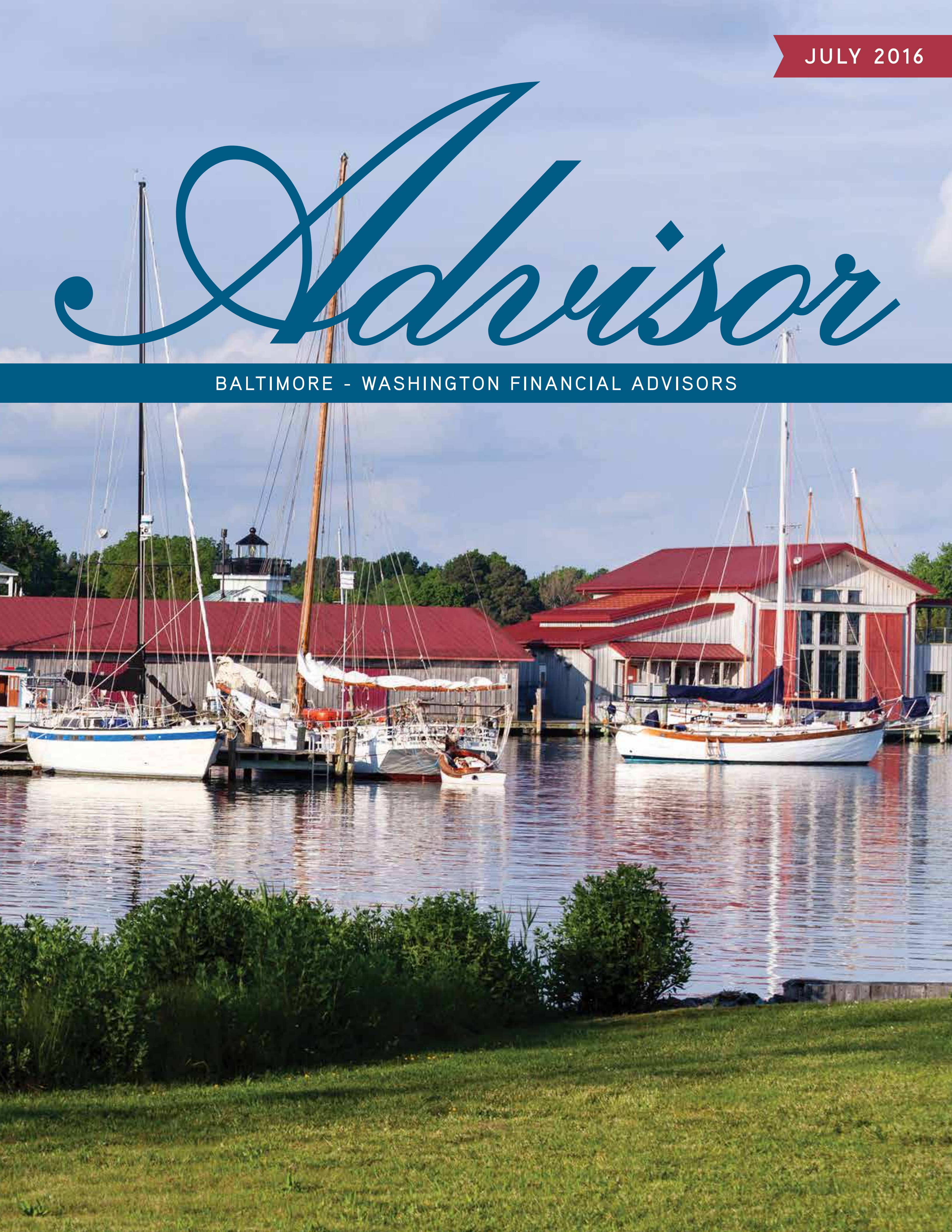
JULY 2016

Advisor

BALTIMORE - WASHINGTON FINANCIAL ADVISORS



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President's Address

NEARING RETIREMENT?

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IF YOU'RE WITHIN 10 YEARS OF RETIREMENT, YOU'VE PROBABLY SPENT SOME TIME THINKING ABOUT THIS MAJOR LIFE CHANGE. THE TRANSITION TO RETIREMENT CAN SEEM A BIT DAUNTING, EVEN OVERWHELMING. IF YOU FIND YOURSELF WONDERING WHERE TO BEGIN, THE FOLLOWING POINTS MAY HELP YOU FOCUS.

REASSESS YOUR LIVING EXPENSES

A step you will probably take several times between now and retirement — and maybe several more times thereafter — is thinking about how your living expenses could or should change. For example, while commuting and dry cleaning costs may decrease, other budget items such as travel and health care may rise. Try to estimate what your monthly expense budget will look like in the first few years after you stop working. And then continue to reassess this budget as your vision of retirement becomes reality.

CONSIDER ALL YOUR INCOME SOURCES

Next, review all your possible sources of income. Chances are you have an employer-sponsored retirement plan and maybe an IRA or two. Try to estimate how much they could provide on a monthly basis. If you are married, be sure to include your spouse's retirement accounts as well. If your employer provides a traditional pension plan, contact the plan administrator for an estimate of your monthly benefit amount.

Do you have rental income? Be sure to include that in your calculations. Is there a chance you may continue working in some capacity? Often retirees find that they are able to consult, turn a hobby into an income source, or work part-time. Such income can provide a valuable cushion that helps retirees postpone tapping their investment accounts, giving the assets more time to potentially grow.

Finally, don't forget Social Security. You can get an estimate of your retirement benefit at the Social Security Administration's website, **ssa.gov**. You can also sign up for a "my Social Security account" to view your online Social Security Statement, which contains a detailed record of your earnings and estimates of retirement, survivor, and disability benefits.

MANAGE TAXES

As you think about your income strategy, also consider ways to help minimize taxes in retirement. Would it be better to tap taxable or tax-deferred accounts first? Would part-time work result in taxable Social Security benefits? What about state and local taxes? A qualified tax professional can help you develop an appropriate strategy.

