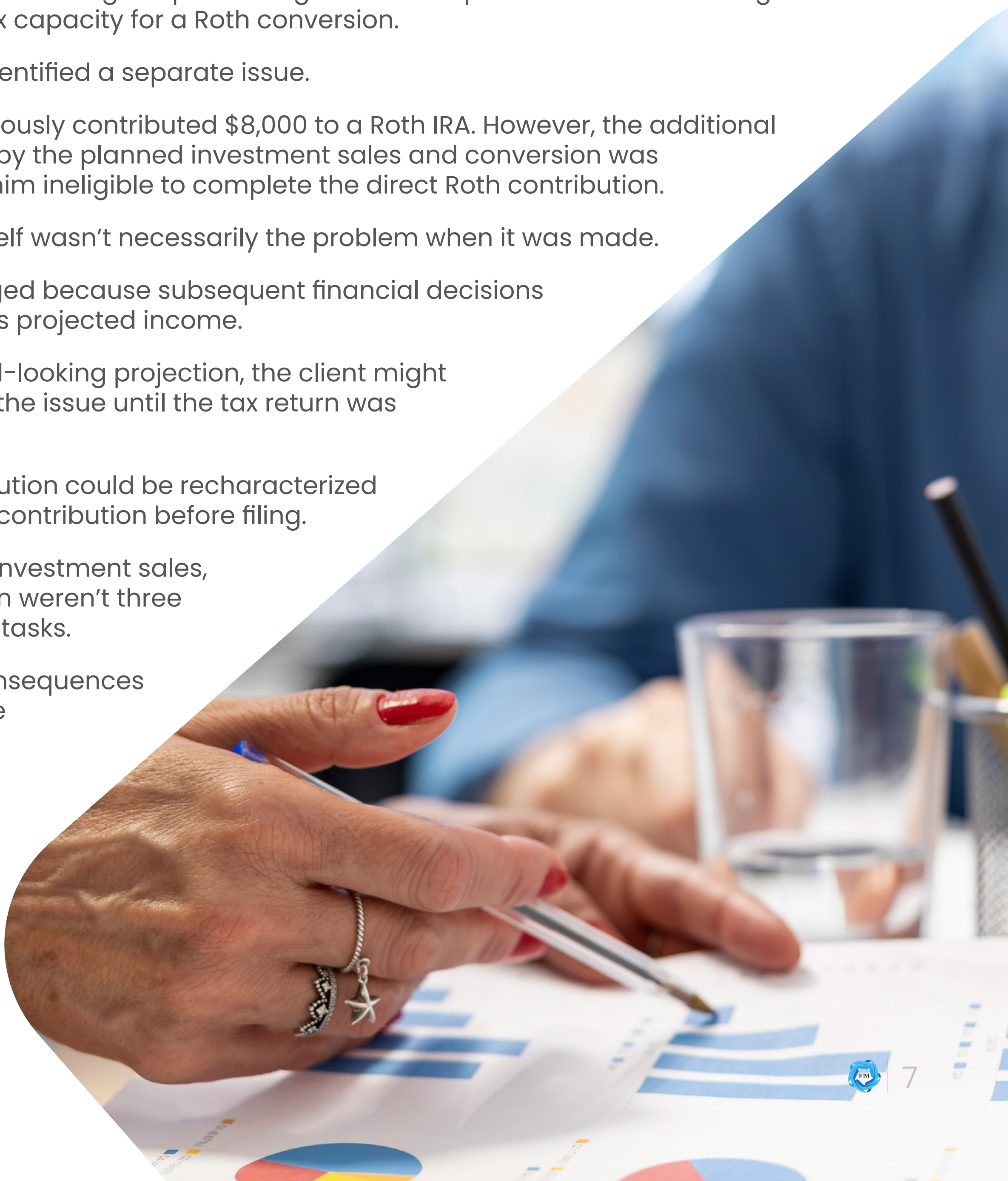
The problem emerged because subsequent financial decisions changed the client's projected income.

Without the forward-looking projection, the client might not have identified the issue until the tax return was prepared.

Instead, the contribution could be recharacterized as a traditional IRA contribution before filing.

The IRA correction, investment sales, and Roth conversion weren't three unrelated planning tasks.

They were three consequences of the same income projection.



The investment strategy was implemented deliberately

Once the client's cost-basis information was available, we could evaluate which positions should be sold and the amount of gain each transaction was expected to create.

The portfolio didn't need to be repositioned all at once.

