THE

ADVISOR

conquer the complex

in this issue:

2019 YEAR-END TAX PLANNING STRATEGIES

4TH QUARTER MARKET COMMENTARY

UNDERSTANDING TAX LOSS HARVESTING

RMD: 3 IDEAS TO CONSIDER

YHB Wealth Advisors

As we fall into the last quarter of 2019, YHB Wealth has $64.7 Million AUM. We have seen substantial growth since the 1st of the year and we are very excited to see how we end. The last quarter of the year can be especially exciting but busy. School has started, the weather is changing and there are more opportunities for family gathering, possible dressing-up, eating delicious food and maybe a gift giving event or two. But remember in all of the bustle of the year end activities, don't forget about yourself. I have prepared a short list of self-care ideas to help keep you focused.

1. Create a task list. Here is where you will place all of the items you would like to do, buy, see and experience
2. Create a gift log. Whether it be charities, children, grandchildren or your best friend, create a budget for each person, write down your intended gift and the price the item should cost.
3. Check your goals. Is there is anything you really wanted to accomplish this year? Paying down debt, planning a vacation, contributing to a 529 account or any career enhancements?
4. Self-Care Bucket List: Do you need your hair and nails done before the family gathering? Any oil changes or tune-ups for your holiday travel? A massage is always a wonderful self-care task.

You can't pour from an empty cup, so taking care of yourself first is important in taking care of the ones we love. We want to be relaxed and have wonderful holiday memories as we head into 2020!

JAMIE BROTHERS

TRIED & TRUE ...with a Twist:

2019 Year-End Tax Planning Strategies

As Autumn begins and the leaves start to fall, our thoughts turn to year-end tax planning for our clients. Although many of the tried and true tax planning strategies may still be advantageous under the recently enacted Tax Cuts and Jobs Act of 2017 (TCJA), there are some new "twists" in the opportunities to reap tax savings, as well as an end to some old favorites.

The old favorite still in play is to defer income and accelerate expenses. This is especially helpful to small business owners reporting on the cash basis who may want to prepay certain costs to capture a deduction or possibly postpone sales or client payments until the New Year. However, individuals may see similar benefits, perhaps by postponing the sale of an investment until the New Year to defer the gain recognition, or as Randy states in his article, possibly harvest losses before year end to offset 2019 gains.

Let's consider a few new "Twists" in Tax Planning for 2019:

Individual Tax Planning:

With the advent of the increased standard deduction ($12,200 Single and $24,400 Married Filing Jointly) and the $10,000 limitation on combined local and state income taxes, many individuals are no longer itemizing their deductions. Therefore, they are losing the deductions for their charitable giving, medical and taxes. Here are a few new Twists to structure your deductions to maximize the benefit:

- **Utilize your IRA Required Minimum Distribution to make your charitable gifts:** If you are over 70 ½, you may elect to send all or part of your RMD to your favorite charity. This reduces the taxable amount of your distribution dollar for dollar, and so, in effect, you receive the deduction "off the top". Therefore, you capture the deduction without having to itemize. The custodian of your IRA must make the payment directly to the charity from your IRA, but you could deliver the check to the charity if you would like. Care must be taken to structure this payment pursuant to the IRS guidelines, but this is a wonderful way to capture the deduction and also reduce your Adjusted Gross Income, which may factor into other calculations on your return.

- **"Bunching" deductions:** Some taxpayers may be able to use a "bunching strategy" to push or pull discretionary medical expenses and charitable contributions into the tax year they do the most good. An example is probably the easiest way to consider this opportunity. Let's say you normally have $6,500 in deductible taxes, and you give $5,000 to your favorite charity. If you are single, this will not exceed the Standard deduction of $12,200. But what if you gave $10,000 to your favorite charity in 2019, and skipped a year in 2020. This would allow you to itemize in 2019 (with $16,500 of deductions), benefit from your charitable giving, and in 2020, you would use the standard deduction. By bunching your charitable deductions, you have increased your deductions by about $4,000 over a two year period and saved additional tax dollars. (This may also be a strategy for bunching medical expenses, or certain tax payments, depending on your particular circumstances.)