PAY OFF DEBT, POWER UP YOUR SAVINGS

Once you have an idea of what your possible expenses and income look like, it's time to bring your attention back to the here and now. Draw up a plan to pay off debt and power up your retirement savings before you retire.

- **Why pay off debt?** Entering retirement debt-free — including paying off your mortgage — will put you in a position to modify your monthly expenses in retirement if the need arises. On the other hand, entering retirement with mortgage, loan, and credit card balances will put you at the mercy of those monthly payments. You'll have less of an opportunity to scale back your spending if necessary.
- **Why power up your savings?** In these final few years before retirement, you're likely to be earning the highest salary of your career. Why not save and invest as much as you can in your employer-sponsored retirement savings plan and/or your IRAs? Aim for the maximum allowable contributions. And remember, if you're 50 or older, you can take advantage of catch-up contributions, which allow you to contribute an additional $6,000 to your employer-sponsored plan and an extra $1,000 to your IRA in 2016.

ACCOUNT FOR HEALTH CARE

Finally, health care should get special attention as you plan the transition to retirement. As you age, the portion of your budget consumed by health-related costs will likely increase. Although Medicare will cover a portion of your medical costs, you'll still have deductibles, copayments, and coinsurance. Unless you're prepared to pay for these costs out of pocket, you may want to purchase a supplemental insurance policy.

In 2015, the Employee Benefit Research Institute reported that the average 65-year-old married couple would need $213,000 in savings to have at least a 75% chance of meeting their insurance premiums and out-of-pocket health care costs in retirement. And that doesn't include the cost of long-term care, which Medicare does not cover and can vary substantially depending on where you live. For this reason, you might consider a long-term care insurance policy.

These are just some of the factors to consider as your prepare to transition into retirement. Breaking the bigger picture into smaller categories may help the process seem a little less daunting. At BWFA we can help you navigate the many retirement planning considerations. Give us a call and set up a time to see us.

Robert Carpenter

COVER PHOTO: St. Michaels Harbour on the Chesapeake Bay

Do you know someone

WHO COULD USE GUIDANCE WITH THEIR INVESTMENTS?

MAYBE YOU KNOW SOMEONE WHO IS RETIRED OR NEARING RETIREMENT AND COULD BENEFIT FROM OUR SERVICES?

WE ASK YOU, OUR EXISTING CLIENTS, TO RECOMMEND OUR SERVICES TO FRIENDS OR FAMILY MEMBERS THAT COULD BENEFIT FROM OUR SUPPORT.

BY HELPING US GROW OUR "FAMILY OF CLIENTS," WE GET TO SHARE OUR PASSION WITH MORE PEOPLE JUST LIKE YOU.

PLEASE CONTACT MEGHAN AT MMANAS@BWFA.COM

JULY 2016 TABLE OF CONTENTS

Financial Planning

ESTABLISHING A FINANCIAL SAFETY NET

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In times of crisis, you do not want to be shaking pennies out of a piggy bank. Having a financial safety net in place can ensure that you are protected when a financial emergency arises. One way to accomplish this is by setting up a cash reserve, a pool of readily available funds that can help you meet emergency or highly urgent short-term needs.

HOW MUCH IS ENOUGH?

Most financial professionals suggest that you have three to six months' worth of living expenses in your cash reserve. The actual amount, however, should be based on your particular circumstances. Do you have a mortgage? Do you have short-term and long-term disability protection? Are you paying for your child's orthodontics? Are you making car payments? Other factors you need to consider include your job security, health, and income. The bottom line: Without an emergency fund, a period of crisis (e.g., unemployment, disability) could be financially devastating.

BUILDING YOUR CASH RESERVE

If you haven't established a cash reserve, or if the one you have is inadequate, you can take several steps to eliminate the shortfall:

- **Save aggressively:** If available, use payroll deduction at work; budget your savings as part of regular household expenses
- **Reduce your discretionary spending** (e.g., eating out, movies, lottery tickets)
- **Earmark current or liquid assets** (those that are cash or are convertible to cash within a year, such as a short-term certificate of deposit)
- **Redirect earnings from other investments** (e.g.,stocks, bonds, or mutual funds)
- **Explore using other resources** (e.g., do you have a cash value insurance policy that you can borrow from?)

A final note: Your credit line can be a secondary source of funds in a time of crisis. Borrowed money, however, has to be paid back (often at high interest rates). As a result, you shouldn't consider lenders as a primary source for your cash reserve.

WHERE TO KEEP YOUR CASH RESERVE

You'll want to make sure that your cash reserve is readily available when you need it. However, an FDIC-insured, low-interest savings account isn't your only option. There are several excellent alternatives, each with unique advantages. For example, money market accounts and short-term CDs typically offer higher interest rates than savings accounts, with little (if any) increased risk.

Note: Don't confuse a money market mutual fund with a money market deposit account. An investment in a money market mutual fund is not insured or guaranteed by the FDIC. Although the mutual fund seeks to preserve the value of your investment at $1 per share, it is possible to lose money by investing in the fund.

In addition, when considering a money market mutual fund, be sure to obtain and read the fund's prospectus, which is available from the fund or your financial advisor, and outlines the fund's investment objectives, risks, fees, expenses. Carefully consider those factors before investing.

It's important to note that certain fixed-term investment vehicles (i.e., those that pledge to return your principal plus interest on a given date), such as CDs, impose a significant penalty for early withdrawals. So, if you're going to use fixed-term investments as part of your cash reserve, you'll want to be sure to ladder (stagger) their maturity dates over a short period of time (e.g., two to five months). This will ensure the availability of funds, without penalty, to meet sudden financial needs.

REVIEW YOUR CASH RESERVE PERIODICALLY

Your personal and financial circumstances change often — a new child comes along, an aging parent becomes more dependent, or a larger home brings increased expenses. Because your cash reserve is the first line of protection against financial devastation, you should review it annually to make sure that it fits your current needs.

