REFLECTIONS

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WINDGATE
WEALTH MANAGEMENT

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FIVE RULES OF ESTATE PLANNING

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Proper estate planning can save your family large amounts of stress – and money – when they are at their most vulnerable. Yet it's not something that most clients want to talk about. Thinking about death is uncomfortable for anyone and facing the reality could mean conquering some emotional demons. Even worse, estate planning often seems complicated and unwieldy.

Still, taking care of your estate now means that you can rest easy while knowing you'll be prepared for whatever happens. Read below to see the Five Rules of Estate Planning.

1. Create a Trust

Some people assume that unless you have a sizable estate, it's not necessary to hire a lawyer to create a will. But an experienced attorney can create a bullet-proof will that won't get held up in court. They can also draft Powers of Attorney for Property and Health Care. Last, they can understand your situation and explain how other planning techniques might save you time and money, such as creating a Trust.

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Creating a trust allows grantors to have more control over what their heirs can do with the money and how they receive it. This can be especially important should something happen to you, and your heirs are too young to take responsibility for the assets. A trust can have specific rules, so your heirs don't receive their inheritance all at once or they can only use them for specific reasons, such as college tuition or medical needs.

By creating a trust you can also transfer property without going through probate court or exposing your assets to public record. An estate attorney can usually create a basic will for a few hundred dollars, and will charge a little more if you need a trust. The cost you pay to create and maintain a trust will likely be far less than the fees that can pile up should assets need to go through a lengthy probate process. It also makes for a simpler and more expedited process for your survivors to handle.

2. Buy the Right Amount of Life Insurance

Life insurance is critical for anyone who has dependents and not enough assets to provide for them indefinitely. If the answer to the question what keeps you up at night is, "What will happen to my children when I'm gone?," then buying the right amount of life insurance is likely your best solution.

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Think of insurance as an expense, not as an investment. Your savings and investments should be your main tools to reaching goals, such as retirement and education. Insurance needs are simply to do one job: replace an economic loss. Fortunately, the right kind of insurance at the right amount is not that expensive. Term insurance, which lasts for only a set period, such as 15 or 20 years (until the dependents you are worried about can take care of themselves), is by far the least expensive and typically most appropriate form of protection.

So how much insurance is right for you? First, you need to calculate the economic loss you are replacing. Then aim for a death benefit large enough to replace that economic loss with earnings from investments. Let's say your salary is $75,000. At minimum, your insurance benefit should be large enough to provide $75,000 annually if it was invested in a diversified portfolio. The total benefit amount will vary based on the length of time needed until your dependents can take care of themselves and your expected investment return.

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3. Plan for Estate Taxes

Individual estates above $5.45 million are subject to estate tax. In 2012, tax law changes made "portability" of the individual estate tax exemption permanent, meaning a surviving spouse can carry over any unused portion of their deceased spouse's $5.45 million exemption. Adding the two individual exemptions together, this means that a couple's estate is not subject to estate tax as long as it is below $10.9 million.

To benefit from the full $10.9 million estate tax exemption, it is required that a surviving spouse timely file a federal estate tax return, known as "Form 706" for short. Form 706 is due on or before nine months after the deceased spouse's date of death.

Republicans have long called for a repeal of Federal estate taxes, and with their party now in control of government all eyes are on potential legislation to eliminate the estate and gift tax in 2017. The reality is that repeal is not certain, leaving the world of estate planning under a cloud of uncertainty. For now, it remains desirable to shift assets out of the estate to avoid future taxes.

The most common strategy is to utilize the annual gift exemption, currently at $14,000 for individuals and $28,000 for married couples. An annual gifting strategy, compounded over many years, can remove incredibly meaningful sums from a taxable estate. Consider gifting appreciated assets as well, allowing you to avoid capital gains tax on investments that might otherwise be sold during your lifetime.

4. Protect Your Business

Entrepreneurs have a unique set of estate planning needs that can unfortunately be catastrophic to their legacy and their business if left unaddressed. Loss of business value, litigation, material dissipation of assets, and tax-inefficiency are all risks that can be avoided with good planning. The following are a few ways you can protect your business.

Buy-Sell Agreement. The first step to creating a solid business continuity plan is drafting a buy-sell agreement. The buy-sell agreement creates an obligation for a pre-selected buyer to purchase ownership interests, based on trigger events. In effect, it provides a self-created exit-strategy. Not only can buy-sell agreements name potential buyers, it can pre-determine valuation methods to be applied at the time of purchase, avoiding potential disagreements and litigation.

