Wealth Management

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REGISTERED INVESTMENT ADVISOR

First Quarter 2020

The Remarkable Decade

As 2019 came to a close, several writers took note of the progress that has been made in recent years. Good news often goes unreported, because it doesn't attract as many clicks or eyeballs in the digital age. But there has been quite a bit of good news.

For example, Nicholas Kristoff wrote in *The New York Times* that "This Has Been the Best Year Ever." Among the glad tidings:

- In 1950, 27% of children died by age 15. Now only 4% do.
- The percentage of people living in "extreme poverty" (defined as subsisting on $2 per day or less) has fallen from 42% in 1981 to 10% today.
- Fifty years ago a majority of people worldwide were illiterate. Now we are approaching 90% adult literacy.
- In recent years, every day another 325,000 people acquired electricity for the first time, and 200,000 got piped water. Every day some 650,000 were able to go online for the first time, according to the World Bank.

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Estate Planning

More Estate Tax Protection

As of January 1, 2020, the amount exempt from the federal estate and gift tax has grown with inflation to $11,580,000 per decedent. For a married couple, should they both die this year, only families with combined estates larger than $23,160,000 need be concerned with the federal estate tax.

However, under current law, that exempt amount is scheduled to fall roughly in half in 2026. What's more, several of the Democratic presidential candidates have announced plans for a wealth tax, an idea that amounts to imposing an estate tax every year instead of once in a lifetime. A middle ground might be to drop the fed-

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The SECURE Act Upends Estate Plans

The Setting Every Community Up for Retirement Enhancement (SECURE) Act [H.R. 1994] passed the House last year on a bipartisan basis, by a vote of 417 to 3, but then stalled in the Senate. A few Republican Senators objected to unanimous consent for the bill. In December, Congress enacted tax-and-spend legislation that included the SECURE Act, taking effect the first of this year.

The Act includes a number of liberalizations that should promote retirement savings. For example, the prohibition on contributing to a traditional IRA upon reaching age 70½ has been eliminated. Required minimum distributions from IRAs and qualified retirement plans may now be delayed to age 72, rather than age 70½.

To pay for the changes that result in delayed tax collections, Congress changed the rules rather drastically for inherited IRAs. Under the old rules, one who inherited a traditional or a Roth IRA was allowed to take minimum distributions from the account over his or her lifetime. For example, a 50-year-old could spread the payments out over 34.2 years. If a great-grandchild inherited the account, the payout period could be as long as 80 years!

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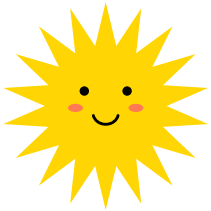
The remarkable decade . . . CONTINUED



There are plenty of problems left to solve in the world, but progress of this sort ought to be recognized for the hope it may inspire.

Doing more with less

In a similar vein, Matt Ridley covered progress in Britain in "We've just had the best decade in human history. Seriously" published in The Spectator. Asia and Africa have experienced faster economic growth than Europe or North America, with the consequence that global inequality is falling. Famine is nearly extinct. Malaria, polio, and heart disease are in decline.

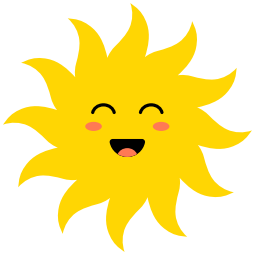
Ridley goes on to assert that we are consuming less, even during periods of prosperity. As one simple example, he notes that in 1959, each drink can contained 85 grams of aluminum. Today, just 15 grams are needed, and most are obtained from recycled material.

Consumption appears to have peaked in Britain about 2000. "The quantity of all resources consumed per person in Britain (domestic extraction of biomass, metals, minerals, and fossil fuels, plus imports; minus exports) fell by a third between 2000 and 2017, from 12.5 tonnes to 8.5 tonnes," Ridley reports. Even though the population has grown since then, that growth has been outpaced by this decline in resource use. The net result is that fewer resources are being consumed in absolute terms.

Increases in agricultural productivity mean that much less land is required to feed even a growing population. In a 2012 study, Jesse Ausubel of Rockefeller University concluded that 65% less land was being used for a given amount of food production compared to 50 years earlier. Less land dedicated to agriculture means that forests are expanding, especially in the richer countries. The return of habitat is accompanied by a rebound in animal and bird populations.

