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## Just Ask Us

*I'm well off financially, but I'm not rich. Do I need to worry about estate taxes?*

Whether you will need to worry about the federal estate tax depends upon when you die, as well as the amount of your wealth. Should you die before the end of 2018, your federal estate tax exemption will be $11.18 million. Next year it will be slightly larger due to an expected inflation adjustment. If you are married and you and your spouse both die this year, your combined shelter from the federal estate tax comes to $22.36 million.

However, if you survive until 2026, it's a different story. The federal exemption drops back to $5 million plus inflation adjustments, unless the Congress acts before then. Also, some politicians have argued to reduce that exemption early.

State taxes are another matter. Most states have dropped their death taxes (estate taxes, inheritance taxes, or both), but those that have retained them typically have much lower exemption levels than the IRS. If you live in one of those states, or own property in one, you may very well need to have tax-sensitive estate planning done.

See your estate planning professional to learn more.



Q QUARTER NOTES

Fourth Quarter 2018

*Paul R. Mancuso*

# Year-end planning for 2018 taxes

The Tax Cuts and Jobs Act enacted last December was perhaps the most consequential tax reform since the bipartisan rewrite in 1986. That makes year-end tax reviews even more valuable than usual. Most individuals will have lower tax burdens for 2018 than they did in 2017 if their financial circumstances did not change. However, the Congressional Budget Office has reported that individual income tax receipts at the IRS are running well ahead of last year's pace, likely due to the fact that economic growth has been stronger than predicted, leading to higher taxable incomes.

## Deductions

The good news is that the standard deduction has roughly doubled, to $24,000 for married couples filing jointly ($12,000 for singles). Many taxpayers who itemized in past years won't need to bother with that for 2018.

Reinforcing that trend is the elimination of many deductions and the capping of others. The key points are the capping of the deduction for state and local taxes at $10,000, and the retention of the deduction for medical expenses

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*QuarterNotes* is written by The Merrill Anderson Company.
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### Year-end financial reviews

This has been another very good year for many investors, as stock market indices have set record after record. As the year comes to a close, take a hard look at your portfolio.

First, taxes on realized gains and losses. Where do you stand? Should there be some additional realizations for improved tax efficiency?

Second, has your portfolio gone out of balance? A passive approach leads to overweighting stocks in an up market. If that's you, are you comfortable with the additional risk that implies?

We can help you with evaluations such as these. We welcome your inquiries.

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Community Brokerage & Investment Services

**What's in, what's out?**

| Not deductible in 2018 | Still deductible in 2018 |
|---|---|
| Moving expenses (except for certain military personnel | State and local taxes up to $10,000 |
| Union dues | Medical expenses above 7.5% of AGI |
| Tax preparation expenses | Mortgage interest on up to $750,000 of acquisition debt |
| Hobby loss deductions | Charitable contributions |
| Investment expenses | Gambling expenses and losses limited to 2018 winnings |
| Miscellaneous expenses | Casualty losses only allowed for federally declared disaster areas |

Source: Internal Revenue Code; M.A. Co.

in excess of 7.5% of adjusted gross income (for 2017 and 2018 only). (See the table above for details.)

Those who take the standard deduction will get no tax benefit from making charitable gifts, and that worries some nonprofits. However, tax breaks are not the motivator for most people's generosity. Time will tell what the real effect of the tax law change will be.

If you find that you will be itemizing this year, but you might not be next year, consider doubling up your charitable gifts in the years when you itemize, for greatest tax efficiency.

**Higher AMT targets**

| Filing status | AMT exemption |
|---|---|
| Married filing jointly | $109,400 |
| Single | $70,300 |
| Married filing separately | $54,700 |
| Estate or trust | $26,000 |

Source: Internal Revenue Code; M.A. Co.

### Alternative Minimum Taxes

The dreaded Alternative Minimum Tax will affect far fewer taxpayers, as the amount exempt has been expanded. What's more, the threshold at which the exemption is phased out has been lifted to $1 million ($500,000 for singles).

Those who had to pay the AMT in the past already had lost the deduction for state and local taxes. Some of these taxpayers may now gain the benefit of that deduction this year, even though it is capped.

### "Kiddie" taxes

The "unearned" income of minor children was taxable at their parents' marginal tax rate under the old law. In a move toward simplification, in 2018 such income will be taxed at the same rates as for estates and trusts if it exceeds $2,100.

### Portfolio moves

Tax consequences shouldn't drive portfolio management decisions, but they do need to be taken into account. Tax efficiency matters.

Capital gains and losses for the entire tax year are netted against each other, according to these rules:

1. Short-term losses are netted against short-term gains.

2. Long-term losses are netted against long-term gains.

3. If one is a gain and the other is a loss, they are netted.

4. Any resulting short-term gains are taxed as ordinary income. Any resulting long-term gains from securities sales are taxed at 15%. At some income levels, the rate is boosted to 20%, and at still higher levels, a 3.8% surtax applies, for a maximum capital gains tax rate of 23.8%.

5. Up to $3,000 of net capital losses may be deducted from ordinary income. Short-term losses are used up first, then long-term losses.

6. Unused capital losses may be carried to future years until death.

The conventional wisdom resulting from these rules is that long-term gains are better than short-term, because they have a lower tax rate. Short-term losses are better than long-term losses, because they shelter income at a higher tax rate. However true this may be in general, it shouldn't be applied to the next transaction until the full range of gains and losses for the year is understood.

