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How To REALLY Get Ready For Your Retirement Years

According to the U.S. Census Bureau, about 77 million "baby boomers"—people born between 1946 and 1964—were alive when the first wave of boomers turned age 65 in 2011. Now, more than 10,000 baby boomers celebrate their 65th birthdays every day, and by 2030 those who are 65 and older will represent an estimated 20% of the entire U.S. population.

If you're part of this demographic surge, it's essential to plan ahead for your pending retirement, which is likely to last much longer than those of previous generations. Someone who's 65 now can expect to live to 84.3, on average, according to the National Center for Health Statistics. So you easily could live for 20 years or longer after you retire.

How can you prepare financially for what's ahead? While there are no guarantees, these three ideas can be sound strategies for the future:

1. Slide into retirement gradually. Retirement doesn't have to be like a bandage that you rip off quickly. Staying on the job longer has obvious financial advantages. If you're still earning a paycheck, you probably won't need to take early Social Security benefits or distributions from your retirement plans or IRAs, and waiting longer to begin your withdrawals will mean bigger payouts. But a gradual transition to retirement also may help in other ways. Many people simply aren't able to cope with such a drastic lifestyle change in one fell swoop.

If you've been an executive, or you're a business owner or partner, you may be able to stop working full time but continue as a consultant. That can help your company, too, and you may retain some valuable fringe benefits. In addition, when you work part time, you can continue to contribute to retirement plans and IRAs.

2. Time your Social Security benefits. Deciding to keep working at least part time can affect when you file to begin receiving Social Security retiree benefits. You can start as early as age 62, but the monthly amount you receive then will be about 25% less than if you'd waited until the normal retirement age for full benefits (age 66 for most baby boomers). If you delay benefits beyond full retirement age, your monthly benefit will increase by 8% each year you delay up to age 70.

Deciding when to begin benefits requires an in-depth analysis of your

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What Do You Think Your Life Will Be Like In Retirement?

Much that is written about or spoken about retirement relates to the need to save for your life after work. How much have you accumulated? How much more do you need to save? How is your money invested? Should you downsize your home? Have you planned far enough into the future?

These are all legitimate questions you'll want to address well in advance of the day you finally call it quits. But are you also asking yourself the "other" question: What will my retirement be like? Your lifestyle is likely to change drastically when you retire, and it's a good idea to try to prepare yourself for the road ahead.

Recognize that the changes aren't just financial. Are you mentally and physically ready for retirement? Often, people who stop working wonder what to do with all of their free time. Here are some of the possibilities you might want to consider:

- Start or expand a hobby.
- Join a gym or take up golf or another sport.
- Become active in a seniors group.
- Volunteer for charity work.
- Travel extensively.
- Go back to school or otherwise learn a new skill.
- Go back to work on a part-time basis (perhaps as a consultant).

These activities may provide purpose and meaning in the years ahead as you focus on the quality of life you hope to enjoy in retirement. It's just as important to set your sights on your personal objectives as it is to save enough money to live on.

Kim Scott, CFP®
Financial Advisor

Keep Eyes On Estate Tax Proposals

In his 2015 State of the Union address, President Obama laid the groundwork for several significant estate tax changes, which were covered in greater detail in the administration's budget plan for the 2016 fiscal year. Although these proposals are a long way from being enacted, it makes sense to know the key concepts now. Here are several:

Capital gains: When you inherit assets, you currently benefit from a "step-up in basis" to the fair market value (FMV) of the assets on the date of death. Say you receive stock acquired for $5,000 that's worth $15,000 when you inherit it—your basis is $15,000. Sell the shares for that amount and you'll owe nothing in taxes. The $10,000 appreciation in value is tax-free forever.

Under the president's proposal, this "trust fund loophole," so-called because it's often used in conjunction with trusts, would be closed. Instead, you would owe tax on the difference between the original basis and the FMV on the date of death through a "deemed sale." In our example, that would mean a taxable gain of $10,000. The proposal does allow a taxable exclusion on such gains of $100,000 per person ($200,000 for a married couple).

