The Trust Company of Virginia

Commentary | News and Trends | FALL/WINTER 2014

Our Equity Investment Strategies ~ *TCVA Investment Group*

Our style and philosophy in asset management has been one of discipline and a methodology which has produced portfolios of above average returns and below market risk levels. On the equity side, the investment strategies at The Trust Company of Virginia include the ***TCVA Global Value Strategy, the TCVA Core Strategy and the TCVA Global Growth Strategy***. Although each portfolio has distinct characteristics and is designed to meet a variety of our client's needs, the process in constructing each strategy is similar in approach.

Value

Core

Global Growth

Our **Value Strategy**, which has been our flagship equity style for over 10 years, has provided an investment niche which most money managers no longer offer. Value portfolios seek stocks of companies that are believed to be undervalued or priced below their intrinsic, long term value. The TCVA Value portfolio is a multi-capitalization and multi-style portfolio where approximately half is comprised of Large Cap Value oriented stocks. The selection of individual securities is designed to produce a higher yield while providing lower levels of portfolio volatility versus the broad market. Investing in companies with high quality fundamentals, strong competitive positions, consistent earnings and dividend growth rates produces a portfolio with reduced market risk and consistent performance. The strategy is designed to be conservatively positioned, utilizing stocks which cover all ten of the S&P 500 sectors and are even further diversified across multiple industries within each sector. For example, within the Health Care Sector, selected companies include medical devices, pharmaceuticals, biotechnology firms and health management. To further enhance equity diversification, the Value Strategy incorporates additional asset classes which take advantage of shifting strategies in the market. Exposure to Small-cap and Mid-cap companies is achieved through the use of Exchange Trade Funds (ETFs). An ETF, which is basket of stocks, tracks a specific market index and allows the portfolio to achieve adequate diversification and exposure to sectors and asset classes at a lower cost than other options. In cases where the weighting of an asset class is too small to diversify properly using individual names, this is the ideal investment vehicle. In the Value Strategy, in addition to Small and Mid-cap allocation, the portfolio maintains exposure in Real Estate (both domestic and international), International and Emerging markets, and Commodities. Value is enhanced by adjusting the sector and asset class weightings to take advantage of changing market conditions. This strategy is ideal for the more conservative investor who still needs exposure to the equity markets, but would also like to generate income without taking undue risk.

The **TCVA Core Strategy** was originally designed to provide smaller accounts a higher level of diversification than was previously achieved through Mutual Funds. As with the Value Strategy, the portfolio has exposure to all sectors of the S&P 500 as well as Small and Mid-Cap, Real Estate, International and Emerging markets and Commodities. However, this particular strategy is a hybrid, combining Large Cap Value and Large Cap Growth through exposure to the individual S&P sectors. Where the Value Strategy focuses on undervalued, individual companies, the Large Cap exposure in the Core Strategy incorporates both Value and Growth. The Large Cap sector is made up of top rated ETFs that provide full exposure to the S&P 500 broken out into individual sectors. This allows our investment team to add value by adjusting sector exposure the same way we adjust sectors in the Value Strategy. This optimizes diversification for smaller accounts, as well as providing active management from our investment team. Because the ETFs take advantage of all the stocks that make up the S&P 500, it is considered more of a Core Investing strategy; some holdings are the same names we use in our Value Strategy, while others are considered more growth oriented. Therefore, the client has a wider range of exposure across Large Cap names. In the Small Cap, Mid Cap, Real Estate, International, Emerging Markets, and Commodities, we use the same ETFs recommended in our Value Strategy. By using high quality, low cost ETFs, we are able to provide a level of active management and higher diversification, for a lower cost than a typical passively managed mutual fund. Through the use of ETFs, we are also able to keep transaction costs and capital gains lower. The Core model can be effective in any size account that is sensitive to capital gains or would like a more Core Investment approach.

The newest member to our investment lineup, the **TCVA Global Growth Strategy**, has been created in order to provide long-term growth of capital through a portfolio of both actively managed and passively managed securities. The idea behind this new strategy was to develop it as a complement to our existing and successful Value Strategy. It provides an option for those clients who desire more capital appreciation, are willing to take increased risks in their portfolio and tend to have longer investment time horizons. We think we've achieved these goals.

