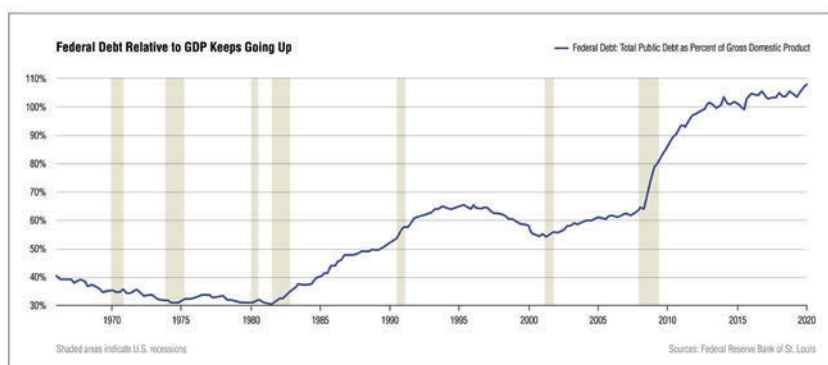


If the Tax Code Changes, Will You be Prepared?

Many readers have seen the staggering numbers: the U.S. federal government has spent more than \$3 trillion on the economic fallout from the pandemic, and more stimulus appears to be on the way. This spending has gone directly to Americans—stimulus checks, unemployment benefits with an extra \$600 a week, emergency grant and loan programs for small businesses, the Paycheck Protection Program (PPP) and more.

All told, the total amount of federal debt relative to U.S. GDP has not been this high since World War II. Drastic times call for drastic measures, but we are fast approaching uncharted territory.



Few would argue against the decision to ramp-up government spending in the current environment. Emergency funds have helped many households and businesses survive the downturn, and the flood of liquidity has arguably supported the stock market's rebound since late March. Looking ahead, however, we think it will be important for all investors and savers to consider an inevitable question: will the government eventually have to raise taxes to pay for all of this?

The short answer is that no one knows, but it seems unlikely that taxes can—or will—move considerably lower from where they stand today. The good news is that changes to the tax code generally happen at a snail's pace and come with a fair amount of warning, meaning investors can use the current moment—and its relatively low tax rates—to make a game plan.

The first step in making a game plan is to survey the playing field, which long-time investors know is constantly shifting with different administrations and policies. For now, we remain confident that the elements of the tax code outlined below will likely remain in force for at least the next year or two,



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giving investors a sizable window to plan. Here are a few key areas to consider:

Gifting. Throughout your lifetime, you are allowed to give \$15,000 per year to as many people as you want (they do not have to be family). Combined with a spouse, the annual gift doubles to \$30,000, which over time can allow you to shrink the overall size of your estate—perhaps in an effort to avoid assets being subject to the 40% estate tax.

Higher Estate Tax Exemption. The Tax Cuts and Jobs Act of 2017 doubled the estate and gift tax exemption from \$5 million to \$10 million with inflation adjustments, meaning that in 2020 an individual can give away \$11,580,000 tax free. Any amount higher than \$11,580,000 would be subject to the 40% estate tax. A key feature of this added exemption is that it only lasts through 2025, which may add some urgency for investors to start making plans soon.

Roth IRA Conversions. If all signs point to you being in a higher tax bracket in the future versus where you are today, then it could make sense to explore converting some of your traditional IRA money into a Roth IRA. Making this conversion means triggering income taxes on the converted amount, but if you or your heirs' taxes are poised to move higher, it could create tax savings over time.

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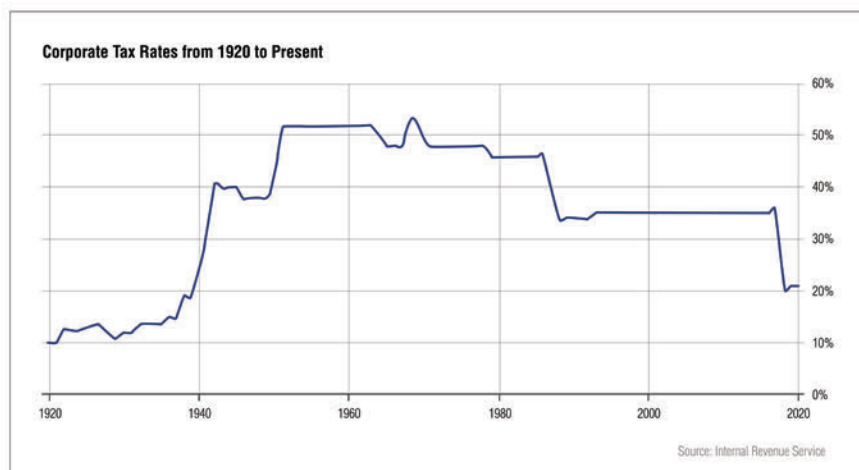
Reviewing Valuations of Closely Held, Family-Owned Businesses. Funeral home and cemetery business owners have an entirely different set of questions to address. Will your children or heirs take over the business, or sell it? If capital gains rates are likely to move higher in the future, would it make sense to sell the funeral service business now versus waiting? Would it make sense to start the process of transferring the business to the next generation sooner rather than later?