Asset Protection. The most well-written estate planning documents are meaningless if a business owner has been sued and lost all their estate assets prior to death. Asset protection vehicles – S corps, LLCs, Limited Partnerships – prevent a creditor of your company to claim your personal assets. As businesses grow, it is often beneficial to create multiple asset protection entities, such as a separate entity to hold a firm's real estate and another for the operating company. In this scenario, real estate assets would be protected against a lawsuit against the operating company.

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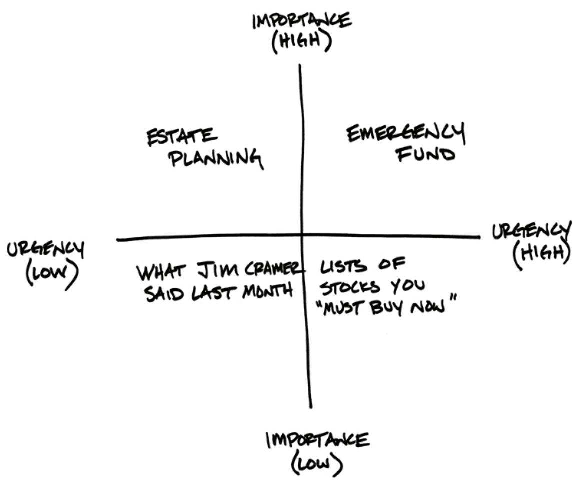
Succession Planning. Not planning for business succession can lead to ruin of wealth that an entrepreneur worked so hard to create. Successor directors and a contingency plan can be named in documents to avoid disorder. In the event of an owner's disability, a Limited Power of Attorney for Business Decisions can ensure that the best individual steps in to keep the firm running. The more general and commonly held Power of Attorney likely leaves a spouse or other individual unrelated to the business with decision-making responsibilities.

5. Talk to Your Heirs.

After you've created your estate plan, talk to your family about how they will be affected by it. Your estate plan may clearly define *which tangible assets* will be passed on to the next generation, but to develop a lasting legacy you need to start a converstion with your family members about what's really going on behind the money.



You can start simple by explaining how the will or trust works, so they don't have to hear it from an attorney first. This might be uncomfortable, but having an honest conversation now instead of worrying if everyone will get along after you're gone can provide great relief.

Estate planning isn't something only the wealthy need to do. No matter the state of your assets, planning for the future can help you make better choices and help your heirs even more.

GLOBAL MARKETS: A YEAR IN REVIEW

As we look back at 2016 and ahead to 2017 and beyond, we'll leave the political discourse and analysis to others and focus our comments on the financial markets. We noted in our year-end review letter accompanying your fourth-quarter statements, that 2016 was the year of the Surprise. We witnessed several sharp reversals in market trends and consensus views during the year. Once the dust had settled, a few calendar year highlights include:

Global stocks performed well both in absolute terms and relative to core bonds this year, with U.S. stocks again taking the lead. Large-cap stocks gained 11.9% (S&P 500 Index) and small-cap stocks surged 21.6% (iShares Russell 2000 ETF). This marked the eighth straight year the large-cap S&P 500 Index had a positive return. This ties the streak from 1982–1989, and only the period from 1991–1999 saw a longer streak, at nine years.

Emerging market stocks were also strong performers, gaining 12.2% for the year (Vanguard FTSE Emerging Markets ETF). Developed international stocks were the big laggards. They returned just 2.7% in U.S. dollar terms (Vanguard FTSE Developed Markets ETF). European stocks did worse, falling 0.4% in dollar terms (Vanguard FTSE Europe ETF). This marked the fourth straight calendar year and the sixth in the past seven that the S&P 500 beat the global ex-U.S. index. Since 2008, this is one of the longest stretches of U.S. outperformance on record.

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Core bonds produced a 2.5% gain for the year. Though core bond prices got off to a strong start with the 10 year Treasury yield dropping to an all-time low of 1.37% in early July, yields then reversed course, rising to 2.5% by year end. In the fourth quarter, the core bond index fell 3.2%—its worst quarterly performance in 35 years—due to rising interest rates. In our balanced portfolios, most of our fixed-income exposure is in actively managed funds, which managed to outperform the bond market for the year. Looking ahead to 2017, we recently added an investment in floating rate loan funds, which we believe offer a compelling yield (4%) and stability in a low-rate environment where income is difficult to find.

Over the course of the year, we also witnessed many sharp reversals in market trends and consensus views. To name a few: value and cyclical stocks beat growth names (for the first time in several years), while "bond-proxy" stock sectors (utilities, consumer staples, and REITs) underperformed. In the commodity markets, crude oil prices rebounded sharply, doubling from their February lows and reversing a dramatic two year slide. That pattern was true for commodity prices in general, with the Bloomberg Commodity Index gaining 20% from its January low (up 11% for the year). The reversal in interest rates, as noted earlier, was also significant. Just as with the U.S. presidential election and the Brexit vote results, very few "experts" predicted these reversals. The consensus was surprised and wrong at the inflection points, as it usually is.

