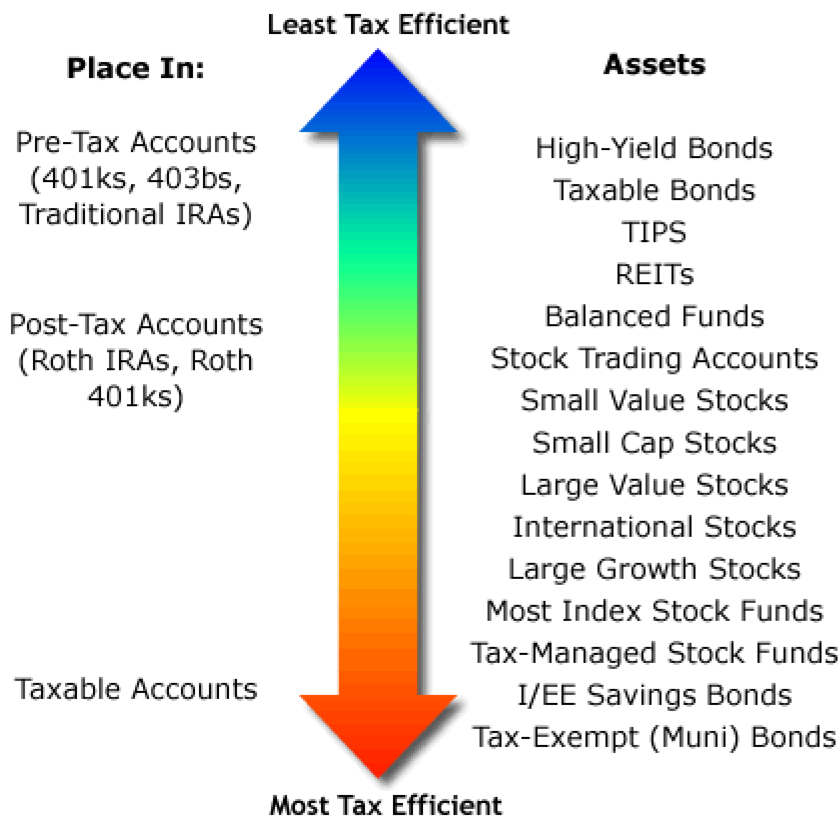
Avista Portfolio Allocations and Tax Minimization Strategies

At Avista, we seek to maximize our client's portfolio return based on their financial goals and overall tolerance for risk. Equally important, however, is the effect that taxes play on long-term returns. After all, what you actually keep is your return *after* taxes. For example, a stock index fund that tracks the S&P 500 will have low turnover and primarily pay *qualified dividends* which are taxed at the lower long-term capital gains rate (max 20%). On the other hand, REITs and bonds tend to distribute a significant amount of their return annually as *unqualified dividends*, which are then taxed as ordinary income (max 39.6%). Therefore, you should try to take advantage of your tax-sheltered accounts as much as possible by placing the least tax-efficient assets there.

Below is a chart that shows the major asset classes sorted by tax efficiency.



We start with our client's least tax-efficient assets and place them in their pre-tax accounts (Regular 401ks, 403bs, Traditional IRAs) first. Then the next least efficient assets should into the post-tax accounts (Roth IRA, Roth 401k). Only what is left after this should end up in taxable accounts.

In general, bonds should go into tax-deferred accounts, leaving stocks for your taxable accounts. Investors can also take advantage of "tax-managed" mutual funds which work hard to minimize any capital gains distributions and are designed specifically to be placed in taxable accounts.