FINANCIAL DECISIONS

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Same-Sex Marriage Law Alters Key Tax Rules

On June 26, 2013, the U.S. Supreme Court handed down its landmark decision in *Windsor v. U.S.*, declaring that section 3 of the Defense of Marriage Act (DOMA) is unconstitutional. That section, which legally defined "marriage" for federal purposes as a union between a man and a woman, is now gone. Same-sex couples now have new financial and tax opportunities that could yield significant benefits.

In the majority opinion, Justice Anthony Kennedy pointed out that the Supreme Court ruling affects more than a thousand federal statutes. We can't cover all of the implications of the new law, but here are five key areas where the change can have a significant impact:

1. Income taxes. Now, same-sex couples will be eligible to file joint tax returns and claim the same benefits as other joint filers. Although filing jointly may save tax dollars for some couples, others in high tax brackets likely will pay more tax, thanks to the so-called marriage penalty, which is a quirk of the tax code that can penalize joint filers. The new law also could affect state incomes taxes, although it's not yet clear how that will play out. Additional guidance from the IRS and individual states is expected.

2. Estate taxes. The same principles affecting federal and state income taxes also extend to estate and gift taxes, and the demise of DOMA opens new estate planning opportunities for same-sex couples. For instance, either spouse now may benefit from the federal marital deduction, which lets most spouses inherit an unlimited amount from each other with no estate tax liability. That provision leaves intact the generous estate tax exemption ($5.34 million in 2014) that can be used to transfer assets to other heirs. The "portability" provision of the federal law now applies to same-sex couples, enabling the estate of a surviving spouse to use any remaining unused portion of the other spouse's exemption. Other provisions, such as a limited exemption for non-citizen spouses ($143,000 in 2013), also apply. State estate laws will also be affected, though not uniformly.

3. Employee benefits. The *Windsor* ruling will result in numerous complexities involving employee benefits, such as health insurance, for same-sex couples. For instance, a non-working spouse of an employee may now be eligible for insurance coverage or extended benefits under COBRA. While same-sex couples will be treated the same way as traditional married couples in terms of federal statutes, differences may still exist under state laws.

4. Retirement plans and IRAs. The ruling will create many changes relating to employer-sponsored

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Planning For Life's Challenges

Of course, we think everyone should work with a financial planner! Like preventative medicine, a well-designed financial plan works best when it has been created before any crisis occurs. Unfortunately, not everyone has a plan in place prior to life's unexpected turns.

Imagine that you are suddenly injured; you, or a family member, receive a terminal diagnosis; or you find yourself newly widowed. Your life is turned upside down. It is during these times of crisis that you need to make crucial and quick decisions, but you may be unable to focus and think clearly about financial matters.

Can you provide for your family now that you are disabled? How do you organize your finances for your heirs if you only have a few months to live? Do you elect the disclaimer in your spouse's will? These questions can be confusing and painful to navigate on your own.

In those challenging times, hiring a financial planner becomes vital. If you find yourself facing such a transition, an advisor can help you navigate the issues at hand and make decisions that are right for you.

Over the years, we have helped many clients navigate just such transitions. If you, or someone you know, are suddenly facing a key life change, we would be happy to help you through it.

Florence Dupont, Ken Gutwillig,

and Linda Schoenthaler

Making Smart Beneficiary Choices

Quick: Who are the beneficiaries of your retirement plan, life insurance policies, and investment accounts? Many people are uncertain, or do not remember who they named as a beneficiary. But it's important to know, especially if your circumstances have changed since you completed the original paperwork.

You probably carefully considered the designations of your financial accounts and life policies when you initially established them. But you may have filed the documents into a drawer and forgotten all about them.

Suppose your family situation has changed. Maybe you have remarried and you have children from an earlier union. Do you still want your former spouse to inherit anything? Should your new spouse be named as a beneficiary? Aging, death, divorce, and other life-events, including the birth of a child or a job-switch, make it wise to periodically review beneficiary choices and ensure your assets go to the people you want to benefit most.