Investment Management

THE RULE OF 72 — FINALLY, A RULE OUR KIDS WILL LOVE!

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IT ALL BEGAN IN 1988, THE YEAR OF MY 13TH BIRTHDAY, THE YEAR IN WHICH I WAS FINALLY ALLOWED TO CRACK OPEN MY FIRST EVER PIGGY BANK.

This was no ordinary piggy bank. It was the size of a small dog, and was the recipient of 13 years of contributions from not only me, but also from family, friends, and anyone else I could convince to feed him.

My 13th birthday was the first birthday that I did not care about opening a single present — I only wanted to crack open that pig! My excitement stemmed not from what I was going to be able to buy with the money, but rather, I wanted to find out what 13 years of savings looked like. In financial advisory language, I was curious about the "growth" of my money. Although, at the time, I did not fully understand that no real growth had actually taken place.

Fast forward to the fall of 1993, my freshman year of college. This is the year I was first introduced to the Rule of 72. The Rule of 72 was definitely an "aha" moment for me. This was a moment that opened my eyes to the power of compound growth and what it means to save, and save early.

The Rule of 72 is a shortcut used to estimate the number of years required to double your money at a given annual rate of return. The rule states that you divide the rate, expressed as a percentage, into 72. For example, if an individual invested $100 today and earned 6% per year, it would take approximately 12 years for the $100 to become $200 (72 ÷ 6 = 12).

THE RULE OF 72 WAS DEFINITELY AN "AHA" MOMENT FOR ME. THIS WAS A MOMENT THAT OPENED MY EYES TO THE POWER OF COMPOUND GROWTH AND WHAT IT MEANS TO SAVE, AND SAVE EARLY.

The Rule of 72 can be an extremely powerful tool for the younger members of our workforce who are just starting out. To illustrate, let us look at two individuals, Jane and Jack, who are both the same age. Jane started saving soon after her first job and accumulated $10,000 by the age of 25, and she never saved another penny the rest of her career. Jack on the other hand, started late — 10 years after Jane. But Jack invested a lump sum of $20,000 (double the amount Jane invested), and he too never saved another penny the rest of his career. Both Jane and Jack earned 8% per year on their investments, which means they doubled their money approximately every nine years. Who do you think had more money at age 65? Although Jack invested double the amount of Jane ($20,000 vs. $10,000), he ended up with $16,000 less than Jane, or approximately $201,000, while Jane's money grew to approximately $217,000. By starting early, Jane was able to invest only half of what Jack invested, and still end up with more money — doubling her money more than four times during her career.

Another important implied lesson of the Rule of 72, is that one must stay the course. The investment path to retirement is certain to have a few twists and turns along the way. However, in order to realize the full benefit of consistent, compound growth, one must remain invested through market ups and downs. A structured investment model must be developed and followed throughout one's career. For those who consistently save and remain focused on the end goal — their retirement "piggy banks" will reward them.

If you have children just beginning their careers, you may want to share the Rule of 72 with them. It is a simple and easy-to-understand calculation to help get them excited about saving for their futures. As illustrated above, initiating an investment plan early can have a significant positive impact on their retirement savings. The Rule of 72 is one rule your kids will thank you for.

FOR THOSE WHO CONSISTENTLY SAVE AND REMAIN FOCUSED ON THE END GOAL — THEIR RETIREMENT "PIGGY BANKS" WILL REWARD THEM.

Feel free to contact a BWFA professional or make an appointment to stop by our office if you would like to discuss your specific investment strategy and objectives.

Investment Management

INVESTOR, KNOW THYSELF: HOW YOUR BIASES CAN AFFECT INVESTMENT DECISIONS

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Traditional economic models are based on a simple premise: people make rational financial decisions that are designed to maximize their economic benefits. In reality, however, most humans don't make decisions based on a sterile analysis of the pros and cons. While most of us do think carefully about financial decisions, it is nearly impossible to completely disconnect from our "gut feelings," that nagging intuition that seems to have been deeply implanted in the recesses of our brain.

Over the past few decades, another school of thought has emerged that examines how human psychological factors influence economic and financial decisions.

This field — known as behavioral economics, or in the investing arena, *behavioral finance*, which BWFA has written on and delivered workshops on in the past and will continue to do into the future — has identified several biases that can unnerve even the most stoic investor. Understanding these biases may help you avoid questionable calls in the heat of the financial moment.

SOUND FAMILIAR?

Following is a brief summary of some common biases influencing even the most experienced investors. **Can you relate to any of these?**

1. **Anchoring** refers to the tendency to become attached to something, even when it may not make sense. Examples include a piece of furniture that has outlived its usefulness, a home or car that one can no longer afford, or a piece of information that is believed to be true, but is in fact, false. In investing, it can refer to the tendency to either hold an investment too long or place too much reliance on a certain piece of data or information.

2. **Loss-aversion bias** is the term used to describe the tendency to fear losses more than celebrate equivalent gains. For example, you may experience joy at the thought of finding yourself $5,000 richer, but the thought of losing $5,000 might provoke a far greater fear.

   Similar to anchoring, loss aversion could cause you to hold on to a losing investment too long, with the fear of turning a paper loss into a real loss.

3. **Endowment bias** is also similar to loss-aversion bias and anchoring in that it encourages investors to "endow" a greater value in what they currently own over other possibilities. You may presume the investments in your portfolio are of higher quality than other available alternatives, simply because you own them.

4. **Overconfidence** is simply having so much confidence in your own ability to select investments for your portfolio that you might ignore warning signals.

5. **Confirmation bias** is the tendency to latch on to, and assign more authority to, opinions that agree with your own. For example, you might give more credence to an analyst report that favors a stock you recently purchased, in spite of several other reports indicating a neutral or negative outlook.

6. **The bandwagon effect**, also known as herd behavior, happens when decisions are made simply because "everyone else is doing it."

