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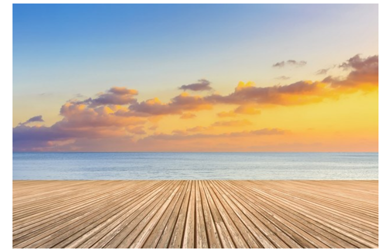
Financial Services & Wealth Management



Financial Planning Newsletter - Summer

Determining the Basis of Inherited Property

Presented by Harriett Barnes

The basis of property inherited upon death is traditionally known as the fair market value (FMV) on the date of the owner's death. You may also hear the term "stepped-up basis." Often, an asset may have increased in value since the decedent purchased it, and the beneficiary can benefit from a tax-free increase (i.e., step-up) in value.

Although there are exceptions—and you should always seek help from your tax advisor—the following fundamental principles offer a good starting point for determining the basis of inherited property.

General rule
The basis of inherited stock is the FMV on the decedent's date of death or on an alternative valuation date (e.g., six months from the date of death) if chosen by the decedent's executor. A beneficiary's basis may be stepped up or down, depending on whether the stock appreciated or depreciated in the decedent's hands. If the beneficiary later sells the stock, any gain will be treated as a long-term capital gain, regardless of how long the beneficiary actually held the stock prior to sale.

This rule does not apply to property inherited from a decedent if you or your spouse gave that property to the decedent within one year before his or her death. In such cases, the basis of the property is the decedent's adjusted basis immediately before death, rather than the FMV.

Surviving spousal joint tenant
Where the property is held by a husband and wife with rights of survivorship, one-half of the property is treated as belonging to the first spouse to die, without regard to either spouse's contribution to the purchase price. Thus, the surviving spouse would receive a new basis in the deceased spouse's 50-percent interest, while the basis of the surviving spouse's 50-percent interest would remain the same.

Surviving non-spousal joint tenant
The general rule is the entire value of the account is included in the deceased's estate, and the surviving joint tenant receives a new basis on the total value of property. If the joint owner can prove each party's personal contribution to the purchase price, however, only a prorated share will be included in the deceased's estate. The basis of the property will be adjusted accordingly. For instance, if the deceased joint tenant contributed 60 percent of the purchase price, only that 60-percent interest would receive a new basis when transferred to the joint tenant. The joint tenant's remaining 40 percent would retain the original basis of the purchased property.

Community property
If one-half of the value of property owned by a couple is includable, for federal estate tax purposes, in the gross estate of the first spouse to die, then both the decedent's and the surviving spouse's one-half interest in the community property would receive a new basis equal to the property's FMV on the decedent's date of death (or on an alternative valuation date).

The one exception to this rule involves separate property that has been converted to community property. If the conversion occurred less than one year before the death of the first spouse, and that spouse didn't originally own the property, then there would be no step-up in basis of the decedent's one-half interest if it passed back to the surviving spouse. The surviving spouse, however, would receive a step-up in basis of his or her one-half interest, as that interest was not received by gift from the deceased spouse.

Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and (for some purposes) Wisconsin are community property states.

This material has been provided for general informational purposes only and does not constitute either tax or legal advice. Although we go to great lengths to make sure our information is accurate and useful, we recommend you consult a tax preparer, professional tax advisor, or lawyer.

2019 Midyear Outlook: A Story of Headlines Vs. Fundamentals

Presented by Harriett Barnes

At the end of last year, the big question was, “Will 2019 bring the end of the recovery?” All of the data seemed to point to an answer of “Not yet.” And so far, that answer still holds. The big picture suggests growth is likely to continue for the rest of the year, which should, in turn, support the financial markets. But there’s more to the story . . .

Headlines Vs. Fundamentals

To date, it has been an eventful year. Markets moved up, pulled back sharply, and then bounced again. The economy was slow to start, picked up during the first quarter, and now may be slowing again. Meanwhile, the political story has included the Mueller report, a China trade deal and then a trade war, a postponement of Brexit, and looming tensions with Iran.

Reacting to all of these headlines would have been a bad strategy. Because while the markets have been more volatile this year, the fundamentals—the underpinnings of our economy—have remained solid.

Take job growth, for example. Although there has been volatility in the monthly job gains, the overall growth rate has remained steady at more than 2 million jobs per year. Over the past 40 years, when job growth has been at this level, a recession has been at least a year away. Yes, we have seen some weakening recently, but the year-on-year trend remains strong.

Similarly, consumer confidence levels remain high, at levels last seen in 2001, and the year-on-year change is positive. We have never had a recession without a decline in confidence of at least 20 points over the previous year. This should buy us another 12 months or more.

Business confidence is weaker than both job growth and consumer confidence, currently sitting at close to its lowest levels of the past several years. Despite that, it is still solidly expansionary, suggesting continued, though slower, growth.

By the Numbers: 2019 Expectations

GDP Growth: 1.50%–2%

Inflation: 2%

Federal Funds Rate: 1.75%–2.25%

10-Year U.S. Treasury Yield: 1.75%–2.25%

S&P 500 Index: 2,900–3,000

Even the yield curve spread shows risk is not likely immediate. Although the yield curve is on the verge on inverting, an inversion would only start the recession clock ticking. Historically, the initial inversion has preceded a recession by a year or more, which once again leaves us in the green for the balance of 2019.

Looking at these fundamentals, it’s clear that conditions are better than the headlines suggest. We have never had a recession with job growth as strong as it is, with confidence where it is, and with the yield curve where it is. Some slowing is likely, but slowing is still growing, with calendar-year expectations for economic growth sitting between 1.5 percent and 2 percent.