Attempting to eliminate the entire $357,000 embedded gain during a single tax year could have produced a substantially larger liability and consumed tax capacity that might have been more valuable in future years.

Instead, the client began the repositioning process gradually.

The sales were divided across two trading days, allowing the implementation to proceed in a more controlled manner rather than treating the adjustment as one indiscriminate liquidation.

The purpose wasn't to make a short-term market prediction.

It was to reduce the concentrated position while retaining control over the amount of gain recognized during the year.

The investment decision determined what needed to change inside the portfolio.

The tax projection helped determine how quickly that change should occur.

The plan changed when the actual gains were higher

Forward-looking planning doesn't mean creating one projection and following it regardless of what happens next.

As the investment sales were completed, the client ultimately realized approximately $57,000 of long-term capital gains.

That was approximately $10,000 more than the amount included in the initial strategy.

The higher gain changed the client's remaining tax capacity.

Had we treated the original Roth-conversion recommendation as a fixed instruction, the client still could have completed the full $30,000 conversion.

However, that would have ignored the updated information.

Instead, we reran the analysis using the gains that had actually been realized.

Based on the revised projection, the recommended Roth conversion was reduced from approximately $30,000 to $20,000.

The lower conversion still allowed the client to reposition a portion of the traditional retirement account.

At the same time, it recognized that the larger capital gain had already used part of the tax capacity assigned to the year.

Even after incorporating the approximately $57,000 gain and $20,000 Roth conversion, the projection showed that the client was expected to remain within the 24% federal income-tax bracket.

The strategy changed because the facts changed.

That flexibility was part of the planning value.

The tax projection became a cash-flow plan

Estimating the client's tax liability wasn't the final step.

The client also needed to know how much cash should be available and when the payments should be made.

After updating the projection for the actual investment gains and revised Roth conversion, we calculated the estimated federal and Pennsylvania tax payments associated with the transactions.

The updated recommendation included approximately:

- $3,300 for the federal estimated-tax payment
- $665 for the Pennsylvania estimated-tax payment

These amounts reflected the projected payments associated with the updated strategy, rather than the client's entire annual tax liability.

The client could reserve the cash and make the payments before the filing deadline.

This reduced the likelihood that the eventual tax bill would create an unexpected cash requirement.

The client didn't need to wait for tax season to learn that the transactions had created an additional obligation.

The expected cost had already been incorporated into the decision.

The measurable result

The client began with approximately $357,000 of unrealized long-term capital gains and a concentrated portfolio position that needed to be addressed.

Through the planning process, he was able to:

- Begin reducing the concentrated investment position
- Realize approximately $57,000 of long-term capital gains intentionally
- Complete an approximately $20,000 Roth conversion
- Identify and correct an $8,000 Roth IRA contribution
- Remain within the projected 24% federal income-tax bracket
- Prepare for the resulting federal and Pennsylvania tax payments
- Keep the coordinated transactions within the broader tax parameters established for the year

The result wasn't the elimination of taxes.

Selling appreciated investments and completing a Roth conversion were expected to create a current-year liability.

However, the liability was evaluated before the transactions were finalized.

The client could compare the cost with the longer-term benefits of reducing portfolio concentration, repositioning retirement assets, and avoiding an excess Roth IRA contribution.

Taxes became one of the inputs into the decision rather than an unpleasant result discovered afterward.

The tradeoffs still mattered

The coordinated strategy didn't create a perfect outcome.

Recognizing the capital gain increased the client's current-year taxes.

Completing the Roth conversion created additional ordinary income.

Reducing the conversion from $30,000 to $20,000 meant less money was moved into the Roth account during that year.

Meanwhile, spreading the investment sales across multiple tax years meant the client would continue holding part of the appreciated position.

Each choice involved a tradeoff.

Selling less could reduce the immediate tax liability but prolong the concentrated exposure.

