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SIA

Signature Investment Advisors®
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THE SIA REPORT

ARE TAX CHANGES ON THE HORIZON?

BY **Sam Miller**
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With President Biden now in office and a Democratic majority in Congress, we believe changes to tax policy are on the horizon. But questions remain as to the specifics and the timing. What might we expect based on what was communicated on the campaign trail and what's transpired since? And are there steps investors should be taking now, to help soften the impact of potentially higher taxes?

Possible changes

While there were many proposals mentioned on the campaign trail, the overarching theme of the Biden tax plan appears to focus on raising taxes on the very highest of earners. The most popular of those proposals include[1]:

- Increasing the top federal income tax rate from 37% to 39.6% for those earning over $400,000
- Increasing the capital gains tax rate to 39.6% for individuals earning over $1,000,000
- Eliminating the step-up in cost basis at death for the assessment of capital gains
- Implementing a 28% cap on itemized deductions
- Applying a 12.4% social security payroll tax on earners making more than $400,000
- Reducing the estate tax exemption

We expect the specifics will almost certainly change between now and implementation, but our general consensus is that the highest earners should expect some sort of tax increase.

Timing

In terms of timing, once a Covid relief package (the administration's first priority) is in place, the focus may then shift to a larger infrastructure and climate change package. This could require some sort of tax legislation to fund the initiatives.

With the narrowest majority in the House in 20 years, and a 50/50 split in the Senate, there may be challenges to passing any legislation. But we expect to see a healthy tax debate at some point during the summer months. If tax legislation is eventually passed, changes may be immediate or retroactive. While rare, there have been instances in the past where tax increases were retroactive to the beginning of the year. It's possible any changes could take effect at the time the legislation is signed into law.

Strategies to consider

- **Tax/estate planning**—There are several strategies you may want to consider depending on your particular financial situation. If you have annual income in excess of $1,000,000, you might explore harvesting some capital gains now; before those rates potentially double. Additionally, if you have a large estate, think about using some or all of your lifetime estate tax exemption before it's potentially lost.
- **Asset location**—As investment advisors, much of our time is spent on asset allocation (the mix of stocks, bonds, and alternative assets in your portfolio), but tax efficiency can be improved by focusing on asset location as well. This refers to 'where' you place the assets you own (tax-free vs tax-deferred vs taxable accounts). Conventional wisdom[2] suggests you should own income-producing investments like bonds inside of non-taxable accounts (to shield that income from taxes). But with low interest rates and low growth expectations, this strategy may no longer prove beneficial. Ultimately, you should strive to hold tax-efficient assets with higher expected returns inside of taxable accounts, and tax-inefficient assets with higher expected returns inside of tax-favored accounts like IRAs.
- **Tax loss harvesting**—While some individuals with higher incomes might consider harvesting gains before their rates potentially increase, for others tax loss harvesting may play

1 The Tax Foundation, as of October 22, 2020
2 Financial Analysts Journal: Integrating Investments and the Tax Code

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I believe successful wealth management is the result of an ongoing collaboration between investor and advisor, built upon trust and maintained according to the highest standards of integrity and expertise.

Brian D. Holmes,
MS, CFP®, CMFC, AIF®, *President & CEO*

ABOUT SIA

Signature Investment Advisors® (SIA) is a Registered Investment Advisor firm offering investment management solutions that are tailored to meet the unique needs of affluent individuals and organizations. In partnership with your wealth manager, we bring our combined experience, expertise and high level of service to provide a dynamic process that can meet your investment objectives and goals.

2021 TAX BRACKETS

Tax rates did not change; however, tax bracket amounts were adjusted to account for inflation:

Rate	Married Joint Return	Single Individual
10%	$19,900 or less	$9,950 or less
12%	Over $19,900	Over $9,950
22%	Over $81,050	Over $40,525
24%	Over $172,750	Over $86,375
32%	Over $329,850	Over $164,925
35%	Over $418,850	Over $209,425
37%	Over $628,300	Over $523,600

Source: IRS

PROTECT WHAT YOU’VE BUILT

BY **Gary Liska**
MS, CFP®, AIF®, CRPC®, AAMS®
Founding Partner, CFO

How to limit the impact of major market corrections

Less than a year ago we saw first-hand how a significant external force (in this case the COVID-19 pandemic) could trigger a major market correction. Unexpected non-financial factors such as wars, political upheaval, terrorism and natural disasters can wreak havoc on global financial markets. But thankfully, these disruptors tend to be relatively short-lived.