- **Donor Advised Funds:** Although these funds have been around for several years, they have become a mainstream choice for tax planning, and are especially helpful in a year you have a large taxable event. A Donor Advised Fund (DAF) allows you to contribute cash or other assets into a "restricted" investment fund, and obtain a current year charitable deduction. Then, you can sprinkle the gifts to your favorite charities over time. There are AGI limitations on the deduction depending on the type of asset you contribute. If you are interested in a DAF, please reach out to Randy or your tax advisor to discuss the funds that are available.

- **Increasing income:** What do you mean, increase my income? Yes, now tax planning includes potentially increasing your taxable income to capture historically low tax rates. Here are few ideas:
  - **Capture the Zero Percent Capital Gain and Qualified Dividend Rate:** If your taxable income is less than $78,950 MFJ or $39,375 for Single filers, you may qualify for a zero percent rate. So, consider realizing gains to adjust your portfolio, or just buy back the same security to get a no-cost step-up in your tax basis. (Note: there is no 30-day restriction on buy backs when you recognize a gain.)
  - **Additional IRA distribution:** If you are in the zero percent bracket, or even a very low bracket and know that the future has higher rates in store for you, take an extra IRA distribution to take advantage of your current low rate.
  - **Roth Conversions:** Convert all or part of your traditional IRA's to Roth IRA's. Although you are required to pay the tax on the date of conversion, a Roth IRA grows tax free, does not have a required distribution, and is tax free for future withdrawals.

Business Tax Savings:

In addition to the "old favorite" - income deferral/expense acceleration, here are a few other tax-saving ideas for 2019:

- **Expanded Business Property Expensing Option:** The TCJA enhanced several key provisions related to business assets.
  - First, businesses can claim a 100% bonus First year depreciation deduction for machinery and equipment (new & used property now qualify).
  - Second, business property expensing is available under IRC Section 179 up to $1,000,000 cost of qualifying property, with a total allowable investment of $2.5M. Expensing is generally available for most depreciable property (other than buildings) and few other exceptions.
  - Third, take advantage of the de minimus safe harbor election to expense certain lower-cost items. If you have an audit (a/k/a "applicable financial statement"), then this amount is $5,000 per item. If you do not have an audit, then the limit is $2,500. As an example, if you buy a desk that costs $2,400, and you don't have an audited financial statement, then you can make this election and write it off. No §179, no Bonus depreciation -- just a straight expense.

Give us a call if you want to discuss potential year-end purchases and qualification under one of these provisions.

- **TCJA 20% Qualified Business Income Deduction:** There was a lot of hype about this new deduction available to qualified businesses. In general, if modified taxable income does not exceed $315,000 for married couples, or $157,500 for all other taxpayers, you may be entitled to a 20% deduction for your qualified business income. There are many factors that go into determining if your business is a "Qualified" business, and there are additional tests if your income exceeds the income thresholds. A detailed discussion of this is beyond the scope of this article, so please contact your tax advisor to discuss planning options to maximize the QBI deduction.

So many planning ideas, and not enough pages to list them all! Careful planning is required to apply to your unique situation, and we welcome the opportunity to help tailor a plan that is right for you.

ELAINE CAIN, CPA

4th Quarter | 2019

Market Commentary

Instead of sailing into a calm and relaxing end to summer, the past few months have brought winds of volatility to the markets and increased risks for the global economy. The treasury yield curve (10 year versus 2 year yields) inverted in August, U.S. and China grappled with tariff's, Brexit outcomes are uncertain, civil unrest in Hong Kong sank tourism trends and a general slowing of the economy in the Eurozone are just some of the imbalances we see around the world. Some of these ongoing uncertainties (and new ones we haven't even yet recognized) will almost certainly continue to bring volatility to the investment markets and weigh on economic prospects for growth as we end 2019 and head into 2020.

The most recent – and perhaps the most important – concern for the investment markets has been the inversion of the 10-year/2-year Treasury yield curve. The yield curve "inverted" which simply means for a period of time, the 10 year Treasury yielded less than the 2 year Treasury – which is not the usual circumstance. This is important because it has preceded every recession in the last 40 years.