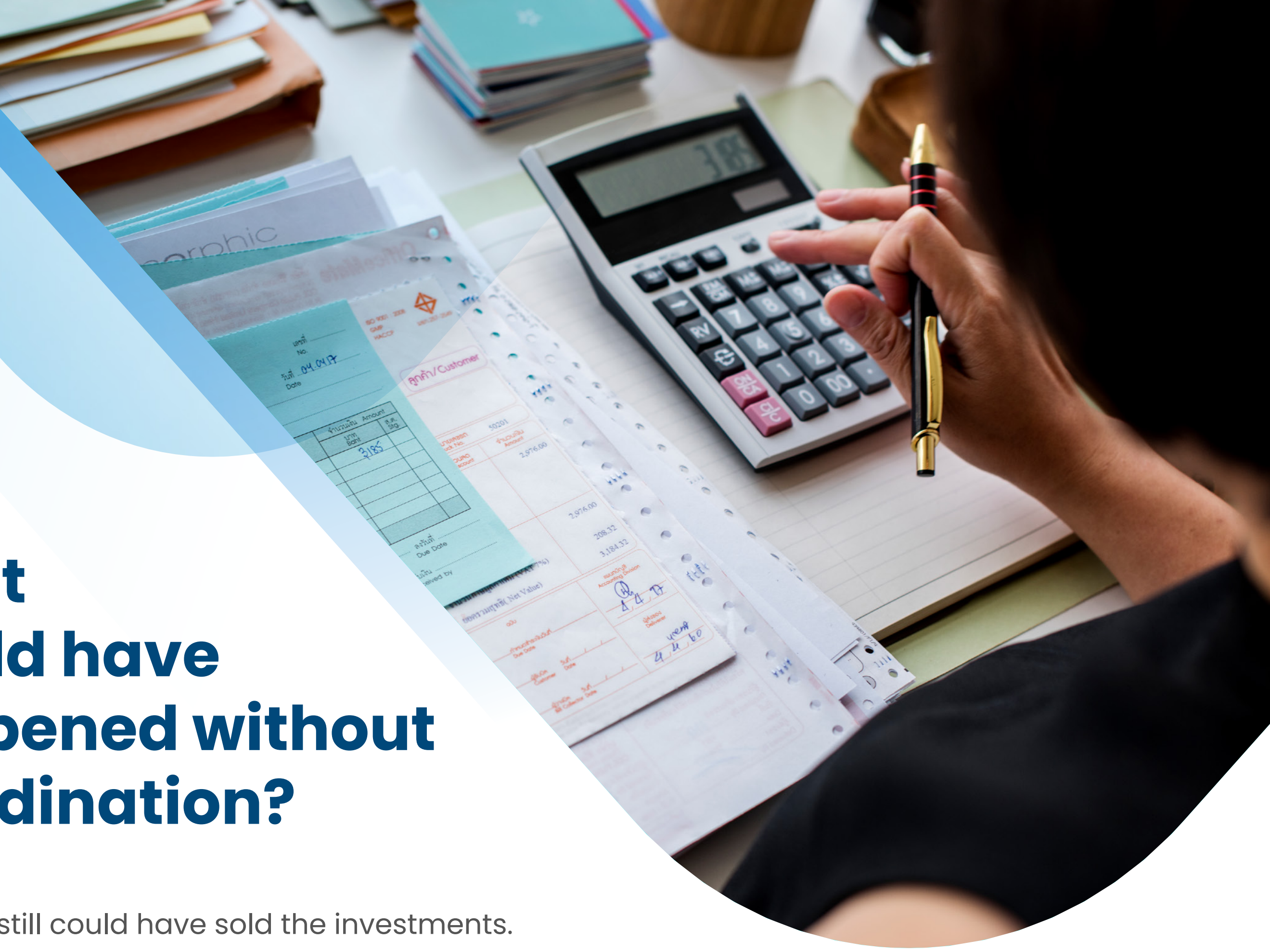
Selling more could accelerate the portfolio transition but consume tax capacity that might otherwise be used for a Roth conversion.

Completing a larger conversion could increase Roth assets but also increase the current-year tax cost.

There wasn't one decision that minimized taxes, eliminated concentration risk, maximized the Roth conversion, and preserved every available planning opportunity at the same time.

The strategy required the client to decide which combination of outcomes mattered most.

Forward-looking planning made those tradeoffs visible.



What would have happened without coordination?

The client still could have sold the investments.

He still could have completed a Roth conversion and contributed to an IRA.

Each institution involved could have processed its individual transaction correctly.

Then, after the year ended, the accountant could have received the tax documents and accurately reported the activity.

However, no one may have evaluated how the transactions worked together while they could still be changed.

The client might have:

- Realized more gain than intended
- Completed a larger Roth conversion than the year's remaining tax capacity supported
- Missed the effect of the transactions on Roth IRA eligibility
- Entered tax season with a contribution requiring correction
- Been unprepared for the additional federal and state tax payments
- Learned the combined cost only after the strategy was irreversible

The risk wasn't necessarily that the tax return would be wrong.

The risk was that the return would accurately report decisions the client might have made differently with better information.

