Fee Only Financial Planning & Investment Management

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Resolute Connections

In this month's newsletter we address a few topics that are in the headlines on a daily basis, and a few issues we run into often in our planning practice. *Common Estate Planning Mistakes* outlines the errors we encounter with the vast majority of our new clients who either don't have an estate plan, or have one but never fully put it into place. *Don't Miss Open Enrollment* provides a quick review of where Obamacare stands today; if you purchase health insurance on the individual marketplace pay attention.

The Challenges of Capturing Bull Market Returns discusses the recent records the stock market has attained, and how we tend to forget that staying invested is actually pretty difficult due to all the white noise that tries to distract us from sound investing principles. *Tax Reform – or Not?* as the title states reviews the current proposals being bandied about in DC and the odds of anything being passed.

If you have any questions about anything we have covered in the articles below, or a specific situation please feel free to give us a call, or visit our website, www.ResoluteFinancial.com.

Common Estate Planning Mistakes

The most common way to transfer assets to your heirs is also the messiest: to have a will that is so out of date that it doesn't relate to your property or estate, to have your records scattered all over the place, to have social media, banking and email accounts whose passwords only you can find—and basically to leave a big mess for others to clean up.

Is there a better way?

Recently, a group of estate planning experts were asked for their advice on a better process to handle the transfer of assets at your death, and to articulate common mistakes. The list of mistakes included the following:

Not regularly reviewing documents. What might have been a solid plan 15 or 20 years ago may not relate to your estate today. The experts recommended a full review every three to five years, to ensure that trustees, executors, guardians, beneficiaries and healthcare agents are all up-to-date. You might also consider creating a master document which lists all your social media and online accounts and passwords, so that your heirs can access them and close them down.

Using a will instead of a revocable trust. This relates mostly to people who want to protect their privacy. When assets pass to heirs via a will, the transfer creates a record that anybody, that's right anybody, can access and read. A revocable trust can be titled in your name, and you can control the assets as you would with outright ownership, but the assets simply pass to your designated successor upon death, privately. This means creditors, nosey neighbors or family members, cannot review to whom assets are passing, how wealthy you were, or what charities you funded.

Failing to fund the revocable trust. You've set up the trust, but now you and your team of professionals have to transfer title to your properties out of your name and into the trust, with you as the trustee. If you forget to do this, then the entire purpose of the trust is wasted.

Having assets titled in a way that conflicts with the will or trust. You should always pay close attention to the beneficiary designations, because they—not your will—determine who will receive your IRA assets. Meanwhile, assets (like a home) owned in joint tenancy with rights of survivorship will pass directly to the surviving joint tenant, no matter what the will or trust happens to say.

Not using the annual gift exemption. People can gift $14,000 a year tax-free to heirs without affecting the value of their $5.49 million lifetime gift exemption. That means a husband and wife with four children could theoretically gift the kids $112,000 a year tax-free. That can reduce the size of a large estate potentially below the gift exemption threshold, and in states where there is an estate tax, it can help there as well.

Not understanding the generation-skipping transfer tax. A husband and wife can each leave estate values of $5.49 million to any combination of individuals. But if there's anything left over, there's a 40% federal estate tax on those additional assets left to heirs in the next generation (the children), and an additional 40% on assets left to the generation after that (the grandchildren). Better to transfer $5.49 million out of the estate before death (tax-free, since this fills up the lifetime gift exemption) into a dynastic trust for the benefit of the grandchildren. You can also transfer that annual $14,000 to grandchildren.

Not taking action because of the possibility of estate tax repeal. Yes, the Republican leadership in Congress includes, on its wish list, the total repeal of those estate taxes. But what if there's no action, or a compromise scuttles the estate tax

provisions at the last minute? Federal wealth transfer taxes have been enacted and repealed three times in U.S. history, so there's no reason to imagine that even if there is a repeal, the repeal will last forever. Meanwhile, dynastic trusts and other estate planning tactics provide tangible benefits even without the tax savings, including protecting assets from lawsuits and claims.

Leaving too much, too soon, to younger heirs. Nothing can harm emerging adult values quite like realizing, as they start their productive careers, that they actually never need to work a day in their lives. The alternative? Create a trust controlled by a trusted family member or a corporate trust company until the beneficiaries reach a more mature stage of their lives, perhaps 30-35 years old.

Don't Miss Open Enrollment

Each year, the Affordable Care Act—popularly known as Obamacare—creates a period when health insurance policyholders can buy or change their coverage through state exchanges or the government website. This year, many locations will feature fewer carriers bidding for your business, but virtually every county in America still has coverage options.

