Sentinel

Personal Financial Management Ideas

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New Music Law Is An Instant Hit

By Shomari D. Hearn, CFP®, EA

U.S. copyright law is seldom a crowd-pleaser in any form, but new legislation has earned a rare standing ovation from most of the music industry.

President Donald Trump signed the Music Modernization Act into law in October 2018, after it unanimously passed through both houses of Congress. Labels, musicians and politicians all celebrated this update to copyright law. While no law arrives entirely without naysayers, by Washington standards, the Music Modernization Act is as close to a universal hit as lawmakers are likely to see.

The 185-page legislation combined three previously introduced bills to achieve several complementary goals. It simplifies the music licensing process, with a particular focus on making it easier for rights holders to get paid when their music is streamed. It also ensures that songwriters and artists will receive proper royalties for songs recorded prior to 1972. And it improves the royalty payout process for producers and engineers whose work is streamed digitally.

I will go into more detail about each of these changes, but the major question artists and songwriters are likely asking is whether this law is good news. On balance, it seems likely that it will be, though like everything else about the U.S. copyright system, the details will be complicated. If it works as designed, this system should make it easier for rights holders to get the full royalties they are owed, paid promptly.

The Music Modernization Act: What We Know

The first major change under this new law is the creation of a single, mechanical licensing database. Music publishers and songwriters will oversee the system, but its costs will be borne by digital streaming services like Spotify. The music licensing collective's board of directors will include 10 representatives from music publishers and four self-published songwriters, as well as three nonvoting advisers, one of whom will represent the streaming services.

One reason that music publishers, labels, streaming services and consumer groups all enthusiastically backed the Music Modernization Act is that the situation prior to its passage was a huge mess for everyone involved. Services such as Apple Music and Spotify, up until now, have been responsible for identifying all the rights holders for each individual song in their massive catalogs. As Meredith Rose told The Verge in an October 2018 interview, streaming services historically had two options: go slowly in order to license each song individually, creating a very spotty catalog of offerings, or go fast and set aside a slush fund with the understanding that you were likely to get sued despite your best efforts at compliance due to the complexity of the licensing process.

A quick primer on music licensing may help explain a little of this complexity. Every song has two copyrights: one that covers the musical composition and lyrics, and another that covers the particular recording. A mechanical license covers the former, and every type of platform pays a flat fee for it. Performance licenses, which cover the particular recordings, vary widely in price and details. Services

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A Standoff, But Not A Standstill

By Larry M. Elkin, CPA, CFP®

The incoming 116th Congress will probably feature a legislative standoff between House Democrats and Senate Republicans, but that does not mean it will be quiet – or that nothing important will come out of the Capitol for the next two years.

Democrats, who gained 40 seats and control of the House of Representatives in the midterm elections, are likely to waste little time before they issue subpoenas and convene hearings over any number of matters involving President Donald Trump and his administration. One early target is likely to be the president's heretofore unreleased tax returns. Under Sec. 6103(f) of the Internal Revenue Code, the new chairman of the House Ways and Means Committee – Rep. Richard Neal, D-Mass. – can seek any tax return or taxpayer information from the Secretary of the Treasury, who "shall" provide that information. However, information regarding any specific taxpayer (including the president) can be released only to the committee when it is meeting in closed session, unless the taxpayer agrees otherwise.

It seems fairly likely that Trump, through Treasury Secretary Steve Mnuchin, will decline to release his returns on grounds that the committee cannot assure his privacy and has no legitimate oversight interest in the president's returns. That may not be a winning argument in court, but it will take some time to play out.

In the meantime, at some point between April and October this year, the president will file his 2018 tax returns, covering his second year in office. In all likelihood Trump will decline to release those returns, too.