These are all big, fairly consequential questions. The upshot is that many of them can be answered with a comprehensive tax planning analysis and some expert advice. A smart analysis would explore ways to lower taxes during retirement, improve lifetime tax savings, and minimize taxes for heirs. Different strategies would produce different tax savings, long-term growth outcomes, and probabilities of success. We think it is imperative to consider every option available.

HOW DO CHANGES TO THE TAX CODE IMPACT FINANCIAL MARKETS?

If, for argument's sake, we assume tax rates move higher in the future to compensate for mounting debt, the next question to ask is whether higher tax rates could adversely impact financial markets.

The immediate response may be that higher taxes would likely lead to lower corporate profits, which in turn would mean weaker stock market performance. But history suggests otherwise. The chart below illustrates the U.S. corporate tax rate from 1920 to present. The biggest sustained increase to corporate tax rates occurred in the 1940s and 1950s, with the rate topping 50%.



As corporate tax rates soared during and after World War II, the stock market was hardly fazed. During the 1940s, the S&P 500's total return was +143.10%, and during the 1950s the index jumped +467.40%. In short, history suggests that the economy and stock market can absorb higher taxes (even if nobody likes them).

A similar picture emerges when we look at the capital gains tax rate. The table below shows major changes to the capital gains rates over the last few decades. The capital gains rate bounces around quite a bit more than the corporate tax rate and personal income tax rates, but does not appear to have a strong impact on the stock market's performance:

Year	Change to Capital Gains Tax	S&P 500 Performance that Year
1981	Cut from 28% to 20%	-4.7%
1987	Raised back up to 28%	+5.81%
1997	Cut back to 20%	+33.10%
2003	Cut to 15%	+28.36%

Source: Internal Revenue Service, NYU Stern

It seems taxes alone may not be powerful enough to drive long-term market performance. The stock market is affected by too many other factors - interest rates, corporate earnings, inflation, economic growth, expected profits, and so on. Taxes matter, of course, but marginal changes to the tax code have not stifled economic growth and/or pulled stocks lower in the process. In our view, a shifting tax environment should impact a person's overall financial plan far more than their investment strategy.

MINIMIZE UNCERTAINTY WITH A COMPREHENSIVE PLAN

Many funeral services professionals reading this article likely are thinking about retirement, quickly approaching it, or already retired. Whether that means you're weighing the future of taxes, economic growth, public health, or interest rates, the takeaway is clear: uncertainty is high, and having a plan is essential to navigating your way through the years ahead.

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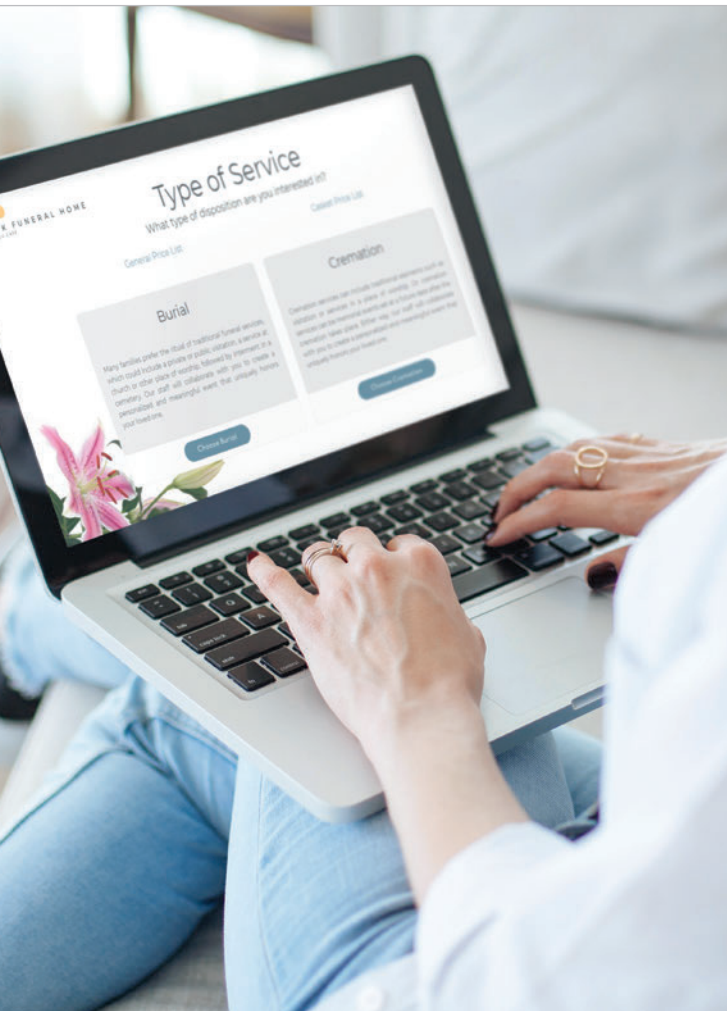
A well-designed, comprehensive financial plan can help you minimize taxes in—and after—retirement and transfer your wealth with maximum efficiency. Done right, a financial plan is the best tool available for ensuring you and your family receive the financial support and security needed for generations to come.

Building a financial plan is a complex process—there is a lot of information to digest and many decisions to make. But do not let that prevent you from taking the first steps, and be sure to lean on your financial advisor for resources and help in building your plan. If you would like to use a Roosevelt Financial Advisor as a sounding board for some of your questions about your financial plan and navigating your way through shifting tax environments, please do not hesitate to reach out to us. We're here to listen and help. ▲

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