But pay attention: the government has dramatically reduced the open enrollment period this year; in most states it starts November 1 and ends December 15. This is very important because you cannot enroll outside of open enrollment unless you have a "qualifying event," such as:

- Marriage,
- Becoming a U.S. citizen,
- Birth or adoption,
- Involuntary loss of other health coverage
- Permanent move to an area where new health plans are available. This only applies in most cases if you already had coverage prior to your move.

Can't you just continue with the coverage you have today? If you're happy with your current policy, that's one option, but prices are going up by an estimated average of 15%; in NH some policies are increasing upwards of 48% while eliminating any MA based hospitals from the network, so it doesn't hurt to look and see if your current insurer is raising rates higher than the competition.

Comparison shopping is not as difficult as it once was. The chief benefit of the ACA is the standardization. You can choose a bare bones bronze plan, a silver plan with lower deductibles and broader coverage, or a gold plan with more of both, and the various plans in each category, to qualify to be on an exchange, have to offer similar coverage features.

A second benefit is that, theoretically, the marketplaces create healthy competition among insurers, who bid for your business by lowering premiums below what they

might have charged if the marketplace didn't force them to match the competition feature-for-feature.

Of course, if you have a significant health issue come up recently, then shopping takes on a new urgency. You might consider switching from a bronze to a silver plan, or silver to gold. Or you might realize that you're not utilizing the medical system as much as you expected, and drop down to a baser metal.

Roughly 85% of the 11 million people who buy through one of the exchanges qualify for tax credits that significant reduce out-of-pocket costs for deductibles and co-pays, and can also reduce premiums. The average monthly premium before tax credits for a silver plan is $433 for 2017, but that drops to as little as $75 with tax credits. However, many uninsured adults aren't aware that they are eligible to receive this assistance. The tax credits are only available to those who enroll in a marketplace policy, and cost-sharing help is only available in the silver plans.

You can get help enrolling and comparing plans by phone or with a local in-person guide, called a navigator. ACA marketplace call centers are available 24 hours a day, every day except holidays. At HealthCare.gov, you can search by city and state or ZIP code to see a list of local organizations that can help you.

The Challenges of Capturing Bull Market Returns

You probably didn't notice, but in early September we marked a milestone: the S&P 500 index's bull market became the second-longest and the second-best performing in the modern economic era. Stock prices are up 270% from their low point after the Great Recession in March 2009—up 340% if you include dividends. That beats the 267% gain that investors experienced from June 1949 to August 1956. (The raging bull that lasted from October 1990 to March 2000 is still the winningest ever, and may never be topped.)

With the benefit of hindsight, it's easy to think that the long eight-year ride was easy money; you just put your chips on the table when the market hit bottom and let them ride the long bull all the way to where we are today. We tend to forget that staying invested is actually pretty difficult, due to all the white noise that tries to distract us from sound investing principles.

Consider, for example, that initial decision to invest in stocks that March. We had just experienced the worst bear market (down 57.7% from the peak in October 2007) since the Great Depression, and were being told many plausible reasons why prices could go lower still. After all, corporate earnings were dropping from already-negative territory. Was that the time to buy, or should you respond by waiting out the next couple of years until a clear upward pattern emerged?

The following year, investors were spooked by the so-called "Flash Crash," which represented the worst single-day decline for the S&P 500 since April 2009. Then came 2011, two to three years into the bull, when the S&P 500 declined 20% from its peak in May through a low in October. The pundits and touts proclaimed that another recession was looming on the horizon, which would take stocks down still further. Surely THAT was a good time to take your winnings and retreat to the sidelines.

By the time 2012 rolled around, there was a new reason to take your chips off the table: the markets were hitting all-time highs. Of course, historically, all-time highs are not indicative of anything other than a market that has been going up. If you decided to take your gains and get out of the market when the S&P 500 hit its first all-time high in 2012, you would have missed an additional 98% gain.

The headline distraction in 2013 was rising interest rates, which were said to be the "death knell" of the bull market. Low rates, it was declared were the "reason" for the incredible run-up from 2009-2012, so surely higher rates would have the opposite effect. (The "experts" were wrong. The S&P 500 would advance 32% in 2013, its best year since 1997.)

