



**SELECT PORTFOLIO
MANAGEMENT, INC.**
Integrated Wealth Management
A Registered Investment Advisor



White Paper

Comparing Taxable and Tax-Free Yields

www.selectportfolio.com • Toll Free 800.445.9822 • Tel 949.975.7900 • Fax 949.900.8181

Securities offered through Securities Equity Group Member FINRA, SIPC, MSRB

Comparing Taxable and Tax-Free Yields

Which is more appropriate: taxable or tax-free bonds?

Whether a taxable or a tax-free bond makes more sense for you depends on your tax bracket. A taxable bond with a higher yield might not pay more after taxes are accounted for. The following table shows the yield a taxable bond would need to provide investors in various tax brackets for its after-tax return to equal that of a tax-free bond.

	Tax Bracket				
	15%	25%	28%	33%	35%
Taxable Yield (%)	Equivalent Tax-Free Yield (%)				
2	1.70	1.50	1.44	1.34	1.30
2.5	2.13	1.88	1.80	1.68	1.63
3	2.55	2.25	2.16	2.01	1.95
3.5	2.98	2.63	2.52	2.35	2.28
4	3.40	3.00	2.88	2.68	2.60
4.5	3.83	3.38	3.24	3.02	2.93
5	4.25	3.75	3.60	3.35	3.25
5.5	4.68	4.13	3.96	3.69	3.58
6	5.10	4.50	4.32	4.02	3.90
6.5	5.53	4.88	4.68	4.36	4.23
7	5.95	5.25	5.04	4.69	4.55
7.5	6.38	5.63	5.40	5.03	4.88

Calculating what a taxable bond would have to yield to equal a tax-free bond

If the yield you're considering isn't on the above table, there's a simple formula you can use to calculate the after-tax yield that a taxable bond would have to provide to equal the yield on a tax-free bond. Let's say you're considering a taxable bond that yields 5 percent. You want to know whether it would be better than a tax-free bond that yields 3.75 percent if you're in the 33 percent tax bracket. Simply use the following calculation:

1. Subtract your tax bracket (in this case, 33 percent) from 100 percent ($100 - 33 = 67$ percent).
2. Divide the yield of the tax-free bond by the result of Step 1.
3. The result is the yield that's necessary for a taxable bond to be equivalent to the tax-free bond.
In this case, a taxable bond would have to yield at least 5.59 percent to equal the tax-free bond's

3.75 percent. Since the taxable bond you're considering pays only 5 percent, the tax-free bond would be the better choice.

Caution: This example does not address state and local taxes.

Calculating what a tax-free bond would have to yield to equal a taxable bond

If you want to see what a tax-free bond would have to yield to equal a taxable bond's yield, the calculation is a little different. Let's say that you're trying to decide between a taxable bond yielding 6.5 percent and a tax-free bond that yields 3 percent.

1. Subtract your tax bracket from 100 percent (for this example, we'll use 33 percent again) ($100 - 33 = 67$ percent).
2. Multiply the yield of the taxable bond by the result of Step 1 ($.065 \times .67 = 4.355$ percent).
3. The result is the tax-free equivalent yield that would equal the taxable bond's 6.5 percent. In this case, the 3 percent tax-free bond does not provide as much income, and the taxable bond would be the better choice.

Caution: This example does not address state or local taxes.

	Tax Bracket				
	15%	25%	28%	33%	35%
Tax-Free Yield (%)	Equivalent Taxable Yield (%)				
2	2.35	2.67	2.78	2.99	3.08
2.5	2.94	3.33	3.47	3.73	3.85
3	3.53	4.00	4.17	4.48	4.62
3.5	4.12	4.67	4.86	5.22	5.38
4	4.71	5.33	5.56	5.97	6.15
4.5	5.29	6.00	6.25	6.72	6.92
5	5.88	6.67	6.94	7.46	7.69
5.5	6.47	7.33	7.64	8.21	8.46
6	7.06	8.00	8.33	8.96	9.23
6.5	7.65	8.67	9.03	9.70	10.00

Disclosures

This material does not constitute the rendering of investment, legal, tax or insurance advice or services. It is intended for informational use only and is not a substitute for investment, legal, tax, and insurance advice.

State, national and international laws vary, as do individual circumstances; so always consult a qualified investment advisor, attorney, CPA, or insurance agent on all investment, legal, tax, or insurance matters.

The effectiveness of any of the strategies described will depend on your individual situation and on a number of other factors. After reviewing your personal situation, we may recommend that you not use any strategy in this document but instead consider various other strategies available through our practice.

Securities offered through Securities Equity Group, member FINRA, SIPC, MSRB

Copyright 2006 Forefield, Inc. All rights reserved.