

# The FINANCIAL UPDATE

**D** DAY & ENNIS, LLC  
FEE-ONLY FINANCIAL PLANNING



Second Quarter 2020

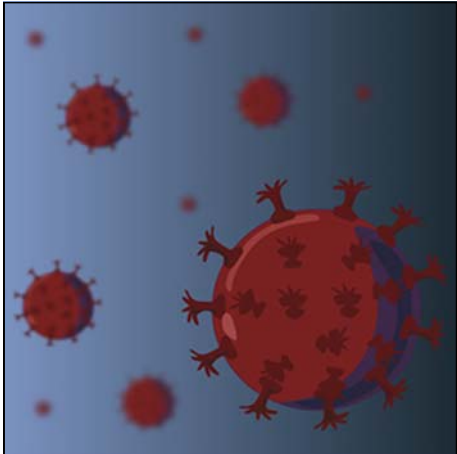
NAPFA - Registered Financial Advisor

(478) 474-7480

## Financial Planning For The Long Run Amid The COVID-19 Epidemic

**A**lmost overnight, the crisis has changed the financial and economic outlook. Change like this is frightening and brings new risks, but it also brings new opportunities. Here's a short list of what to do now.

**Do Not Despair.** As grim as things are, the models forecast an end to the epidemic. It's not a permanent condition. It will end. The Institute of Health Metrics and Evaluation (IHME), which is funded by the Bill and Melinda Gates' foundation, may turn out to be imprecise about the exact date of the end of COVID-19 deaths, and a second wave of the virus is a risk. Life may not be quite the same, for at least a couple of years and possibly longer, but life goes on. A survivor of the 1918 Spanish flu epidemic, according to *The Wall Street Journal*, said it took a couple of years before social, and, in turn, economic conditions returned to normalcy.



**Stocks.** The Standard & Poor's 500 lost about a one-third of its value from an all-time closing high on February 19 through the ultimate low on March 23 and it then has subsequently rebounded off its low. Lower stock valuations may present a unique tax and financial planning opportunity. For

example, if you own securities with large losses in a taxable portion of your portfolio, you might consider selling those assets at a loss. This concept is known as tax-loss harvesting. Losses on assets held for more than one year can be used to offset capital gains realized on other assets. So long as you do not buy securities that are

identical or substantially the same, you can buy a similar asset to match your portfolio's risk level. The replacement asset will then have a lower cost-basis and more of your investment will ultimately be subject to favorable long-term capital tax treatment.

**Roth IRA Conversions.** Lower stock values may present an opportunity to convert some portion, or all, of a traditional IRA to a Roth IRA. Traditional IRAs are taxed as ordinary income upon withdrawal, while Roth IRAs are always tax free upon withdrawal. However, when you convert any portion of a traditional IRA to a tax-free Roth account, you must pay tax on the withdrawn amount at your current income tax rate. With asset values having been lowered by the bear market, the taxes owed on assets you wish to convert are commensurately

## Main Street vs Wall Street

**L**iz Ann Sonders is the Chief Investment Strategist for Schwab. She recently reflected that as the bad news continues to roll in about the economy, civil unrest and COVID-19, many question the disconnect between Main Street and Wall Street. What is propelling the markets?

She sees two major factors being the surge in liquidity from the Federal Reserve and hopeful news about virus treatment or a vaccine. Between relief programs from Congress and stimulus programs from the Fed, investors may wonder why we're not seeing inflation. But that's because none of this has led to velocity of money in the economy. Without it, inflation tends to be absent in the real economy—yet quite evident in asset prices (like stocks).

The second factor, hope of a virus treatment or vaccine, lifts the market every time an advance is reported. Since mid-April, the four best-performing days for the Dow Jones Industrial Average, came on days there was a significant announcement associated with the virus.

What's next? A major concern is investor complacency. There is no shortage of potential negative catalysts, including a second wave of the virus, growing tension between the US and China and rising civil unrest. Investors must remain vigilant and diversified.

Sincerely,  
Day & Ennis, LLC

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# Coronavirus Tax Planning Alert

**A**s mandated by the Coronavirus Aid Relief & Economic Security (CARES) Act on March 27, individuals harmed by the epidemic may make withdrawals from an IRA, 401(k) or 403(b) account before age 59½ without facing the usual 10% federally-imposed early withdrawal penalty.

On May 4, the IRS published an 1800-word statement which identified those individuals eligible for this special tax break and they subsequently promulgated special rules implementing Section 2202 of the massive CARES Act financial relief legislation.