The two approaches (Value vs. Growth) employ very different objectives and differ in the types of companies being held in the portfolios. Typically, growth investors tend to focus on companies that are trading at higher valuations than the overall market, have higher earnings growth rates, typically don't pay dividends and tend to exhibit a little more price movement than the broad market. Value investors, on the other hand, tend to purchase companies/stocks that are trading at discounts to the broad market and their intrinsic values, have stable earnings growth, typically pay a dividend and carry somewhat less risk than the overall market.

We've developed and formed the Growth strategy in a similar fashion to our other strategies by using primarily the same asset allocation framework and asset class weightings. Diversification is achieved by investing in Small-Cap, Mid-Cap, developed International Markets, Emerging Markets, Real Estate and Commodities. Due to the nature of the growth investor, the Growth Strategy is a good vehicle in which to offer two new asset classes that are not appropriate to hold in the Value or Core Strategies. The Growth Strategy will initiate positions in both Energy Infrastructure and Alternative asset classes.

Which strategy is appropriate for an investor is based upon the individual's goals and objectives. The Value Strategy is ideal for the patient investor who needs exposure to the equity markets, but would also like to generate income without experiencing undue risk. The portfolio is conservatively designed to provide high quality diversification. Conversely, the Growth Strategy tends to meet the goals of those investors who desire higher levels of capital appreciation, are willing to take on additional risk and typically have longer time horizons to reach these objectives. For those investors who fall somewhere in the middle and favor a more passive management style, the Core Strategy may be the best fit. Whichever strategy, an in-depth conversation discussing individual goals with your portfolio manager is necessary to make sure all are on the right path for financial success. ■

Put Your Trust Assets to Work for You – a case study

A Richmond couple in their early 70s wanted to buy a new home before their existing home, valued at $1.2 million and mortgage free, could be sold. Although the couple's annual income was $500,000, there were extenuating circumstances which made this a more complicated situation than a simple "bridge" loan.

These clients had a comprehensive financial plan, and their assets were held in their trust accounts at The Trust Company. They needed a credit line for $600,000 to be available within six business days in order to secure the new home. While they could have liquidated assets in their trust accounts, they were reluctant to do so because their assets were carefully invested under a long-range strategic asset allocation plan, and also because there could tax consequences. We contacted our lending partner, The Bancorp Bank, who agreed to use the trust assets as collateral for a securities backed line of credit (SBLOC). This line of credit allowed the couple to retain their liquid assets while bridging the purchase of their new home. The Bancorp Bank worked closely with the trust administrator to facilitate this loan.

The new home purchase took place within the six-day period, and the transaction minimized negative tax consequences as a result of the SBLOC's ability to offset capital gains. The SBLOC was fully paid off with the proceeds of the sale of the existing home, which happened six months later. The clients especially appreciated the seamless partnership between The Trust Company and The Bancorp Bank which provided such an efficient solution to their problem. ■

Doing the Limbo in 2014: Tax Planning Stagnation

~ *Frances F. Goldman, JD, CPA.*

Dear Taxpayers: We, your Congresspersons, apologize for the inconvenience, but we will not be able to create or propose, much less vote on, any tax laws until at least early December, after the mid-term elections. We realize that this may cause an inconvenience to those of you trying to make tax-planning decisions, such as whether or not to use your IRA's RMD (required minimum distribution as of age 70 ½) for direct charitable contributions, since we have not yet voted to extend many of the laws that expired on December 31, 2013. It may even be January before we can come to any agreement on tax proposals (remember 2012-13).

That will leave you about two weeks at best to make all your tax planning decisions, making your investment advisors, lawyers, and accountants scramble to fill your wishes. No problem though, you are used to it after this having been our pattern for the past several years.

Besides not knowing whether we will pass the "IRA direct contribution to charity" law, we also will have to decide whether to extend the Section 179 business asset write-off on new equipment (it was $500,000 last year but drops to $25,000 in 2013 if we don't act), 50% bonus depreciation, and whether to modify the shared responsibility provision of the new Health Care Act (ACA). Of course, it is doubtful that we can justify the Section 179 deduction, since the economy has picked up and the small business stimulus is not as important as the lost revenue. The bonus depreciation may be safe enough; it is not as costly and is a nice perk for a small business (and more so for a large one, we might add).

We do not know if you noticed, but a Tax Court case caused the IRS to rule that taxpayers can only have ONE rollover of an IRA annually effective in 2015, even if you have IRAs in several different banks or investment firms (a Trustee to Trustee transfer is still allowed). Oh, and the education tuition and fees deduction also expired in 2013, but the American Opportunity Credit is still around!