For most of America's 140 million or so taxpayers, the more pressing question about taxes in this Congress is apt to be what sort of legislation is likely to come out of it. The answer is probably going to either be "nothing" or, at least, nothing especially bad. Republicans, who now hold a 53-47 edge in the Senate, are apt to reject any attempts by the House to roll back provisions of the 2017 tax overhaul, including a greatly increased estate tax exemption, much lower corporate tax rates, somewhat lower individual tax rates coupled with a higher standard deduction, and the new partial exemption for most income earned by individuals through pass-through business entities such as partnerships, S corporations and limited liability companies.

Except for the corporate tax rate cut, most of these provisions are scheduled to expire at the end of 2025. This expiration date may prove to be the basis for one potential area of compromise between the two parties. Democrats are largely opposed to the new law's limitation on deductions for state and local taxes, which disproportionately affects residents of the high-tax coastal states that favor their party. Sometime in the next two years, it's possible that Republicans may agree to relax the SALT deduction cap in return for an extension of other individual tax cuts beyond 2025. Democrats might be willing to gamble on that deal in hopes that, if they take control of the Senate and the White House in the 2020 elections, they can make further tax changes (read: higher rates for higher-income taxpayers and businesses) down the road.

Over in the Senate, an expanded majority will give Republican leader Mitch McConnell considerably more leeway to shepherd federal judges and executive branch nominees through the confirmation process. Democrats will continue to use the chamber's procedural rules to slow things down, but McConnell will no longer need to count on support from the two least-reliable Republican votes, Susan Collins of Maine and Lisa Murkowski of Alaska, to force a tie that can be broken in the GOP's favor by Vice President Mike Pence. Thus, the overhaul of the federal trial and appellate level judiciary in a more conservative direction is likely to proceed at a brisk pace for the next two years. This process is likely to be further energized by the promotion of Sen. Lindsey Graham of South Carolina to chairman of the Judiciary Committee, replacing Iowa's Sen. Chuck Grassley, who moved over to head the Senate Finance Committee.

Graham drew the national spotlight last fall when he verbally tore into Judiciary Committee Democrats over their treatment of Supreme Court nominee Brett Kavanaugh. "Boy, y'all want power," Graham told the panel's Democrats. "I hope you never get it." In this Congress and on that committee, Graham will wield the most power, amplified by the departure of frequent Trump critic Sen. Jeff Flake of Arizona.

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Sentinel

INVESTMENT FOCUS

Young Workers Rush Toward Retirement

By Larry M. Elkin, CPA, CFP®

One of the questions a financial planner gets asked most often is "Can I afford to retire at age [fill in your personal blank]?"

I am often bemused by this, because the answer is almost always "Yes, you can." It is also almost always "No, you can't." Nowadays, however, I may need to make room for a third possibility, namely: "Maybe, but why would you want to do such a thing?"

In the past, the retirement age question was usually posed by someone at least in his or her 30s or 40s, usually asking about a potential retirement at some point in their 50s, 60s or even older. In this traditional situation, retirement planning is a little like dieting. Dollars coming in via wages or investment earnings create a reserve of fat – that is, savings – for the financial winter ahead; dollars going out, in the form of pre- and post-retirement spending, consume those reserves. The question is whether the reserves can last as long as you do. And the answer can be whatever you choose, depending on what assumptions you make about income and spending, and how realistic those assumptions eventually prove to be.

The new twist arises because some young workers question the wisdom of spending their most productive years producing income for a later retirement. They want financial independence right away, or at least as soon as possible, and they want to retire early, too – sometimes at age 40 or sooner. The movement that has grown up around this desire is called "Financial Independence, Retire Early," often abbreviated FIRE.

Can it work? Sure it can, but also no, it can't. And would you really want to do this even if you could?

The first stage of the FIRE approach is to spend as little as possible, so as to save (and invest) as much as possible. FIRE adherents usually cite the figure of a net worth 25 times greater than the individual's annual expenses as fulfilling the "financially independent" part of the equation. Some people go further, pursing what they call "fatFIRE," the ability to maintain at least an upper-middle-class lifestyle.