   For an example of this, one might look no further than a fairly recent and much-hyped social media company's initial public offering (IPO). Many a discouraged investor jumped at that IPO only to sell at a significant loss a few months later. (Some of these investors may have also suffered from overconfidence bias.)

7. **Recency bias** refers to the fact that recent events can have a stronger influence on your decisions than other, more distant events. For example, if you were severely burned by the market downturn in 2008, you may have been hesitant about continuing or increasing your investments once the markets settled down. Conversely, if you were encouraged by the stock market's subsequent bull run, you may have increased the money you put into equities, hoping to take advantage of any further gains. Consider that neither of these perspectives may be entirely rational given that investment decisions should be based on your individual goals, time horizon, and risk tolerance.

8. **A negativity bias** indicates the tendency to give more importance to negative news than positive news, which can cause you to be more risk-averse than appropriate for your situation.

OUR OBJECTIVE VIEW AT BWFA CAN HELP!

The human brain has evolved over millennia into a complex decision-making tool, allowing us to retrieve past experiences and process information so quickly that we can respond almost instantaneously to perceived threats and opportunities. However, when it comes to your finances, these gut feelings may not be your strongest ally, and in fact may work against you. Before jumping to any conclusions about your finances, consider what biases may be at work beneath your conscious radar. BWFA can help identify any biases that may be clouding your judgment. Clients who entrust BWFA with day-to-day investment decisions reduce the risk that their biases will work against success, thus improving their opportunity to achieve their goals and dreams!

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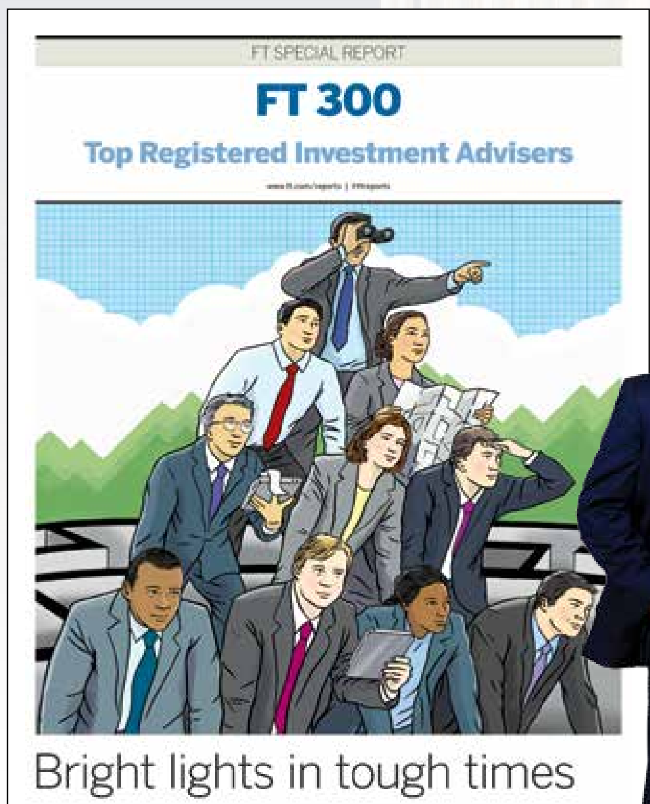
RECOGNIZED AS ONE OF THE *FINANCIAL TIMES* TOP 300 FINANCIAL ADVISERS

3rd Year in a Row!

TODAY'S INVESTMENT LANDSCAPE IS MORE COMPLEX THAN IT HAS EVER BEEN. INCREASINGLY, IT TAKES A TEAM OF DEDICATED EXPERTS TO EFFECTIVELY MANAGE YOUR MONEY, AND MORE AND MORE PEOPLE ARE REALIZING THE VALUE OF WORKING WITH A FEE-ONLY INVESTMENT ADVISOR SUCH AS BWFA.

Recently, the *Financial Times* recognized 300 top RIAs*, based on criteria including: assets under management (AUM), AUM growth rate, years in existence, compliance record, industry certifications (such as CFP® and CFA), and online accessibility.

While it's gratifying to be recognized, BWFA's main objective continues to be serving our clients with undivided loyalty. We provide impartial advice and work exceptionally hard at helping our clients achieve their goals. As always, we are dedicated to serving our clients' best interests.




FT 300 Top Registered Investment Advisers

What are the characteristics of an adviser in the Financial Times Top 300? *Loren Fox explains*

As baby boomers retire, the demand for top-quality advice accelerates

Robert Carpenter

*"RIA," as used in the **Financial Times** article, is an abbreviation for Registered Investment Adviser and is not a designation. Registration as an investment adviser does not constitute an endorsement of the firm by securities regulators nor does it indicate that the adviser has attained a particular level of skill or ability.*

FT FINANCIAL TIMES | Top Financial Advisers 2016

FT 300 Ranking June 2016

Maryland firms in the FT 300

FT 300 Top Registered Investment Advisers

Firm name	City	Retail (individuals with less than $1 million)	HNW (individuals with $1 million - $10 million)	Ultra HNW (individuals with $10 million+)	Institutional
		Client Segments Served			
MARYLAND					
Baltimore Washington Financial Advisors	Columbia	✓	✓	✓	✓
FBB Capital Partners	Bethesda	✓	✓	✓	✓
Greenspring Wealth Management	Towson	✓	✓	✓	✓
Heritage Investors Management	Bethesda	✓	✓	✓	✓
Wagner Bowman Management Corp	Baltimore	✓	✓	✓	✓
WMS Partners, LLC	Towson		✓	✓	

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NOTE: Above results are listed in alphabetical order and do not represent numerical ranking.