### Asset allocation

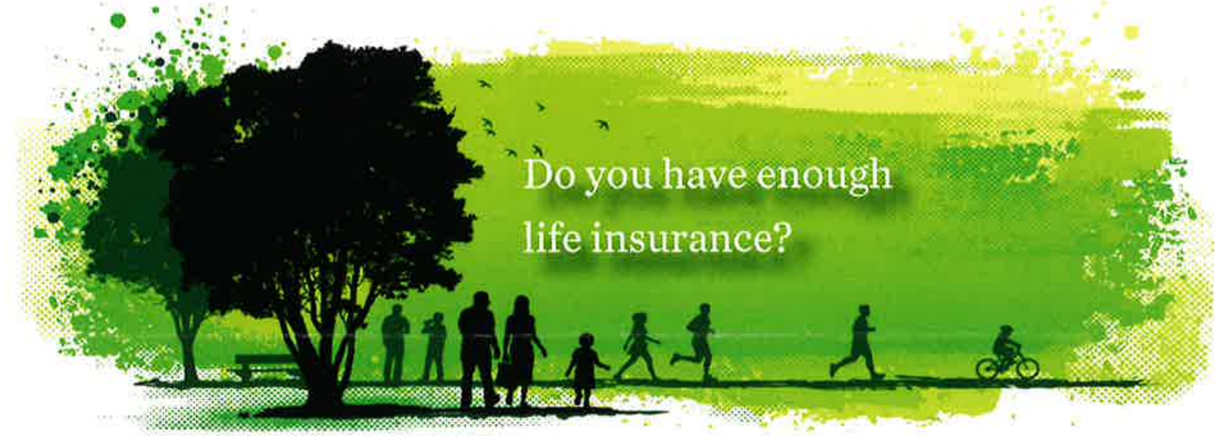
Year-end is also a good time to check on the asset allocation in one's portfolio. Rising stock prices may have changed the balance between asset classes, and that will change the risk exposure.

As a simplified example, assume that an investor begins the year with 60% of the portfolio in stocks, 40% in bonds. The markets have rewarded stocks to such an extent that the investor now has 70% in stocks, while bonds have fallen to 30% of the portfolio. By doing nothing, the investor now has taken on more investment risk. Whether that is good or bad must be determined on a case-by-case basis. An investor who is satisfied with the income generated by the bonds might cheerfully accept the additional portfolio growth and do nothing. One who has more concern about capital preservation might choose to adjust the holdings to restore the balance and risk parameters.

However, there are tax and transaction costs to take into consideration as well.

### May we be of service?

We don't provide tax advice, that's a job for lawyers and accountants. Investments are our core competency, including investing for tax efficiency. Should you have portfolio management questions in connection with your year-end financial review, we will be pleased to provide you with our insights.




Each year the life insurance trade association LIMRA surveys attitudes that Americans have about their insurance coverage. Roughly 60% of Americans have some life insurance coverage, many through their employers. LIMRA discovered 84% of Americans agree that most people need life insurance, yet only 70% said that they themselves needed any. In other words, 30% of respondents felt that they were in the 16% group that needs no insurance! That does not add up.

For those who have no life insurance, the biggest reason given was that insurance is too expensive. But when asked to estimate the cost of life insurance for a healthy nonsmoker, only a third of the respondents came close, and just 7% underestimated the cost. Millennials guessed three to four times too high, by far the worst guessers.

### Coverage needs

Two questions need to be addressed in assessing the need for life insurance: How much, and how long?

For the how much part of the equation, estate planner Alan Gassman reviewed the "6/3" rule of thumb in *Forbes* magazine ("How to Assess if Your Life Insurance Policy is a Good Fit," August 31, 2018). The maximum rate of return on the investment of insurance proceeds is assumed to 6%, the minimum 3%. Divide the amount the family will need to live on by 3% to get the target amount of coverage, and compare that to any coverage already in place.

*Example.* Jack is sole breadwinner for his family, earning $90,000 per year. He has $1 million worth of life insurance already. Dividing the $90,000 by 3%, one gets $3 million as the target. Jack needs to buy an additional $2 million of coverage to be confident that the insurance proceeds will cover his family's financial needs when he dies. If the proceeds actually earn 6%, the family will have income of $180,000 before taxes.

### How long?

Does Jack need temporary life insurance coverage, perhaps just for 20 years until his children have finished their education? If so, term life insurance may be appropriate. Term insurance is less expensive and less complicated to understand. When the term expires, the insured may look to renew if insurance is still wanted, but the rates go higher as one ages.

On the other hand, permanent life insurance (or "whole life" insurance) offers additional financial benefits on a tax-preferred basis. Cash values build up over time, which never exceed the amount of the premium level. The cash value may be available to supplement retirement income. A whole life insurance policy may be thought of as a forced savings plan that includes a guarantee to be fully funded if the insured dies prematurely.

### Get an insurance checkup

How long has it been since you assessed your life insurance requirements? How about your disability insurance, to replace your income if something happens but you *don't* die? Insurance plays a critical role in creating family financial security.

If you need some answers in this area, call on us for guidance.

The cost and availability of life insurance depend on factors such as age, health, and the type and amount of insurance purchased. Before implementing a strategy involving life insurance, it would be prudent to make sure that you are insurable by having the policy approved. As with most financial decisions, there are expenses associated with the purchase of life insurance. Policies commonly have mortality and expense charges. In addition, if a policy is surrendered prematurely, there may be surrender charges and income tax implications. The guarantees provided by the insurance company are contingent on the claims-paying ability of the issuing company.