A key section of the lengthy IRS statement says you are qualified for special tax treatment if:

- You are diagnosed with the virus SARS-CoV-2 or with coronavirus disease 2019 (COVID-19) by a test approved by the Centers for Disease Control and Prevention;
- Your spouse or dependent is diagnosed with

SARS-CoV-2 or with COVID-19 by a test approved by the Centers for Disease Control and Prevention;

- You experience adverse financial consequences as a result of being quarantined, being furloughed or laid off, or having work hours reduced due to SARS-CoV-2 or COVID-19;

- You experience adverse financial consequences as a result of being unable to work due to lack of child care due to SARS-CoV-2 or COVID-19; or

- You experience adverse financial consequences as a result of closing or reducing hours of a business that you own or operate due to SARS-CoV-2 or COVID-19.

If you pay yourself back within

three years, the new rules effectively enable you to give an interest-free, tax-free loan to yourself using your retirement savings. However, there is a major caveat: Borrowing from your retirement account at any time before you truly retire is a bad idea, and withdrawals which are taken but never paid back are an even worse idea. It's a giant financial step backward.

But if you have no other choice, tapping your retirement savings under the new law requires careful planning and forethought.

The IRS guidance implementing the CARES Act is effectively a newly enacted reform to U.S. tax law and we will keep you posted on its

implementation in the weeks ahead.

This tax alert for individuals affected by the pandemic requires personalized tax and legal guidance beyond the scope of this article. If you have questions about CARES withdrawals from your retirement plan assets or IRA account, please contact our office with questions. ●



# Expect An Outbreak Of Financial Fraud

**P**redictions of a crash in commercial real estate are rampant, as are forecasts of explosive growth in tech and biotech. Should you believe them?

Every crisis spawns new sales pitches and outright frauds, and the unprecedented nature of the Coronavirus epidemic makes it harder to know what to believe. Here are some facts to keep in mind as financial gurus, Wall Street seers and outright fraudsters bombard shell-shocked investors with predictions of which sectors will prosper most in from the epidemic.

This scattergraph shows the history of the Wall Street strategist sector performance based on their predictions

published in Barron's for the past 13 years. If Wall Street strategist predictions had been correct, the black dots would all fall along the red line or cluster around it. The randomness of the picks shows that Wall Street's predictions of the best sectors are not working.

This data was compiled by economist Fritz Meyer, a strategist at one of the world's largest investment companies for over a decade before going independent in 2009. We periodically share Mr. Meyer's updates to this chart and it's worth repeating amid these surreal times.

If Wall Street strategists' predictions had been correct, if Wall Street could predict which industry is doomed and

which will prosper the most, then the black dots would all fall along the red line.

The randomness of the picks shows that Wall Street's top strategists' picks and pans, as published in Barron every year since 2009, were usually way off the mark. Past performance is not indicative of future results, but the Covid 19 epidemic does not suddenly make it easier to predict which industry sector will be best or worst in 2020.

Instead of trying to predict the future, rebalancing into undervalued sectors is a prudent choice. It's not as exciting as the stories spawned by Coronavirus financial schemes, but it can provide a sensible, low-expense choice for investors over the long run. ●

# A Primer On Setting Up A Trust Fund

**T**rust funds used to be the realm of the wealthy, providing a tool to pass money to heirs and charities.

Nowadays, though, they are becoming a means for more people to engage in smart estate planning.

Trusts are legal arrangements allowing you to put assets into accounts that benefit another person or an organization, like a charity or college. They are often complicated and require a lawyer to put together — although there are online alternatives if you want to attempt to do it yourself.

The basic idea is to control who gets your assets, either when you're alive or afterward. A trust can help you lower estate taxes and avoid probate, the often-arduous legal procedure that proves a will is valid.

**First Steps.** As you set up a trust, you need to settle a few key questions:

1. What assets go into the trust: stocks, bonds, mutual funds, cash or property?
2. Who are the beneficiaries, meaning the people who receive the trust's benefits?
3. Who will be the trustee, the person who manages the assets and oversees the trust? The best thing is to appoint someone you know, who also is familiar with your financial situation and your beneficiaries. Plus, this person should be financially astute, and knowledgeable about taxes and investing.
4. How will assets be invested and

managed, and when will they be paid out? For instance, you might not want your children to receive the benefits until they're 35, as an established adult.

5. What is the duration of the trust, and under what conditions will it end operations? Is it paid out over time, or all at once?