FT 300 Disclosure: The 2016 Financial Times Top 300 Registered Investment Advisors is an independent listing produced by the Financial Times (June, 2016). The FT 300 is based on data gathered from RIA firms, regulatory disclosures, and the FT's research. As identified by the FT, the listing reflected each practice's performance in six primary areas, including assets under management, asset growth, compliance record, years in existence, credentials and accessibility. Neither the RIA firms nor their employees pay a fee to The Financial Times in exchange for inclusion in the FT 300. Third-party rankings from Financial Times and other publications are no guarantee of future investment success. Working with a highly ranked adviser does not ensure that a client or prospective client will experience a higher level of performance results. These rankings should not be construed as an endorsement of the adviser by any client.

Investment Research

GROWTH AND VALUE: INVESTMENTS THAT MAY APPEAL TO MILLENNIALS

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Whether an investor calls himself a value or a growth investor, both the business' growth potential and its valuation are always relevant. When seeking appropriate investments for client portfolios, the valuation of the applicable security is always assessed. However, the company's potential for growth factors into the determination of an investment's underlying value. Investment legend Warren Buffett is best known of as a value investor; however, he does not dismiss the importance of growth in the investment equation. **In fact, Buffett has said the following:**

> *Most analysts feel they must choose between two approaches customarily thought to be in opposition: "**value**" and "**growth**." Indeed, many investment professionals see any mixing of the two terms as a form of intellectual cross-dressing.*
>
> *We view that as fuzzy thinking (in which, it must be confessed, I myself engaged some years ago). In our opinion, **the two approaches are joined at the hip**: Growth is **always** a component in the calculation of value, constituting a variable whose importance can range from negligible to enormous and whose impact can be negative as well as positive.*

INVESTING FOR INCOME

Because retiree portfolios, in particular, need to generate current income, some of the companies held in client portfolios are expected to deliver modest growth and pay a generous dividend.

We typically classify such businesses as Growth & Income (G&I) holdings within client portfolios. Johnson & Johnson and PepsiCo fall into this category[1]. These companies are growing, albeit at a slow pace. They are most likely mature companies. Of course, for companies like J&J and Pepsi, the maturity phase can last for a considerable period. Our goal is also to avoid those that are on a decline that is unlikely to reverse (typically referred to as "value traps.")

INVESTING FOR GROWTH

However, average lifespans are increasing, which means that a retiree's assets need to last longer than they used to. This increases the need for investors to generate more than just income from their portfolios. Growth, too, is needed to help ensure they do not outlive their assets. In addition, investors who are still funding their retirements are less interested in meeting current income needs and more concerned with the appreciation of their capital so they may be better prepared for retirement. These factors make it more important to find companies we believe can deliver above-average growth. One good source of such companies is those that look to be well-positioned to benefit from key demographic trends. Millennials make up the largest generation in U.S. history, so companies are paying considerable attention as they enter their peak spending years. It is reasonable to believe that over the next two decades, stocks will likely rise and fall based largely on the spending power of the millennial generation. It is important to consider that spending power while investing in the stock market.

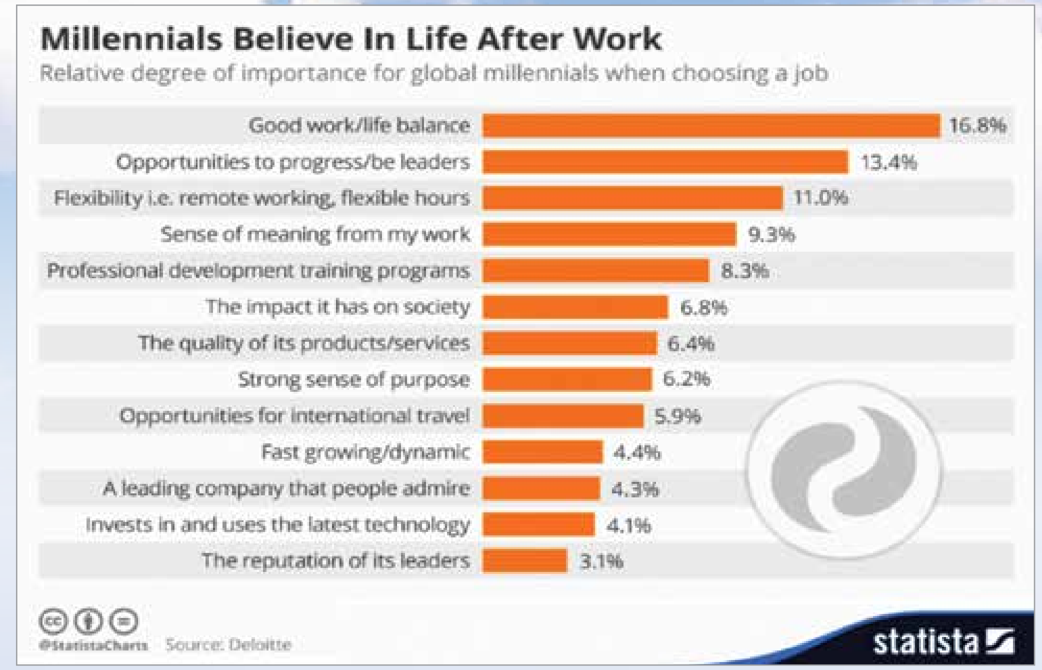
THE IMPACT OF MILLENNIALS

In many ways, millennials are different than the generations that came before them. They favor experiences over things. (Earlier this year we initiated positions in Priceline and Walt Disney to try to take advantage of this trend.[2]) They are less interested in living in large homes. They believe strongly in having a good work/life balance. When compared to previous generations, millennials are believed to try to direct their consumption trends to companies in whose missions they believe. This heightens the importance of corporate culture. Corporate culture is important when these individuals are looking for jobs. They are also relevant when looking at potential investments.

INVESTMENT EXAMPLES

Google (now called Alphabet)[3] is a company whose culture is highly regarded. It is known to treat its employees extraordinarily well and its management team is very focused on the long term. Google also has a strong global brand that commands significant customer loyalty. The company has also been building machine learning tools for years; those investments are playing an increasingly important role in Google's business. In 2014, Google acquired DeepMind, a leading start-up in what is known as "deep learning." While much of what DeepMind does is still a mystery, readers may be aware of Google's most significant public breakthrough in the field of artificial intelligence (AI). Earlier this year, DeepMind's AlphaGo program defeated the world's best Go player, Lee Sedol. Go is a challenging board game; so beating the world's best player is not an easy task, making this an important step forward for AI.