Where the value was created

The value didn't come from one hidden deduction or a single tax-saving product.

It came from determining:

- How much gain could be recognized within the client's tax budget
- Which investments should be sold to begin repositioning the portfolio
- How the gains would affect total taxable income
- How much capacity remained for a Roth conversion
- Whether the conversion amount should change after the sales occurred
- How the combined transactions affected Roth IRA eligibility
- Which correction needed to be completed before filing
- How much cash should be reserved for federal and state taxes
- Which actions needed to occur before the year ended
- How the investment and tax strategies supported the client's longer-term goals

Without that process, each transaction could have appeared reasonable on its own.

The planning value came from evaluating the space between those transactions.

The takeaway

Tax preparation and forward-looking tax planning serve different purposes.

Tax preparation documents the income, gains, deductions, contributions, and other financial activity that already occurred.

Forward-looking tax planning evaluates the decisions that are still available and shows how one choice may change the cost or feasibility of another.

For this client, the return would eventually report approximately $57,000 of realized gains, a $20,000 Roth conversion, and the corrected IRA contribution.

However, the value had already been created before the return was prepared.

The client understood the expected tax cost.

The Roth conversion was adjusted when the investment gains changed.

The IRA issue was identified before filing.

The necessary federal and state payments were anticipated.

Most importantly, the client could decide whether the strategy remained worthwhile before committing to each action.

That's how our two-phase planning process comes together.

Our Tax Mitigation Strategies identify opportunities to reduce, defer, or more intentionally manage taxes before the available choices disappear.

Our Wealth Optimisation Plan then coordinates those tax decisions with the client's investments, retirement accounts, cash flow, risk exposure, and personal financial objectives.

The objective isn't simply to prepare a more accurate tax return.

It's to help ensure that the financial decisions eventually reported on that return were made intentionally in the first place.

Where in your own situation might several financial decisions be competing for the same tax capacity without anyone connecting them?

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PETER DONISANU, ChFC®, AIF®
Chief Wealth & Tax Strategist

Franklin Madison Private Wealth

At Franklin Madison Private Wealth, we believe your wealth should work as hard as you do. That's why I created the Premier Wealth Blueprint—to simplify finances, align wealth with your goals, and empower you with confidence for the future.

During my two decades in the wealth management industry, I've seen too many clients overwhelmed by disorganized finances, paying more in taxes than necessary, and lacking the confidence to make informed financial decisions. This stemmed from generic advice that prioritized product sales or investment outcomes over meaningful results.

You've worked hard for your wealth, but without personalized guidance, you're stuck guessing whether your decisions will actually get you closer to your goals.

The Premier Wealth Blueprint is my response to this problem. It's a proven framework that transforms financial chaos into simplicity, providing clarity, confidence, and peace of mind through an end-to-end, professionally curated service.

Because if you're not consistently executing on a clearly defined plan, then every day is a missed opportunity to maximize your wealth and secure your family's future.

Quick Facts

- **Current Role:** Principal at Franklin Madison Private Wealth (2019 – Present).
- **Previous Experience:** Senior Investment Strategy Analyst at Wells Fargo Investment Institute (2001 – 2019).
- **Public Service:** Economic Development Commissioner, Antioch, CA (2015).
- **Education:** MBA in Finance, City University of Seattle; BA in Business, Western Governors University; American College, Certified Financial Planner Education
- **Credentials:** Chartered Financial Consultant®, Accredited Investment Fiduciary®, Series 7 License, Series 65 License
- **Public Speaking & Media:** Bloomberg, Yahoo Finance, PBS Newshour, Nikkei, WSJ, Financial Times
- **Personal Interests:** Marathon, Ultramarathons and Triathlons.

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Diversification, asset allocation, dollar cost averaging, and rebalancing do not protect against loss in declining markets or guarantee profits. Dollar cost averaging involves buying securities regardless of price fluctuations, and risk tolerances should be carefully considered when continuing to purchase during periods of high or low prices.

It is not possible to invest directly in an index. Economic or financial forecasts are inherently limited and should not be relied upon as indicators of future investment performance.

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Investments in certain industries or sectors may involve risks related to sector concentration or allocation. Commodities investing holds additional risks, including regulatory factors, price volatility, changes in interest rates, credit risk, economic fluctuations, and adverse political or financial events.

Fixed-income securities involve risks such as prepayment risk, credit quality declines of issuers, market volatility, and yield fluctuations. Bond prices typically rise when interest rates fall.

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