6. Can its conditions be changed? Some trusts are irrevocable, meaning they are chiseled in stone. Others are revocable, meaning for instance you can shift the beneficiary to be your daughter instead of your younger brother.

7. What stipulations do you want? Maybe the money will go to your son for everything except paying off his creditors. Or your daughter, but not your son-in-law if she should die.

Beyond these considerations, it's wise to find a good, experienced estate attorney. The lawyer will craft a document called a declaration of trust, which will set up the trust fund and establish its conditions.

**Timing.** Next, the trust fund is registered with the IRS, allowing it to file its own tax returns and legally open financial accounts at banks or other institutions. Then, you transfer the assets into the trust, a process called retitling.

Do you want the trust to take effect now or at your death? And should it be revocable or irrevocable? The argument for revocable is that your beneficiary,

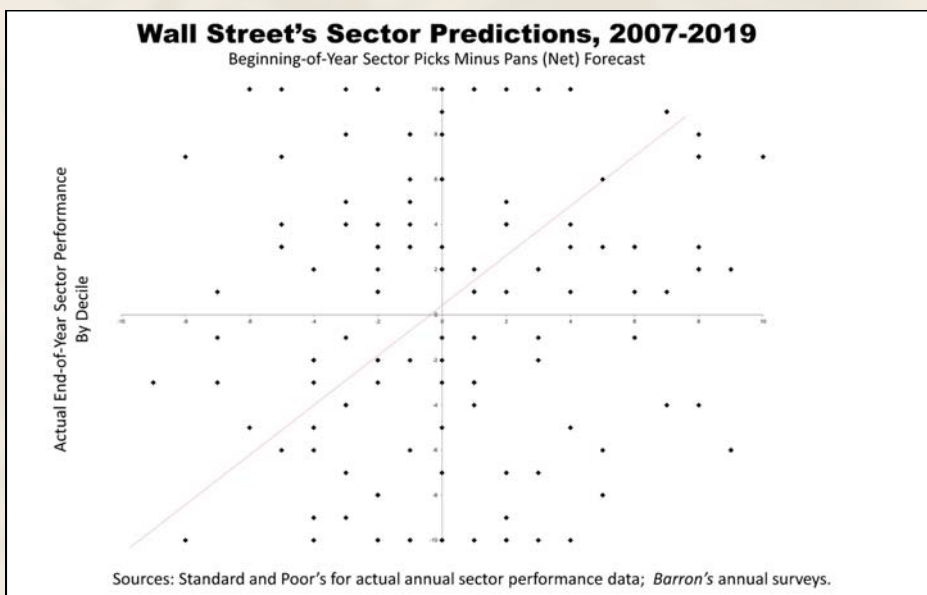
perhaps a young person, may not grow into someone who deserves your generosity. The case for irrevocable is if you want to earmark the assets to support an activity whose necessity won't likely change, such as educating a child or supporting a charity.

The question of how long the trust will stay around, before its last assets are paid out, is a tricky one. Common law is structured against letting trusts persist indefinitely. But many states let you get around that by setting up a so-called dynasty trust, which permits the wealth to grow for a long time without being taxed.

**Types of Trusts.** Aside from whether the trust is revocable or not, its structure can be very complex and carry advantages and disadvantages. Some examples:

- Generation-skipping trust, aka a dynasty trust. This lets you transfer money tax-free to beneficiaries who are two generations younger than you. The goal is to avoid the assets being taxed twice: once when they go to your grown children, and again when that generation passes the assets along to their own kids — namely, your grandchildren.
- Bypass trust. Here, you bequeath an amount up to the estate tax exemption (in 2020, that's up to \$11.58 million from a single giver or double that from a couple). The rest goes to your spouse tax-free. After your spouse dies, you can stipulate that what's left goes to the kids.
- Qualified terminal interest property (QTIP) trust. This is best at singling out which particular relatives to direct your largesse to. A QTIP is often helpful in families where there are divorces, remarriages and stepchildren. Your surviving spouse can receive income from it, and once that spouse dies, the remaining principal goes to specific younger relatives.

For you, the donor, creating a trust fund gives you peace of mind that the legacy you want to leave is well-constructed and wisely directed. This article is not intended as personal advice, but rather as an educational resource about planning techniques available when working with a financial professional. ●



# The Federal Reserve's Powerful New Toolset

**T**he Coronavirus financial crisis is being compared to the near collapse of the global financial system in 2008 and The Great Depression from 1929 to 1939, but there is one big difference this time: The Fed. The Federal Reserve Bank is using innovative new tools to contain the financial damage of the Coronavirus epidemic.