I'm not sure there has ever been a financial planner who would accuse a client who is otherwise happy with life of saving too much. Perhaps more to the point, living an ultra-frugal lifestyle during one's working career might indicate a capacity for similar frugality in retirement. The less money going out, the longer the available pool of savings can last. So, sure – if you can save enough and survive contentedly on small enough spending, you can theoretically retire at almost any age.

This isn't the FIRE model, but think of a trust fund baby who is born with a hefty pile of money accumulated by someone else. In theory, and sometimes in practice, this person need never earn anything at all, as long as his or her spending is commensurate with the available wealth and the individual avoids destructive investments or excessive charity.

The new twist arises because some young workers question the wisdom of spending their most productive years producing income for a later retirement.

For the 99.9 percent of the population (my estimate) not covered by the trust fund baby scenario, the situation is a little different. During the working phase of life, must that person do something she really doesn't enjoy, just to accumulate enough money to stop doing this work as soon as possible? Can spending be kept so low as to accumulate

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...Retirement

the necessary funds without making life so bleak in the meantime as to make the exercise pointless and depressing? Can a person who buys into the FIRE philosophy find happiness with another soul whose priorities are different – or should FIRE have its own dating app? For all I know, it already might.

But the biggest question of all, in my mind, is what is meant by the concept of “retirement” at all. When Social Security was established eight decades ago, it was just a means of financial survival for someone whose body was typically worn out by the rigors of farm or factory work. Later it became a period of “golden years” leisure, often followed by a decline into a prolonged period of physical or mental frailty in advanced old age. But in all these cases, a person spent his or her most productive years being productive, in his or her own way. This, I think, is how nature built us.

Can a person who buys into the FIRE philosophy find happiness with another soul whose priorities are different – or should FIRE have its own dating app?

What does someone do when required to do nothing?

The answer, I suppose, is whatever that person wants. Early retirement from income-driven labor can be liberating. The young retiree is free to pursue community service, activism, art, politics or anything else the heart desires. In many cases, such pursuits may not generate a lot of income, but they generate enough for a frugal person (as a typical FIRE practitioner would be) to get by. This helps extend the previously accumulated nest egg.

When Social Security was established eight decades ago, it was just a means of financial survival for someone whose body was typically worn out by the rigors of farm or factory work.

But if a person truly had nothing to do except sit around all day and consume media, is this a good use of time? Is it even emotionally healthy? I have seen people who were forced out of the workforce early (sometimes due to corporate acquisitions or layoffs) obsess over investments or politics, merely to keep themselves mentally engaged. But too much cable news is bad for your emotional health. It is better to focus on loving the Yankees and hating the Red Sox, or vice versa – but even that leaves a long off-season to fill.

When I started doing retirement counseling about 30 years ago, a psychologist taught me that it’s useful to encourage clients to retire to something, rather than merely retire from something. I believed that advice then, and I still do.

Is the FIRE philosophy constructive or destructive? As with every question about retirement planning, I believe the answer is yes, it is. And also no, it’s not.

This blog post originally appeared on palisadeshudson.com in November 2018.

Welcome To 2019!

While we kept busy celebrating our 25th anniversary in 2018, we at Palisades Hudson are not easing slowly into the new year. We have opened a new office in Miami to better serve our clients in South Florida; the contact details are available on our website (palisadeshudson.com). You can also find the Miami office’s details on our brand-new Entertainment & Sports website, phentertainmentandsports.com, which showcases this growing practice area for our firm. And on Jan. 4, we released a fully revised second edition of our book, *Looking Ahead: Life, Family, Wealth and Business After 55*. We hope you have a productive, enjoyable and prosperous 2019.

