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Client Newsletter

WINDGATE
WEALTH MANAGEMENT
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SMART TAX MOVES: THE TOP 10 STRATEGIES TO INCREASE YOUR SAVINGS

Tax planning often falls into the category of tasks we would rather avoid, with a common tendency to delay it until the last minute. The good news is there is still time to make a few decisions that might save you money. Here are ten recommended tax-planning strategies that could lower your tax bill.

1. Maximize Your Retirement Contributions

Maximizing your retirement contributions is one of the best ways to minimize your tax liability. This is because retirement plans offer useful tax advantages that are not available if you were to simply put your money in a savings account. There are several accounts to consider, depending on your unique circumstances:

- 401(k), 403(b), and 457 Plans: These accounts allow you to contribute up to $22,500 for 2023 and $23,000 annually for 2024 ($30,500 if over age 50). Not only that, but pre-tax contributions will not show up as part of your annual income. This is a great way to defer taxes until your retirement years when you could

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potentially be in a lower tax bracket. Self-employed individuals can put away even more with a solo 401(k) plan.

- Traditional IRA: Contributing to a traditional IRA is another way to reduce your tax liability if your income is within certain limits. You can contribute up to 6,500 for 2023 and $7,000 for 2024, with a $1,000 catch-up contribution limit for those over age 50. Unlike the qualified retirement plans listed above, contributions to a traditional IRA can be made up until the April 15th tax filing deadline.
- Roth IRA: This is an attractive savings vehicle for many reasons, including no Required Minimum Distributions (RMDs), tax-free withdrawals after age 59½, and the ability to pass wealth tax-free to your heirs. The contribution limits are the same as traditional IRAs. However, Roth IRAs have income restrictions, and you may not be able to open an account outright if you are above certain limits.

2. Maximize Your Retirement Contributions

If you are outside of the income eligibility threshold for Roth IRAs but still want to take advantage of the Roth tax benefits, a Roth conversion could be the right strategy for you. It works by paying the income tax on your pre-tax traditional IRA and converting the funds to a Roth IRA. This strategy can be especially powerful to new retirees who find themselves in a lower tax bracket before Social Security and/or Required Minimum Distributions start.

You could also consider the Mega Backdoor Roth and Backdoor Roth IRA strategies:

- Mega Backdoor Roth: With this strategy, you would convert a portion of your 401(k) plan to a Roth. This involves first maximizing the after-tax, non-Roth contributions in your plan, then rolling it over to either a Roth 401(k) or your Roth IRA. With the Mega Backdoor Roth, you convert a portion of your 401(k) plan to Roth dollars.
- Backdoor Roth IRA: In this case, you would make an after-tax (non-deductible) contribution to a traditional IRA. You then immediately convert the funds to a Roth IRA to prevent any earnings from accumulating. This strategy makes sense if you do not already have an IRA set up yet.

All three Roth conversion strategies will allow the contributions to grow completely tax-free and allow you to avoid future RMDs, which is helpful if you expect to be in a higher tax bracket in the future.

3. Contribute to a Health Savings Account

An efficient but underutilized way to maximize your savings and minimize your taxes is to contribute to a Health Savings Account (HSA). HSAs offer triple tax savings: contributions are tax-deductible, earnings grow tax-free, and you can withdraw the funds tax-free to pay for medical expenses. Unused funds roll over each year and will become an IRA at age 65, at which point you can withdraw funds penalty-free for non-medical expenses. You must be enrolled in a high-deductible health plan in order to qualify for an HSA.

HSAs can be a great tax-management tool if you are able to pay medical expenses out of pocket and leave the HSA funds to grow. The 2023 contribution limits for HSAs are $3,850 for individuals and $7,750 for families. (The 2024 limits will increase to $4,150 and $8,300, respectively.) If you are 55 or older, you may also be able to make catch-up contributions of $1,000 per year. You have until April 15th for your contributions to count for the previous year's tax return.

4. Contribute to a Donor-Advised Fund

If you itemize your tax deductions because of charitable contributions, you may want to consider investing in a donor-advised fund (DAF). You can contribute a lump sum all at once and then distribute those funds to various charities over several years. With this strategy, you can itemize deductions when you make the initial contribution and then take the standard deduction in the following years, allowing you to make the most out of your donation tax-wise.

