U.S. Treasury Obligation State Tax Exemption

A Practical Guide for RIA Firms

Prepared by Village Financial Services | villagefs.com

TL;DR — Too Long; Didn't Read

If your clients hold funds like SNSXX, SGUXX, IEF, IEI, SCHP, SCHO, SCHR, or SCHQ in taxable accounts, a portion of their dividend income may be exempt from state income tax — but it won't show up on their 1099. Schwab doesn't break it out. You have to find it, calculate it, and give it to their tax preparer, or at the very least, make them aware. This guide tells you exactly how.

When to Start

Schwab publishes its Supplemental Tax Information document in early February, and 1099s post from mid-February. Run the positions screen in January so impacted households are identified and ready to calculate as soon as the 1099s are available. Starting early means clients and their tax preparers have what they need well before filing deadlines.

1. Understanding the Gap

Many mutual funds and ETFs hold U.S. Treasury obligations as part of their portfolio. The income these funds distribute to shareholders is fully taxable at the federal level — but in most states, the portion of that income derived from U.S. government obligations is exempt from state income tax.

The problem is that this exemption does not appear on the 1099. The line item for "Interest on U.S. Savings Bonds and Treasury Obligations" shows $0 for these funds because they are funds holding Treasuries, not direct Treasury bonds. The pass-through exemption requires a separate calculation using supplemental data that fund companies publish each year.

Which custodians break this out on the 1099?

Custodian / Broker-Dealer	On 1099?	Supplemental Doc?
Schwab	❌ No	✅ Yes — published early February

Vanguard	✅ Yes	✅ Yes
Fidelity	❌ No	✅ Yes

> **Important Limitation**
>
> The Schwab firm-wide positions export described in this guide reflects current holdings only. Accounts that held a qualifying fund during the year and sold out before year-end will not appear in the report. Advisors should cross-reference their memory and/or transaction history to catch any liquidated positions before concluding the review.

2. Qualifying Funds to Watch

The following funds are commonly held in client portfolios and have meaningful U.S. government obligation percentages. This is not an exhaustive list — refer to the Schwab Supplemental Tax Information document and equivalent reports from BlackRock, Vanguard, etc. for a complete listing each year.

Ticker	Fund Name	Example UST Obligation %
SWRSX	Schwab Treasury Inflation Protected Securities Index Fund	100.00%
SNSXX / SUTXX	Schwab U.S. Treasury Money Market Fund	99.99%
SCHP	Schwab U.S. TIPS ETF	100.00%
SCHO	Schwab Short-Term U.S. Treasury ETF	100.00%
SCHR	Schwab Intermediate-Term U.S. Treasury ETF	100.00%
SCHQ	Schwab Long-Term U.S. Treasury ETF	100.00%
SWSBX	Schwab Short-Term Bond Index Fund	67.97%
SWAGX	Schwab U.S. Aggregate Bond Index Fund	44.06%
SWGXX / SNVXX / SGUXX	Schwab Government Money Fund	36.20%
SGVT	Schwab Government Money Market ETF	36.66%
SCHZ	Schwab U.S. Aggregate Bond ETF	44.18%
IEF	iShares 7-10 Year Treasury Bond ETF	~100%
IEI	iShares 3-7 Year Treasury Bond ETF	~100%
SGOV	iShares 0-3 Month Treasury Bond ETF	~100%

Example percentages are from a recent Schwab Supplemental Tax Information document. iShares percentages are approximate; confirm with the BlackRock supplemental report for exact figures. Percentages change every year, so always use the current year's documents.

3. How to Pull the Schwab Positions Report

The first step in identifying impacted accounts is exporting the firm-wide positions report from Schwab Advisor Center. Upon request, we will grant you access to our screening tool. Follow these steps:

Step 1: Export the Positions Report

1. Log in to Schwab Advisor Center and navigate to the Positions tab.
2. Select the firm level or master account level view, depending on how your firm is set up.
3. Switch to the Securities view.
4. Export the entire list. This will be uploaded into the Village screening tool to generate a PDF showing all impacted positions.