There is more to the Google's AI story. AI now drives Google's core internet search business. Each and every time someone searches using Google, the platform learns and gets smarter for all subsequent searches. Over time, we should be able to tell that Google is doing a better job of pulling information based not on the words we type but rather the true intention behind those words. Over time, AI is expected to play an even larger role in other Google features.



For example, during its first quarter 2016 earnings conference call, Google's CEO Sundar Pichai said, "In the long run, I think we will evolve in computing from a mobile first to an AI first world." Google is also at the forefront of driverless car technology, which could potentially have a positive societal impact.

Mobile payment company PayPal[4] is another company that could benefit from preferences of the millennial generation. PayPal was spun off from eBay in 2015.

The company's technology platform enables digital and mobile payments on behalf of consumers and merchants. Millennials are not as willing to go to their local bank branches as were previous generations. Using PayPal can help reduce the number of times consumers go to the bank. The company also has an app called Venmo. Venmo allows individuals to send money instantly from their phones. They can even sign up through Facebook. One of the favorite uses of Venmo happens when a group of friends goes out to dinner and splits the check. One person can pay the bill and then have her friends transfer their share to her bank account using Venmo before they leave the restaurant.

CONCLUSION

Ideally, a well-diversified portfolio will have a mix of stocks operating in different industries with different growth prospects. Some will be expected to provide a stream of income via dividends. Others will be expected to add more growth and share price appreciation. Our goal is to construct portfolios holding companies that provide a mixture of capital appreciation and current income with the potential to deliver solid, long-term growth. Whether the primary purpose of holding a stock is to add current income or to provide capital appreciation, valuation is always a consideration.

[1] Shares of Johnson & Johnson (JNJ) and PepsiCo (PEP) are currently on BWFA's "Buy/Hold" list and may be held in client portfolios.

[2] Shares of Walt Disney (DIS) and Priceline (PCLN) are currently on BWFA's "Buy/Hold" list and may be held in client portfolios.

[3] Shares of Alphabet (GOOGL) are currently on BWFA's "Buy/Hold" list and may be held in client portfolios.

[4] Shares of PayPal (PYPL) are currently on BWFA's "Buy/Hold" list and may be held in client portfolios.

Tax Services

ESTATE, GIFT, AND GST TAXATION AND TRUSTS

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HOW ARE TRUSTS TREATED FOR FEDERAL ESTATE, GIFT, AND GST TAX PURPOSES?

A trust is created when you (the grantor) transfer property to a trustee for the benefit of a third person (the beneficiary). The act of transferring property to a trust is generally treated no differently than if it were transferred to an individual outright. That is, transfers of property (whether into a trust or otherwise) may be subject to excise taxes known as transfer taxes. There are three types of transfer taxes: (1) estate tax, (2) gift tax, and (3) generation-skipping transfer (GST) tax. Estate tax may be imposed on transfers of property made after death (these are called bequests). Gift tax may be imposed on transfers of property made during life (these are called gifts). GST tax is imposed on transfers of property (either bequests or gifts) made to "skip persons." A "skip person" is someone who is more than one generation younger than you (e.g., a grandchild or great-nephew).

ESTATE TAXATION OF TRUSTS

Trust property may be included in your gross estate for estate tax purposes if you have retained certain rights in the trust or if the trust is created at your death. The estate representative (executor) is responsible for filing an estate tax return on Federal Form 706 within nine months of your death (or at a later time if an extension is granted) and paying any estate tax owed from the estate proceeds.

GRANTOR RETAINED INTEREST

In general, a trust may be includable in your gross estate if you (the grantor) have retained an interest in the trust at the time of death--or given such interest away within three years of death.

Such interests include:

- **Life estate:** A life estate is the right for life to (1) receive trust income, (2) use trust property, or (3) specify who gets to enjoy the trust income or use of trust property. If any of these rights are retained, the entire value of the property is includable in your gross estate.
- **Reversionary interest:** A reversionary interest means that the trust property will revert to you (the grantor) if the beneficiary does not survive you. A reversionary interest is includable in your gross estate if, immediately before your death, the value of the interest exceeds 5 percent of the value of the trust.
- **Rights of revocation:** The right to revoke, amend, or alter the trust brings the trust back into your estate for estate tax purposes.
- **"Incidents of ownership" in life insurance:** The value of life insurance proceeds is includable in your gross estate if, either at the time of your death or within the three years prior to your death, the proceeds were payable to your estate, either directly or indirectly, or you owned the policy, or you possessed any right to benefit economically.
- **Annuity interests:** If you (the grantor) retain an interest in annuities in the trust, part or all of the trust may be includable in your gross estate.

GENERAL POWER OF APPOINTMENT

A power of appointment is the right to say who gets the trust property. The person holding the power is called the powerholder. The powerholder can be the grantor (creator of the trust) or anyone the grantor names. A general power of appointment is one that is exercisable in the powerholder's favor directly or in favor of the powerholder's creditors, estate, or estate's creditors. In other words, there are no restrictions on the powerholder's choice of appointees (i.e., beneficiaries), and the powerholder can use the trust for his or her own benefit.

A general power of appointment held by the powerholder on the date of his death is subject to estate taxes. Because the general powerholder has the right to declare himself or herself as the owner of the property, the IRS deems that he or she is, in fact, the owner of that property. That means that the entire value of the property over which the power is held is includable in the powerholder's gross estate for federal estate tax purposes.

TRUSTS CREATED AT DEATH

A trust that is created upon your death (i.e., a testamentary trust) is generally includable in your gross estate for estate tax purposes.