Estate and gift tax exemptions: The president would roll back the estate and gift tax exemptions to 2009 levels. Thus, the $5.43 million exemption in 2015 (inflation-indexed increases have moved it up from an original $5 million) would revert to a $3.5 million exemption, and so would the generation-skipping tax exemption. And whereas the current exemption can be used for a combination of gifts made while you're alive and at your death, the new $3.5-million exemption would apply only to estates. There would be a separate $1-million lifetime exemption for gift taxes. Finally, the top estate tax rate would be raised from 40% to 45%.

Grantor retained annuity trusts: The grantor retained annuity trust (GRAT) has been in the crosshairs of the Obama administration for some time. With this estate planning technique, you create an irrevocable trust for a specified term, funding it with assets, and then an annuity is paid to you based on IRS-approved interest rates. Eventually, the remaining assets go to your beneficiaries tax-free.

The president's proposals would curtail the tax benefits by (1) requiring a minimum term of 10 years, (2) imposing a minimum remainder interest of 25% of the assets transferred to the trust, or $500,000, whichever is greater, and (3) prohibiting the grantor from participating in a tax-free exchange of assets with the GRAT. These changes effectively would eliminate future GRATs.

Of course, you shouldn't overhaul your estate plan based on these proposals, but do be prepared to update your plan if it looks as if they may become law. ●

Here's What You Can't Do In An IRA

If you have an IRA, you know how easy it is to move assets from one investment to another. You're able to choose from a wide array of investment options, and to take out money whenever you want, although you'll have to pay tax when you do. But there are some things you can't do with an IRA. There are strict rules against certain "prohibited transactions," which are spelled out in the tax laws. And there could be adverse consequences if you don't comply with the requirements.

The IRS defines a prohibited transaction as any improper use of an IRA by the owner, his or her beneficiary, or any "disqualified" person. That last includes IRA fiduciaries and members of the owner's family. An IRA fiduciary is someone who (1) exercises any discretionary authority or control in managing the IRA or exercises authority or control in managing or disposing of its assets; (2) provides investment advice to the IRA for a fee, or has any authority or responsibility for doing so; or (3) has discretionary authority or responsibility for administering the IRA.

What can't you do with your IRA? You're prohibited from:

- Borrowing money from it;
- Selling property to it;
- Using it as security for a loan;
- Buying property for personal use with IRA funds.

You can, however, effectively take a short-term loan from your IRA by withdrawing funds from it and then depositing the same amount back into the same or a different IRA within 60 days. That is technically a "rollover" and is not treated as a prohibited transaction.

If a prohibited transaction occurs, your account stops being an IRA as of the first day of the year of the violation. The net effect is that you're treated as having received a distribution of all of

The Reality Behind 6 Estate Planning Myths

Some people avoid estate planning at all costs. But putting aside the inevitable emotions involved in looking ahead to your own demise, it's crucial to understand the process. A good place to start is by debunking these six common but potentially damaging myths:

Myth #1: My estate is too small to need an estate plan.

Reality: You don't need a small fortune for your heirs to benefit from estate planning. For instance, what if you decide to divide your assets among several beneficiaries, instead of designating just your spouse or another person? That could be very important if you're in a second or third marriage and have children from a previous marriage. In addition, you might want to leave some of your estate to charity. Wanting to help your family avoid the delays of probate, seeking to reduce estate taxes, and choosing who will administer your estate also call for estate planning.

Myth #2: I don't need an estate plan because my spouse will inherit everything.

Reality: This is closely related to the first myth. Just because you have left everything to your spouse under your will—and your spouse has returned the favor—doesn't mean you won't benefit from estate planning. What happens if your spouse dies first at a relatively early age, or if you die together in an accident? What then? There might be complications because of how assets are titled, who are named as beneficiaries of your life insurance policies and your retirement plans, or the estate laws of your state.

Myth #3: If you're wealthy, there's no way to avoid estate taxes.

