Trust Company *of* Vermont Quarterly Update

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Brattleboro ◆ Burlington ◆ Rutland ◆ Manchester ◆ St. Albans

Employee-owned & Vermont-based www.tcvermont.com

What Can You Learn in an Airport?

Chris Cassidy, Portfolio Manager

This past January, I was stranded in one of my least favorite places, JFK Airport. Wanting a distraction from the dreaded monitor teasing me about yet another delay, I opted for a highly caloric snack and a copy of Money Magazine Investor's Guide 2015. The magazine contained an article entitled "*Sizing Up Tech's Titans"* in which they rated Apple a buy, Google a hold and Amazon a sell for 2015.

Articles forecasting how financial markets will move, and which stocks to buy and sell, for the upcoming year are more ubiquitous than holiday fruit cakes. The problem is that year-to-year movements in markets and stocks are very difficult to predict. In 1928 the S&P 500 gained over 43%. In 1931 the S&P 500 fell more than 43%. In 2008 the S&P 500 fell over 37%, but in 2013 the S&P 500 gained more than 32%. It is hard to imagine that company fundamentals changed so much in just a few short years to warrant such dramatic swings, but markets are fickle in the short-term.

As I write this, the S&P 500 is up just 0.25% for 2015. For the year ahead, most financial analysts predict the flattish trend in equity returns to continue. Goldman Sachs believes that the S&P 500 will "tread water" and finish the year just 2% above its current level. Similarly, Credit Suisse expects the S&P 500 to finish just 4% above current levels by year-end. Morgan Stanley issued a note claiming that investors should prepare for an era of below average returns. On the fixed income side, many analysts fear that a rising interest rate environment could pressure bond prices in 2016. In December, the Federal Open Market Committee raised the Fed-funds rate for the first time since June 2006. If the Fed raises rates too quickly in 2016 it could cause volatility in both fixed income and equity markets.

It is understandable that stock market expectations are low for 2016. Global economic growth has been slowing due to emerging market weakness, and fears about a "hard landing" in China persist. Commodity prices remain at depressed levels, which should continue to pressure many emerging economies in 2016. Furthermore, equity market valuations are on the high side historically. Earnings per share for the S&P 500 have declined due to a strong dollar and major weakness across the energy sector. Using trailing 12 month earnings, the S&P 500 trades close to 20 times earnings, which is well above historical averages. While many analysts' projections for financial markets are on the pessimistic side, I am always cautious about short-term predictions.

Looking back at the Money Magazine article, the stock that they rated a sell has performed the best in 2015 while the stock that they rated a buy has performed the worst. Within the article, the authors laid out many positives for all three companies as far as balance sheet strength and long-term competitive advantages. Any investor who owned any of these stocks for the past three, five or ten-year periods has been generously rewarded. It is far easier to evaluate a quality investment's long-term prospects than how it will perform over a one-year period.

What did I learn from my miserable airport experience?

1) be very wary of short-term predictions,

2) invest with a long-term time horizon focusing on quality and

3) never eat an entire bag of cheddar cheese Combos in one sitting.

Wishing you a healthy, happy & prosperous New Year!

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Direct IRA Distributions to Charity Made Permanent

In a nutshell: Are you over 70½ and taking a required minimum distribution (RMD) from your IRA? Do you also plan on making any charitable gifts in 2016?

On December 18, 2015, under the tax act "Protecting Americans from Tax Hikes Act of 2015" Congress and President Obama made permanent the Qualified Charitable Distribution (QCD) rules for making a tax free distribution from your IRA (Individual Retirement Account) or Inherited IRA directly to a charity.

What does this mean for you? You could effectively transfer all or part of your RMD, up to $100,000, to a qualified charity and avoid taxes on the amount withdrawn. By planning what your charitable contributions are, you can elect to have this amount paid directly to one or more charities. As this amount would count towards your RMD, not only are you complying with tax law but, lowering your taxable income and satisfying your charitable intent all at once.

This option is also available if you are the beneficiary of an Inherited IRA and have reached the age of 70½. Roth IRAs are also included, but since distributions from Roths are tax free if all criteria is met, it would be beneficial to use funds that would be taxable first.