Perhaps the most surprising statistic is that total energy consumption in Britain has fallen by 10% since 1970, even though the population is up 20% and the economy has tripled. Improved energy efficiency gets part of the credit. However, another factor is that some energy-intensive industries, such as the steel, aluminum, and chemical companies, have relocated offshore. Imports of these commodities include embedded energy usage that doesn't show up in the tallies.

Can we keep it going?



The Dow Jones Industrial Average opened the last decade at 10,430.49. It closed at 28,538.44. It was a great decade to invest in stocks, unlike the first decade of this century when the DJIA finished lower.

There are at least two schools of thought. One is that the current bull market has the longest duration of any in U.S. history, and it is overdue for a correction. When we are at record highs, the upside potential is smaller than the downside risk.

The other theory is that the fundamentals of the American economy remain very strong, especially the employment numbers. Although recessions may be inevitable, there isn't one on the horizon as of yet. ■

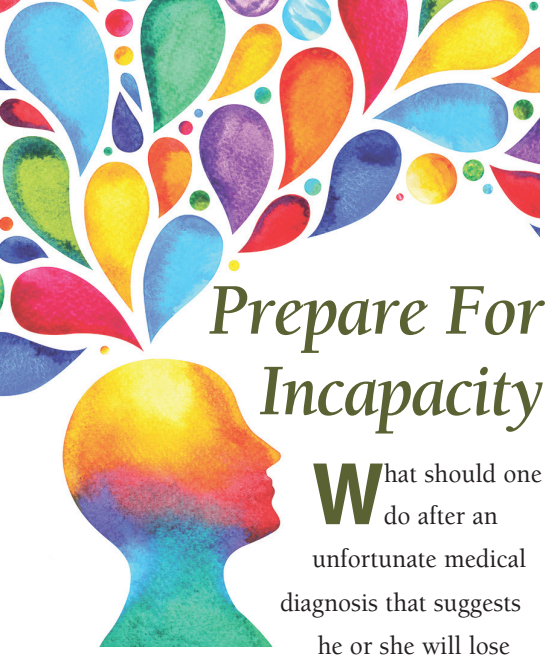
Protection . . . CONTINUED

eral exempt amount earlier than 2026.

The amount exempt from federal estate and gift tax has never been reduced, although reduction has been threatened twice, most recently in 2011. The possibility of increased taxes on accumulated wealth has triggered some estate planners to recommend "use it, don't lose it" strategies for locking in today's larger exemption. This may be achieved by making taxable gifts large enough to consume the lifetime gift tax credit (that is, $11,580,000 or more).

In November, the IRS issued final regulations on what happens if the estate tax exemption falls in the future. In short, the Service blessed the idea that if one takes advantage of the larger gift tax credit today, the tax benefit won't be lost in the future when estate tax obligations are calculated.

The vast majority of families no longer need to worry about the federal estate tax. A minority of states continue to impose estate or inheritance taxes (or both) at death, and the state exemption levels are much lower than the federal one. If you live or own property in such a state, you'll want to review your choices with your estate planning advisors. ■



Prepare For Incapacity

What should one do after an unfortunate medical diagnosis that suggests he or she will lose mental and physical abilities in the near term? Key concerns: testamentary dispositions, health care preferences, long-term care preferences, and substituted decision making.

Estate planning

Usually, estate planning involves a substantial amount of guesswork and ambiguity. How far into the future will it be before the plan is needed? What family circumstances might change in the interim? What will the assets be? What will the tax laws be like?

Many of these uncertainties may be swept away when someone is on the verge of incapacity, because this could be the final review of testamentary documents. Beneficiaries need to be reviewed.

This is also a good time to determine if any of the probable beneficiaries has a disability. If so, care needs to be taken so that their inheritance does not compromise their access to government benefits.

Revocable living trusts

A revocable living trust is a superior tool for asset management in case of incapacity, because a trustee typically will have an easier time dealing with brokers and banks than would an attorney-in-fact. The trust document also needs to be reviewed carefully if an onset of incapacity is expected.

For example, should the trustee be empowered to make distributions to heirs before the trust creator's death? Or is the trust to be for the sole benefit of the trust creator and perhaps spouse? The trust needs to be crystal clear on this point.

If individuals will serve as trustee instead of a corporate trustee, when should *they* be removed for incapacity? What standard should be used? Should the opinion of a physician be required?

Health care at the end of life

Typically, we expect heroic medical procedures for those who have a long and productive life ahead of them. The specter of incapacity may change this calculus. How aggressive does the individual want treatments to be? Are there treatments that should be avoided?