Reality: That's simply not true. On the federal level, your estate can benefit from a generous $5.43 million exemption for those dying in 2015 (and that amount is indexed for inflation and will rise in future years). What's more, because you or your spouse can use the other's leftover exemption, the effective amount the two of you can shield from estate taxes is almost $11 million. Trusts and other tax- saving vehicles can further reduce estate tax exposure. Although state inheritance tax rules aren't always as generous, professional guidance may help there, too.

Myth #4: Everything is covered in my will so estate planning isn't necessary.

Reality: While a will is a good starting place for an estate plan, it's not likely to be enough on its own. There may be numerous other loose ends to tie up. In addition, depending on your state's laws, your heirs may have to go through a lengthy probate process that can be even more drawn out if you owned property in several states. A revocable living trust can help you pass some assets to your heirs without probate, and your will probably also should be accompanied by a durable power of attorney authorizing a family member or a professional to act on your behalf if you're incapacitated.

Myth #5: I don't have to worry about life insurance and retirement plan designations.

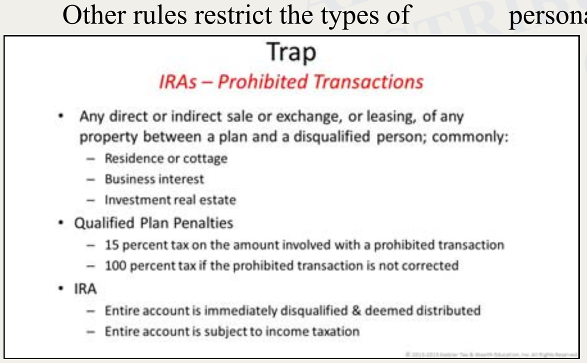
Reality: This is overstating the case. Although the beneficiary designations you've made for life insurance and retirement plans, as well as for your IRAs, are a good start, you still need to coordinate those choices with other aspects of your estate plan. You might want to revise your designations, for example if you get divorced or a spouse dies, or you could need to add secondary or contingent beneficiaries. Also, proceeds from life insurance are included in the taxable estate of the insured, although the proceeds generally will be excluded if you transfer ownership of the policy to someone else or a trust.

Myth #6: Once my estate plan is complete, I don't have to do anything else.

Reality: Nothing could be further from the truth. Your family and financial circumstances almost certainly will continue to evolve, and your estate plan needs to reflect significant changes. Marriage, divorce, or the birth of children or grandchildren all could have an impact. And the best-laid plans could be affected by a disability or unexpected death of a spouse. Finally, your plan may have to be fine-tuned to take other events into account, especially if the estate tax laws are revised again. So be sure to review your plan periodically and revise it when necessary. ●

the IRA assets equal to their fair market value (FMV) on January 1 of that year. Assuming the total FMV exceeds your basis in the assets, you owe tax on the difference, just like you would on any other withdrawal. Plus, you're generally required to pay a 10% penalty if you're younger than 59½.

Other rules restrict the types of investments you can make in an IRA. For instance, you can't invest in life insurance or collectibles such as works of art, stamps, precious stones, or jewelry. With a few limited exceptions, IRA funds also can't be invested in gold or silver coins. And the IRA can't hold any property that you personally use, such as your primary residence or a vacation home. Holding certain other types of real estate, however, such as undeveloped land, may be permitted.



The tax law gives you plenty of leeway with regard to IRAs, but there are limits to that freedom. Make sure not to step over the line. ●

Raiding A Roth Early? No Woes

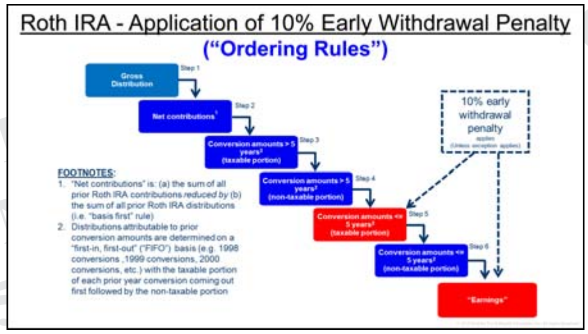
What happens if you take funds out of a Roth IRA well before retirement? The tax ramifications might not be particularly dire. Early payouts are frequently tax-free, or mostly tax-free, even if you don't meet the requirements for "qualified" distributions.

