ALTIUS Financial — Empowered Future Report

Short term thoughts about long term matters

January 8th, 2013

Quote of the Day:

"During my eighty-seven years I have witnessed a whole succession of technological revolutions. But none of them has done away with the need for character in the individual or the ability to think." --Bernard Baruch

Happy New Year!

This is that time of the year that many of us are motivated to begin anew with our aspirations and you may be wondering what the best course of action is to reach your goals. As is our tradition, we sent out our goal framework a couple weeks ago (if you didn't get yours, let us know) and I'm happy to be getting feedback already on all the exciting plans. And that's part of what I want to remind you of – to turn those goals into reality. Your plan needs to consist of laying out a series of steps (large and small) that will guide you down the path toward success over the next 12 months and beyond. Here are some ideas for helping with that plan:

- ***Create Clarity Around Your Goals*** - You've heard of SMART goals? Specific, Measurable, Achievable, Realistic and Time-bound. Having shorter term milestones allows you to "eat the elephant, one bite at a time".
- ***Compartmentalize Your Goals*** – Use our framework to have goals in the various areas of your life; not just money or health or relationships.
- ***Attach Emotion to the Activities*** – Use both positive emotions and negative emotions to encourage the good and steer clear of the bad habits.
- ***Get an Accountability Partner*** - It usually takes 21 days to turn an activity into a habit. Don't think you have to do it all on your own.
- ***Celebrate Minor Victories*** – A big part of goal achievement is momentum so get in the habit of enjoying the progress little by little.

If you follow these steps, you will soon find that you have created a blueprint for yourself and your 2013 goals. And that blueprint—if you consistently follow it—will turn those goals into realities. Consistency, consistency, consistency! Following it is tough and perhaps the most difficult part is throwing off discouragement when it comes…because it will.

Aaahhhhhhhh!

Well, I guess we went over it (the fiscal cliff) - if only for a day or so. Yes, our leaders in Washington went down to the 11th, 12th, and 13th hour to come up with an agreement called The American Taxpayer Relief Act of 2012. I'm not sure taxpayers feel any relief and it did very little to resolve the major fiscal issues we face. There will be more headlines and congressional battles this year over the same topics we've been hearing about for the last 3 years. Here's a very brief rundown of what they accomplished:

- It did make the existing tax brackets permanent (if there is such a thing with the tax code) for most Americans. Those earning $400,000 (single) or $450,000 (married filing jointly) and more will have their highest ordinary income bracket increased to 39.5% and their capital gains bracket will also increase to 20%. These more productive earners will also pay a Medicare Surtax of 3.8%.
- The "payroll tax holiday" is over. This means that everyone who draws a paycheck will go back to having more automatically withheld for FICA (from 4.2% back up to 6.2%). This holiday was enacted to give a little more current income to wage earners in the hopes that they would feel a "wealth effect" and spend that money to help the economy. Fallacies abound with this thinking. Unfortunately, our congress believes it worked and the economy no longer needs this help or that since Social Security does not have enough funds so they need to go back to increasing this revenue.
- The new law offers some clarity around estate taxation: unified federal estate and gift tax exemption of $5 million -- adjusted annually for inflation -- and a 40 percent maximum tax rate (up from last year's 35 percent rate). For 2012, the exemption amount was $5.12 million after being adjusted for inflation. For 2013, the inflation-adjusted exemption amount is expected to be approximately $5.25 million. The new law also makes permanent the right to leave your unused federal estate and gift tax exemption to your surviving spouse (the so-called "exemption portability" feature).
- Congress typically tries to amend or patch AMT rules to prevent millions more households from getting hit with this add-on tax. This time the patch consisted of allowing larger inflation-indexed AMT exemption amounts and allowing various personal tax credits to offset the AMT. Thankfully, the

new law makes the patch permanent, starting with 2012. As a result, about 30 million households a year will be kept out of the AMT zone.

- As always with these tax law changes, there were numerous tweaks to various deductions, exemptions, allowances, etc. This time they made "Marriage Penalty Relief" rules more permanent, gave a larger Child Tax Credit, more favorable Child and Dependent Care Tax Credit Rules as well as more favorable Student Loan Interest Deduction Rules and Coverdell Education Savings Accounts.
- Last, the phases out rules for higher-income taxpayers are back. One can potentially lose up to 80 percent of their write-offs for mortgage interest, state and local income and property taxes, and charitable contributions if your adjusted gross income (AGI) exceeds the applicable threshold. The total amount of your affected itemized deductions is reduced by 3 percent of the amount by which your AGI exceeds the threshold. However, the reduction cannot exceed 80 percent of the total affected deductions you started off with. For both personal/ dependent exemptions and itemized deductions, the AGI thresholds are $250,000 for singles, $300,000 for married joint-filing couples, $275,000 for heads of households, and $150,000 for married individuals filing separately.

Of course there is much more to this tax law change. I've only tried to summarize the major provisions. I'd advise you to speak with us and your tax preparer to see how the new law may affect your specific planning going forward.

Economic Outlook and Portfolio Construction

As we head into the new year, I think it's important for you to understand how we think about the economy and how that view affects where we invest your money. We'll continue to hold our Capital Market Outlook workshops and encourage you and guests to come with questions. (We welcomed a number of new clients this past year who were introduced to us at our workshops - we truly appreciate the referrals you provide). As the year unfolds I'll write more about our "Pillars of Productivity" since this is the fundamental framework that we use for evaluating the strength of the overall economy.

While the fiscal cliff discussion is over for the moment, as I mentioned above there will be ongoing uncertainty regarding the US and world economy. Here are several unpleasant facts that we know:

1. The U.S. remains in the grip of a debt-induced economic funk – many say we're starting to grow, many say we aren't; but no one believes we have healthy, organic growth without the Fed's stimulus policy. While personal levels of debt have eased some, most of the improvements have come by shifting debts from private balance sheets to public (government) balance sheets. One thing that heavily indebted – individual, company or government – most fear is… rising interest rates.
2. Despite the debt, interest rates remain near historic lows – well below the norm. At some point they will revert to the mean or much higher.
3. Other than dramatic economic growth, I don't see non-disruptive way to resolve the debts. There is no magic wand (or Trillion dollar coins) that can be waved in order to make those debts go away. There is no politically convenient time to take the difficult measures needed to rebalance the budget and get the nation's finances in order. This most recent debate shows how difficult it is for our officials to make substantive progress.
4. Inflation remains the only politically viable way to continue down this path.

Given these facts, we will continue to manage our portfolios for the long term with protection against inflation and toward capital/purchasing power preservation. I am an optimist and do believe there will come a time when we'll want to be very aggressive but we aren't there yet. Focus on opportunities, but best anyone can do is focus on their circle of control – the things they can directly influence; their daily actions, spending and savings habits, their thoughts.

Calendar Notes

We'll announce our schedule of Capital Markets Outlook workshops sometime in the next few weeks. Also, we'll be communicating other key dates and best times to schedule your planning and portfolio reviews. In the meantime, we hope you enjoyed the holidays and that your new year is off to a fantastic start!

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