As last February and March perfectly demonstrated, resulting declines can be precipitous—but often, so too is the subsequent recovery. The S&P 500® dropped 8.4% in February and then plummeted another 12.5% in March with lockdowns shuttering much of the economy. Yet over the next three months, the index (+20.54%) recovered all those losses and subsequently went on to set new all-time highs—finishing the year up 16.3%.[1]

Similarly, when the stock market finally reopened after the September 11th terrorist attacks two decades ago, within five trading days the S&P 500 Index had dropped 11.6% and the Nasdaq had fallen 16%. Within a month’s time, however, both indexes had regained their pre-9/11 price levels.[2]

In both cases, despite the profound human and economic costs associated with these events, investors quickly came to view them as temporary external impediments. And because financial markets are forward-looking, once the initial shockwave was absorbed, it didn’t take long for a recovery to ensue. But what happens when corrections are driven by internal rather than external factors?

A longer road to recovery

When corrections are the result of fundamental internal economic and market changes such as rising inflation, monetary and tax policy, or cyclical overvaluation of prices relative to earnings, the resulting recession and recovery tend to be more prolonged—a matter of years rather than months. During the 17-month bear market period from October 2007 to March 2009, the S&P 500® lost nearly 50% of its total value. Although it took a full four years for the index to recover those losses, in the decade that followed the post-financial crisis bottom on March 9, 2009, the market ultimately went on to generate a cumulative return in excess of 400%.

The consistent theme in every one of these examples, however, is one of recovery. We may not be able to predict when a correction will happen, how deep and prolonged it will be, or the duration of the eventual recovery. But we can be historically confident that at some point in the future the market will again be setting new highs.

Mitigating your risk

So, what should investors do? The easiest answer is to do nothing—to not panic when the market swoons and simply allow time to be your greatest ally. There are, however, a variety of effective strategies that can help reduce your investment risk and help you better prepare for whatever the market may have in store.

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1 “S&P 500® Index Data,” Morningstar, January 2021
2 “How September 11 Affected The U.S. Stock Market,” Investopedia, December 2020
* Investing involves risk including the potential loss of principal. No investment strategy can guarantee a profit or protect against loss. Past performance is no guarantee of future results.

2021 INTERNATIONAL WOMEN'S DAY

Monday, March 8th marked International Women's Day – a global day to celebrate the social, economic, cultural and political achievements of women. It's hard to imagine a more striking example of these achievements than the incredible female leadership we continually witnessed over the course of a pandemic-ravaged 2020.

From BioNTech's chief medical officer Ozlem Tureci (co-developer of the world's first effective COVID vaccine) and Melissa Moore, chief scientific officer (in charge of the mRNA technology) at Moderna, to female heads of state like Jacinda Ardern in New Zealand, Tsai Ing-wen in Taiwan, Sanna Marin in Finland, and Erna Solberg in Norway who all brilliantly navigated their nations through the pandemic in far better shape than most countries. And let's not forget Kamala Harris, the first female Vice President of the United States.

As a global community, we continue to strive for greater equality—because a more equal world is a more empowered and enabled world—one that's healthier, wealthier and more harmonious.

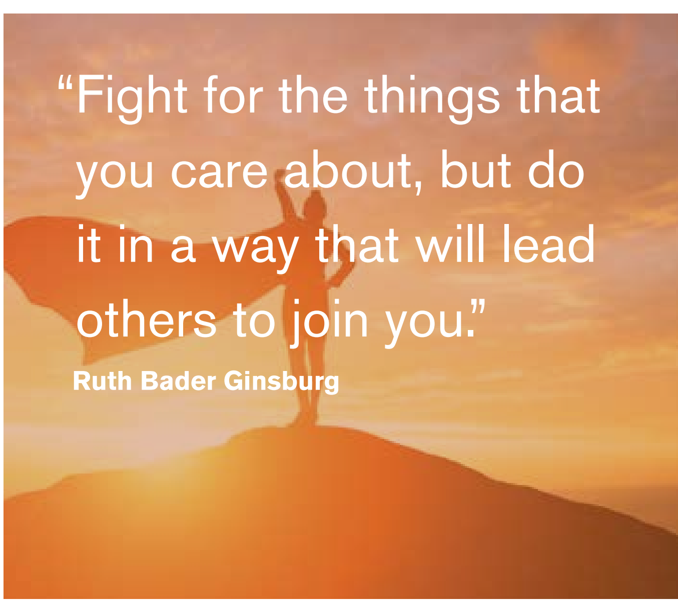
At SIA, we embrace the belief that equality isn't just a women's issue, it's a business issue. Gender equality is essential for economies and communities to thrive. And we're proud and honored to have so many women assuming leadership and key roles throughout our organization including:

Sabina Pinsky
Marketing & Events Specialist
October 2005

Alina Barrass
Director of Client Services
January 2013

Liselotte Richards
Compliance & Operations Specialist
August 2014

We're inspired by all of these incredible contributors, and look forward to cultivating future generations of empowered women. To learn more about what you can do each and every day to help foster equality, please visit internationalwomensday.com.



THANK YOU!

CENTURY CITY, CA

Rachel Otto
May 2015

Richelle Parra
October 2015

Vanessa Garcia
October 2017

Ariana C. Rodriguez
November 2017

Ellen Baldecchi
July 2018

Katharine Neary
July 2020

Marlene Escobedo
October 2020

Briana Bowker
January 2021

a more important role in portfolio management to mitigate the impact of higher taxes. Tax loss harvesting refers to the process of realizing a loss on an asset for tax purposes. In any given year, the market and its component parts (individual stocks) go up and down—sometimes wildly. Even a year like 2020, where market returns were strong by year-end, more than 400 stocks in the S&P 500® experienced a drawdown of 25% or more[3].

- **Municipal bonds**—Higher tax rates may mean that municipal bonds (bonds that are exempt from federal and most state taxes) become relatively more important within a portfolio. When selecting a municipal bond strategy, we believe that strong active management is important to capture opportunities that exist in a complex and sometimes opaque asset class.

In the coming months, we will likely have greater clarity around Biden's tax plan and the specific items that will be part of that package. As these details start coming into focus, make sure to consult with your SEIA advisor to develop a mitigation strategy as part of your overall financial and investment plan.

3 Bloomberg

Investing involves risk including the potential loss of principal. No investment strategy can guarantee a profit or protect against loss. Past performance is no guarantee of future results. Federal tax laws are complex and subject to change. This information is not intended to be a substitute for specific individualized tax or legal advice. Neither Royal Alliance Associates, Inc., nor its registered representatives, offer tax or legal advice. As with all matters of a tax or legal nature, you should consult with your tax or legal counsel for advice.

PROTECT WHAT YOU'VE BUILT *continued from page 2...*

- **Rebalance your investment portfolio:** Over time, especially during an extended market run-up, you're your asset allocation can shift drastically from its target. Because of the far more substantial appreciation of stocks relative to bonds, a typical 60/40 moderate risk portfolio (60% stocks and 40% bonds) that you and your advisor created a decade ago may today have shifted to a very aggressive 80/20 allocation. By periodically rebalancing, you can keep your investment risk in check and lessen the impact of future corrections.*
- **Dial back risk when warranted**: Have you achieved important goals such as funding your children's education, or are close to reaching other goals like saving enough for retirement? If so, you can afford to be more conservative with your investments. Similarly, if retirement is close on the horizon (within three years) you should also consider reducing your overall portfolio risk as the market may not have time to sufficiently recover before you begin drawing down your assets for income.
- **Consider gifting highly-appreciated stocks**: It's a strategy that accomplishes two goals at once; it supports the charitable organizations and causes that you care about, while at the same time helping to rebalance your portfolio by reducing your stock holdings. And it does so without triggering any capital gains and providing you with a charitable tax deduction for the full fair market value of the stock.
- **Keep bond maturities shorter**: Given the current low interest rate environment (and the potential for rates to rise in the future) look for higher coupon bonds with shorter durations rather than longer maturity government bonds. Talk to your advisor about possibly increasing your allocation to high yield corporate bonds and/or floating-rate bonds where interest rates adjust (often monthly or quarterly) to help lessen the impact of any future rate increases.
- **Talk with your advisor about more sophisticated strategies**: Depending on your individual circumstances and needs, your advisor may be able to suggest additional risk mitigation strategies to further protect your wealth.

The market has come a long way in the decade plus since the bottom of the Great Recession. Nobody knows when the next leg down will occur or how long it will take for the subsequent recovery. But there are ways that you and your financial advisor can help better position your portfolio to weather any storms that may be on the horizon.

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