

Lenox Advisors

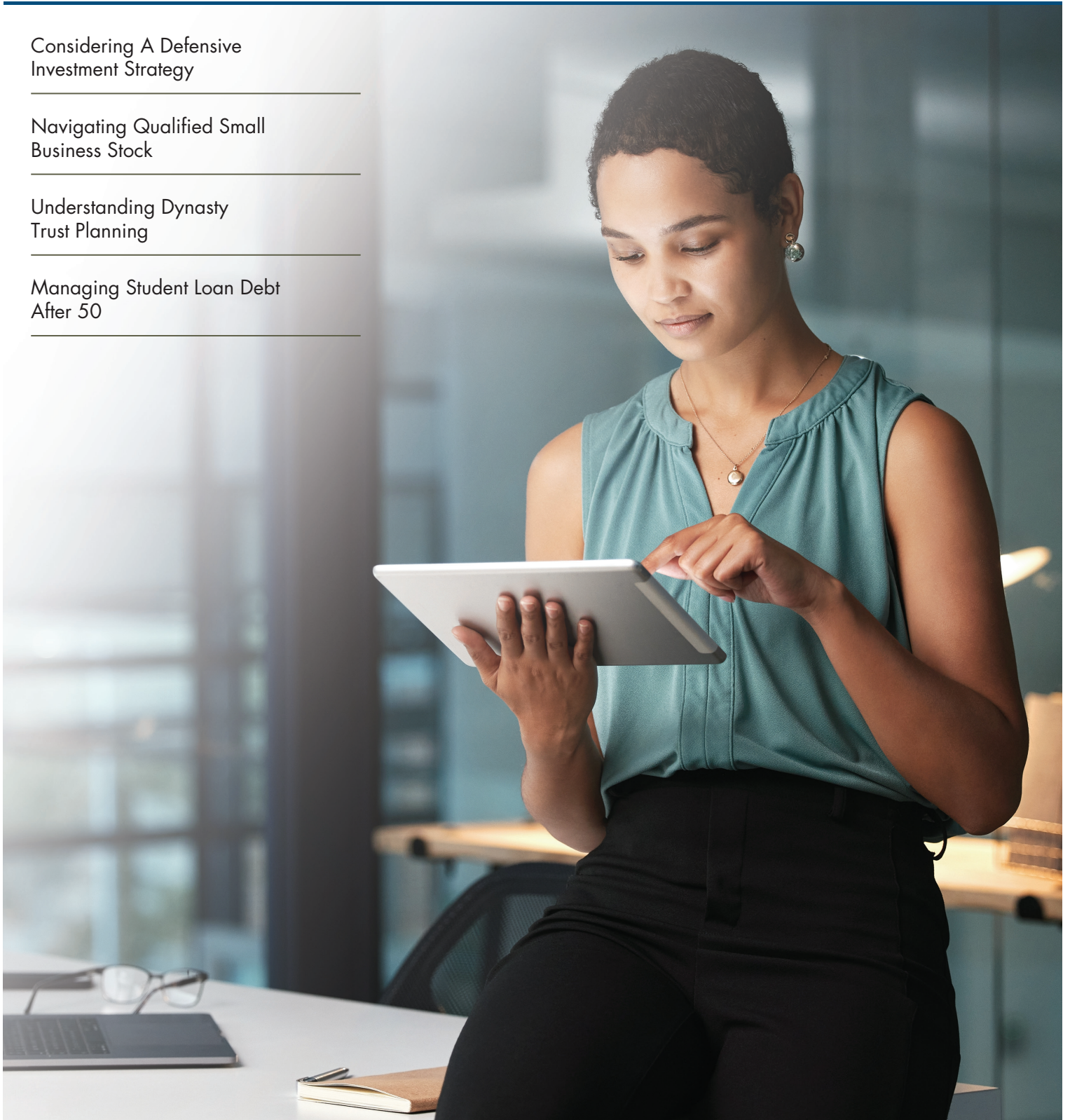
QUARTERLY UPDATE

Considering A Defensive
Investment Strategy

Navigating Qualified Small
Business Stock

Understanding Dynasty
Trust Planning

Managing Student Loan Debt
After 50



Considering A Defensive Investment Strategy

Certain investments, such as stocks, are almost always volatile. But you may feel as though you need a particularly strong stomach these days. Stocks still provide the best long-term returns over other major asset classes (such as bonds and cash) and are generally appropriate for retirement accounts that won't be needed in the next decade or more. But if you're closer to retirement or simply require greater peace of mind, here are several defensive investing strategies you might want to consider.

