

Wealth Management Ideas

2014



- Income, safety or growth?
- Elder law essentials
- Hidden Social Security strategies
- "Back to basics" estate planning

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Trustworthy advice. Now more than ever.

There isn't a single best way to manage money. Every family, and every individual, presents a unique set of circumstances, resources, aspirations. For every objective in the financial planning realm, there are a number of sound alternatives to evaluate.

From understanding and making these choices comes the plan that will be best for you and your family.

Here we present for your consideration a sampling of the planning opportunities worthy of your consideration this year. From building your capital to retirement and, finally, to managing family wealth transfers, we can be a valuable resource for you, as demonstrated within these pages.

When you are ready, we will be pleased to be of service.

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Income, safety or growth?

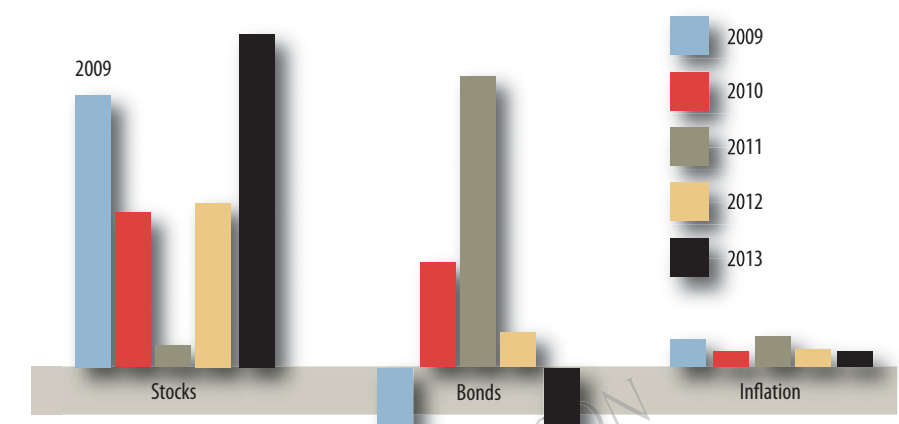
Steps to steady your portfolio

Investors in recent years have been looking at financial markets that are largely without precedent. Short-term interest rates have been at rock bottom for an extended period of time, and longer-term rates are not much higher. Bond investors have the twin worries of low current yield and the possibility of principal loss on paper should interest rates begin moving higher. Stock markets have been buffeted by a variety of international forces. Although market performance has been exceptional, the lingering cloud of unsatisfactory employment numbers hangs over the U.S. economy.

Stocks and bonds have been on a roller-coaster ride during this volatile economy. After suffering a 37% collapse in 2008, the large company stocks represented by the S&P 500 grew by 26% in 2009 and 15% in 2010 (including dividends). Bonds delivered almost a mirror image, gaining nearly 26% in 2008, then losing nearly 15% the following year, as stocks returned to favor. Last year stocks returned an eye-popping 32.39%, while long-term bonds lost 11.36%. Here is more detail on the recent performance of the indices:

BALANCING ACT

To avoid the extremes of one asset class or another, one needs to employ an asset allocation strategy for smoothing portfolio performance. Much of the riskiness of an investment portfolio can be mitigated by the mix chosen. Here are the returns for various mixes of stocks and bonds in the five-year period 2009-2013.



Source: M.A. Co.



Questions for my advisor

What are the risk exposures of my current investment portfolio?

When should I rebalance my portfolio?

How much upside is left for stocks?

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PORTFOLIOS: GROWTH OF VARIOUS MIXES (IN %)

Year	100% stocks	70% stocks, 30% bonds	50% stocks, 50% bonds	30% stocks, 70% bonds	100% bonds
2009	26.46%	12.97%	4.49%	-3.58%	-14.90%
2010	15.06	14.52	13.70	12.53	10.14
2011	2.11	10.07	15.34	20.56	28.23
2012	16.00	12.42	9.91	7.32	3.31
2013	32.39	17.70	8.69	0.26	-11.36

Source: M.A. Co. Data: 2014 Ibbotson SBBI Market Report

An asset allocation plan will employ many more than two asset classes. The historical performance of the asset classes is the starting point; the degree to which the classes move in sync or not is determined mathematically. With these coefficients in hand, the portfolio may be optimized. That means expected performance may be maximized for a given level of acceptable investment risk. Alternatively, risk may be minimized for a target level of return.