GIFT TAXATION OF TRUSTS

A gratuitous transfer of property to a trust during life may be a taxable gift, just as if you had given the property outright. However, with respect to a trust, the taxable event may occur either at the time the property is transferred or at some later time. You (the grantor) are responsible for filing Federal Form 709 and paying any gift taxes owed. The taxes are due on April 15 of the year following the year in which the transfer is made.

TAXABLE GIFT OCCURS IMMEDIATELY UPON TRANSFER

Transfers made into an irrevocable trust in which the grantor (the creator) is not a beneficiary or retains no interest are taxable upon transfer.

TAXABLE GIFT OCCURS UPON DISTRIBUTIONS TO BENEFICIARY

A transfer made to a revocable trust, a trust in which the grantor is a beneficiary, or a trust in which the grantor has retained an interest is not a taxable gift at the time the transfer is made.

TAXABLE GIFT OCCURS UPON POWERHOLDER'S EXERCISE, RELEASE, OR LAPSE OF THE POWER

A taxable gift may occur if a powerholder (either the holder of a power of appointment or the holder of Crummey withdrawal powers) exercises or releases the power or allows the power to lapse. These are considered gifts made by the powerholder to the beneficiary. These gifts are not being made by the grantor but by the powerholder and are thus taxable to the powerholder.

GST TAX TAXATION OF TRUSTS

Generation-skipping transfer (GST) tax may be imposed if the beneficiaries of the trust are skip persons (i.e., persons who are two or more generations below you). The GST tax is imposed in addition to gift and estate tax. GST tax transfers are taxed at the maximum gift and estate tax rate in effect at the time the transfer is made. Whether a transfer to a trust is subject to GST tax depends upon who the transferor is and how the transfer is classified (i.e., a direct skip, taxable termination, or taxable distribution). GST tax is reported on Federal Form 706 if the transfer is a lifetime gift or Federal Form 709 if the transfer is a bequest.

TAXABLE TERMINATION

A taxable termination is a termination of an interest in a trust, which results in the skip person(s) holding all the interests in the trust. Termination can result from death, lapse time, release of a power, or otherwise. A taxable termination is taxable at the time the termination occurs. But, there is no taxable termination if gift and estate tax is imposed on the nonskip person.

The taxable amount of a taxable termination is the net value of all property that goes to the skip person. As opposed to the direct skip, a taxable termination is tax inclusive. That means that the skip person receives the property after tax.

TAXABLE DISTRIBUTIONS

A taxable distribution is any distribution (other than a direct skip or a taxable termination) of income or principal from a trust to a skip person (or from a trust to another trust if all interests in the second trust are held by skip persons) that is not otherwise subject to gift and estate tax. Generally, gift and estate tax is owed when the trust is funded, not when the funds are distributed. The taxable event occurs when the distribution is made. The amount subject to the GST tax is the net value of the property received by the distributee (the recipient) less anything the distributee paid for the property. Like a taxable termination, a taxable distribution is tax inclusive. The distributee is obligated to pay the tax. If the trust pays the tax, the payment will be treated as an additional taxable distribution.

There is an exemption of $5,450,000 in 2016 and there are exclusions and deductions available that may help to reduce your gross estate as well as reduce any taxable transfers or taxable gifts.

If you have tax questions, BWFA's professionals are here to help.

Business Services

SELLING YOUR BUSINESS TO ANOTHER CORPORATION

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Once you have decided to sell your business, one of your most important jobs will be finding a buyer and getting the best possible deal. A merger & acquisition advisor can help you evaluate different kinds of potential buyers and target those who would most likely have some interest in purchasing your business. One option you might want to consider is selling your business to another corporation. Any corporation interested in buying your business — whether it be a large, publicly owned corporation or a small private firm — will have its own strategic reasons for wanting to do so. For example, the purchasing corporation might want to expand its market, eliminate competition, or acquire your business's assets and real estate location.

Selling to another corporation involves exchanging your business's assets or corporate stock for either cash or stock (or both) in the acquiring corporation. Tax consequences and other issues will depend largely on the form of payment you receive. Working with your mergers & acquisitions advisor along with a tax advisor and/or attorney can help you structure the sale so as to maximize your profit.

Mergers and acquisitions (M&A): A merger is the process of joining the assets and liabilities of your company with those of another company. This can result in the formation of an entirely new corporation (sometimes called a consolidation) or the absorption of one company into the other (merger).

An acquisition occurs when another company purchases your company and runs it as a subsidiary under a larger corporate umbrella. Choosing one of these options may result in an all-cash buyout and it could also involve some kind of stock swap. Although structuring M&As can be complicated and time consuming, they offer certain tax benefits and may allow you to retain an ownership position if you do not want to completely sever all ties with your business.

STRENGTHS

Selling to a corporation can be more profitable: Corporations, particularly large ones, tend to have more disposable capital than private parties. They also tend to take a more strategic, long-term approach. They look beyond immediate profits and focus on potential future gains that can be realized through the acquisition of other companies. For these two reasons, a corporation could be willing to pay a higher price for a viable business than would a private party with limited capital and a more short-term approach.

You may be able to retain some control: If you structure the sale of your business as an M&A transaction, you may be able to balance your desire to sell with your desire to retain some control. If you do not want to cash out entirely and pursue something else, an M&A transaction may give you expansion capital for your business while at the same time allowing you to retain an ownership position.

TRADEOFFS

It can be difficult to find a corporate buyer: Corporations have strategic reasons for everything they do. In general, most corporations only consider buying companies that have solid track records, strong market positions, and promising growth potential. Thus, you may have difficulty finding a corporation that wants to buy your business, especially if your business has been less than a star performer in its industry. A mergers & acquisitions advisor can confidentially market your business to multiple corporations to ensure that you obtain the best offer available in the market.