SPREAD RISK AROUND

Even those who are bullish on the market and relatively risk-tolerant should consider diversifying their portfolios across different asset classes, industries and geographies. But if you're risk-averse, this strategy is essential.

Whether you mainly invest directly in securities or access the market via mutual or exchange-traded funds, decide how you want to allocate percentages in stocks, bonds and cash (money-market accounts). You may also want some international exposure and to invest in such areas as real estate and commodities.

If you buy funds, pay attention to their sector allocations and the number and weighting of individual holdings. For the most part, more diversified funds will carry lower short-term risk. This is because

different types of securities tend to move in different directions. So if some types of investments are falling in value, others may be rising at the same time, resulting in steadier overall performance.

BUY ON THE CHEAP

Value investing, or buying "cheap" stocks, is a classic strategy made famous by such investing icons as Warren Buffett and Benjamin Graham. Value investors look for companies priced low relative to their business fundamentals and such investment ratios as price-to-earnings. Usually these stocks have reacted negatively to some form of bad news, such as poor quarterly earnings, or are depressed because the general market has

declined and punished stocks across the board.

Because they're relatively inexpensive, value stocks typically have less distance to fall when the larger market declines. But most value strategists are in it for the long term. There's a common misconception that buying bargain-priced stocks leads to immediate returns. In fact, it can take years before a value stock becomes what its investors consider fully valued.

ROLL WITH ECONOMIC CYCLES

Even experts have trouble predicting recessions. But certain indicators frequently coincide with economic downturns. For example, many professionals suggest caution when bond markets exhibit a



moderate or flat yield curve and widening credit spreads. Another red flag can be a Purchasing Managers Index reading below 50, indicating that the manufacturing sector is contracting.

If the economic cycle seems to be shifting into lower-growth territory, some investors favor consumer staples (think toothpaste and soap companies), utilities and health care stocks. These sectors may offer goods and services that people buy regardless of the economic climate. Also, because gold is perceived as having an “intrinsic” value, it’s usually considered the ultimate defensive investment.

In the same scenario, cyclical investors may ease up on consumer discretionary (such as travel and



luxury goods) stocks, technology and biotech (which tend to be heavily leveraged) and companies in the financial services and energy industries. Much depends on specific indicators, such as inflation and interest rates.

BEST FOR MOST

Although reallocating investment portfolio holdings can possibly help

you reduce short-term volatility, attempting to “time” the market is rarely successful. For most investors (and especially those with less investing expertise) the best strategy is to build a diversified portfolio that reflects your financial goals, time horizon, risk tolerance and other personal factors, and then leave it alone.

You’ll want to rebalance portfolio allocations when there are major market changes. For example, if bonds do particularly well one year, a bond fund may grow disproportionately to other holdings and it probably makes sense to rebalance your portfolio. Contact us for help building a diversified portfolio and to discuss such issues as volatility and rebalancing.

Navigating Qualified Small Business Stock

Qualified small business stock (QSBS) isn’t new: It’s been in the tax code for more than 30 years. But this powerful tax break, which allows investors or business owners to exclude 100% of their gain on sales of eligible stock, received a substantial upgrade under last year’s One Big Beautiful Bill Act (OBBBA).

Key improvements include expanding the definition of “qualified small business” to

larger companies, allowing partial exclusions for shorter holding periods and increasing the per-issuer lifetime limit on QSBS exclusions. Here’s a summary of QSBS rules and requirements.

WHO’S ELIGIBLE?

Under Section 1202 of the Internal Revenue Code, individuals and other noncorporate taxpayers, including U.S. trusts and estates, generally can exclude up to 100%



of capital gains on the sale of eligible stock in a qualified small business (QSB). QSBs are domestic C corporations engaged in “active” trades or businesses whose aggregate gross assets (including the assets of more-than-50%-owned subsidiaries) didn’t exceed \$50 million before or immediately after the stock was issued. Note that professional services, finance, farming, mineral production and hospitality C corporations don’t qualify. (This list of industries *isn’t* exhaustive.)