Recessions are inevitable and occur at the end of every economic cycle, so the U.S. economy is destined to have one, eventually. The unknown factor is the amount of time until it arrives. While the inversion of the Treasury curve has historically been a reliable predictor of recession, its use as a timing mechanism leaves a lot to be desired. The lag time between an inversion and the start of a recession has varied between 7 months and 2 to 3 years – with the average lead time of 14 months.

Recessions, though necessary (and some would argue beneficial), part of the business cycle, can be like sailing through stormy seas for the broad economy and the equity market. Going back to the early 1950's the equity markets have witnessed returns ranging from -35% to +18% during the recessionary period, and if you go back far enough to include the Great Depression the range of returns widens all the way from -76% to +29%.

It is my opinion, the odds of a recession appearing during the final few months of 2019 are remote, primarily because the biggest driver of U.S. economic growth – consumer spending – is still chugging along. At 60%+ of total GDP, the U.S. consumer is a vital component of economic growth and, up to this point, consumer confidence has remained solid on the backs of access to easy and cheap credit, positive wage growth and a tight labor market.

With the domestic manufacturing sector weak and most of the Eurozone mired in recession, the U.S. consumer looks to be the last bastion of hope to keep the U.S. economy growing. Tightening of credit standards, a future uptick in unemployment, or a decline in wage growth that causes weakness in consumer confidence would be a strong confirmation of the impending recession predicted by the Treasury curve inversion.

Now, let me point out two "outliers" that could possibly cause sharply increased volatility in the equity markets in 2020: a blowup in the credit markets due to excessive debt levels and uncertainty around the political landscape.

On a longer term basis, without question the biggest potential problem impacting future global economic growth is the sheer massive amount of debt that has built up during the past decade of artificially low interest rates. Debt in and of itself isn't always bad, and may even be good if used for productive purposes. The problem today is the vast majority of the debt outstanding hasn't been used in a constructive manner.

Individuals have used access to low rate debt as a way to finance spending above the level their incomes will allow. Companies have floated literally trillions of dollars of debt to buy back their own stock at lofty valuations, finance poorly managed business operations or make questionable and costly acquisitions. Governments have issued bushels of debt to avoid even the appearance of trying to balance their budgets and finance social programs they know are unaffordable otherwise.

As can be clearly seen by the precedent set in Japan and Europe, excessive government debt accelerations depress business conditions, which reduce economic growth, and leads to even lower rates. When real yields are low (or even negative) investors and entrepreneurs will not earn returns commensurate with the risk. Decreased capital returns will prolong poor economic growth, and the government lowers rates even more in an effort to try and spur increased economic activity. The cycle continues over and over.

There are now about $17 trillion worth of negative yielding bonds outstanding, mostly in the sovereign space. That's about 25% of the entire global bond market, and 43% of all the bonds in force outside the U.S. This has never before happened in history, so there is no precedent upon which to draw conclusions about how it will end – but I am confident in predicting it won't be good.

Think of it – the German government can issue 30 year bonds with a -0.22% interest rate. In fact, as of this writing, the entire yield curve for German bonds is negative! The European countries can't afford to continue funding their massive social programs without saddling their citizens with huge tax increases.

That is a distasteful reality which would bring unwanted social unrest and more than likely major political upheaval, so the European Central Bank (their Fed) has brought down their borrowing cost to less than zero by creating (as Bloomberg calls it) “pixie dust” money and buying the bonds issued by individual Eurozone governments. Now they can continue to fund bloated government programs at literally zero cost. The term “land of the free” means something totally different in Europe!

And it’s not just governments that can borrow at negative yields. Siemens AG, a German company, recently issued $3.9 billion worth of bonds at an average yield of -0.3% and there were more buyers than bonds available! And some Danish banks are now offering home mortgages at a -0.5% rate!! When you read the “fine print” on the loans, the underwriting fees cost the borrowers a little more than the -0.5%, but they are still able to buy that new home at essentially a zero mortgage rate.