PHES
PALISADES HUDSON
ENTERTAINMENT & SPORTS

...Standoff

The Senate's Republican majority now lines up much more solidly behind the president, not only due to Flake's retirement, but also that of Tennessee's Bob Corker and the death last summer of Sen. John McCain. Although they voted with the White House and congressional Republicans much more often than not, these three senators were all outspoken critics of the president's conduct and temperament, and often of his policy pronouncements as well.

The role of Republican critic is apt to be filled in the new Congress mostly by Mitt Romney. The 2012 presidential nominee enters the Senate, at age 71, as a freshman GOP senator from Utah. The question we might ask is why he bothered to run. The seat vacated by Orrin Hatch's retirement would have gone to pretty much any Republican candidate in the Beehive State. Given his age and his resume, Romney is presumably not hoping to rise very far through the Senate's seniority system. But perhaps he remembers that the late Sen. Strom Thurmond of South Carolina remained in the Senate past his 100th birthday.

More seriously, serving as a member of the Senate's most junior class for the next two years seems to offer Romney nothing except a platform from which to criticize the president, or possibly to challenge him for their party's nomination next year. During the 2016 primaries, Romney described Trump as a "phony" and a "fraud," and he remained one of the most strident members of the party's "never-Trump" wing up to Election Day. He has not warmed toward the president since then, either.

After the November midterms, Romney received a benediction of sorts from retiring House Speaker Paul Ryan, his 2012 vice presidential running mate. Ryan pronounced that Romney could follow McCain (the unsuccessful 2008 presidential candidate) as the GOP "standard-bearer."

Ordinarily, a sitting president would be considered his party's standard-bearer, particularly if that president is expected to run for re-election. Trump actually carried the Republican banner into the White House, while McCain and Romney both lost. In fairness, some might observe that McCain and Romney were bested by Barack Obama, who was the political equivalent of the NBA's Golden State Warriors. Trump defeated Hillary Clinton, whose closer basketball analogue is the New York Knicks.

This brings us to what might be the most important point about the 116th Congress: It is really just the prelude to the 2020 elections, which will usher in another legislature and perhaps another president. We are just about one year away from the Iowa caucuses and, right behind that, the New Hampshire primary. Even before 2019 is over, most of the political world will turn its attention to the 2020 campaign. At that point, except for top-priority matters, Congress is not apt to do much of anything.

It is therefore highly unlikely that this Congress will tackle long-term issues like Social Security and climate legislation in any significant way. Neither the consensus nor the will exists to deal with those subjects. And although it has been a centerpiece of both parties' platforms for years, health care is also most likely to be a nonevent for the next two years. Even the annual budgeting process, which was comparatively smooth under single-party rule in the last Congress (at least until a December 2018 imbroglio over border wall funding), is likely to be more fraught this time around.

Possibly the most fruitful area for action, apart from tax legislation, might be immigration, which is similarly high on both parties' agendas. But there is always room for surprises.

Here is one final thought to consider: Might Trump, who was something of a surprise candidate and even more of a surprise winner, decide that one term is enough? He could declare that he has made America great again and voluntarily become an ex-president four years earlier than most people assume. He likely would position Pence as his successor. You might even call Pence the newly anointed standard-bearer, which would be a way of Trump repaying Romney for his verbal abuse. Romney, the failed candidate, might be left to run against a vice president who would carry Trump's record without hauling Trump's baggage.

Could Trump be so vindictive, or just so reluctant to risk leaving the White House as a loser, as to walk out on the world's most powerful job? Might the man famous for declaring "you're fired" decide to simply quit rather than hear those words from the American electorate?

We will see in due course. In the meantime, get ready for a year of political stalemate, but don't expect it to be boring.

...Music

where listeners can't pick the next song, such as Pandora, can pay for a license the way that radio stations do; this lets them pay a single, blanket fee to both performers and songwriters for every song. But user-controlled interactive streaming services do not have that option.