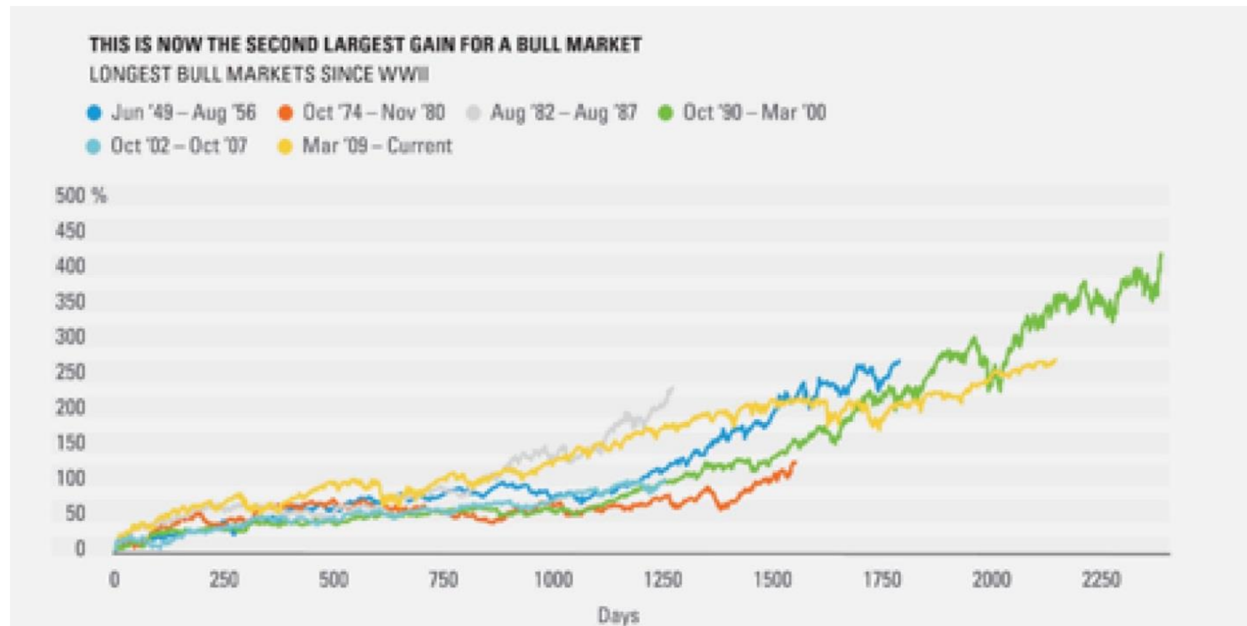
In 2014, the U.S. dollar index experienced a strong advance, as markets began to expect the U.S. Fed to end its QE program. A falling dollar and easy Fed money were said to be responsible for the "aging" bull market, so this surely meant that it was time to head for the exits. Instead, the index ended 2014 with a 13.7% gain.

The following year, a sharp decline in crude oil prices was said to be evidence of a weakening global economy. The first Fed rate hike (in December 2015) since 2006 led many institutional investors to sell their stocks in the worst sell-off to start a year in market history. The 52-week lows in January and February were said to be extremely bearish; the market, we were told, was going much lower. Instead, the S&P 500 ended 2016 up 12%.

Today, you'll hear that the bull market is "running out of steam," and is "long in the tooth." New record highs mean that there is nowhere to go but down. In other words, you are, at this moment, subject to the same noise—in the form of extreme forecasts, groundless predictions, prophesies and extrapolation from yesterday's headlines—that has bombarded us throughout the second-longest market upturn in history.

This is not to say that those dire predictions won't someday come true; there is definitely a bear market in our future, and several more after that. But investors who tune out the noise generally fare much better, and capture more of the returns that the market gives us, than the hyperactive traders who jump out of stocks every time there's a scary headline. As we look back fondly at the yellow line in the middle of the graph, let's recognize that holding tight through big market advances and allowing

your investments to compound is never easy. But it can be extremely profitable in the long run.



Tax Reform—or Not?

You can be forgiven if you're skeptical that Congress will be able to completely overhaul our tax system after failing to overhaul our health care system, but professional advisors are studying the newly-released nine-page proposal closely nonetheless. We only have the bare outlines of what the initial plan might look like before it goes through the Congressional sausage grinder:

We would see the current seven tax brackets for individuals reduced to three — a 12%, rate for lower-income people (up from 10% currently), 25% in the middle and a top bracket of 35%. The proposal doesn't include the income cutoffs for the three brackets, but if they end up as suggested in President Trump's tax plan from the campaign, the 25% rate would start at $75,000 (for married couples), and joint filers would start paying 35% at $225,000 of income.