Does the Fed move the market?

The great temptation for investors is to “time” the market, to buy at the bottom and sell at the top. Especially when overall returns are poor, the temptation can be very strong. However, calling market tops and bottoms with any degree of accuracy is chancy at best. Studies have long shown that missing as few as the five best days in a market can cut total return for a year by half or more. Hence, the conventional wisdom that “time in the market is more important than timing the market.”

But what if you knew with confidence which days led to excess market returns? A recent staff paper by economists at the Federal Reserve Bank of New York suggests that the exceptional days have been identified.

Eight times each year the Federal Open Market Committee (FOMC) meets to set monetary policy. Since 1994 the outcomes of the meetings have been announced

publicly at scheduled intervals. The economists looked at the performance of the S&P 500 during the three-day window surrounding those announcements.

They found a persistent, abnormal rise in stock prices in the 24 hours preceding the FOMC announcements. Interestingly, the increase did not continue after the announcement, nor was it dependent upon the announced direction for interest rates. What’s more, the phenomenon also was observed in international markets.

According to the researchers, “more than 80% of the equity premium [in the S&P 500] has been earned over the twenty-four hours preceding scheduled FOMC announcements.” The researchers were surprised by these results, and they were unable to explain them with existing models of investor behavior.

Monetary policy is a shifting variable that investors must factor into their decisions.

FOMC announcements are the moments when the uncertain becomes certain, at least until the next announcement. Apparently, as that moment of clarity approaches, sellers become less willing to sell, as they await the resolution. Buyers may be extra optimistic, hoping that the next Fed action is more likely than not to be stimulative.

Whatever the reasons behind the phenomenon, it appears that owning stocks on the day before a Fed announcement is likely to be a good idea. Now that professional traders also know this secret, the pattern might become even more pronounced.

Elder law essentials

An AARP study of fraud victims released in 2011 found that their average age was 69. According to the report, older adults are apparently more trusting than younger ones; they are more open to hearing sales presentations; and they are more likely to accept propositions that should be recognized as too good to be true—guaranteed high investment returns with no risk, for example.

National Public Radio reported on two studies that suggest aging may be associated with a declining ability to pick up on risk cues. When presented with photos of people who could be considered trustworthy, neutral or untrustworthy, older adults scored the neutral and trustworthy faces the same as younger ones did. However, they also rated the untrustworthy faces as much more trustworthy than did the younger participants. Subsequent tests with brain imaging suggested that the part of the brain that processes risk and danger has relatively lower activity in older adults.

The net result is that retirees may be vulnerable, at a time when financial fraud is a growing problem. They need to keep their guard up, and their family members need to help them do it.

A new specialty in legal practice, “elder law,” has emerged over the past few decades, in part in response to this need. Retirees and senior citizens have some special laws and programs that apply only to them, and the laws that apply to all of us may take on a new aspect when applied in the unique circumstances that the elderly face. The core areas about which elder law attorneys provide advice include:

- health and long-term care planning;
- access to public benefits, including Medicare, Medicaid and Social Security;
- older persons’ legal capacity;
- surrogate decision-making, including both medical and property management decisions;
- wills, trusts and estates.

Although any attorney may include elder law advice in his or her practice, some are now becoming specialists in this field, and national organizations have been created for specialist certification. To achieve a specialist designation, an attorney must be able to help with insurance, housing, long-term care, employment and retirement issues.

Planning for health-care needs

Most retirees will not need to consult an attorney to secure their routine Medicare benefits or Social Security payments. Medicaid benefits are another matter, as they are subject to an array of complex rules that an attorney can help sort through.