Under the OBBBA, the gross asset threshold was increased from \$50 to \$75 million for QSBS acquired after July 4, 2025. It’ll be indexed for inflation after 2026. To qualify for the 100% exclusion:

- An investor must acquire stock through an original issuance directly from the corporation in exchange for money, property (other than stock) or services,

- The investor must hold the stock for at least five years, and
- The stock must have been issued after September 27, 2010.

For QSBS acquired after July 4, 2025, investors may claim a 50% exclusion for stock held at least three years and a 75% exclusion for stock held at least four years. The taxable portion of the gain will be taxed at 28%. That means gain eligible for the 75% exclusion will be taxed at an effective rate of 7% and gain eligible for the 50% exclusion will be taxed at an effective rate of 14%.

WHAT’S THE LIFETIME LIMIT?

Sec. 1202 places a lifetime cap on the amount of gain that can be



excluded on sales of a particular issuer’s stock of \$10 million (or, if greater, 10 times the investor’s adjusted basis in the stock). The OBBBA increased the cap to \$15 million for QSBS acquired after July 4, 2025. This cap is indexed for inflation after 2026.

Keep in mind that the cap is per issuer. So, for example, an investor who acquires QSBS in two QSBs could exclude up to \$15 million in gain per company, for a total of \$30 million.

HOW CAN IT BE USED FOR ESTATE PLANNING?

The original issuance requirement doesn’t apply to QSBS received by gift or inheritance. So investors who gift QSBS to family members also transfer the ability to exclude up to 100% of the gain. This is an enormous advantage over ordinary gifts of appreciated stock, which are subject to capital gains tax when sold. Plus, the donor’s holding period is tacked on to the recipient’s for purposes of the holding requirement.

KEEP YOUR ESTATE PLAN LIMBER

Last year’s One Big Beautiful Bill Act made the \$15 million gift, estate and generation-skipping transfer (GST) tax exemptions “permanent” (meaning there’s no expiration date, though the amount will be annually indexed for inflation). For now, this provides greater certainty in estate planning. However, because Congress could change the exemption in the future, you might want to take steps to improve your estate plan’s flexibility.

One potential option is to use an irrevocable trust that removes assets from your estate but gives your trustee (or a “trust protector”) the authority to take actions that would bring the assets back into your estate. Why? Your trustee might determine that it would yield a better tax outcome. Other potential tools for improving estate plan flexibility include special power of appointment trusts, limited powers of appointment and disclaimer trusts.

In addition, donors can use a technique called “stacking” to maximize the tax benefits of QSBS. Dividing gifts of QSBS among several family members may enable you to multiply the per-issuer cap, shielding more capital gains from tax.

Suppose, for example, that you own \$36 million worth of QSBS (acquired pre-OBBBA) with a basis of \$6 million. If you sell the stock, the lifetime cap would limit your

exclusion to \$10 million in gain. If, instead, you gifted \$12 million in stock to each of your two children before the sale (either outright or through a carefully designed trust), you’d each enjoy a \$10 million cap, allowing you to exclude the entire \$30 million gain.

IS IT RIGHT FOR YOU?

QSBS offers extraordinary tax-planning opportunities for investors and business owners alike, and

the benefits are even more attractive under the OBBBA. However, these investments aren’t right for everyone. Business owners, in particular, need to weigh the advantages of tax-free capital gains against the potential costs (including double taxation of dividends) of operating as a C corporation. Talk to a professional tax advisor about potential tax mitigation strategies.

Understanding Dynasty Trust Planning

What legacies do you hope to leave your children and grandchildren? They could include values such as honesty, activities such as philanthropy or even a family home passed down for generations. Many people, however, associate the word legacy with a financial inheritance.

For example, legacy trusts enable wealthy individuals to leave assets to loved ones while minimizing potential tax liability. What differentiates them from other types of trusts is that they’re designed to limit estate and gift taxes that might otherwise deplete bequests made over multiple generations. Here are some common FAQs about dynasty trusts.



WHY WOULD YOU NEED ONE?

Here’s what usually happens without a dynasty trust: If a parent leaves assets to children, the bequest is subject to federal estate tax at the time of the initial transfer to the second generation. It’s taxed again when the assets pass from

the children to the grandchildren. This can continue for generations. Although the federal gift and estate tax exemption continues to grow and can shield most assets from tax, the top federal estate tax rate on the excess is currently 37%, a hefty amount.