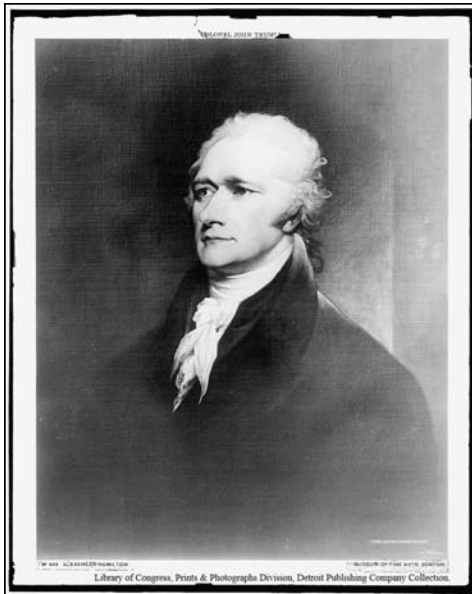
In the financial crisis of 2008, the chairman of the Fed at the time, Ben Bernanke, an academic who had spent decades studying previous financial crises, repeatedly deployed a technique called quantitative easing (QE). QE expanded the Fed's balance sheet to buy back U.S. Government bonds on the open market, thus, lowering long-term interest rates.

Never before had the tactic been used by a central bank in a major economy. It worked, however, and QE was one of the reasons the U.S. emerged successfully from The Great Recession of 2008 and 2009. The Fed's present response to the Coronavirus crisis is literally 10 times more powerful.

Under the \$2.2 trillion Coronavirus Aid, Relief, and Economic Security ("CARES") Act enacted March 27, 2020,

the U.S. Government allocated \$454 billion to Federal Reserve Bank Special Purpose Vehicles that the central bank can leverage 10 to 1, thus enabling it to lend up to \$4.54 trillion to companies in financial distress.

That sum is reportedly more than all U.S. commercial and industrial loans outstanding at the end of 2019, plus all the new corporate bonds issued during 2019 combined! Although the expansion of the



Fed's power has been widely criticized as a step toward a centrally planned economy, such government action limits the risk of potentially massive corporate bond defaults and corporate bankruptcies.

The U.S. led the worldwide economic recovery following the global financial crisis of 2008, in part because of the Fed's innovative approach. And now, this most recent display of Yankee ingenuity — in the form of the Fed's new tools — is at play once again in fighting the Coronavirus-induced financial crisis.

In these frightening times, the Fed's new toolset is likely to become a mere footnote in history books that will be written about the pandemic in the decades ahead. Ever since Alexander Hamilton established the first U.S. central bank in 1791 to respond to the financial crisis that followed the Revolutionary War, the uniquely American central bank has enabled the progress of civilization through financial crises for generations. The Federal Reserve's response to the Coronavirus financial crisis is a shining example of what makes America exceptional among the nations of the world. ●

## ...Amid The COVID-19 Epidemic

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lower, making the cost of converting to a tax-free Roth account less costly and lowering your tax bracket in the years ahead on withdrawals from the Roth IRA.

**Paycheck Protection Program (PPP).** On Friday, March 27, 2020, the Coronavirus Aid Relief Economic Security Act, a history-making \$2.2 trillion stimulus law, allocating \$349 billion in loans to business owners in need, and the loans are to be forgiven if you spend the money within the proscribed eight-week time frame to retain your employees. PPP is the primary relief program sponsored by the U.S. Government to aid business

owners. PPP is expected to distribute its \$349 billion by late April. Additional funding from Congress is widely expected, but it should be noted that the forgivable loans are distributed on a first-come, first-served basis. With 30 million small businesses, this is the one thing business owners want to get right. Contact us if you have questions about how to proceed.

**Wealth Transfers.** For individuals with taxable estates, unprecedented low interest rates make it smart to consider the use of specially-designed trusts, such as a:

- Grantor Retained Annuity Trust (GRAT)
- Intentionally Defective Grantor Trust (IDGT)
- Generation Skipping Trust (GST)

**Estates Currently In Administration.** If you are a beneficiary of an estate in the administrative process of distributing assets, the change in asset values may have created a tax-loss harvesting opportunity. In addition, the lower asset values make it prudent for spousal beneficiaries of a qualified retirement account under administration to evaluate a partial or complete disclaimer of inherited assets.

**Stay In Touch.** The strategic opportunities for individuals described above do not necessarily contemplate your unique personal situation. If you have a specific question about any of this, or how it may apply to you, please contact us. ●