In my opinion, this pattern of ever declining rates globally will force the U.S. Federal Reserve to continue to lower domestic rates, and we may even see our rates close to zero by the end of this cycle. That will be negative for savers and the most conservative investors who are averse to putting their hard earned money into anything other than traditional income choices. It will force many other investors to increase the risk in their “income” investments by adding to their equity allocation, expanding into lower quality income offerings, or even delving into “alternative” investment strategies in their reach for higher yield.

The real danger in this global race to the bottom in rates is that the buyers of this unrealistically priced paper begin to demand higher returns for the increased levels of risk. Higher rates would be a serious negative (and could be a death knell) for governments and companies addicted to a world where money has a zero cost and there is no penalty for poor management of resources. That would lead to massive failures and loss of capital for investors. Most likely, this will not be the case in the next year, but is a possible “black swan” outcome in the future.

The second outlier that could drive increased volatility in the equity markets in 2020 is the looming Presidential campaign. This not a political statement – my interest in the conduct of the campaign and the eventual outcome is related to the impact it could have on the investment landscape and the potential for increased volatility. From that perspective, my opinion is the best we can hope for is continued gridlock. Based solely on current campaign platforms, a Democratic Congress and White House would likely mean increased taxes and possibly the implementation of some form of Modern Monetary Theory (MMT – Google it for a more detailed understanding). A Trump re-election would likely mean four more years of volatility driven by random tweets. Choose your poison wisely.

The possible silver lining for equity investors is that the response by the Fed to any increased turmoil, or sharp deceleration in economic activity is surely to be either rate cuts, or the reinstatement of Quantitative Easing (asset purchases by the Fed) or both. Neither will likely fix the underlying problems in the longer term, but could be effective at inflating the asset bubble (equity market) to new all-time highs in the short term.

The trick for individual investors will be to properly allocate to benefit from any potential inflation of equity market valuation levels caused by the Fed’s meddling, but to also try and sidestep the majority of any temporary (or permanent) loss of capital from any resultant significant decline. As Warren Buffett famously says, “No one rings a bell at the top of the market”. It is impossible to time the market, and most investors are smart enough to understand this reality. However, it is prudent to understand the risks and be prepared for the possibility of more bouts of volatility.

Our suggestion, and the way in which we are approaching the management of our client portfolios in light of the foregoing discussion, is to keep a diversified portfolio with an appropriate amount of equity exposure relative to each client’s individual risk tolerance and time horizon. Within the equity allocation, we currently favor U.S. equities over international, large caps over small caps, and with an overall weighting toward more defensive sectors.

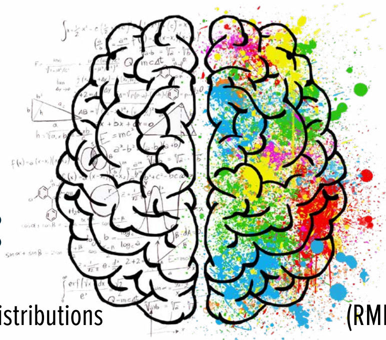
On the income side of the allocation, we continue to favor high quality individual bond issues, primarily with an intermediate term where we can still reap the benefit of some positive yield while realizing potential price appreciation if rates continue to decline. We will also add limited exposure to specialized income instruments (like preferred issues or Real Estate Investment Trusts) to enhance yield where appropriate.

Though we may find ourselves sailing through choppy seas as all these variables in the investment, economic and political arenas are resolved over time, if we are attentive to the direction of the wind, pay attention to the expected forecast and keep our ship in sound working order, we can navigate our way through to the calm waters beyond the storm.

Achieving this objective however requires each individual investor to be diligent in their efforts to develop a sound financial plan, implement a solid investment strategy and regularly rebalance their portfolio to ensure it remains in line with their overall goals. As always, we encourage current clients of YHB Wealth to reach out to us with any questions and consistently work with us to ensure their financial plan is up to date. We also welcome inquiries from clients of YHB CPA that may want to discuss their specific financial situation with us personally.