There can be disadvantages to receiving stock as payment: In some cases, selling to a corporation will require you to accept the corporation's stock as partial or full payment for your business. Receiving stock can prove to be a boon on the one hand if the value of the stock rises over the long term. However, there are risks involved in owning another corporation's stock, whether that corporation is public or privately held.

How to do it: Hire a mergers & acquisitions advisor to assist you with planning the sale. Take the necessary steps to prepare your business for sale. Determine the value of your business, perhaps through a professional appraisal. Have a personal financial plan completed to ensure that the sale will fit into your overall personal financial objectives. Confidentially find a corporation interested in purchasing your business. Negotiate a sale price as well as form(s) of payment. Once you have reached an agreement, have a qualified attorney with mergers & acquisitions experience draw up the documentation outlining the terms.

Please contact the mergers & acquisitions team at BWFA and set up a free initial consultation to discuss the various options available to you when selling your privately held business.

Community Spotlight

MANNEQART 2016 SCULPTURAL ART COMPETITION

ManneqART Sculpture on the Human Form

BRINGING WORLD CLASS ARTWORKS TO HOWARD COUNTY

THE 4TH ANNUAL MANNEQART SCULPTURAL ARTWORKS COMPETITION NOW UNDERWAY IN HOWARD COUNTY, HAS ONCE AGAIN ATTRACTED AMAZING "SCULPTURE ON THE HUMAN FORM" FROM AROUND THE U.S.

This year's competition features new artworks from 20+ states, including pieces created for New Zealand's world famous World of Wearable Art Competition by U.S. artists from Washington state and Alaska.

Artworks are made of non-traditional materials such as wood, metal, glass, recycled plastic and fibers of all kinds. Awards totaling $10,000 are again being offered for the best theme creations, best hair and makeup, and best artworks from middle and high school, and college-level artists. This year's themes are Flora, Fauna, Action and Androids.

ManneqART is an arts and education non-profit based in Howard County. It is the brainchild of wearable art designer/manufacturer Lee Andersen, a resident of Laurel, Maryland. "The community's response has been wildly enthusiastic," Andersen reported. "In 2015, ManneqART artworks were also shown at the Renwick Gallery in Washington and in the 2015 Hair Ball Parade at the Visionary Arts Museum in Baltimore." ManneqART's vision is to be a catalyst for inspiring people to create "Sculpture on the Human Form."

Through a variety of events planned for 2016, ManneqART seeks to showcase the best in imaginative sculpture, hair, and special effects makeup — Sculpture on the Human Form. Besides skills workshops, collaboration with students, and appearances at events around the region, ManneqART sponsors three annual events. This year, June 26 was the date of ManneqART Madness — Sculpture, Hair, and Makeup Event at Historic Savage Mill, where all the new artworks were introduced to the public and professionally photographed for the 2017 ManneqART Calendar.

From September 10-25, ManneqART will have its annual public exhibition of all 2016 artworks at multiple sites around Howard County, including The Mall in Columbia. **On October 30, ManneqART will host the ManneqART Masquerade and Annual Awards** Gala at Ten Oaks Ballroom in Clarksville. Tickets are available at the ManneqART website.

Longer term plans for ManneqART include establishing a ManneqART Gallery in or near Howard County, where visitors can see a collection of sculptural artworks from all of the competitions. Since 2013, ManneqART has attracted more than 200 artworks from 100+ artists around the U.S. Another goal is to become a "hub" for sculptural art in the U.S. so that artists have a stage to show their artworks beyond their local art guilds.

Businesses, individuals, and organizations are encouraged to support ManneqART by becoming artwork and event sponsors or by providing donations — cash or in-kind. Volunteers of all kinds are needed.

More information is available at the ManneqART website: **manneqart.org** or email your inquiry to **Manneqart@gmail.com.**

What's Happening at BWFA

BWFA PORTFOLIO STATEMENTS — A NEW LOOK

MEGHAN MANAS
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After much careful consideration and deliberation, we have revamped the client portfolio statements that clients receive in BWFA quarterly mailings. Based on feedback and suggestions from clients and members of BWFA's Client Advisory Board, we have endeavored to incorporate more charts and graphs to better illustrate adherence to the client's chosen investment model. In the updated statements, you will find the same data and information you are accustomed to receiving, but it has been inserted into a new and improved layout.

We welcome your feedback on the updated statements. Please do not hesitate to be in touch if you have any questions or suggestions.

ADMINISTRATIVE PROFESSIONALS' DAY DID NOT GO UNNOTICED AT BWFA! We treated our Client Services Team to car detailing by On the Spot Mobile Car Detailing!

TAKE YOUR CHILD TO WORK DAY AT BWFA! We were pleased to welcome future BWFA Advisors Estella Kelly, Tyler Hornor, Joe Caputo, Jr., and Miriam Manas on April 28, 2016. They went right to work helping out on multiple projects around the office. We look forward to having them back next year!

Congratulations

BWFA FAMILY NEWS!

BWFA's Chief Information Officer, Joe Caputo and his wife Liz, welcomed **JACK** on June 14, 2016.

CONGRATS TO THE NEW FAMILY.

Upcoming Events

JULY 7, 2016 6:00 P.M. – 7:30 P.M.
Savvy Social Security Planning: Maximizing Your Benefits

JULY 12, 2016 11:45 A.M. – 1:00 P.M.
What You Need To Know About Retirement Before You Retire

JULY 26, 2016 11:45 A.M. – 1:00 P.M.
Have You Updated Your Estate Plan Lately? Guest Speaker Raj Goel from Offit Kurman

AUGUST 4, 2016 11:45 A.M. – 1:00 P.M.
Selecting Your State of Residence in Retirement

AUGUST 9, 2016 11:45 A.M. – 1:00 P.M.
Book Review: The 5 Years Before You Retire

AUGUST 25, 2016 11:45 A.M. – 1:00 P.M.
What is Your Retirement Number?

AUGUST 31, 2016 11:45 A.M. – 1:00 P.M.
Choosing a Retirement Plan • Guest Speakers CBC Retirement Partners

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