Investor's**Edge**

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Cash an important element for financial strategies

While cash isn't often the first term investors think about when developing a well-balanced wealth plan, cash has an important role to play. That's why you may want to consider how liquidity can strengthen your portfolio.

Indeed, liquidity management may play a fundamental role in the relationship you have with your financial professional, because it helps provide flexibility within a well-balanced financial strategy. Liquidity includes everyday living and lifestyle cash needs, strategic borrowing and generating an income during retirement.

In addition, conversations about your cash needs with your financial professional may help him or her better understand your short- and long-term goals.

Cash for major lifestyle expenses

Next to purchasing a home and paying for college for children and/or grandchildren, health care and long-term care costs in retirement may be the largest expenses most investors need to prepare for in life. Increasingly, financial professionals are recommending clients consider retirement health care insurance options, including Health Savings Accounts and prescription drug plans, and long-term care insurance. It's important to have liquidity available in times of medical needs.

Lastly, liquidity management includes working to generate additional income during retirement. Retirees typically live 30+ years post-retirement; thus, continued investing to generate income is vital. Financial professionals work with other professionals, like tax and legal advisors, to structure retirement income portfolios for tax efficiency during the pre-retirement years and to liquidate assets in a tax-efficient way during retirement.

Operating cash, core cash and strategic cash

Operating cash is the necessary cash you need to support your lifestyle. This includes managing everyday expenses—car loans, mortgage or rent, insurance premiums, utility bills, etc. Operating cash generally resides in your checking account to satisfy these short-term needs. The expectation for this cash is immediate use, and often the account holding this cash is a non-interest bearing checking account.

Core cash is available for you to access and easily convert to operating cash.

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Pivotal Wealth Management is an independent advisory firm that delivers customized planning solutions for its clientele along with an exceptional engagement experience.

Cash an important element for financial strategies, continued

Core cash includes savings and escrow cash held to pay for taxes or insurance. Some instruments include savings accounts or money market funds. Core cash may be held in certain financial instruments that produce slightly higher yields or may include short duration instruments such as short-term CDs (1-, 3-, 6-month terms) or certain treasury products (T-bills, treasury bond funds, etc.). Traditionally, the goal for this cash is principal return plus a slight rate of interest or yield with a six- to 12-month time horizon for its use. A good example of core cash is saving for a trip, a wedding or a home purchase.

Strategic cash is surplus cash and intended for longer-term investment opportunities. The time horizon for this cash is generally one year or greater. This cash can sustain moderate volatility, and you have a wide variety of choices to enhance the yield performance on it. These include short-term bond funds as well as certain mutual funds or ETFs, with a focus on controlling risk and maintaining a focus on principle preservation.

How does liquidity help?

Liquidity management helps when consulting on home mortgages and refinancing loans, small business expansion or equipment purchases, or selecting credit cards, car loans, and even considering securities-based lending. This kind of borrowing optimizes investment opportunities while offering liquidity when needed. Many high-net-worth and ultra-high-net-worth clients make prudent use of credit strategies to gain short-term funding to purchase a second home, expand their business, purchase equipment or fund other wealth management goals until other financing options are secured.

An RBC Credit Access Line may be an appropriate tool when you need short-term portfolio liquidity, like covering a larger-than expected tax bill or seizing a timely real estate investment opportunity. Financial professionals also recognize the importance of helping investors borrow against eligible securities in their portfolio to diversify their portfolios or invest in additional stocks or bonds. In this case, a margin loan available through RBC Express credit may offer a way to finance the purchase of securities.

What is a good cash balance to maintain?

Inflation and taxes are known challenges for cash because both reduce the purchasing power of money over time. Working with your financial professional to develop a strategic wealth plan can assist with minimizing inflation and tax risks. You may also want to ask your financial professional to recommend tools to help you to track cash needs to support your lifestyle. This includes designating appropriate cash allocations into appropriate market instruments to generate additional yield to minimize the inflation effect.

Incorporate a cash plan into your wealth plan

Ask your financial professional how liquidity could strengthen your wealth plan to better meet your goals.

RBC Credit Access Line is a securities-based, demand line of credit offered by Royal Bank of Canada, an Equal Opportunity Lender and a bank affiliate of RBC Capital Markets, LLC. Subject to Credit Approval. Securities-based loans involve special risks, are subject to minimum collateral requirements, and are not suitable for everyone. Additional restrictions may apply. You should review the provisions of the RBC Credit Access Line agreement and related disclosures, and consult with your own independent tax and legal advisors about any questions you have prior to using RBC Credit Access Line.