RANDY BEEMAN

Required Minimum Distributions:



3 Ideas to Consider

Created in the Tax Reform Act of 1986, required minimum distributions (RMDs) are set dollar amounts the government mandates you take a distribution from your retirement accounts once you reach the age of 70 ½. Once this age is reached, you have until April 1 of the year following turning 70 ½ to take the distribution from your retirement account or accounts. For each year after, the RMD must be taken by Dec 31. A few details here are important to be mindful of.

1 – Each retirement account has its own RMD. Traditional IRA, SEP IRA, SIMPLE IRA, and all employer-sponsored retirement and profit sharing plans are included. See the IRS RMD Worksheet for more details on how to calculate your RMD. Note: your IRA / Employer-sponsored plan custodian should also be providing you with your RMD amount, but the burden ultimately falls to you

2 – If you are employed when you reach 70 ½, and are not a 5% owner (directly or indirectly) of the company, generally your employer-sponsored retirement plan RMD could be delayed until the year you retire, BUT your corresponding IRA accounts will still have RMDs regardless of being employed. Self-employed individuals usually are unable to avoid this exception.

3 – Roth IRAs do not have RMDs

4 – The penalty for failing to take your RMD may be up to 50% of the amount of the RMD that has yet to be taken

5 – Your RMD is still your money. While your RMD will contribute to your income level for the corresponding tax year, and taxed accordingly, you are still able to move the balance of these funds into a taxable account to either invest or use to support your lifestyle.

6 – You're able to withhold tax directly from your RMD to help manage tax liability

7 – You may satisfy separate IRA RMDs all from one account, but you may not satisfy Employer plan RMDs with IRA RMDs and vice versa.

Now that we've covered some basics, let's look towards some ideas to consider when preparing to take your RMDs:

Year 1:

Don't let year of your required minimum distribution sneak up on you! Since you're able to delay until April 1 of the year following turning 70 ½ this gives us a bit of a grace period. However, if you do delay, you should be aware that you will be taking two RMDs in the same tax year. For example, if you turn 70 ½ in 2019 you have until April 1 to take your 2019 RMD. If you delay taking your 2019 into 2020, you will then be taking the 2019 and 2020 RMDs in the tax year of 2020. Both RMD amounts will then count toward your 2020 taxable income. Will this increase your tax bill? Are you prepared if it does? Remember (listed above) you may withhold tax directly from your RMD, to help manage your tax liability, but it's important to talk to your financial advisor and tax advisor about these impacts.

Qualified Charitable Distributions (QCDs):

If you already make charitable contributions this may be something to consider. A QCD is a distribution that goes directly from your IRA (not employer sponsored plan) directly to a qualified charity of your preference. While benefitting your preferred charity this strategy could have a significant impact on your taxes while also satisfying RMD requirements. You're allowed to distribute up to $100,000 annually from your IRA using this strategy; so it is especially worth considering if you are a substantial charitable donor. (See Elaine's article)

Change Your RMD Amount:

While the IRS has a uniform table that determines the amount of your RMD you may be able to take a little more ownership over the amount they require you must take. Whether you are currently taking an RMD, are soon to be taking an RMD, or are looking to diversify your tax strategies in/near retirement you do have options in managing your RMDs carefully. Converting a portion of your Traditional IRA (or employer plan) to a Roth IRA would help to limit the amount of RMD required year over year, allow for tax-free growth, and even provide tax-free income. By decreasing the account balance, upon a conversion, this would then decrease the amount of RMD you're required to take as RMDs are calculated based upon account balances. It is important to note that your conversion is a taxable event, so you'll pay tax on the front end, and the management of your tax liability cannot be overstated. Taking advantage of a year with a low marginal tax bracket could provide a good opportunity to do this. A conversion needs to be carefully managed in order to not create an oppressive or crippling tax liability, so working with an advisor is of paramount importance. Note: RMDs themselves are not eligible for conversion (or rollover) from one IRA to another/Roth IRA, this conversion should be done either prior to or after satisfying your RMD.