You can also donate appreciated stock, which can further maximize your tax savings. By donating the appreciated position, you avoid paying the capital gains tax that would have been due upon sale of the stock and you are effectively donating more to your charities of choice than if you had sold the stock and donated the proceeds.

5. Make a Qualified Charitable Donation

If you own a qualified retirement account and are at least 70½, you can use a qualified charitable distribution (QCD) to receive a tax benefit for your charitable giving. Since this is an above-the-line deduction, it can be used in conjunction with other charitable tax strategies. A QCD is a distribution made from your retirement account directly to your charity of choice. It can also count toward your RMD when you turn age 73, but unlike RMDs, it will not count toward your taxable income. Individuals can donate up to $100,000 in QCDs per year, which means a married couple can contribute a combined amount of $200,000.

6. Utilize Tax-Loss Harvesting

Tax-loss harvesting involves selling investments at a loss in order to offset the gains in your portfolio. By realizing a capital loss, you are able to counterbalance the taxes owed on capital gains. The investments that are sold are usually replaced with similar securities in order to maintain the desired asset allocation and expected return.

With the ups and downs of the market in 2023, chances are you have some capital losses that can be utilized. For example, if you are expecting a large capital gain this year, sell an underperforming stock, and harvest the losses to offset your gain.

Tax-loss harvesting can also be used to reduce your ordinary income tax liability if capital losses exceed capital gains. In this case, up to $3,000 can be deducted from your income, and capital losses greater than $3,000 can be carried forward to later tax years.

7. Understand Long-Term vs. Short-Term Capital Gains

Understanding the tax implications of long-term versus short-term capital gains can go a long way in reducing your tax liability. For instance, in 2023 a married taxpayer would have paid 0% capital gains tax on their long-term capital gains if their taxable income falls below $89,250. That rate jumps to 15% and 20% for taxable incomes that exceed $89,250 and $553,850, respectively. Understanding where you fall on the tax table is an important part of minimizing your liability.

Gains that are short-term in nature (held less than one year) will be taxed at your marginal tax bracket, which could be up to 37%. Knowing both the nature of your gain, as well as your tax bracket, is crucial information if you want to minimize your tax liability.

8. Take a Qualified Business Income Deduction

Business owners involved in partnerships, S Corporations, or Sole Proprietorships can take a Qualified Business Income Deduction (QBID) to help reduce taxable income and maximize tax savings. This allows for a maximum deduction of 20% of qualified business income, but limits apply if your taxable income exceeds a certain threshold. To qualify for this deduction, consider reducing or deferring income so that you can remain below the phase out threshold. A wonderful way to do this is to maximize your retirement contributions to tax-advantaged accounts (as discussed in point #1).

9. Consider Estate Tax-Planning Techniques

Estate tax-planning techniques can also be an effective way to reduce current-year tax liability. For 2024, the lifetime exemption for assets that can be given gift-tax free is estimated at $13.61 million for individuals and $27.22 million for married couples ($12.92 million for 2023).

The annual gift tax exclusion is estimated to increase to $18,000 per recipient in 2024, up from $17,000 in 2023. This is the annual amount taxpayers can give tax-free without using any of the above-mentioned lifetime exemption. Not only that, but the annual exclusion applies on a per-person basis, so each taxpayer can give $18,000 per person to any number of people per year.

Though gifting and other estate tax-planning strategies are not tax-deductible, they can help to significantly reduce your taxable estate over time.

10. Make Sure Your Advisory Team Is Working Together

Beyond consulting with a tax professional, you will want to be sure your entire financial team is working together to provide cohesive oversight and guidance. This should include professionals like CPAs, financial advisors, investment advisors, and estate attorneys. Your finances do not exist in a bubble and so neither will your tax-minimization strategies. When your advisory team works together, strategies are easier to identify and execute, and proactive tax solutions become much easier to implement, reducing stress and your tax bill.

Maximizing your retirement contributions is one of the best ways to minimize your tax liability.

CAN THE SMALL CAP RALLY CONTINUE?

Small cap stocks (as measured by the Russell 2000 Index) returned 22% in the final two months of 2023, nearly twice as much as the 12% return for large cap stocks (S&P 500 Index). This was notable as small cap stocks have underperformed large cap stocks over the past several years. Could the recent small cap outperformance indicate a longer-term shift in the cycle?