Step 2: Export the Account Level Positions Report

1. Still in Schwab Advisor Center, navigate to the Accounts level and export the positions data.
2. Open the exported spreadsheet. Add a new column with the following formula to truncate account numbers to the last 4 digits only (do not upload full account numbers):

   =RIGHT(A9, 4) — where A9 is the first cell containing account numbers. Drag the formula down to apply to all rows.
3. Highlight the new column, copy it, and paste as Values Only (to remove the formula).
4. Delete the original column containing full account numbers.
5. Save the file and upload it into the Village screening tool when prompted. The tool will hide rows that do not contain qualifying tickers and rows that are retirement accounts, leaving only taxable accounts (individual, joint, trust, organization, etc.) with impacted positions.

Step 3: Review the Output

1. The tool will generate a filtered spreadsheet formatted as a sortable, filterable table.
2. Download this output for review.
3. Identify which households to prioritize for further review.

▶️ **Watch the demo:** Village Fin Pods Walkthrough (Loom)

4. Pulling the 1099s

Once impacted households are identified, you will need the 1099 for each account to get the actual income figures for the calculation. Schwab Advisor Center gives you two options: download 1099s one account at a time (steps below), or download tax forms in bulk as a ZIP file at the master account level from the Documents tab. The bulk ZIP includes original and corrected Composite 1099s, 1099-Rs, and 5498s for every account on the master, so it pairs

best with the Fin Pods AI bulk upload tool. For a short list of households, individual downloads are usually faster.

1. In Schwab Advisor Center, navigate to each identified client account.
2. Download the 1099-DIV for the applicable tax year.
3. Note the Box 1a (Total Ordinary Dividends) amount for each qualifying fund held in the account.
4. Upload the 1099s into your chosen analysis tool (Fin Pods AI or MFPCO) for calculation. Clean PDFs downloaded directly from the custodian work best.

Time-Saving Tip

For firms with large numbers of impacted accounts, prioritize by balance size first. Accounts with larger positions in qualifying funds will generate the most meaningful state tax savings and are most worth the effort to review. Smaller accounts can be assessed in subsequent years once a workflow is established.

5. Tools for Analysis

Two tools have been validated by the RIA community for calculating the state tax exemption amounts. Both serve slightly different purposes and for high-volume users, using both is recommended.

	Fin Pods AI (finpodsai.com)	MFPCO (mfpco.com)
Data Input	Upload 1099 directly — AI extracts data automatically	Manual entry of income figures from 1099
Calculation	Automatic per fund, with work paper output	Automatic once data is entered
Fund Database	Continuously expanding; municipal funds now included. Uncovered funds are typically added within one week of request.	Broader database; industry veteran
What It Covers	Direct federal obligations, state muni amounts, and municipal funds	Direct + indirect federal obligations, state muni, AMT, Corporate DRD, foreign income
Bulk Upload	Yes — bulk tool now supports all major custodian 1099s. Additional formats can be added from clean custodian PDFs.	No — fund-by-fund process
Work Papers	Yes — PDF + Excel with source citations	Yes — fund-level output
Ticker Lookup	Yes	Yes — recently improved
Auditability	Source page references included; built for state tax board documentation	Fund company data; widely accepted
Security	SOC 2 Type 2, AWS-only, no external AI/LLMs, burn-after-read, zero-access sharing, post-quantum secure	Standard web application
Pricing	$50/month or ~$600/year (2 months free annual)	$150/yr — single user $290 — 2–5 users $430 — 6–10 users $570 — 11–25 users
Best For	Firms uploading multiple 1099s; compliance-conscious workflows	Comprehensive fund coverage; lower volume; budget-conscious

Fin Pods AI Features Worth Knowing

Fin Pods AI continues to add features that change what firms can do with the tool. If you evaluated it in the past, these are worth a second look:

- Bulk 1099 support — the bulk tool handles all major custodian 1099 formats, with additional formats added on request from clean custodian PDFs.

- Municipal fund coverage added — muni funds are now included alongside federal obligation calculations.
- IRS transcript pulling with structured data extraction — currently available to firms with a tax professional on staff (EA, JD, or CPA) or firms that file five or more tax returns.
- Fund coverage gaps are typically resolved within one week of request, so an unmatched fund is no longer a dead end.