The elder law attorney also should be consulted for drafting a living will, to provide guidance on making medical decisions when one is terminally ill. Among the questions to consider before executing a living will:

- How do you feel about ventilators, surgery, drugs or tube feeding if you become terminally ill? If you are unconscious and not likely to awaken? If you become senile?



Questions for my advisor

How can I protect my finances if I become incapacitated?

When should I give my house to my kids?

Am I too wealthy for Medicaid planning?

DOCUMENTS FOR DELEGATING

Planning at the end of life involves the delegation of various responsibilities to others, who must act on behalf of the one doing the delegating. Here are the types of documents that one may encounter.

DOCUMENT	WHAT IT DOES
MEDICAL:	
Living will	Provides guidelines for medical decisions when an individual becomes terminally ill
Do not resuscitate order (DNR)	Specifically requests that cardiopulmonary resuscitation not be used if one's heart or breathing stops
Power of attorney for health care	Identifies an individual to make medical decisions when one is unconscious or incapacitated.
FINANCIAL:	
Power of attorney	Delegates authority to an agent to make financial decisions. The agent's authority ends when the principal is incapacitated.
Durable power of attorney	Delegates financial decision power to an agent, even if the principal is incapacitated. In some cases, the power "springs" into being upon incapacity or other identified event.
Revocable living trust	Transfers assets and full financial management authority to a trustee. The trust may continue into incapacity, even beyond the death of the trustor.

Source: M.A. Co.

- What sort of mental, physical or social abilities are important for you to have in order to enjoy living?
- What kind of medical treatment would you want if you had a severe stroke or other medical condition that made you dependent upon others for all your care?

A living will tries to answer such questions, yet one readily can see that answers are almost impossible. No one can guess what medical emergency might be faced in the future, nor what medical advances might be made in the coming years to deal with it. In fact, some studies have shown that similarly situated patients tend to get the same care whether or not they have living wills.

That's why most experts advise having a *durable power of attorney for health care* in addition to a living will. This document identifies an individual whom you have chosen to make health care decisions on your behalf, when you are unable to make your wishes known. Most importantly, this document provides effective guidance before a diagnosis of terminal illness is made. For example, withholding of nutrition and hydration generally cannot be authorized by a living will, but they can be ordered under a power of attorney for health care.

Advance financial directives

Getting advance financial directives in place is one sound way to combat potential financial fraud.

The most basic tool for delegating authority to make financial decisions is the *power of attorney*. The power normally is drafted by an attorney, such as an elder law specialist, and the authority that it creates may be as broad or as narrow as needed. However, a traditional power of attorney is effective only so long as the person who created it is competent. Therefore, a *durable power of attorney* may be a better choice, because it continues in force regardless of the competence of the person whose affairs are being managed. In some cases, a power of attorney doesn't become effective until the occurrence of a future event, such as the onset of a disability. Such an approach is called a *springing power of attorney*.

The more comprehensive approach to financial management at the end of life is the *revocable living trust*. Investment assets are placed in the care of a *trustee*, who manages them consistent with the terms laid out in a trust agreement. The trustee may be empowered to handle routine financial chores—paying bills and taxes, for example—as well as the more demanding duties associated with portfolio management.

A living trust provides continuous financial protection in the event that the trust grantor becomes incapacitated. There's no need to involve a court in a public proceeding for a guardianship or conservatorship to handle financial matters.

Are you ready?

We don't practice law, elder law or otherwise. For that, you must seek advice from an attorney. We do provide investment management and trusteeship services. One of today's most cherished luxuries is attentive, personalized service from people who not only know their business but also enjoy helping others. We work hard to provide our living trust customers with that standard of service. You can gauge our capabilities by talking over your own plans with one of our asset managers. Why not make an appointment this month?