One reason it's so important to get beneficiary designations right is that when you name a beneficiary on your retirement accounts and life insurance policies, those assets will be transferred without going through probate or facing other complications. Moreover, the designations for financial accounts and insurance policies trump whatever it may say in your will. So, even if you change your will to cut out an estranged relative, that person still could benefit unless the beneficiary designations also are changed. And if there are discrepancies, the matter could end up in court—probably the last thing you would want.

Furthermore, getting the beneficiaries right may affect estate taxes. For instance, if you name your spouse as the beneficiary of your 401(k) and IRAs, those accounts won't be included in your taxable estate (although the assets eventually could be subject to estate tax when your spouse dies).

Another important thing to remember is to look at your full estate plan when choosing a beneficiary. Only by looking at all of your assets can you see how much each heir will inherit, and determine whether the distribution of assets is in line with your wishes. For example, if you designate one child as a beneficiary of an account that is invested with greater risk (and possibly greater return), while another is the beneficiary of a more stable account, one child may inherit significantly more than the other depending on market performance at the time of your death.

Finally, if you name a charity as an account beneficiary, the asset will pass to the charity tax-free. In addition, your estate will be entitled to a charitable deduction, which may reduce or eliminate tax liability.

For these and other reasons, it's crucial to get beneficiary designations right, and to revise them when necessary as your circumstances change. Going to the trouble of regularly reviewing your designations could be time well spent. ●

Don't Chase After The Market News

Did you read the newspaper today or check the news online? Invariably, the stock market will be heading up or down, with the movement triggered by anything from company earnings announcements to a change in economic indicators or even a political event such as the recent U.S. government shutdown. And, more often than not, financial pundits may respond by urging investors to buy or sell something.

But you can drive yourself crazy, if you haven't already, by making stock market decisions based on what has just occurred or what you think will happen next. In fact, chasing after the news is a common investment mistake. Here are some good reasons to avoid this temptation like the plague:

The stock market usually moves ahead of the news.

There was no "all clear" signal that the severe stock market downturn of 2008-2009 had abated. But the market hit bottom on March 9, 2009, and embarked on a long, profitable climb even as other financial news remained dire. Typically, stocks move about six months ahead of economic developments, reflecting the collective knowledge, trends, and inclinations of investors. If you try to beat the market by reacting to the latest news, you'll probably be much too late to benefit.

You don't have all the necessary information.

Markets tend to move based on the decisions of mutual fund managers or professional analysts who monitor and interpret financial data for a living. They have a lot more information than you do, and they get it much sooner than you—and millions of others like you—who will hear it on television or find it on the Internet. That puts you at a decided disadvantage.

You can't believe all the hype.

In this electronic age, media reports are often prone to hyperbole, as

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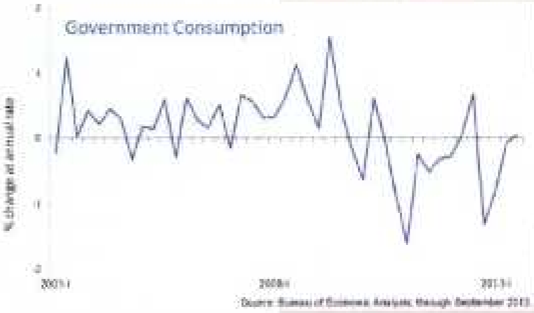
The Hidden Strength Of The Recovery

Economics 101 teaches you that growth in the economy is measured by gross domestic product (GDP), but investors should be mindful that factors included in the GDP calculation are masking an important trend in the economy.