Proactive Planning Features

These features shift this work from reactive cleanup to proactive planning:

- Large capital gains distribution identification — flagged when investment statements are uploaded, or viewable through the Fund Tax Center, so advisors can see distributions coming before they hit.
- Mutual funds with exchange-to-ETF privileges — a list to help advisors identify opportunities for better tax efficiency.
- Money market screener (in development) — calculates 7-day SEC yield with state tax considerations built in.
- Schwab bulk tax document processing (in development) — Fin Pods is building processing that works from the Schwab master-level bulk tax form export to produce client tax letters and their supporting data in bulk, instead of pulling transactions account by account.

Why This Matters for Next Season

Most of this work has historically been reactive — waiting for 1099s, then scrambling before the filing deadline. The capital gains distribution flagging and money market screener change that. Firms that adopt these tools before year-end can identify exposure and make fund selection decisions while there is still time to act, rather than reporting on what already happened.

Note: Village Financial Services has no financial relationship with either tool and receives no compensation for referrals. These tools were identified through community research and direct evaluation.

6. A Note on Fund Selection

Advisors looking to simplify this process going forward may consider reviewing their cash management fund selection. Funds with higher U.S. Treasury obligation percentages both maximize the state exemption and reduce the complexity of the annual review.

SGOV (iShares 0-3 Month Treasury Bond ETF) holds ~100% U.S. Treasuries at an expense ratio of just 0.09% — compared to 0.34% for SNOXX, for example. The tradeoff: as an ETF, SGOV requires crossing the bid/ask spread on trades, which becomes a more meaningful cost drag as interest rates decline. In a falling rate environment, a money market fund may offer better net yield.

Ultrashort bond funds are another strong option — particularly for clients who don't require the underlying to be risk-free. Many include corporate bonds in addition to Treasuries, providing additional yield pickup. Most major fund companies offer a version of this category.

> **Portfolio Construction Consideration**
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> Reviewing cash management fund selection annually — weighing Treasury obligation percentage, expense ratio, bid/ask spread, and the current rate environment — can reduce both the tax reporting burden and the cost drag on client portfolios over time.

7. Special Consideration: Oregon Clients

Oregon is the only state we are aware of with a rule on the books (OAR 150-316-0525) that extends the federal obligations deduction to certain qualified account withdrawals — not just taxable investment account income. If you have clients who are Oregon residents, this is worth reviewing with their tax preparer specifically.

8. Annual CRM Workflow Template

The following task sequence is designed to be added to your CRM (e.g., Advyzon, Redtail, Wealthbox) as a recurring annual workflow. Village CSAs can add this workflow to your CRM on your behalf — see the call to action at the end of this document.

#	Task	Timing	Owner
1	Pull Schwab firm-wide positions export and run through screening tool to identify accounts with qualifying funds in taxable accounts	Early February	CSA
2	Cross-reference transaction history for any accounts that held qualifying funds and sold out during the year (not captured in positions export)	Early February	Advisor / CSA
3	Share filtered positions report with advisor for household prioritization	Mid February	CSA

4	Confirm Schwab Supplemental Tax Information document has been published and save to firm file	Early February	CSA
5	Pull 1099s for prioritized households from Schwab Advisor Center (per account, or master-level bulk ZIP from the Documents tab)	Mid–Late February	CSA
6	Upload 1099s into Fin Pods AI and/or MFPCO for calculation; download work papers	Late February	Advisor / CSA
7	Prepare client communication using tax letter template; attach supplemental document and work paper as backup for tax preparer	Late February – March 15	Advisor
8	Send to client and copy to CPA/tax preparer if applicable; educate preparer if they are unfamiliar with the exemption	By March 15	Advisor
9	Note in client file which funds were reviewed, income amounts, and state exemption calculated. Flag for following year.	Upon completion	Advisor / CSA
10	Review capital gains distribution exposure and fund selection — consider whether higher-Treasury-obligation funds or lower-expense alternatives are appropriate	Q4 / Annual Review	Advisor

9. How Village Can Help

Village Financial Services partners with independent RIA firms custodying at Schwab to remove administrative burden. Here is what we can do for your firm on this specific workflow:

- Pull the Schwab firm-wide positions export and run it through our screening tool to identify impacted accounts — at your request, at no additional charge for current Fractional CSA clients
- Manually pull 1099s for prioritized households upon advisor direction
- Add the annual CRM workflow template from this guide into your CRM on your behalf
- Assist with client communication preparation using the email templates included with this guide
- Help evaluate and onboard Fin Pods AI or MFPCO for your practice

Ready to get started?