We believe there are several reasons small cap stocks may have stronger relative performance to larger stocks in the years ahead. First, valuations among small cap stocks are near the largest discount to large cap stocks in history. This means that investors can purchase small cap companies at levels that are far less expensive than their large cap cousins. Valuations alone may not be a reason to spark a rally among smaller stocks, but historically the starting price of an investment greatly impacts the degree of a rally once it begins.

Identifying a catalyst is difficult, but the list of potential triggers is long today. First, sentiment toward smaller companies is incredibly low, so even a small improvement in investor demand would push shares higher. Consider this: Apple has a market capitalization of $3 trillion. This is more than the entire Russell 2000 universe of 2,000 small cap stocks combined. If investors took even 1% of Apple shares and re-invested in small cap companies, the impact on demand would be noticeable.

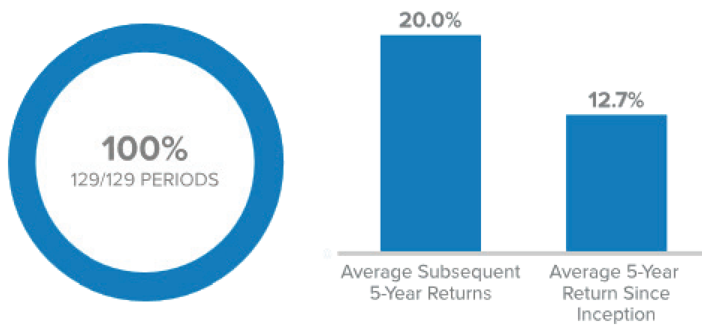
Other catalysts include the moderation of inflation, pause in interest rates by the Fed, a stronger economy, and smaller companies reporting stronger earnings growth. The slowing of inflation and pausing of rate hikes was confirmed at the end of 2023, contributing to the small company rally to end the year. Stronger earnings growth is also possible in the coming years, and in our view, the long-term potential for smaller companies is very promising.

According to a 9/30/2023 report by Royce Funds, a study of history also reveals great possible optimism for future small cap performance. Small caps by their nature experience boom and bust periods. They have a well-established pattern where periods of low performance are followed by those with above average returns. According to the Center for Research in Security Prices (CRSP)*, there have been 130 five-year periods in the past 78 years when small stocks (CRSP 6-10) produced less than a 5% annualized return. We are currently in one of these periods. In the past, the subsequent five-year annualized return for the previous 129 periods was a very impressive average return of 20% annualized. That translates as an average 20% per year return, each year, for five years. This is noticeably better than the overall 12.6% average for all five-year periods since 1946.

Also noteworthy is that small cap returns were positive 100% of the time following periods when they had averaged less than 5%. While past performance is no indication of future results, we cannot help but be optimistic about the next five years for small-cap performance.

Small Cap Five Year Cycles

Subsequent Average Annualized Five-Year Performance for the CRSP 6-10 Following 5-Year Return Ranges of Less Than 5%



* Important Disclosure

The Center for Research in Security Prices (CRSP) is a vendor of historical time series data on securities. The CRSP (Center for Research in Security Prices) equally divides the companies listed on the NYSE into ten deciles based on market capitalization. Deciles 1-5 represent the largest domestic equity companies and Deciles 6-10 represent the smallest. CRSP then sorts all listed domestic equity companies based on these market cap ranges. By way of comparison, the CRSP 1-5 would have similar capitalization parameters to the S&P 500, and the CRSP 6-10 would have a similar capitalization parameter to those of the Russell 2000.

YOU KNOW THE BENEFITS OF WORKING WITH A FINANCIAL ADVISOR. DO YOUR FRIENDS & FAMILY?

As a current client, you know firsthand how tough it can be to take the first step in hiring a financial advisor you can trust. But you also know that having an experienced financial professional in your corner can provide you with the foresight and knowledge to help you grow your wealth and steer you away from costly mistakes.

What you may not realize is that much of our business at Windgate Wealth Management has been built on introductions from clients. Being introduced to someone who may have a financial need we can help with is the highest compliment, and we do not take it lightly. So, thank you to everyone who has introduced us to friends and family over the years.

When a Financial Advisor Can Help

Even if your friends or family feel confident in their finances, they may not realize the common mistakes they are making or the investment opportunities they are missing. A financial advisor can look at every piece of your finances and help you understand the larger picture of how to achieve true financial security.