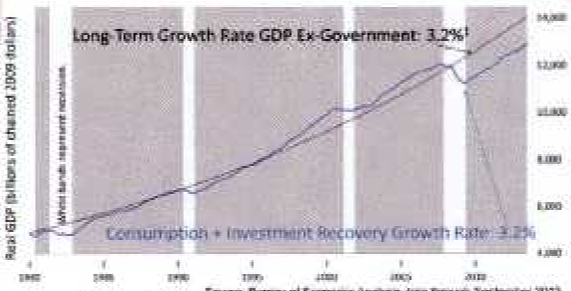
Source: Bureau of Economic Analysis, through September 2013

GDP is the sum total of consumer spending (C), investment made by the private-sector (I), government spending (G), and net exports. The formula econ teachers have always taught students is GDP = C + I + G + Net Exports. But changes in attitudes toward government spending over the last three decades belie the reliability of the old formula for economic growth. The notion that government spending should be part of a measure of economic output is questionable, and including government spending in the GDP growth figure masks the strength of the private sector in the current recovery.

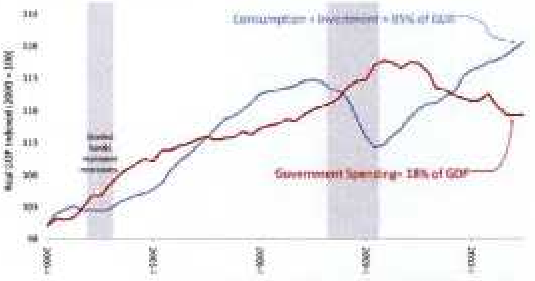
In recent years, government spending has been cut sharply, with the deepest cuts sustained by state and local government agencies. The chart below showing state, local, and federal government spending's contribution to the rate of growth in GDP illustrates the sharp cuts by government following the global financial crisis of 2008-2009.

Many economists would argue that reducing government spending will increase economic growth in the long run by leaving more resources available for reinvestment by the more productive private sector. While the long term impact of the reduction in government spending remains to be seen, in the short run it's clear that cuts in government spending have reduced GDP growth in recent years.

Removing government spending from the calculation of GDP conveys a very different story about recent U.S. economic growth. Excluding government spending from the GDP formula, according to data compiled by Fritz Meyer Economic Research, an independent research firm, puts the rate of growth of the current economic recovery in line with the long-term economic growth rate since 1980.



Source: Bureau of Economic Analysis data through September 2013.
[1] Compound Annual Growth Rate (CAGR) [2] CAGR for three-years ended September 2013.



Source: Bureau of Economic Analysis, data through September 2013.

From 1980 through 2008 the GDP grew at approximately 3.0% per year. In contrast, the annual GDP growth rate over the three-year period ending September 30, 2013 was only 2.1%, weak by comparison to the long-term trend. However, entirely excluding government spending from the calculation tells a different story. Consumer spending and investment (C+I) grew 3.2% in that recent three year period, matching the long term growth rate of C+I from 1980 to 2013.

GDP is intended as a measure of economic output. Since measuring economic output is more difficult than measuring consumption, however, government consumption is used as a proxy for output. Consumption and output are thought to be interchangeable because they are so intertwined. That's arguably flawed because the government does not produce anything and sell it.

While debate over the merits of government spending is politically charged, the practical implication of including government consumption in GDP is that it has masked the underlying strength in the other components of GDP. This may provide insight regarding how stocks were able to rise so sharply after the financial crisis despite what appeared to be a lackluster economic recovery. ●

the pressure to generate interest from a fickle public continues to increase. That could lead producers to overreact to news tidbits or sensationalize minor events. One small incident usually doesn't portend a complete economic collapse, so take reports of impending doom with a grain of salt. It isn't likely that the sky is falling! **Market timing is difficult, if not impossible.**

To be successful at market timing, you have to be extremely skilled or lucky, or both. Over the long term, buying or selling based on what you hear or read almost never beats a consistent, methodical long-term approach. It's better to make investment decisions based on financial particulars rather than on instincts and hunches.