Now that we have dispensed with the nutshell, is there something hiding in the nutshell that may not be apparent? We think it is the scheduled RMD. If your trust officer or your accountant tells you the RMD amount and you don't factor in the charitable deductions in advance, you may take more out than intended, and you cannot correct it after the fact.

As always, we recommend that you talk to your tax accountant before making any tax decisions.

~ Jeanne Gilbert & Angela Bowman

Flip the Pyramid

Jack Davidson

Growing up in our family, the rule was to have a job after school, unless extracurricular activities got in the way. Thus, my career started as a paper boy. I liked it. No boss. Just get the paper out in time. I then migrated to the corporate world, where my parents expected me to stay until I retired. My first stop was a part-time job while still in school.

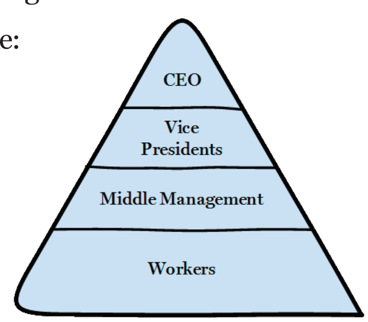
I enrolled at Bohack.

Bohack was a supermarket chain on Long Island and my first job was as a bottle boy. On the first floor, bottles were returned and sent by conveyor to a revolving drum in the basement to be sorted and boxed. I stayed in the basement for approximately a year and then was promoted to the first floor. My job was to take care of one aisle. I would bring up boxes from the basement, and in a fraction of a second, my knife cutter would remove the top. Then I would quickly draw from my holster a pricing gun, set the price, and within 5 seconds I could price 24 cans. I was John Wayne of Aisle 2. My aisle was perfect. My career was promising. I was going to be tested in marketing. I was asked to set up a display of 46 ounce Dole pineapple cans. I created a pyramid of cans and topped it with an eye catching display. I thought it was brilliant and my career would take me to new heights.

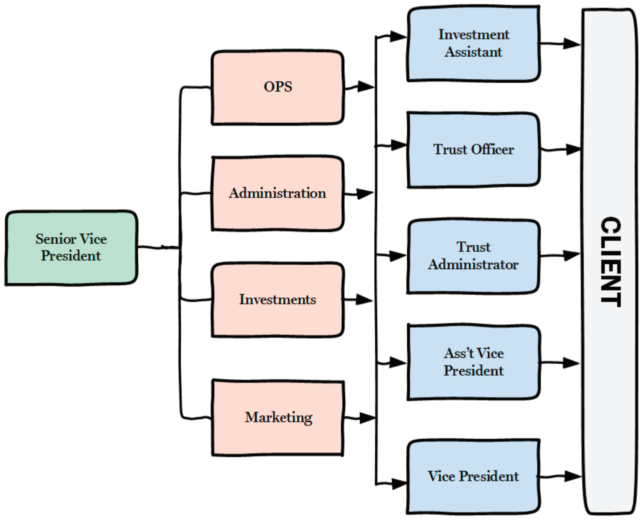
This is what it looked like:

When the head boss saw my "creativity", I overheard his comment to my boss. *"This is idiotic...our customers are afraid to touch it."* I was demoted. Fortunately, it was not a destination job once I graduated from college. Little did I know that the pyramid would continue to haunt me even to this day.

The corporate world is in transition, but still dominated by hierarchial structure and is typically visualized as a pyramid. For an organizational chart this is what the shape might look like:



During my tenure as the head of the Trust Department at Vermont National Bank, I was once asked to submit an organization chart. Perhaps haunted by the pyramid, I flipped the Pyramid. It was now horizontal and it looked like this:



In my view, management was simply a support system to those who would have client relationships; the trust officer, or the person who answered the phone, and the flow was not top down. It was, instead, left and right and right to left and everyone participated in the design and implementation of a service or a product.

I suspect it was not well-received by senior management. Not a word was said when I submitted my chart and the chart simply disappeared. Perhaps management simply understood that I have a troublesome relationship with pyramids.