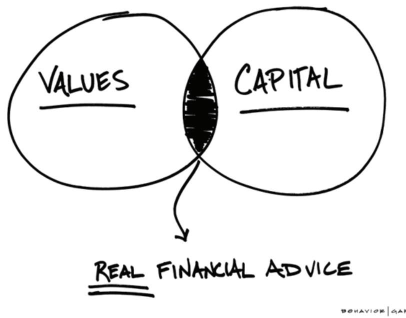
Common life events we have been asked to consult on include:

- Significant changes to income
- Buying or selling a house
- Having a child
- Planning for higher education
- Transition to retirement
- Stock ownership and company exit planning
- Questions about investments
- Questions about tax-management strategies
- Legacy planning for heirs

Do You Know Someone We Can Help?

At Windgate Wealth Management, we strive to provide honest and accurate financial advice without all the stress and anxiety that comes with the process. We are happy to say that many of our clients are referrals from other clients. If you know someone who would benefit from a collaborative advisor-client relationship, please send them our way. Consider sharing this article with them.

Aligning Personal Values with Financial Goals



What do your values truly mean to you, and how do they manifest in your life, relationships, work, home, and finances? In our age of abundance and overwhelming information, it is vital to clearly create a framework that supports your value system.

Although aligning personal values with your financial situation may seem straightforward, it can be a complex undertaking that often requires an outside perspective. We invite you to read the following guide to help you make the connection between your personal values and your financial goals and dreams.

Identify Your True Values

Start by separating your values into two categories: the values you were taught, and the values that truly make you happy. There may be some overlap between the two, but the goal is to find out if there is a difference between the values you think you have and the values that are truly meaningful in your life. For example, you may have been taught to work hard and pour your soul into a job that pays well, but maybe that is not bringing you any personal satisfaction. You might find more fulfillment from a vocation that pays less but whose mission and excellent work you believe in. To start this process, psychologist Jim Taylor recommends answering the following three questions:

- What do you choose to do in your life on a daily basis?
- What activities are you passionate about that bring you true joy when you participate in them?
- What experiences and people cause you to feel deeply engaged and connected to the world?

Digging into these questions can uncover the values you hold that truly fulfill you and bring joy to your life. If you are constantly unhappy, whether that be from your job, your financial behaviors, or something else, this is a sign that you may not be living according to your true values.

Understand Your Money Mindset

You also need to take stock of your money mindset. Your money mindset has been cultivated from your life experience. You may have learned good financial habits from your parents. You may have even learned bad financial habits if you watched your parents fail financially. Whatever your experiences have been with personal finances, they are the key to understanding why you behave the way you do around financial matters.

Understanding your money mindset is important because it allows you to grow intentionally. Identifying a toxic or substandard financial mindset is the first step to changing that mindset. By knowing what you want to change, you have more control over how and when you change it.

Sync Your Ideal Life with Your Lived Life

After all this reflection, your ideal life probably looks a bit different from your reality. To reach that ideal lifestyle, you must synchronize your "living life" with the values you identified that make you happy. Remember that these are the values that connect you to the activities, experiences, and people which bring you the most fulfillment.

So how do we do this? There is an old saying that the checkbook and the calendar do not lie. Show someone how you spend your money and how you spend your time, and they will know what is important to you. Take a moment to be honest with yourself: does how you spend your time and your money align with what really matters to you?

If not, it is time to create financial goals that truly reflect your values. When financial goals are connected to your values, your money becomes the tool that allows you to reach the real goal, rather than being the end goal in and of itself. From this vantage point, you are ready to experience long-lasting happiness.

Money Can Buy Happiness

While we all know that the satisfaction gained from most material purchases can be fleeting, money can buy happiness if it is aligned with your values. Author and Harvard "happiness professor" Arhtur Brooks suggests that while money alone will not buy happiness, there are ways money can enhance well-being and life satisfaction depending on the person. Here are a few examples:

1. Invest in Experiences
2. Support Others
3. Invest in Education
4. Reduce Stress
5. Give Back

An Advisor That Connects to Your Values

While everybody wants a clean, straight line between their current reality and their goals, life does not work this way. You may have a child, sell a business, or come upon unexpected expenses. Your situation is always changing and therefore your goals themselves may change. We all have our own financial blind spots – when situations change, a good advisor can help you spot them and make course corrections.

By considering your values and what matters most to you, an advisor can collaborate to make smart choices that align your dreams with your actions. Then you can spend less time worrying about your money and more time focusing on what is important to you and your family.

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