Building a diversified portfolio combining stocks and bonds can help you progress toward your financial goals—and it can help you stop worrying about what you hear on the news. ●

Please remember that different types of investments involve varying degrees of risk, and there can be no assurance that the future performance of any specific investment, investment strategy, or product (including the investments and/or investment strategies recommended or undertaken by Financial Decisions, Inc.), or any non-investment related content, made reference to directly or indirectly in this newsletter will be profitable, equal any corresponding indicated historical performance level(s), be suitable for your portfolio or individual situation, or prove successful. A copy of the Financial Decisions, Inc.'s current written disclosure statement discussing our advisory services and fees is available upon request.

Investors Shift Toward Boutique Wealth Managers

A survey from the Luxury Institute shows that high-net-worth investors (with $5 million or more in assets) prefer boutique wealth management firms over Wall Street giants. Those who opt for boutique firms cite quality, exclusivity, and other factors.

The Wealth Management Luxury Brand Status Index (LBSI) survey from the independent Luxury Institute in New York scores respondents' answers based on each firm's quality, exclusivity, and ability to deliver special client experiences. The average respondent reported $15 million in net worth and income of $720,000.

"Reputations for honesty and superior client service are what make the smaller firms standouts in this survey," says Luxury Institute CEO Milton Pedraza.

Investors have been shifting toward independent advisors for years. The number of independent Registered Investment Advisors, for instance, surged 31% between 2004 and 2010, according to Cerulli Associates Inc. A report by Charles Schwab, the 2013 RIA Benchmarking Study, indicates that by the end of 2016, about one-third of advisor firms will have doubled in size over the previous 5 year period, largely due to revenues from new clients.

The trend is partially due to technology, as smaller firms are now able to offer access to many of the specialized investment vehicles and services that were once the province only of larger corporations with more resources. Declining trust in larger firms in the wake of the 2008 financial crisis is another factor.

Smaller firms enjoy a reputation of being more likely to put clients' needs first, while large firms are believed more likely to push in-house products. Another widespread belief is that smaller firms offer more in-depth, personalized service.

Many investors remain with big-name firms, however, especially if they are primarily looking for investment services that include access to high-end alternative investments. Even though access has become more widespread through technology, many of the larger firms still have an edge in terms of cost.

Some investors have even more specific reasons for sticking with the larger companies. For instance, an executive at a big, publicly traded company who has stock options may want to work directly with the financial services firm that handles that company's options.

Still, many investors have shifted to smaller, independent firms, which tend to offer more comprehensive wealth management services and more coordination among investment, tax, legal, and other advisors.

If you are looking for a financial advisor, consider interviewing advisors from small firms; you may find them more in touch with your own needs and goals.●

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retirement plans, IRAs, and Social Security. For instance, a 401(k) is generally required to pay a married participant's benefits in the form of a "qualified joint and survivor annuity," unless the participant elects otherwise. In addition, if a participant is married, funds in the account can be left to a non-spouse heir only with the consent of the spouse. Rules for "required minimum distributions" from retirement plans tend to be more favorable for married couples, and same-sex couples now should be able to take advantage of beneficiary rollover options when an IRA owner dies. Social Security benefits will also be affected.

5. Divorce. Like traditional married couples, same-sex couples who split up will face wide-ranging legal and financial consequences, and they may want to take precautions that could minimize the fallout. For example, spouses might decide to protect their retirement plan benefits with a qualified domestic relations order (QDRO). When a QDRO is used, a spouse has the right to share in benefits available to the other spouse, but the spouse who receives the benefits will be taxed on them. Otherwise, the spouse who earned the benefits would be liable for the entire amount of the tax.

Remember that the *Windsor* ruling applies only on the federal level—and that makes it essential to investigate possible implications under varying state laws. Under current rules, a marriage that is recognized in one state may not remain legally enforceable if a couple moves to a state in which same-sex marriages are not recognized—a confusing situation.

Same-sex couples would do well to research the impact of DOMA and seek professional guidance because the rules are likely to be clarified in the months ahead and the financial consequences can be significant. ●