Before the Music Modernization Act, there was no entity allowed to issue a blanket license to companies that wanted one. That was largely because no one database tracked royalty information. Instead, individual publishers, labels and artists were responsible for tracking down the royalties they were owed. Some songs have been misattributed, meaning the wrong person got paid; others were not assigned to anyone, so no one got paid.

Previously, streaming platforms that lacked the data to pay rights holders issued Notices of Intent, often abbreviated NOI, to the U.S. Copyright office. These notices indicated that the service had tracked a mechanical royalty but could not identify its owner. This process was meant to shield them from liability, but the problem of missing rights information was so persistent that the Copyright office was buried in them; the office received more than 50 million by the end of 2017, according to Billboard.

The Music Modernization Act creates a new legal process for handling unclaimed royalties connected to mechanical licensing. Now the music licensing collective will keep track of rights holders, creating and maintaining a public database of song ownership information. Songwriters will be able to quickly identify instances where they did not receive proper attribution, and services will be able to avoid lawsuits stemming from identifying rights holders for a song incorrectly. Services that want a blanket license will now rely on the database to make sure all the right people get paid. The new system both creates transparency for artists and removes liability for music services.

In addition, the law changes how the copyright royalty board sets royalty rates for services licensing music to stream. Prior to this legislation, the law forbade federal rate courts from considering sound recording royalty rates as a relevant factor in determining the rates for public performance royalties. Now rights holders will be able to present evidence, including rates for other services within the recording industry, in the pursuit of fairer royalty rates.

It also changes the way royalty disputes will be decided. The American Society of Composers, Authors and Publishers (ASCAP) and Broadcast Music, Inc. (BMI) serve as the two leading "performing rights organizations" in the U.S., which means they are party to nearly all royalty rate disputes for the music industry. Formerly, each organization was assigned one judge from the Southern District of New York, who adjudicated all rate dispute cases for the organization. Under the new law, a group of judges from that district will consider these cases in rotation. This new system is intended to provide a situation in which judges evaluate each case on its own merits, rather than based on cumulative impressions from other cases.

Recordings made prior to 1972 were formerly not protected under federal copyright law, but instead a patchwork of state-level laws.

While the new process for handling streaming royalties understandably made the most headlines, the other two components of this law are also important, if less far-reaching. Recordings made prior to 1972 were formerly not protected under federal copyright law, but instead a patchwork of state-level laws. Artists who made these recordings largely received royalties, if at all, according to whatever terms their contracts had dictated – and, understandably, none of these contracts included language about digital or streaming rights. The new law specifies that 50 percent of streaming royalties for pre-1972 recordings will go to the label, and 50 percent will go to the artists.

The final piece established a legal procedure for producers and engineers to collect royalties when satellite or online radio stations play their recordings. Their right to royalties is not new, but previously it was sometimes hard to collect. The new process looks similar to that already used by SoundExchange, the organization that collects and distributes digital performance royalties for sound recordings. SoundExchange allows artists who opt in to pay producers and engineers their royalty shares directly. In essence, the law formalizes the existing process to make sure these royalty holders get what they are due.

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...Music

Controversy

While this law garnered widespread support from artists, labels and publishers, a few individuals and groups have raised concerns.

One of the responsibilities of the music licensing collective that will maintain the royalty databases and administer blanket licenses will be to hold unclaimed royalties. The law stipulates that the entity must hold these royalties for at least three years, after which it can distribute them to copyright owners on a market-share basis if they remain unclaimed. Since the system is based on market-share, the largest publishers stand to benefit most from unclaimed royalties, even if they don't own the copyrights to the songs in question.

Some opponents of the bill worry that this system would disadvantage smaller industry players, especially as the system pertains to unclaimed mechanical royalties at the time the law takes effect. No one knows exactly how many notice of intent filings are currently on hold at the U.S. Copyright office – other than "a lot" – so there could be a substantial amount of money already in play. It is also unclear whether the collective will stick firmly to the three-year deadline or allow a longer grace period, especially at first. Such uncertainty has made some rights holders nervous.