Planning for dementia and health care

There are many unknowns when it comes to planning for health care. Unfortunately, one of the possible health care concerns—dementia—comes with a high financial price, making it important for families to include in their health care planning.

Today, more than five million Americans are living with Alzheimer's, according to the Alzheimer's Association. That number is anticipated to double by 2040 because of the large cohort of aging baby boomers. Age is a primary risk factor for dementia.

From the outset, a dementia diagnosis necessitates services and care that bring about a mountain of expenses. Early on, families tend to step in as caregivers and coordinators, helping with everything from routine activities, like shopping and medical appointments, to daily tasks, like bathing and dressing. This can add to the financial burden in the form of lost wages, career disruptions and out-of-pocket expenses.

Following a dementia diagnosis, people generally live an average of 4.5 years. As the disease advances, the patient needs more care than most family members can handle, eventually requiring professional home and transition care and generally culminating in the need for a residential skilled memory care facility. In fact, most people with dementia spend 40% of their time after diagnosis in such a facility. This kind of care is expensive, and in 2019, was $90,155 a year, according to Genworth's Cost of Care Survey.

Covering expenses

Most of the nonmedical care costs associated with dementia are not covered by Medicare or traditional health insurance. Even for those with supplemental long-term care insurance, these care costs can be significant. For many, they can be so great that they lead to significant financial hardship.

Planning ahead can make all the difference between effectively managing the financial burden of a cognitive decline diagnosis and sustaining severe financial hardship. This is especially important if there is increased risk of dementia in your family, including hereditary factors and prior injuries.

Plan early

Families can take steps to mitigate the risk of the costs associated with a dementia diagnosis. Hybrid insurance policies that include a long-term care component as well as some life insurance policies may provide financial relief. But the key is to have the insurance in place before the diagnosis, particularly if there is a family history of dementia, so planning ahead is crucial.

The four warning signs of dementia include:

1. Changing routines
2. Repeating requests
3. Unexpected relationships
4. A change in risk profile

Upon diagnosis, it is important to act swiftly to protect the patient and family from financial missteps, abuse and liability. Planning should include having key legal documents and arrangements—like powers of attorney, health care directives and wills—in good order, as well as making sure assets are properly titled and beneficiary designations are current. Also set up a trusted contact for all accounts. This trusted family member or close friend is there to review financial statements and transactions on a regular basis and can act as a fail-safe when your financial professional suspects fraud or detects a decline in the client's judgment.

Consider the benefits of trust and professional executor services, especially in the absence of a trusted and competent personal executor (generally a family member).

Your financial professional can help you navigate these tough waters and help you take steps to reduce the risk of financial missteps and fraud.

Get a head start on 2020 tax filing

Many tax provisions happened in 2020 due to economic uncertainty caused by the COVID-19 pandemic and government passing new laws. As you look ahead to preparing your taxes for 2020, use this checklist to remember what financial changes you may have made, so you can share the information with your tax advisor.

Tax prep checklist

- Did you withdraw Required Minimum Distribution funds in 2020? The Coronavirus Aid, Relief, and Economic Security (CARES) Act changed the requirement for RMDs in 2020. If you took your RMD earlier in the year and redeposited that RMD back into an IRA account prior to August 31, 2020, be sure to share the relevant statements with your tax advisors to confirm that the withdrawal and redeposit are properly reflected on your 2020 tax returns. Or, if you had taxes withheld from your RMD withdrawal and redeposited that RMD back into an IRA account, make certain that your withholding is properly reflected on your annual tax statements and credited back to you on your 2020 tax returns.
- If you received unemployment compensation, verify that appropriate amounts were withheld from your unemployment compensation, and be prepared for any required income tax payments.
- Some companies participated in the payroll tax withholding option between Sept. 1 and the end of 2020. Those deferred taxes are to be repaid in 2021. If you are among the relatively few employees impacted by this deferral, discuss the amount of payroll taxes that is being deferred from your paycheck and develop a plan for repaying those taxes in 2021.
- The CARES Act allowed individuals impacted by COVID-19 to take a taxable distribution from their retirement account without an early withdrawal penalty. If you took a coronavirus-related distribution from your retirement account, ask your tax advisors what information they will need to certify that you were impacted by the coronavirus within the meaning of the tax code. When you receive your annual tax statements, verify with your tax advisors as soon as possible that the coronavirus-related distribution is properly coded, and request a revision if necessary. Discuss with your tax advisors whether to pay all of the income tax liability in 2021 or to spread the liability over three years, as permitted.
- For business owners who incurred tax losses during 2020 and are scheduled to make estimated income tax payments in January, discuss whether those payments may be reduced in light of expected losses.