Performance Reversals in 2016		
Since:	**Previous Two-Year Return**	**Return Since**
Emerging Markets Low in January		
Emerging-Market Stocks	-25.5%	28.2%
Oil (WTI)	-68.7%	82.4%
U.S. Market Low in February		
U.S. Small-Cap Stocks vs. U.S. Large-Cap Stocks	-18.0%	19.5%
U.S. Value Stocks vs. U.S. Growth Stocks	-7.7%	10.8%
U.S. Value Stocks vs. U.S. Momentum Stocks	-11.2%	14.1%
10-Year U.S. Treasury Yield Low in July		
U.S. Core Bonds	9.1%	-3.3%
U.S. Treasurys (7–10 Year Index)	14.8%	-7.0%
U.S. Presidential Election in November		
Consumer Staples Stocks vs. S&P 500	6.3%	-6.2%
Utilities Stocks vs. S&P 500	4.3%	-5.2%
Energy Stocks vs. S&P 500	-25.5%	4.0%
Financial Stocks vs. S&P 500	-3.4%	11.8%

Source: Morningstar. Returns through 12/31/16. Two year returns are cumulative.
Past performance does not guarantee future results.

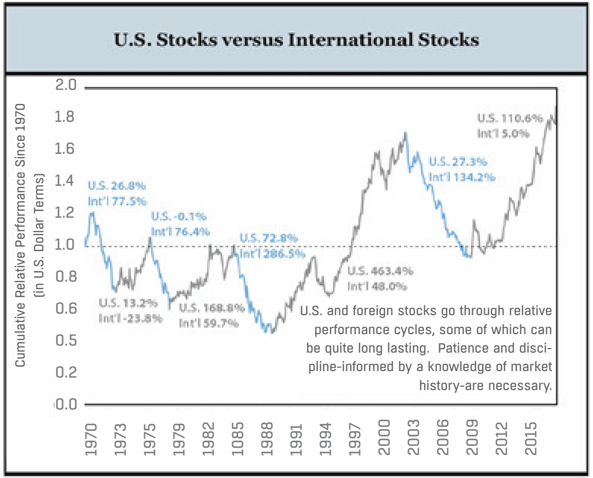
In constructing globally diversified portfolios, we know that there will be periods of time when asset classes will be temporarily out of favor. But diversification also means gaining exposure to a wider set of investment opportunities, and sticking with them when our analysis convinces us of their favorable long-term return prospects. While some areas of the markets and our portfolios delivered strong performance this year, others faltered. Since no one can predict ahead of time which market sectors will do well, or for how long, it pays to own a wide selection of investments with attractive and differing risk and return drivers.

THE CASE FOR INTERNATIONAL STOCKS

Since the end of 2009, the S&P 500 has returned a cumulative 131%. In contrast, developed international stocks have gained a cumulative 32% and emerging market stocks a measly 1.3% in dollar terms. Because of their globally diversified long-term equity allocation, asset allocation portfolios have lagged compared to a purely U.S. stock portfolio. While foreign stocks' underperformance is trying, we continue to believe, supported by our analysis, in maintaining large strategic allocations to foreign stocks particularly after this prolonged period of underperformance.

Our analysis implies that from current price levels, both European and emerging market stocks are likely to generate higher returns than U.S. stocks over a time horizon of three-to-five years. While valuations remain inexpensive overseas, there is much optimism already baked into current prices at home. This optimism accelerated post-election and makes U.S. stocks particularly vulnerable to a negative surprise.

Though there are risks to our European and emerging market equity positions, current valuations suggest these are fairly—though not fully—discounted. News flow regarding political uncertainties from rising nationalism in Europe and related economic/breakup risks facing the Eurozone, or the negative ramifications for emerging markets of China's huge public debt build-up (to name a few big ones) has contributed to their poor stock market performance in recent years. With investors discounting lots of risks and bad news, the news must only be "less bad" for sentiment and stock prices to improve. That typically happens when the market least expects it.



Source: Morningstar Direct as of 12/31/16. International stocks are represented by the MSCI World ex USA Index from 1970 to 1988 and the MSCI ACWI ex USA Index from 1988 onward.

We believe the key earnings growth and valuation assumptions that underlie our base case five-year scenarios for these markets are reasonably conservative. We do consider more bearish scenarios and outcomes in our analysis, which is why we don't have larger tactical positions to these markets. However, we believe the overall risk/reward, the combination of the likelihood of certain scenarios playing out and the magnitude of gains or losses across those scenarios, continues to support a modest investment overseas. Unless or until our analysis suggests making an allocation change, we will remain patient and confident you will be rewarded.