Learn more about our Fractional CSA service and how we can take this — and other operational burdens — off your plate.

www.villagefs.com/fractionalcsa

hello@villagefs.com | 941-337-9600

This white paper was prepared by Village Financial Services for informational purposes only. It does not constitute tax, legal, or investment advice. Fund percentages, tool features, and pricing are subject to change. Advisors should verify all information before sharing with clients and consult with their compliance department regarding tool usage and client communication. Village Financial Services has no financial relationship with Fin Pods AI or MFPCO.

10. Sample Client Email Language

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How to Use This Template

The email templates below are designed to be sent to individual clients whose accounts hold qualifying U.S. Treasury obligation funds in taxable accounts. Placeholders appear in [brackets] — replace these with the client-specific details before sending. Two versions are provided: a standard version and a shorter version for clients who have received this communication in prior years.

Important: This email is informational only and should be reviewed by the advisor before sending. It does not constitute tax advice. Always ensure the supplemental document from the relevant fund company is attached.

Version 1: Standard (First-Time Communication)

Subject: Important Tax Information — U.S. Treasury Income in Your Account

Hi [Client First Name],

As part of our annual tax review process, I wanted to share some information that may be helpful when you or your tax preparer complete your state income tax return.

Your account holds [Fund Name(s)] (ticker: [TICKER]), which earns income from U.S. Treasury obligations. While this income is fully taxable at the federal level, a portion of it may be **exempt from state income tax** — a deduction that is easy to miss because it does not appear directly on your 1099.

Here is how it works:

- According to [Fund Company]'s [Year] Supplemental Tax Document, [X]% of the income distributed by [Fund Name] was derived from U.S. government obligations.
- Your 1099 shows $[Total Dividend Income] in ordinary dividends from this fund.
- Applying the [X]% factor, approximately $[Calculated Amount] of that income may qualify for the state tax exemption.

The exact tax benefit will depend on your state of residence and your marginal state tax rate. For a client in [State] with a [X]% state income tax rate, this could represent a savings of approximately $[Estimated Savings].

I have attached the relevant supplemental tax document from [Fund Company] for your tax preparer’s reference. Please share this email and attachment with them when filing your [Year] state return.

Please don’t hesitate to reach out if you have any questions.

Warm regards,

[Advisor Name]

[Firm Name]

Version 2: Short Version (Returning Clients)

Subject: [Year] U.S. Treasury Supplement — Action Needed for Your Tax Return

Hi [Client First Name],

As we've done in prior years, I'm sending along the supplemental tax information for [Fund Name(s)] held in your account. A portion of the income from this fund is derived from U.S. Treasury obligations and may qualify for a state income tax exemption.

For your [Year] return:

- Fund: [Fund Name] ([TICKER])
- U.S. Treasury obligation %: [X]%
- 1099 ordinary dividend income from this fund: $[Amount]
- Estimated exempt amount: $[Calculated Amount]

Please forward this email and the attached supplemental document to your tax preparer. Feel free to reach out with any questions.

Warm regards,

[Advisor Name]

[Firm Name]

Quick Reference: Placeholder Guide

Placeholder	Where to Find It
[Client First Name]	Client record in your CRM
[Fund Name]	Positions export or 1099
[TICKER]	Positions export or Schwab Supplemental Tax Document
[X]% (Treasury %)	Schwab / Vanguard / fund company Supplemental Tax Document — available early February
[Total Dividend Income]	Client's 1099-DIV, Box 1a
[Calculated Amount]	Box 1a income × Treasury obligation %
[Estimated Savings]	Calculated amount × client's marginal state tax rate
[State]	Client's state of residence in CRM
[Fund Company]	BlackRock (iShares), Vanguard, Schwab, etc.

[Year]	Applicable tax year
[Advisor Name]	Your name
[Firm Name]	Your firm name

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