Preparing for unexpected bills

It's important to work closely with your financial professional and tax advisors throughout the year to continuously plan for tax changes and prevent painful tax bills. But sometimes it's impossible to fully prepare for a tax situation. Flexible financing options such as securities-based lending may provide you the opportunity to leverage eligible investments in your portfolio to fund opportunities or cash flow needs without disrupting your long-term investment objectives.

One client discovered she owed nearly $500,000 in unexpected income and capital gains taxes from the recent sale of her business. She had a liquidity event expected in a year, so she connected with her financial professional, asking if she could liquidate some of her investment portfolio to cover the bills. Rather than interrupting her long-term investment strategy, the financial professional advised her to set up a securities-based line of credit. She was approved to borrow $500,000 against her portfolio for the 12-month period until she expected her next liquidity event to occur. The client plans to use that event to pay off the line.

By utilizing a securities-based line of credit, the client saved $150,000 in additional taxes from liquidating assets, and kept her portfolio working toward her long-term goals.

Contact your financial professional if you need information about your finances to share with your tax advisor and about the possibility of setting up a securities-based line of credit so it will be available if you need it to cover an unexpected tax bill.

Client stories are for illustrative purposes only. They do not necessarily represent the experiences of other clients, and they do not indicate future performance. Results may vary.

Securities-based loans involve special risks and are not suitable for everyone. You should review the provisions of any agreement and related disclosures, and consult with your own independent tax and legal advisors about any questions you have prior to using securities-based loans or lines of credit. Additional restrictions may apply. If the securities in your account decline in value, so does the value of the collateral supporting your loan, and, as a result, the firm can take action, such as to issue a call and/or sell securities in order to maintain the required equity in the account.

Our firm does not provide tax or legal advice. All decisions regarding the tax or legal implications of your investments should be made in consultation with your independent tax or legal advisor.

Teach your children financial literacy

A quarter of American parents admit they don't do a good job of preparing their children to manage money, indicating a large number of children in the next generation will be affected with financial illiteracy.

This February during I Love to Read Month, consider targeting financial literacy with your children, no matter how young or old they are. If you plan to transition your wealth to the next generation, give them the tools they need to be responsible managers of that money. Spending time with your children when they're young learning financial literacy may pay off many times in their future.

Young children

As soon as they're old enough to understand the concept of money, they're ready to learn about saving, spending and sharing—lessons they'll need for the rest of their lives.

Teenagers

Financial goals become important as children grow interested in higher-value items like cars, travel and higher education. This is an age where evaluating needs versus wants is put to the test, giving your children good practice for future financial planning as they get older.

Early adults

As they enter adult life with family financial support starting to ease, budgeting is a lesson many college-age children need to learn. This is also an age to learn about investing concepts, especially as these early adults begin to understand their future goals, including retirement and health care costs.

Young professionals

Young professionals start to adopt investing habits in their 20s, which will last them for the rest of their lives. They're learning how to be successful investors, maintaining a regular investing schedule and learning the importance of staying the course when markets swing up and down.

Using financial literacy to successfully transition wealth

Financial literacy shouldn't only cover the topics of managing and growing money. It's also important when you intend for your children to inherit your wealth and successfully preserve it. A 2017 RBC Wealth Management study found most Americans are unprepared when leaving or receiving an inheritance. Unfortunately, this fact lends credence to the "shirtsleeves to shirtsleeves" proverb saying wealthy families often lose their fortunes in three generations.

This is where a wealth transfer plan comes into play. It includes components of communicating with younger generations about the family wealth and educating them about how to manage it. A wealth transfer plan can help your heirs feel confident in the financial decisions they need to make when they take ownership of the family wealth. For your legacy to last, it's important to transfer your knowledge about money management before it is time to transfer your wealth.

Your financial professional has financial literacy information available to help teach children how to become money smart, fund future goals and set up savings. Be sure to ask for this information, and also for background on how you, as the parent or grandparent, can talk with the younger generation in your family about money and transitioning wealth.