The major opponent to the Music Modernization Act prior to passage was SiriusXM, which argued that the law would subject it to unfair restrictions compared to its terrestrial radio competitors. But due to several changes just prior to Senate approval, including the 50-50 split for artists and labels for pre-1972 recordings, Sirius ultimately reversed its position and stated its support for the legislation.

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What Rights Holders Should Do

First, I will state that I am not a lawyer, and this legislation is brand-new. This means that your lawyer or business manager will likely have a better sense of what particular facets of this complex law most directly affect your career. However, songwriters, musicians and others who have copyright claims on audio recordings would be wise to take some basic steps to prepare for the changes the Music Modernization Act will implement.

If you do not already have a detailed catalog of your work, go ahead and take stock of the recordings you have worked on in the past. To the extent you are able, identify streams for which you have not yet been paid mechanical royalties using statements provided by streaming services or examining stream counts of recordings of your composition in the music service where they have streamed and comparing them with your payments. The music licensing collective will not arrive overnight; the parties involved will need to agree on board members and draft regulations, not to mention the work involved in actually creating the database. The more detail you can track down in advance, the easier it will be to check your information once the database is live and ensure you receive proper credit for your work. If it functions as designed, the database will make correcting errors and filling in missing information much easier than it currently is, and it will pay to be ready to make the most of it.

Publishers and songwriters must register with the music licensing collective somehow, but it is not yet clear what this process will look like or how much individual artists will need to do to ensure their rights are protected. It is wise to keep an eye on this process as it unfolds and comply with any requirements promptly as they arise.

Digital streaming services and copyright owners have nine months to reach an agreement on the specifics of how to fund the collective for its first two years. The collective must begin operations by Jan. 1, 2021, which is when blanket licenses also take effect. Between now and then, anyone with a stake in recorded music should make an effort to prepare to make the most of a system better designed to make sure everyone gets their due.

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Wisconsin Offers Balm For SALT Wounds. Wisconsin joined the parade of states seeking to offer workarounds for the new $10,000 itemized deduction limit for state and local taxes. The Badger State's approach is to offer pass-through entities – partnerships and S corporations – the option to pay a flat entity-level tax of 7.9 percent, which is still deductible as a business expense. In exchange, the entity's owners would receive an offsetting income tax exclusion for their share of the taxable income generated by the company. The 7.9 percent rate matches Wisconsin's tax on corporate income, and it is higher than the state's top personal income tax bracket of 7.65 percent. As a result, the new approach will be beneficial to some companies and some owners, but not to others. *Public Act 368*, 2018 STT 243-28.

Regulations Proposed For Opportunity Zone Tax Break. The Treasury Department and Internal Revenue Service issued proposed regulations to implement the Opportunity Zone tax incentive that was enacted under the 2017 tax overhaul. The program allows taxpayers to defer taxes on capital gains by investing in a "qualified opportunity fund" within 180 days. Tax on up to 15 percent of the deferred gain may be forgiven if the investment is held for at least seven years, but any remaining deferred gain is reported on the taxpayer's 2026 return. If the qualifying investment is held for at least 10 years, tax on any appreciation above the original investment through 2047 is also forgiven. *IR-2018-206*.

Untying The Knot Is More Expensive In 2019. Couples that were unable to finalize a divorce by Dec. 31 will find that, as a rule, breaking up is costlier in the new year. The longstanding rules that made alimony deductible to the payer (and taxable to the recipient) were repealed under a provision of the 2017 tax overhaul that had a delayed effective date to avoid catching soon-to-be-ex-spouses unawares. Because payers tend to be in higher tax brackets than alimony recipients, the change means the IRS will now collect a bigger slice of the divisible pie. The new provision does not affect unmodified divorce decrees that were finalized before 2019. It also does not affect child support or property settlements, neither of which had any tax effect under either the old or the new law.

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