I was not a very good paper boy, but I liked being a paper boy. There was no management structure. I loved autonomy and I thought everyone else felt the same way. I would learn by my mistakes and enlighten others. When it snowed, I delivered hell or high water and when it snowed on Long Island it became water, very quickly. My customers forgave me when I failed to deliver the paper on a sunny day.

Starting in the 50s, many businesses started to see the negative impact of a strict top-down structure. Adherence to rules was paramount. It was not just the blue collar worker who had to clock in. Gradually, worker autonomy started to weave through the hierarchial structure. The pyramid might still look the same, but worker autonomy started to surface. 'Theory X" and 'Theory Y" were developed by Douglas McGregor at the MIT Sloan School of Management in the 1960s. These theories addressed two contrasting models of workforce motivation. The autocratic Theory X manager started losing power and the collaborative Theory Y manager started to emerge.

Vignettes also started to emerge. Simple pictures that suggest the transition to different theories of management would grow more complex. I went to a one day training for mid-managers. I was one of thirty participants. We were asked the question: "If you have a subordinate who is doing a very good job, would you require this person to report to you on a regular basis." Twenty-nine voted yes. The one negative vote was the one who had a problem with pyramids.

I met a lawyer from a large corporation that started to promote from within. His observation: when you promote the victims of X Theory managers, they become X Theory managers. Perhaps transitioning to Theory Y should focus on those who are not accustomed to the pyramid.

I also learned something else that some or many will dispute. Find the right people, and, if the bottom line cannot afford high salaries, offer autonomy and you will get a better bottom line and less need for management. Less management equates to less cost as well. Simply hire people who are smarter and/or work harder than you, and you will survive.

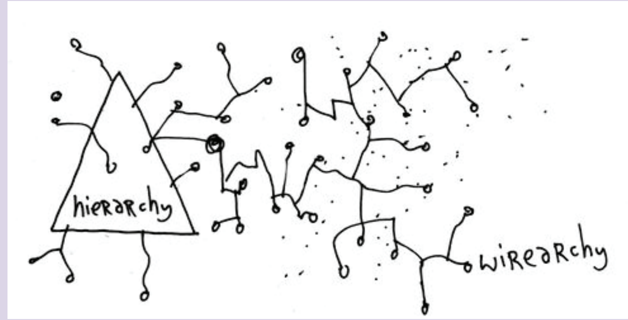
And I discovered Robert Townsend. Robert Chase Townsend (July 30, 1920 – January 12, 1998) was an American business executive and author who was responsible for transforming Avis into a rental car giant.

Quoting Townshend's *Organization Charts: Rigor Mortis: "In the best organizations people see themselves working in a circle as if around one table.*

One of the positions is designated chief executive officer, because somebody has to make all those tactical decisions that enable an organization to keep working. In the circular organization, leadership passes from one to another depending on the particular task being attacked - without any hang-ups. This is as it should be. In the hierarchical organization, it is difficult to imagine leadership anywhere but at the top of the various pyramids" [1.]

Early in my career I discovered that in my dealings with senior management, it was easier for them to approve a personal computer then hire a secretary. So I bought IBM PCs (the Operations Department said no to a Mac). Then I discovered that the trust department staff could work at home and avoid the pyramid which tended to reinforce hierarchal behavior. So in our department, we found the internet and started using e-mail in 1985. We also encouraged a one-day-work-at home. Most did not take the one day. Autonomy in a corporate world takes time.

Perhaps I was prescient? I kind of think I was simply hierarchy-avoidant; I did not see Wirearchy coming.



Wirearchy

an organizing principle

"A dynamic two-way flow of power and authority, based on knowledge, trust, credibility and a focus on results, enabled by interconnected people and technology."

Source: Jon Husband at www.wirearchy.com

As centuries change, phrases emerge. In the 20th century, a common phrase was "a century ago most people walked to work". My prediction is that the phrase for the 21st century will be "wirearchy will rule". To be honest, I did not know the term existed until I stumbled upon it last month.

