

Tax-Loss Harvesting with Low-Turnover Bond Portfolios

Separately managed fixed-income portfolios can offer the flexibility to pursue tax-reduction strategies by generating losses at the security level to offset realized gains on other investments.

What is tax-loss harvesting?

Tax-loss harvesting is a strategy designed to reduce taxes and thereby increase overall after-tax returns.

In most cases, the profit realized when an investor sells an asset at a higher price than they originally paid is called a **capital gain**. This profit is typically subject to taxation.

If an investor with realized capital gains also owns another asset whose price has declined below its purchase price, they can sell this other asset to realize a **capital loss**. Realized capital losses can be used to offset capital gains, up to a limit, which will reduce the investor's overall tax liability.

Consider the following example:

- › An investor qualifies for the 20% long-term capital gains tax bracket
- › They own a portfolio with a current market value of \$100,000
- › Investments sold from their portfolio over the course of the year generated \$5,000 in realized capital gains.

The investor takes no additional action in **Case 1**. But in **Case 2**, the investor sells a bond position for a \$4,000 loss.

Case 1:

Portfolio Value before Taxes	\$100,000
↓	
Capital Gain on Sale	\$5,000
↓	
- Capital Loss on Sale	\$0
↓	
Net Profit	\$5,000
↓	
Tax Liability	20% x \$5,000 = \$1,000
↓	
Portfolio Value after Taxes	\$99,000

Case 2:

Portfolio Value before Taxes	\$100,000
↓	
Capital Gain on Sale	\$5,000
↓	
- Capital Loss on Sale	\$4,000
↓	
Net Profit	\$1,000
↓	
Tax Liability	20% x \$1,000 = \$200
↓	
Portfolio Value after Taxes	\$99,800

The starting value of the portfolio is identical under both scenarios whether or not they sell the bond for a capital loss. If the investor chooses to generate a loss, they can still maintain market exposure by redeploying the sale proceeds into a different bond with similar characteristics.

The only significant difference between these two cases is the tax obligation:

- › In Case 1, the investor has \$5,000 in capital gains, producing \$1,000 in taxes.
- › In Case 2—given the sale of \$4,000 in bonds at a loss to partially offset the \$5,000 gain—the investor produces only \$200 in taxes, increasing their overall after-tax return by \$800.

SEI Fixed Income Portfolio Management's Tax-Loss Harvesting Service

The SEI Fixed Income Portfolio Management team (SFIPM) intentionally pursues low-turnover, buy-and-hold strategies to help minimize the tax impact of trading decisions. Sometimes, however, investors can generate a greater tax benefit through the opportunistic sale of specific positions to realize capital losses.

Many bonds trade at a premium to their par value, and the price of a premium bond will amortize down to par as it approaches maturity. Investors who sell these bonds below their purchase price prior to maturity can generate capital losses despite earning income during their holding period.

SFIPM's tax-loss harvesting service provides our clients with the flexibility to direct the sale of specific positions from their fixed-income portfolios. Unless instructed otherwise, we will redeploy the sale proceeds in the portfolio to maintain market exposure. Clients also have the option to withdraw sale proceeds.

We are dedicated to helping our investors reach their objectives. As we work to serve our investor's needs, SFIPM's tax-loss harvesting service—available to investors within our taxable and tax-exempt strategies—may be worth consideration.

Important Information

SEI Fixed Income Portfolio Management is a unit of SEI Investments Management Corporation (SIMC).

There are risks involved with investing, including loss of principal. Bonds and bond funds will decrease in value as interest rates rise.

This information is intended for educational purposes only. SIMC does not represent in any manner that the tax consequences described as part of its tax-management techniques and strategies will be achieved or that any of SIMC's tax-management techniques, or any of its products and/or services, will result in any particular tax consequence. The tax consequences of the tax-management techniques, including those intended to harvest tax losses, and other strategies that SIMC may pursue are complex and uncertain and may be challenged by the IRS. This information is not intended to provide investment and/or tax advice. Neither SIMC nor its affiliates provide tax advice.

Please note that (i) any discussion of U.S. tax matters contained in this communication cannot be used by you for the purpose of avoiding tax, penalties and/or interest which may be imposed by the IRS or any other taxing authority; (ii) this communication was written to support the promotion or marketing of the matters addressed herein; and (iii) you should seek advice based on your particular circumstances from an independent tax advisor. Accordingly, investors should confer with their personal tax advisors regarding the tax consequences of investing with SIMC and engaging in the tax-management techniques described herein (including the described tax loss harvesting strategies) based on their particular circumstances. Clients and their personal tax advisors are responsible for how the transactions conducted in an account are reported to the IRS or any other taxing authority on the Client's personal tax returns. SIMC assumes no responsibility for the tax consequences to any Client of any transaction.