Highly unlikely that we will tinker with the 2013 provisions to fund ACA such as the 3.8% surtax on investment income that kicks in at $250,000 of adjusted gross income for a married couple (and $200,000 for an unmarried person). Same is true for eliminating the .9% Medicare tax on wages (wages include self-employment net income) that exceed those same thresholds. The income that is subject to the 3.8% tax consists of interest, dividends, annuities (but not IRA distributions), rents and royalties, capital gains, and passive business income. The 39.6% tax bracket along with 20% capital gains rate is effective at $457,600 of taxable income for a married couple ($406,750 for an unmarried person) is not being changed either. You may notice that the 3.8% and .9% thresholds are not indexed for inflation. The 39.6% tax bracket, however, is indexed. Slight oversight on our part, but no, this will not get fixed either, probably ever.

We realize that Trusts and Estates bear a very high tax burden, since the new taxes we noted in the last paragraph kick in when the Trust or Estate has taxable income of $12,150. But you can plan for this, if you have flexibility in your Trust or Estate distribution provisions. We strongly suggest you contact your Trust Company of Virginia advisors soon to try to mitigate the impact of our inaction. Sorry, but politics as usual prevail. ***Best of Luck!*** ■

__Frances Goldman__ is President of The Tax Complex, a strategic partner of The Trust Company of Virginia. She is currently responsible for trust and estate tax compliance, post-mortem planning including estate administration, and tax and estate planning.

Allan Keyes Retires...

We cannot write about investments at The Trust Company of Virginia without a tribute to Allan Keyes, our Chief Investment Strategist, who retired on September 30 after 19 years. A husband, father and grandfather, Allan graduated from Virginia Tech, served overseas during the Vietnam War, and is an avid reader and a lover of the game of golf. Allan's devotion to the financial services industry was paramount. His enthusiasm for the markets, domestic and foreign economies, geopolitical events and American politics was matched only by his unique ability to convey his insights to others. Allan's genuine, caring nature was apparent to all who had the privilege to know and work with him. The client always came first and his dedication to each and every individual will be missed. His impact and contribution to TCVA will never be matched and although we are sad over his departure, we wish him health and happiness as he begins his retirement.

Events around the Company

■ We have been holding Client Forum luncheons across the state since 2002, sometimes in the spring and sometimes in the fall. These lunches are meant to be an educational forum on topics we hope will interest our clients, covering the gamut from economics and market comments to caring for a loved one with Alzheimer's.

■ Most recently we had two presentations at our Richmond Fall Forum, "What every Woman should know about Health and Legal Issues." Dr. Christine Allan of the Executive Health Group focused on the two leading causes of death for women: heart disease and cancer with breast cancer far and away the leading type of cancer in women. She presented the risk factors for heart disease, primarily high blood pressure, high cholesterol, and sleep apnea. Not surprisingly, diet and exercise are critical to maintaining cardiac health. October is Breast Cancer Awareness month (The Trust Company made a donation to the Breast Cancer Society in recognition of this) and Dr. Allan reviewed both the risk factors as well as the various screening methods available today.

■ Elizabeth Horsley, a partner in the law firm Williams Mullen, gave a lively presentation on the legal documents every woman should have on file and the purposes of each: a will, a trust, a power of attorney, and an advanced medical directive. She reviewed legal considerations in caring for aging parents and for adult children. Few in our audience had considered the need to have access to our adult children's social media and/or their passwords in case of their incapacity – she strongly recommended that adult children have at minimum a Power of Attorney in place so that business can be conducted while they are incapacitated.

■ Our Roanoke and Williamsburg offices had their client forum luncheons in the spring, so are planning evening events this fall. On October 21, Roanoke is hosting an evening with Beth Macy, an author whose recent book, Factory Man, has enjoyed wide spread acclaim. The book is about the furniture executive and factory owner John Bassett who successfully fought off moving the operation off shore, saving hundreds of jobs by keeping the factory in Bassett, Virginia. Williamsburg clients are invited to an evening at the William and Mary Alumni Hall with a presentation by Margaret Pritchard, Senior Curator with The Colonial Williamsburg Foundation, who is going to talk about antique maps on October 30. In December, Northern Virginia clients and friends will enjoy a musical evening at the Washington Golf and Country Club. Also, our Lynchburg office is planning a holiday open house for friends and clients.