Whether wirearchy will become a household word, the concepts are simply staring us in the face, or more precisely the face on the iPad or iPhone under the table during the holiday dinner. That said, it is not really about technology.

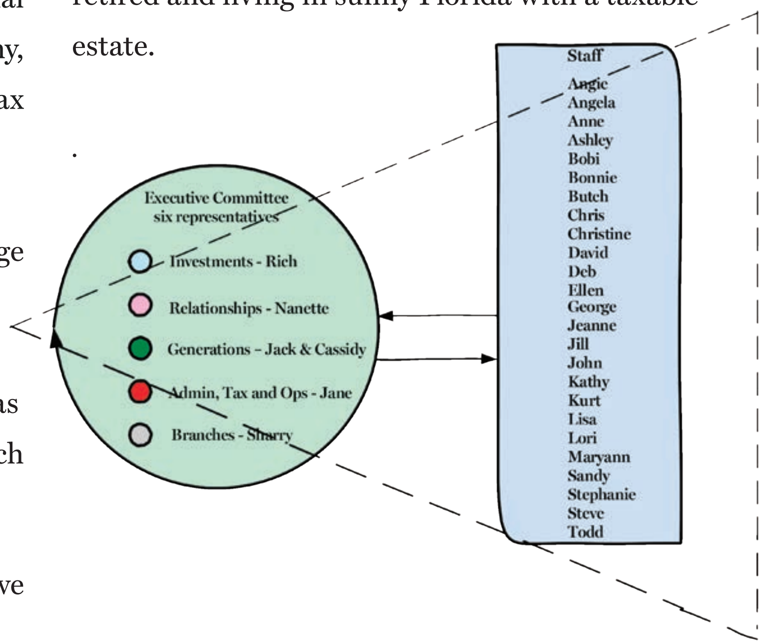
Quoting Jon Husband: *"There's one common misconception that I'd like to clear up first, which is that wirearchy is mainly about technology. If anything, wirearchy is about the power and effectiveness of people working together through connection and collaboration ... taking responsibility individually and collectively rather than relying on traditional hierarchical status".*

The prevailing view of the pyramid is based on the assumption that leaders higher in the hierarchy had better information for making decisions, to wit: the boss makes the best decisions and the rest of us will have a job thanks to the decision making process. As we approach the new year, I think it might be a good time to say goodbye to the pyramid representing a hierarchial structure of the 20th century. In our company, knowledge is the core of our services: investments, tax law, accounting law, and family dynamics.

Most of us in our company have been sharing knowledge for years. Technology simply makes it much easier. The managers now meet once a week via video-conferencing. The administrators meet once a week as well and vote, often daily, on trust-related issues such as approving requests from family members.

Our company is an employee-owned company and we are creating an organizational chart. In this group, it has not been difficult to flip the pyramid. Below is our version of what we have created.

Bye Pyramid. No hard feelings. If I had checked with my boss before I built you many years ago, I might be retired and living in sunny Florida with a taxable estate.



[1] *"Up the Organization," published in 1970, was on the New York Times nonfiction best-seller list for 28 weeks. For seven of those weeks it was No. 1 on the list.*

Estate Planning Alert - Do you own a timeshare?

The rules governing timeshares are determined by the state laws where the property resides.

Sometimes timeshares will morph from an attractive asset to an unpleasant liability or somewhere inbetween. Recently, we are seeing timeshares in estates that require probate, and the cost of probate would be greater than the value once sold.

There are ways to avoid probate with real property such as gifting to children or holding timeshares in trusts. Both strategies may be fraught with unlikable consequences. The typical timeshare requires annual maintenance and simply walking away may still create continuing liabilities. Gifting to a child who cannot afford the maintenance may result in a "gift", not of an asset, but a poor credit rating. Adding timeshares to trusts may create the possibility that other trust assets may bear the cost of incurring ongoing maintenance until final settlement, a process that may be drawn out by design, without specific strategies such as "Declarations for Trusts" designed to isolate just the timeshare. It is important that your lawyer is aware of any timeshares.

Your Executor and/or Trustee, and/or beneficiaries will thank you. Sunny days in a timeshare may create unpleasant weather for others.