Hidden Social Security strategies

To have a successful, financially secure retirement, one must have enough income to live on. The larger one's Social Security benefit is, the easier it is to meet that need. So it's something of a puzzle that so many individuals are deciding to take their benefits early. A recent study from the Government Accountability Office (GAO) reported that 72.8% of retirees begin their benefits before reaching normal retirement age.

Early benefits are lower benefits. The table on the next page shows just how much benefits will be reduced, based upon the year of one's birth. Note that the spousal benefit will also be reduced, creating the potential of financial insecurity for the widow or widower.

For those in their early 60s this year, normal retirement with full benefits may begin at age 66. Retiring at age 62 triggers a 25% cut in benefits. Looked at another way, one can boost one's Social Security benefit by fully one-third by waiting until age 66 to begin drawing it. What's more, if one continues working from age 62 to age 66, the additional earnings record and Social Security taxes paid also will increase the eventual benefit. That larger benefit will be the basis for future inflation adjustments and so can translate into substantially higher lifetime.

Still, the thought process of someone who is 62 might go something like this. If I don't take my early benefits, how much am I leaving on the table? How many years of collecting "full" benefits will it take to offset the four years of taking no benefits at all? The answer is 12 years. One needs to live to age 78 to "break even" on the decision to wait for the full retirement age. At age 62, that's pretty far off on the horizon. Perhaps the early retirees are not being so irrational after all.

Another perspective

Some people are under the impression that Social Security is not a good investment. On the contrary. The GAO study referred to above offered an interesting illustration.

Imagine that Don's annual benefit at normal retirement age would be \$16,000 per year, and he chooses to begin an early benefit of \$12,000 per year at age 62. When he reaches age 66, Don realizes that he really will need \$16,000 per year after all. To achieve that, he buys a single-life annuity of \$4,000 per year. Could he buy that with the \$48,000 in early benefits he's collected? No, he could not, not even close. According to the study, the commercial cost of an inflation-adjusted, single-life \$4,000 annuity for a male would be \$71,000 (higher for females, who have longer life expectancies).

As a group, retirees are living longer and longer. Most people will live to "break even" on a decision to delay their retirement.



Questions for my advisor

I'm 64 years old this year and collecting my Social Security benefits. I'm thinking about going back to work—how much can I earn before my benefits will be cut?

I'm divorced. When can I start collecting benefits on my ex-spouse's earnings record?

How do we decide if "file and suspend" is right for us?



Planning for couples

When a husband and wife each have earnings records, the choices are more complicated, and more important to understand. Each partner has a basic benefit plus a spousal benefit, but may only collect the larger benefit. However, one may begin collecting a spousal benefit and then switch to one's own benefit later, allowing that benefit to grow to its full value or more. For example, the higher earner in a couple might file for spousal benefits at retirement age, letting the larger benefit continue to grow until he or she switches to it at age 70, when the delayed retirement credits are maxed out.

Another strategy is to "file and suspend." For example, a husband might file for his benefits at age 66, but suspend them, allowing his benefit to grow until he reaches age 70. Meanwhile, the wife can go right ahead and collect the spousal benefit based upon the husband's benefit at age 66.

A recent study has concluded that if couples optimized their Social Security benefits with these strategies, the cost to the Social Security Administration would be nearly \$24 billion per year in increased payments. That's the amount the married couples are "leaving on the table" if they each simply claim their own Social Security benefits and fail to take account of their potential spousal benefits.

THE EARLY RETIREMENT TRADE-OFF

Early retirement means collecting a smaller benefit for a longer period of time. In the aggregate, the theoretical total benefit is exactly the same. This table shows how benefits will be adjusted based upon the year of birth.

			AT AGE 62			
Year of birth	Normal retirement age	Months from age 62 to full retirement age	A \$1,000 retirement benefit would be reduced to	The retirement benefit is reduced by	A \$500 spouse's benefit would be reduced to	The spouse's benefit would be reduced by
1943-1954	66	48	\$750	25.00%	\$350	30.00%
1955	66 and 2 months	50	\$741	25.83%	\$345	30.83%
1956	66 and 4 months	52	\$733	26.67%	\$341	31.67%
1957	66 and 6 months	54	\$725	27.50%	\$337	32.50%
1958	66 and 8 months	56	\$716	28.33%	\$333	33.33%
1959	66 and 10 months	58	\$708	29.17%	\$329	34.17%
1960 and later	67	60	\$700	30.00%	\$325	35.00%

Source: Social Security Administration; M.A. Co.