Does the individual want a durable power of attorney for health care decisions? Who should be the power holder? The power will need to comply with the Health Insurance Portability and Accountability Act of 1996 (HIPAA).

An *advance medical directive* is also advisable for setting out expectations for medical treatment. What artificial means of extending life should be used? What should be avoided? These issues need to be discussed with family members to minimize future misunderstandings and conflicts.

Long-term care

A diagnosis of impending incapacity makes the need for planning for long-term care urgent. Step one is to determine how long someone may be able to stay in the home. Does the design of the house present obstacles to remaining there? Can they be fixed?

Who will provide the long-term care?

Most such care is provided without charge by family members, such as a spouse or adult children. However, as dementia sets in, professional help may be required.

Will the person's income be sufficient to cover the costs of a nursing home? Is long-term care insurance part of this picture? The analysis can be daunting. If the income will not be sufficient, a plan may be needed for the orderly liquidation of assets to cover those costs.

Substituted decision making

Who will make decisions when the individual loses the capacity to do so? For asset management, the trustee of a living trust may handle those duties. For legal, medical, and personal issues, the durable power of attorney will be used. In general, a family member will be given this responsibility.

Should the power of attorney include the power to make gifts? If so, how broad should the power to make gifts be? Should the class of recipients be limited or unlimited? Should the amounts of the gifts be limited to the annual federal gift tax exclusion ($15,000 this year)?

The attorney-in-fact will not automatically be able to handle tax matters. The IRS requires the filing of Form 2848 for this purpose. Similarly, the Social Security Administration requires a person to be appointed Representative Payee to be able to affect a third party's benefits. The law recently has been changed in this area. The Strengthening Protections for Social Security Beneficiaries Act of 2018 included a provision for designating representative payees, and the Commissioner of Social Security was directed to come up with a procedure for implementation. The change in law becomes effective April 13, 2020. ■

This planning strategy was known as the "stretch IRA," and it was understandably popular. To assure that the IRA was not invaded prematurely, some people paired the stretch IRA with a trust plan.

The SECURE Act largely eliminates the stretch IRA. The general rule now is that the IRA assets must be distributed over the ten years following the account owner's death. Exceptions are made for these designated beneficiaries:

- a surviving spouse;
- a minor child or children;
- a disabled beneficiary;
- a chronically ill individual; and
- beneficiaries who are less than ten years younger than the account owner (such as a brother or sister).

The exception for the minor child lasts only until he or she reaches the age of majority, because then the ten-year rule kicks in. For the other categories of designated beneficiaries, the delay in distributions ends at death when a ten-year distribution must begin.

Eliminating the stretch IRA accelerates the taxes on the retirement savings, shortens the deferral period, and it also makes it more likely that the distributions will occur during the beneficiary's high-earning years instead of being delayed until retirement. If a large IRA will be a significant element of your estate, you should consider meeting with your estate planning advisors early this year.

Sample questions and answers

I turned 70½ in 2019, so am I excused from taking a required minimum distribution now? Or next year? Sorry, the change does not affect you. Only those who turn 70½ in 2020 or later get the benefit of waiting to age 72 for required minimum distributions. You will have to take a minimum distribution for the 2019 tax year (if you haven't already) as well as the 2020 tax year.

I inherited an IRA three years ago from a parent and have been taking minimum distributions over my lifetime. Does that have to change now, do I take the rest over ten years? Good news, the new law does not affect you. IRAs inherited from those who died after December 31, 2019 are the ones affected by the new law.

My children are adults, but my grandchildren are not. Can they get the benefit of waiting until they reach their majority for the ten-year rule to apply? Sorry, no. The exception only is for minor children of the account owner, not grandchildren, nieces, or nephews. These more remote relatives will need to withdraw everything from the account over ten years. ■

Collectors Corner

Dwight Clark Shepler, *Sun Valley / Union Pacific,* circa 1940

Sun Valley was created as a destination resort to encourage people to ride the railroad out west. It was the brainchild of Averill Harriman, Chairman of the Board of Union Pacific Railroad, who was himself an avid skier. The Ketchum Idaho area was scouted out by Count Felix Schaffgotsch who reported back to Harriman that "it contains more delightful features for a winter sports center than any other place I have seen in the United States, Switzerland or Austria."

This vintage poster for Sun Valley will be offered at auction on February 13 by the Swann Auction Galleries. The estimated value is $8,000 to $12,000.

Image courtesy of Swann Auction Galleries

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