The Fed and Monetary Policy

Given the healthy data mentioned above, we could have reasonably expected inflation to rise—and it did, but not by much. More, the most recent data suggests that, with slowing growth, inflation has started to pull back again. Although the Fed decided in 2018 that the risks of not raising rates were greater than those of raising them, in 2019 it has put that policy on hold because of this slowdown.

Expectations are for no more increases this year, plus a real possibility of cuts. Inflation is now expected to stay below 2 percent, and longer-term rates should end the year around current levels, with the yield on the 10-year Treasury between 1.75 percent and 2.25 percent.

What About the Stock Markets?

Steady growth and interest rates suggest that global stock markets are likely to continue to trade on fundamentals, such as revenue and earnings growth. Here in the U.S., revenue growth remains healthy, and while earnings growth has slowed, it is expected to remain positive. This should support the markets through the rest of the year.

With earnings growing, the real issue will be valuations. Historically, high confidence levels have driven up valuations, and we have seen that in recent years. As confidence moderates and growth slows, however, we can expect valuations to stop rising, meaning further appreciation will depend on earnings growth.

Continued:

Given projected earnings growth and steady valuations, the S&P 500 is likely to end 2019 between 2,900 and 3,000. There is upside potential if earnings growth surprises or if valuations recover to the high levels seen in 2016 and 2017. But there may be more downside risk, if economic growth slows or if valuations drop on lower confidence. Still, this estimate is reasonable.

Prospects Bright, but No Guarantees
Solid economic fundamentals should continue to support markets through the remainder of 2019, with moderate appreciation likely—if current trends hold. None of this, however, is guaranteed. Here in the U.S., we'll need to keep an eye on potential impeachment of the administration by the Democrat-controlled House; the ongoing trade war between the U.S. and China; and, most notably, the upcoming debt ceiling confrontation between Congress and the administration. Abroad, we have pending issues in Europe, including Brexit and Italy, as well as a rising confrontation with Iran.

Even if growth does slow, though, or we see any of the other potential issues erupt, the underlying strength of the economy is likely to limit the damage. We've seen many similar situations in the not-so-distant past—and they didn't knock the economy or markets off their paths.

When you look back at the recovery so far, this scenario is very similar to what we have seen for most of the past 10 years: slow growth threatened by multiple risks. And, just as we have seen over the past 10 years, although the concerns are real, the big picture is very much like what we have become accustomed to. Despite the worries, it's still not a bad place to be.

Certain sections of this commentary contain forward-looking statements based on our reasonable expectations, estimates, projections, and assumptions. Forward-looking statements are not guarantees of future performance and involve certain risks and uncertainties, which are difficult to predict. Past performance is not indicative of future results. All indices are unmanaged and investors cannot invest directly into an index. The S&P 500 Index is a broad-based measurement of changes in stock market conditions based on the average performance of 500 widely held common stocks.

Fiction:

Not all app and operating system updates to my phone are necessary.

Fact:

Outdated apps and mobile operating system software leave your phone open to security vulnerabilities. To save time, make sure your apps are configured to update automatically, and be sure to install mobile operating system updates as soon as you are notified.

Financial Tip: Test Your Knowledge of Social Security Spousal Benefits

Social security spousal benefits are designed to provide retirement income to spouses who've earned significantly less than their spouses have during their working careers. So, if your social security income is less than half that of your spouse's, you may be eligible to receive a social security spousal benefit to make up the difference.

For example, Jon, age 70, has been married to Patty for 40 years. Jon reached full retirement age at 66 years old, but he waited until age 70 to claim his social security retirement benefits, earning him delayed retirement credits. When Patty reached her full retirement age, she filed for spousal benefits based on Jon's record.

True or false?
Patty's social security spousal benefits will be 50 percent of Jon's retirement benefits, including his delayed retirement credits.

Answer: False.
Once Patty reaches full retirement age, she is eligible for a maximum spousal benefit equal to half of Jon's primary insurance amount, or the amount Jon would have received at his full retirement age. Spousal benefits do not increase with delayed retirement credits.

If Jon were to die before Patty, however, her survivor's benefit would be based on the amount Jon was claiming at the time of his death. This would include Jon's delayed retirement credits.

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A REPUTATION TO BE PROUD OF

We are proud to be affiliated with Commonwealth Financial Network®, a Registered Investment Adviser–broker/dealer with a singular commitment to serving independent advisors and their clients. The latest demonstration of that commitment can be found in the J.D. Power 2019 U.S. Financial Advisor Satisfaction Study.

For the sixth time, the J.D. Power study ranks Commonwealth:

"#1 in Independent Advisor Satisfaction Among Financial Investment Firms"*

Again, the results were no surprise to us. But it's what this achievement means for our clients - on a daily basis - that makes the difference.

Commonwealth's entire organization is built around doing whatever it takes to satisfy not only the advisors who work with the firm, but the clients of those advisors as well. It's that infrastructure—and the always expanding wealth of resources it provides—that makes it easier for our firm to provide you with the best possible guidance and the prompt, personal service you expect and deserve.

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*Commonwealth Financial Network® received the highest score in the independent advisor segment of the J.D. Power 2010, 2012, 2013, 2014, 2018, and 2019 Financial Advisor Satisfaction Studies of customers' satisfaction among financial advisors. Visit jdpower.com/awards.

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