"Back to basics" estate planning

The nontax elements of estate planning can be essential to family harmony.

The traditional "hot button" that motivates people to see their lawyers about estate planning is taxation. Death taxes—inheritor taxes, estate taxes, federal taxes, state taxes—have taken a notorious toll on unplanned estates over the years. With sound planning, that burden can be lightened or even eliminated. In many cases, the tax savings easily cover the cost of the attorney's fees for creating the estate plan.

That hot button has cooled considerably this year, as the federal estate tax exemption equivalent is \$5.34 million through 2014. Married couples can double this, to \$10.68 million, at relatively little cost. Accordingly, most families may be forgiven for feeling that they are no longer a tax target. But estate planning always has been about much more than tax planning. Estate planning always has been about financial protection for beneficiaries, with tax minimization just a means to that end.

If you haven't attended to your estate planning, don't use the excuse of tax uncertainties to put it off any longer.

Evaluate

To begin, you have to know what you are working with.

- **Inventory assets.** Your estate plan will have to dispose of everything that you own; otherwise the state's law of intestacy will apply. Bank accounts, stocks, bonds, real estate, business interests, of course. Don't overlook insurance policies and retirement plan benefits. You'll need to know *how* as well as *what*. Which property is owned jointly, which is owned outright.
- **Check beneficiary designations.** If you have an IRA or an employer-provided retirement plan, you already have started on your estate planning when you made your beneficiary designations. These designations should be reviewed periodically, especially when there have been changes in family circumstances, especially a divorce.
- **Identify beneficiaries.** A surviving spouse and children are the usual persons to be protected. You may have more distant relatives to include, and you may want to remember some charities in your estate plan. Don't overlook the need to care for your pets after your death.
- **Weigh trust benefits.** Trusts offer a wide range of financial benefits, especially valuable when beneficiaries need help with money management. Trusts may be established and funded during life (the *living trust*) or in a will (the *testamentary trust*). See "Intro to trusts" on the next page for more.



Questions for my advisor

Will my estate be exposed to estate taxes, inheritance taxes, or both?

What's the difference between per capita and per stirpes?

Where should I keep my will?

A NEW WRINKLE IN TAX PLANNING AT DEATH

Estate taxes historically have been imposed at higher rates than income taxes—the current federal estate tax is a flat 40% of the amounts above the exemption for most estates. That high rate was rationalized by the fact that death also wipes out taxes on unrealized capital gains. The tax basis of inherited assets generally has been their fair market value at the decedent's death, even if the decedent's tax basis was very low. The estimated "tax cost" of this forgiveness has been large, but the alternative of "carryover basis" has been found to be almost impossible to administer. The person with the best knowledge of the basis of the assets has died, after all.

In contrast, when a transfer is by gift, instead of through an estate, the donee takes the donor's basis. When the donor is alive, he or she can provide the details for establishing basis. With gifts, the donee could be exposed to significant taxes on the capital gain when the asset is sold later.

Given the shelter of the permanently enlarged and indexed federal exemption from estate taxes, the focus of tax management for many estates has shifted to the income tax. More attention needs to be given to the income tax consequences of any wealth transfer idea.

Example. Grandmother plans to give \$14,000 worth of stock to Grandchild. She can select from her portfolio either Lot A, with a basis of \$13,500, or Lot B, with a basis of \$1,000. The gift should be made of Lot A, because Grandchild then will be concerned with only \$500 worth of gain. If Grandmother holds Lot B until her death, its basis will be stepped up to fair market value.

Implement

The next steps require the advice of an attorney and the execution of legal documents.