While the government created the RMDs to curtail the building of wealth inside tax-sheltered accounts, there are still strategies that are useful for the organized and disciplined investor. The years of age 60-70 provide prime opportunity to both maximize retirement contributions, prepare for tax diversification strategies, and manage income as it pertains to RMDs. Managing your RMDs carefully can create excellent opportunities for thriving in and successfully navigating retirement.

JT TRIMBLE

Every Investor Should Understand the
BENEFITS OF TAX LOSS HARVESTING

Even in the best of times, not every investment will be a winner. Fortunately, losing investments do have a silver lining: You may be able to use them to lower your tax liability and better position your investment portfolio going forward. This strategy is called tax-loss harvesting, and it's one of the many tax-smart strategies that investors should understand and consider using when appropriate.

Tax-loss harvesting is a strategy in which certain investment assets are sold at a loss in order to reduce your tax liability at the end of the year. You can use tax-loss harvesting to offset capital gains that result from selling an investment in securities, or another investment asset at a profit. You can also use tax-loss harvesting to offset up to $3,000 in non-investment (ordinary) income.

Tax-loss harvesting is a strategy that you can only apply to taxable investment accounts. Tax-deferred retirement accounts like IRAs and 401(k)'s grow deferred, so they aren't subject to capital gains taxes, and therefore you can't use any losses in these accounts to offset capital gains either in the accounts themselves, or another investment asset.

The Basic Strategy

Imagine you're reviewing your portfolio and you see that your holdings in a particular sector or individual stock have risen sharply, while some of your holdings in another sector or individual stocks have dropped in value. As a result, perhaps you now have too much of your portfolio's value concentrated in one sector. To realign your investments with your preferred allocation, you sell some of the appreciated stocks and use those funds to rebalance. In the process, you end up recognizing a significant taxable gain.

This is where tax-loss harvesting comes in. If you also sell the stocks that have declined in value, you could use those losses to offset the capital gains from selling the appreciated stocks, and reduce your tax liability.

In addition, if your losses are larger than the gains, you can use the remaining losses to offset up to $3,000 of your ordinary taxable income (for married couples filing separately, the limit is $1,500). Any leftover losses can be carried forward to future tax years and used to offset capital gains or ordinary income down the road.

Some Issues to Consider

As with any tax-related topic, there are rules and restrictions to be aware of before utilizing tax-loss harvesting, including:

- Tax-loss harvesting isn't useful in retirement accounts such as a 401(k) or IRA, because the losses generated in a tax-deferred account cannot be deducted.

- There are restrictions on using specific types of losses to offset certain gains. A long-term loss would first be applied to a long-term gain. A short-term loss would be applied to a short-term gain. If there are excess losses in one category, these can then be applied to gains of either type.

- When conducting these types of transactions, you should also be aware of the wash-sale rule, which states that if you sell a security at a loss and buy the same or a "substantially identical" security within 30 days before or after the sale, the loss is typically disallowed for current income tax purposes.

The Bottom Line

It's important to understand that the primary purpose of tax-loss harvesting is to defer income taxes. That's the process of delaying the payment of taxes many years into the future. This allows an investment portfolio to grow and compound at a faster rate than it would if the money to pay taxes were withdrawn from the portfolio every year that gains occurred. The benefit will be fully maximized if you can defer the liability until after you stop working, when you will presumably be in a lower tax bracket.

Tax-loss harvesting is an investment principle well worth every investor putting in the time and effort to understand and properly utilize in their investment strategy.

RANDY BEEMAN

RANDY BEEMAN
randy.beeman@YHBwealth.com
540.545.8702

JT TRIMBLE, CFP
jt.trimble@YHBwealth.com
703.840.0702

JAMIE BROTHERS
jamie.brothers@YHBwealth.com
540.545.8702

Want to keep up with the latest news? Check out our Podcast at YHBwealth.com/news

LETS TALK investing

hosted by randy beeman

"Let's Talk Investing" provides a market update and common sense investing insights from a value based perspective. Listen as host Randy Beeman and guests help make the complex simple in each easy to understand 20 – 40 min episode.

50 S. Cameron St.
Winchester, VA 22601

YHB Wealth Advisors