Furthermore, the generation-skipping transfer (GST) tax of 40% applies to certain transfers made to grandchildren, thereby discouraging transfers that skip a generation.

By contrast, with an irrevocable dynasty trust, assets are taxed just once, when they're initially transferred to the trust. There's no estate or GST tax due on any subsequent appreciation in value. This can save some families millions of tax dollars over the trust's duration. When the assets are subsequently sold, any gain will be taxable. Note that the basis of the assets will be determined at the time of the initial transfer, though depending on the circumstances, the "step-up in basis" rules may help to reduce the taxable amount.

WHAT ROLE DOES YOUR STATE OF RESIDENCE PLAY?

Many states originally adopted a "rule against perpetuities," which prohibited trusts from lasting more than a certain number of years. But in recent years, most have reversed these rules or extended the time period.

For instance, California now limits a trust's duration to a generous 90 years. And a handful of states, including Delaware, Alaska and Florida, have not only abolished perpetuity limitations but encourage nonresidents to set up dynasty trusts in their jurisdiction. As you can guess, it's important to work with a professional estate planner knowledgeable about your state's rules.

HOW DO YOU SET ONE UP?

A legacy trust can be established during your lifetime, as an inter

vivos trust, or part of your will as a testamentary trust. With an inter vivos transfer of assets, you'll avoid estate tax on any appreciation in value from the time of the transfer until your death. Generally, though, with an inter vivos transfer the assets won't be eligible for a step-up in tax basis at your death.

Because the emphasis is on protecting appreciated property, consider funding your trust with securities, real estate, life insurance policies and business interests. Naturally, you should retain sufficient assets in your personal accounts to maintain your lifestyle.

DON'T DO IT ALONE

You shouldn't try to set up a legacy trust on your own. This is a sophisticated instrument that is typically used with other estate planning tools to accomplish multiple goals. Contact your estate planning advisor for more information.

Managing Student Loan Debt After 50

It's become more common for middle-aged adults to carry student loan debt. Whether you owe money borrowed for your own education or your children's, juggling student loan payments alongside other financial priorities can feel overwhelming. Many people focus on paying off student loans quickly, even if it means pushing pause on retirement savings. But that's not always a good decision.

YOU CAN'T BORROW FOR RETIREMENT

It can feel satisfying to eliminate debt. But if you're in your 50s, for example, you need to prioritize retirement. Every dollar you don't currently contribute to a 401(k) plan or an IRA loses years of potential growth. Aggressively paying down loans while neglecting retirement savings could leave you debt-free but unprepared for old age.

Instead, contribute enough to your work-based retirement plan to receive an employer match. That's free money you shouldn't forfeit. At the same time, keep up with minimum payments required by your student loan servicer. Defaulting on student loans can lead to bad credit and other serious consequences.

CONSIDER REPAYMENT OPTIONS

If your student loans are federal, you may qualify for income-associated repayment

plans. These plans can lower your monthly obligation, freeing up cash for other goals, such as saving for retirement.

Consider refinancing if it would significantly reduce your interest rate. Just know that refinancing government debt into a new private loan generally removes federal safety nets that protect borrowers who become unemployed or who might be eligible for forgiveness programs.

WEIGH ALL PRIORITIES

In addition, your financial well-being (or at least your peace of mind) depends on having emergency savings, health insurance and, if you're married or have minor children, life insurance. Budgeting for all of these needs can be hard, so consider prioritizing obligations in the following order:

- 1. Cover the essentials.** Maintain an emergency fund of three to six months' expenses and obtain health insurance through your employer or the government's Marketplace.
- 2. Save for retirement.** Prioritize contributions eligible for an employer match and increase your



contribution rate as you receive raises and pay off debt.

3. Repay high-interest loans.

It's always smart to prioritize paying off high-interest debt (credit cards) before lower-interest debt (a mortgage or student loans).

4. Manage student loans strategically.

If necessary, look into repayment plans or refinancing.

STRIKE A BALANCE

To keep student loans from derailing your retirement plans, strike a balance between debt repayment and saving. Contact a financial professional for additional advice.

