2025 will mark the third consecutive strong year for the financial markets with strong returns across US, International, and Fixed Income markets. We continue to hear concerns particularly about Artificial Intelligence (AI) and government sectors. AI stocks continue to perform well and investment in these sectors is continuing. Technology is becoming more accessible for the masses and time will tell whether they will be able to create the profitability the market is currently anticipating. Government concerns throughout the year relate to the tariff-driven market decline in April and the government shutdown earlier this quarter. As Legacy usually recommends, we stayed the course through all these tumultuous times in 2025, and portfolios benefitted. As capital gain distributions and dividends pay out in the fourth quarter, most of that cash goes back into the fixed income (bond) side of the portfolio to try and keep them close to the risk tolerance chosen between clients and relationship managers. That will help us prepare for the inevitable next market decline whether it comes in 2026, 2030, or somewhere in between. On the heels of three straight very strong market years, one subject that has continued to arise with clients, in articles, and in our recent client survey is how to best engage in conversations about generational wealth transfer. The growing interest in this topic has many layers and we will attempt to address its importance in the rest of this commentary.

What is generational wealth transfer?

At Legacy, when we discuss generational wealth transfer not only are we referring to the trillions of dollars that are being passed down from those of the Baby Boomer generation to their families, but also and more importantly, we are talking about how this wealth is being transferred. Taking the time to review exactly how much and what types of accounts are in place today and how best to fulfill the desires of the grantor while working to minimize taxes and protect assets from creditors and divorce is critical. Historically, people think of this conversation as downward (grandparents to parents to children); however, recently, we've seen this conversation take a multitude of forms with people living longer and parents/children far more likely to help take care of and help grandparents/parents. Additionally, this topic is often considered in the context of estate tax planning, but with the estate tax exclusion currently near $14 million per person, it is far more likely that the driving factor will be income tax planning, which can benefit people of all asset levels.

Why is generational wealth transfer becoming more discussed?

Baby Boomers are entering retirement as the wealthiest and most populous generation in history. Baby Boomers are estimated to number between 60-70 million people with approximately $100 trillion in assets. Successfully transferring those assets in a way that minimizes the potential tax burden on the families throughout generations can save thousands if not millions of dollars over the long term.

What are the financial planning implications?

Understanding the financial situation of all parties can help us provide the most impactful advice, which differs from family to family. In some cases, like in Family 1 below, the tax savings can be substantial by thinking through generational taxes without changing any type of financial access or timing of the wealth transfer. Family 2 shows a very similar situation that can have a smaller tax impact but still creates savings even when the planning advice is contrary to that offered to Family 1.

When it comes to when and how to plan for wealth transfers there are a lot of variables to consider, most notably, family size, account types, tax brackets, income, and state of residence.

Family 1:

- Bill and Betsy Goodman
- Married
- TN Residents
- $100,000 annual income (pension, social security, IRA withdrawal)
- 22% federal tax rate (married filing jointly)
- 0% state tax rate
- $1 million IRA invested (largely maintaining current value with growth offset by withdrawals)

- Bonnie Goodman
- Single
- NY Resident
- $500,000 annual income
- 35% federal tax rate (single)
- 6.85% state tax rate

Under current law, if Bonnie inherits the $1,000,000 IRA, she has 10 years to take it out. If she takes $100,000/year for 10 years she would pay 41.85% tax and pay $41,850 per year on that withdrawal or $418,500 over 10 years.

If Bill and Betsy convert the IRA to a Roth IRA, they add $100,000 to their income each year and pay 22% tax owing $22,000 per year on that withdrawal or $220,000 over 10 years.

Bonnie then inherits the Roth IRA tax free. This keeps Bill and Betsy's income under $200,000 so it does not impact their Medicare bracket.

The family saves nearly $200,000 on taxes by having a clear understanding of what might pass and the specific tax structures of both family units.

Family 2:

- John Lennon
- Single
- NY Resident
- $100,000 annual income (pension, social security, IRA withdrawal)
- 24% federal tax rate (single)
- 6% state tax rate
- $1 million IRA invested (largely maintaining current value with growth offset by withdrawals)

- Jacob and Joanne Lennon
- Married
- TN Resident
- $135,000 annual income
- 22% federal tax rate (married filing jointly)
- 0% state tax rate

Same situation here but different incomes and tax rules for the children. Here the advice would be to leave the dollars in the IRA because if John takes it out, he would be paying ~2% higher federal income tax, 6% higher state tax, and would also go up a Medicare bracket.

Jacob and Joanne can pull the funds out when they inherit them at the 22% bracket and might climb into the 24% bracket. That means they would save 2% on some of the funds, and the 6% state level tax on all the funds.

Here the family saves up to 8% ($80,000) in taxes plus keeps lower Medicare premiums by having John keep the funds in the IRA and having the children inherit the IRA where they will withdraw the funds for 10 years.

How do I have these conversations?

Starting the conversation is often the hardest part and there are many reasons for this. A recent Fidelity study found that 97% of families recognize the importance of having conversations about estate planning but nearly one-half have yet to engage in these conversations. They then go on to talk about how to shift the conversation from a "Yes….But" to "Yes….And" dialogue. A few of their examples from the article are:

- Yes, wealth can disincentivize kids…AND talking about wealth can help them make sense of their experiences, now and in the future
- Yes, fairness is a hard topic in families…AND not talking about it is a missed opportunity to learn about each other's perspective and make informed decisions.
- Yes, you don't want to be a burden on your kids with your later-in-life planning…AND you won't know what they consider a burden unless you ask them.
- Yes, in-laws can add a level of complexity…AND they are part of your family system and an important influence on your children.
- Yes, you need to align as a couple…AND you don't have to have everything buttoned up before having incremental conversations with your kids.

At Legacy, we're here to help. When we work across generations, we are often able to do some of our best and most impactful financial planning. Sometimes by understanding the family dynamics we can help plan and eliminate the need for such conversations. At other times, our recommendations can help facilitate family conversations. As with all families, sometimes these conversations go well and sometimes they can be hard and uncomfortable. By having them, we can help everyone get on the same page and create a better financial plan.

If you haven't thought much about generational planning either for your children or for your parents, talk to your relationship manager. There may be a need for further discussion or a new/updated financial plan.