As Warren Buffett wonderfully and concisely put it, "A simple rule dictates my buying: Be fearful when others are greedy, and be greedy when others are fearful." Much easier said than done.

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2016 MARKET RETURNS

Foreign Markets	
U.K. (FTSE 100)	19.07%
Germany (DAX 30)	6.87
France (CAC 40)	4.86
Canada (MSCI)	-21.82
Japan (NIKKEI 225)	0.42
Hong Kong (Hang Seng)	0.39
India (Sensex)	1.95
Russia (MSCI)	48.89
China (Shanghai)	-12.91
Mexico (iPC)	6.20
Brazil (Ibovespa)	38.93
Argentina (Merval)	44.90

Commodities	
Gold	8.63%
Corn	-1.78
Cattle	-15.17
Soybeans	5.35
Silver	15.84
Wheat	-13.19
Platinum	1.11
Oil	45.03
Copper	17.35

U.S. Industry Performance	
Basic Materials	16.80%
Consumer Discretionary	5.97
Consumer Staples	4.98
Financials	22.59
Health Care	-2.76
Industrials	20.00
Energy	28.03
Technology	15.01
Telecomm	22.76
Utilities	16.07

USD vs	
Euro	2.88%
British Pound	19.44
Canadian Dollar	-3.19
Yen	2.87

Bond Yields (Change)	bps	Ending Yield
30-yr T-bond	0.05	3.06%
10-yr T-bond	0.18	2.45
3-month T-bill	0.35	0.51

U.S. Stocks	
Dow Industrials	16.50%
Nasdaq Composite	11.96
Russell 2000	21.31
Wilshire 5000	10.84

IRA CONTRIBUTIONS DEADLINE

Don't forget, 2016 contributions for IRAs and Roth IRAs must be made by April 15, 2017. Maximum contributions are $5,500 per individual ($6000 if you are age 50 or over). Income limits for contributing to Roth IRAs or making deductible contributions to Traditional IRAs are below. You can also still benefit from tax-deferred growth in a traditional IRA by making non-deductible contributions should your income exceed the limits. Remember, contributions can be made from both cash on hand or from your taxable investment accounts. Give us a call to determine if this is the right option for you.

IRA 2016 INCOME LIMITS

Filing Status	Roth IRA Can contribute if your Modified AGI is	TRADITIONAL IRA Can deduct contributions* if your Modified AGI is
Single or Head of Household	<$132,000	<$71,000
Married Filing Jointly	<$194,000	<$118,000
Spousal IRA (Those with spouse who earns no income)	N/A	<$194,000

*If you are not covered by an employer plan, you can deduct 100% of IRA contributions regardless of income.

Source: IRS.com.

QUOTES ON MONEY, WORK AND HUMOR

Money can buy happiness, but words are free. Here are a few of our favorite quotes regarding money, work and humor.

- "The expected never happens; it is the unexpected always." - John Maynard Keynes
- "I never lost a game. I was only behind when the time ran out." - Vince Lombardi
- "What if everything is an illusion and nothing exists? In that case, I definitely overpaid for my carpet." - Woody Allen
- "An eye for an eye makes the whole world blind." - Mahatma Gandhi
- "The best argument against democracy is a five-minute conversation with the average voter." - Winston Church
- "No matter how rich you become, how famous or powerful, when you die the size of your funeral will still pretty much depend on the weather." - Michael Pritchard
- "Starbucks say they are going to start putting religious quotes on cups. The very first one will say, 'Jesus! This cup is expensive!'" - Conan O'Brien
- "If I had asked people what they wanted, they would have said faster horses." - Henry Ford
- "It is not the strongest of species that survives, nor the most intelligent, but the one most responsive to change." - Charles Darwin
- "Stop worrying about the world ending today. It's already tomorrow in Australia." - Charles Schulz

"It's hard to compete in a global economy when you're not allowed to cross the street.'

"No, it's fine, I've just never seen coupons used in an acquisition."

"I retire on Friday and I haven't saved a dime! Here's your chance to become a legend!"

Any opinions expressed in this article are general in nature and cannot be guaranteed to be suitable for every individual. Individual needs and situations vary. Talk to your financial advisor to help you consider what options might be right for you.

The information provided herein represents the opinion of Windgate Wealth Management and is not intended to be a forecast of future events, a guarantee of future results, nor investment advice. The information is neither a recommendation to buy or sell a security or invest in a specific sector. Past performance is not indicative of future results.

Perritt Capital Management, Inc. is the registered investment advisor for Windgate Wealth Management accounts.

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