The dreaded alternative minimum tax, which was created to ensure that upper-income Americans would not be able to finesse away their tax obligations altogether, would be eliminated under the proposal. But there is a mysterious notation that Congress might impose an additional rate for the highest-income taxpayers, to ensure that wealthier Americans don't contribute a lower share than they pay today.

The initial proposal would nearly double the standard deduction to $12,000 for individuals and $24,000 for married couples, and increase the child tax credit, now set at $1,000 per child under age 17.

At the same time, the new tax plan promises to eliminate many itemized deductions, without telling us which ones other than a promise to keep deductions for home mortgage interest and charitable contributions. The plan mentions tax benefits that would encourage work, higher education and retirement savings, but gives no details of what might change in these areas.

The most interesting part of the proposal is a full repeal of the estate tax and generation-skipping estate tax, which affects only a small percentage of the population but results in an enormous amount of planning and calculations for those who ARE affected.

The plan would also limit the maximum tax rate for pass-through business entities like partnerships and LLCs to 25%, which might allow high-income business owners to take their gains through the entity rather than as income and avoid the highest personal brackets.

Finally, the tax plan would lower America's maximum corporate (C-Corp) tax rate from the current 35% to 20%. To encourage companies to repatriate profits held overseas, the proposal would introduce a 100% exemption for dividends from foreign subsidiaries in which the U.S. parent owns at least a 10% stake, and imposes a one-time "low" (not specified) tax rate on wealth already accumulated overseas.

What are the implications of this bare-bones proposal? The most obvious, and most remarked-upon, is the drop that many high-income taxpayers would experience, from the current 39.6% top tax rate to 35%. That, plus the elimination of the estate tax, plus the lowering of the corporate tax (leading to higher dividends) has been described as a huge relief for upper-income American investors, which could fuel the notion that the entire exercise is a big giveaway to large donors. But the mysterious "surcharge" on wealthier taxpayers might take away what the rest of the plan giveth.

But many Americans with S corporations, LLCs or partnership entities would potentially receive a much greater windfall, if they could choose to pay taxes on their corporate earnings at 25% rather than nearly 40%.

A huge unknown is which deductions would be eliminated in return for the higher standard deduction. Would the plan eliminate the deduction for state and local taxes, which is especially valuable to people in high-tax states such as New York, New Jersey and California, and in general to higher-income taxpayers who pay state taxes at the highest rate?

Currently, about one-third of the 145 million households filing a tax return — or roughly 48 million filers — claim this deduction. Among households with income of $100,000 or more, the average deduction for state and local taxes is around $12,300. Some economists have speculated that people earning between $100,000 and around

$300,000 might wind up paying more in taxes under the proposal than they do now. Taxpayers with incomes above $730,000 would hypothetically see their after-tax income increase an average of 8.5 percent.

Big picture, economists are in the early stages of debating how much the plan might add to America's soaring $20 trillion national debt. One back-of-the-envelope estimate by a Washington budget watchdog estimated that the tax cuts might add $5.8 trillion to the debt load over the next 10 years. According to the Committee for a Responsible Federal Budget analysis, Republican economists has identified about $3.6 trillion in offsetting revenues (mostly an assumption of increased economic growth), so by the most conservative calculation the tax plan would cost the federal deficit somewhere in the $2.2 trillion range over the next decade.

These cost estimates have huge political implications for whether a tax bill will ever be passed. Under a prior agreement, the Senate can pass tax cuts with a simple majority of 51 votes — avoiding a filibuster that might sink the effort — only if the bill adds no more than $1.5 trillion to the national debt during the next decade.

That means compromise. To get the impact on the national debt below $1.5 trillion, Congressional Republicans might decide on a smaller cut to the corporate rate, to something closer to 25-28%, while giving typical families a smaller 1-percentage point tax cut. Under that scenario, multinational corporations might be able to bring back $1 trillion or more in profit at unusually low tax rates, and most families might see a modest tax cut that will put a few hundred extra bucks in their pockets.

Alternatively, Congress could pass tax cuts of more than $1.5 trillion if the Republicans could flip enough Democratic Senators to get to 60 votes. The Democrats would almost certainly demand large tax cuts for lower and middle earners, potentially lower taxes on corporations and higher taxes on the wealthy. Would you bet on that sort of compromise?

For more information on these topics or for a free consultation, contact Resolute Financial, LLC at (978) 463-8771 ext. 1003.

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