It all has to do with the "ordering rules" for Roth IRAs. It's important to get a firm grasp on these rules so you can plan your withdrawals accordingly.

Contributions to a Roth IRA are never tax-deductible, but qualified distributions are tax-free. For this purpose, "qualified" means withdrawals made from a Roth you've had for at least five years if you've reached age 59½; the payout is because of your death or disability; or you use the funds to pay qualified homebuyer expenses (up to a $10,000 lifetime limit).

But sometimes you just can't wait until age 59½ or for the Roth IRA to hit the five-year mark. In this case, and **assuming you don't have another viable alternative**, you can raid the Roth for the funds you need. Is it a tax disaster? Not usually. The tax is computed under generous rules that can save you from owing anything. Specifically, distributions from a Roth IRA are treated as if they occurred in the following order:

- Roth IRA contributions. Because you didn't get a tax break when you put in this money, you aren't taxed when you withdraw it.
- Contributions from converting a traditional IRA into a Roth. The same principle applies here. Because you already were taxed on the distribution from the traditional IRA that went into your Roth, you can take out those funds without being taxed again.



- Contributions from converting nontaxable traditional IRA balances into a Roth. These, too, aren't subject to regular tax when you withdraw them from the Roth.
- Roth IRA earnings. These, finally, are taxable when withdrawn unless they meet the definition of qualified distributions.

These ordering rules can work in your favor. For example, suppose you have $100,000 in a Roth you established four years ago—$25,000 in contributions, $50,000 in taxable conversions, $15,000 in nontaxable conversions, and $10,000 in earnings. If you withdraw $35,000, the distribution is treated as having come from the $25,000 in contributions and $10,000 from taxable conversion contributions. So the entire payout is tax-free even though it isn't a qualified distribution.

Note that you'll have to pay tax at ordinary income rates for nonqualified distributions. In addition, there's normally a 10% tax penalty on such withdrawals made before age 59½.

Remember that withdrawing funds early from a Roth IRA isn't optimal, because it reduces the amount you'll have available in the future. However, it's comforting to know that you may be able to pull out cash tax-free if you need to. ●

Get Ready For Your Retirement

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circumstances. Also, keep in mind that you may have to forfeit some Social Security benefits if you're still working before your full retirement age. Usually, it doesn't make sense to apply for benefits if you then have to give back part of the monthly payout.

3. Take systematic withdrawals. When it comes time to start taking distributions from the assets you've accumulated—and the longer you can postpone this, the better—it's wise to be systematic about it. One traditional method is to use a 4% solution, withdrawing 4% of your account balances in the first year and then adjusting subsequent distributions based on market performance, inflation, and other factors. Yet there are limitations to that approach, and we can work with you to assess your personal situation and create a customized, systematic approach that works for you.

However you proceed, there are a few basic guidelines about when to tap each of your sources of retirement income. It's normally best to start with taxable accounts, such as stock and mutual fund holdings that aren't in tax-advantaged retirement accounts. Generally, these distributions will result in long-term capital gains, taxed at a maximum rate of 15% for most investors and 20% if you're in the top tax bracket for ordinary income. Then you can take money from traditional IRAs and retirement plans such as 401(k)s; that income will be taxed at your ordinary income rates. You'll likely want to save Roth IRAs for last. Unlike with other retirement accounts, which generally require you to take minimum withdrawals after age 70½, you can leave your money in a Roth as long as you like, and distributions from these accounts generally won't be taxed.

These three strategies aren't all you'll need to consider in positioning yourself for a long retirement. But making a gradual transition into your retirement years, figuring out the best timing for your Social Security benefits, and tapping your assets in a logical order can go a long way toward improving your chances for a successful retirement. ●