- **Make a will.** Your will contains instructions for the disposition of your property. It also nominates an executor or personal representative to manage the settlement of your estate.
- **Make a living will.** This document addresses your expectations for medical care at the end of your life. You also may want to execute a power of attorney for health care to identify an individual to make medical decisions on your behalf.
- **Execute a durable power of attorney.** Identify an individual who can make financial decisions on your behalf.
- **Create a document locator.** Your family needs to know where your will and powers of attorney are kept. Your executor will need to know the location of all your other important papers, such as tax returns, account statements, property deeds, and insurance policies.
- **Make arrangements for any safe-deposit box.** Very often a safe-deposit box is closed upon death and cannot be opened until probate. That makes it a poor choice for keeping documents that will be important at death.

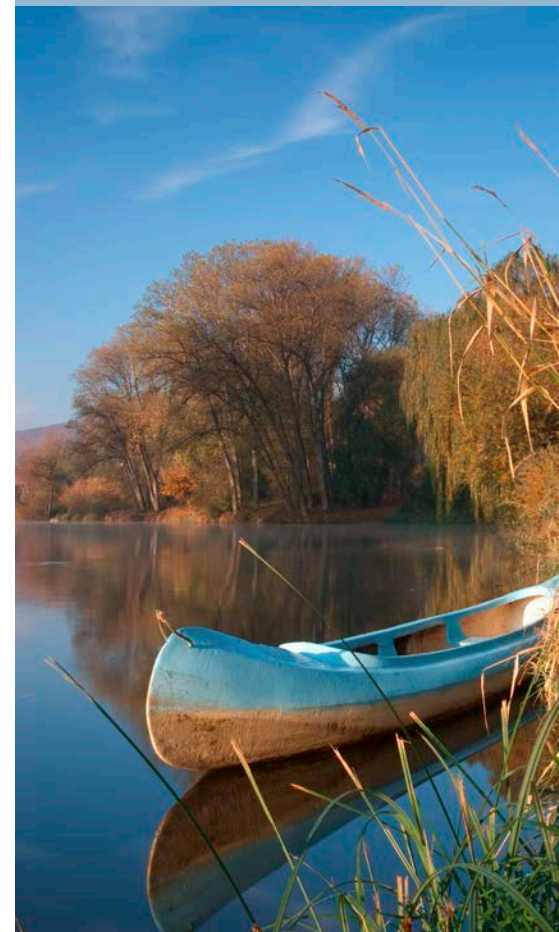
These steps are not complete; they are simply suggestive of the ranges of issues that you will need to address in your estate planning.

INTRO TO TRUSTS

A great variety of financial protection strategies may be implemented with careful trust planning. Among the choices to evaluate:

Marital trusts	Several options are available to provide lifetime asset management and financial protection for a surviving spouse.
Credit shelter trust	A married couple may expand the benefits of federal estate tax exemptions with this trust.
Support trust	For an adult child who needs a permanent source of financial support, with the trust principal protected from the claims of creditors, a support trust may provide a solution. The beneficiary's interest is limited to just so much of the income as is needed for his or her support, education and maintenance.
Discretionary trust	The trustee has sole discretion over what to do with the income and principal, just as the grantor does before the trust is created. The beneficiary has no interest in the trust that can be pledged or transferred. When there are multiple beneficiaries, the trustee may weigh the needs of each in deciding how much trust income to distribute or reinvest, when to make principal distributions, and who should receive them. The trust document often will include guidelines on such matters.
Spendthrift trust	The beneficiary is forbidden to transfer any financial interest that he or she has in the trust and may not compel distributions.

Source: M.A. Co.



Take your next step

On matters of wealth management, we have experience and perspective on the full financial life cycle, all the issues that will affect family financial security. We tailor our services to meet the unique needs of each of our clients.

We are available to follow up on the strategies discussed in this brochure, or to explore other wealth management topics. To learn more about our capabilities, call us soon to arrange for a meeting with one of our officers at your convenience.

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