Financial Services Advisory
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Live Longer And Prosper In Your Golden Years

Are you part of the baby boomer generation that now is surging into retirement? Or are you a member of "Generation X," which isn't far behind? In either case, some traditional ideas about retirement no longer may apply.

For one thing, people now live longer than in the past, which means that their golden years will last longer, too. The average life expectancy for someone in the U.S. who now is age 65 is 84.3 years. And that number, which has grown steadily for many decades, is expected to go even higher.

Maybe the "new" 65 is 70 or even 75.

What is the main implication of this change? By living longer, it's likely you'll have to save more for retirement, or figure out ways to stretch your dollars further if you want to maintain a comfortable lifestyle. If you do nothing, you could run the risk of outliving your retirement savings. You'll also have a lot less, if anything at all, to pass on to your heirs.

Fortunately, there are several potential solutions to this dilemma. Consider these six options:

1. Invest for the longer term. You're already in it for the long haul. But some additional tinkering with your investment portfolio may allow your assets to last even longer. For example, you could minimize some risks of a market downturn by making sure you have a well-diversified portfolio with an exit strategy. Of course, there are no guarantees against a loss of principal, especially in a declining market.

2. Bulk up your 401(k) and IRAs. Assuming you're still working full-time, do whatever you can to boost your annual contributions to your 401(k) plan and IRAs. For 2017, someone age 50 or over can contribute a maximum of $24,000 to a 401(k) and $6,500 to an IRA. (The 2017 figures are $18,000 and $5,500, respectively, for younger savers.) Your IRA contribution could be split between a traditional IRA and a Roth IRA.

3. Postpone Social Security benefits. Although you can receive your full Social Security retirement benefits at your "full retirement age" (FRA)—age 66 for most baby boomers—you're entitled to even higher monthly benefits if you postpone taking benefits until as late as age 70. This may be preferable if you expect to live a long time.

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Convert To A Roth IRA Now To Avoid Higher Taxes Later?

Should you convert your traditional IRA to a Roth IRA? A key factor in this decision is taxes. If you expect to be in a higher tax bracket during retirement than you are now, a conversion may make perfect sense. But if you anticipate being in a lower tax bracket then, you could decide to sit tight.

With a traditional IRA, contributions may be wholly or partially deductible, but distributions generally are taxed at ordinary income rates. You never can deduct Roth contributions, but payouts from a Roth after five years are tax-free if you've reached age 59½ by then. The trick is to figure out whether the promise of future tax-free distributions is worth the current tax price on a conversion. The amount you convert will be treated as a distribution and taxed at your rate for ordinary income.

As you weigh your options, don't overlook the favorable tax rates for joint filers. For instance, a taxable income of $200,000 puts you in the 33% bracket as a single filer, but if you're married, that same income level puts you in only the 28% bracket as a joint filer. Remember, though, that if one spouse is significantly older than the other or in ill health, a surviving spouse may end up paying higher tax in retirement as a single filer. Similarly, an inheritance could push you into a higher bracket at that point.

Give us a call for help determining whether or not a Roth conversion can help you achieve your retirement goals.

Kim Scott, CFP®
Financial Advisor

Lending Money? Watch Your Tax Step

Doug Burnside is in a quandary. His daughter, Megan, needs money to get a new business venture going. But Doug can't afford to give her the money outright and she has had trouble getting a loan from a bank.

What can be done? One idea is for Doug to lend his daughter the cash. Megan can repay Doug, with interest, if the business succeeds. Everyone wins.

But this kind of intra-family loan brings several potential tax pitfalls. As long as the loan is for \$10,000 or less, there won't be a problem. However, if the borrowed amount is larger and he doesn't charge the going rate of interest, the IRS will "impute" interest for him, based on its own assumptions. He'll end up being treated as if he had charged his daughter interest, even though he hadn't, and he'll owe tax on that "phantom income" that he didn't receive.

In such cases, if the loan is for \$100,000 or less, the interest you will be considered to have received annually for tax purposes is limited to the amount of your child's net investment income for the year. And if that amount doesn't exceed \$1,000, you can avoid taxable interest income on the intra-family loan. But the IRS may still intercede if it suspects that you're trying to dodge the tax liability.

How do you figure out what the "going rate" for interest is? It depends on several factors, including the type of loan, its length, and the interest rates in your local area. You might be able to charge slightly less than a local bank would get, but you can't go overboard.

What happens if Megan's business fails and she can't pay Doug back? The IRS could determine that the "loan" was always meant to be a gift. To avoid that problem, it's best to have an attorney draft a formal loan document. It should include the usual terms that would be found in a bank loan. For instance, the document will usually indicate:

- The amount of the loan;
- The time allowed for repayment;
- The interest rate structure;
- A description of the collateral securing the loan.

Finally, have the loan document witnessed and notarized. This is the best proof you can have if the IRS ever challenges the deal. Be sure to give us a call to discuss any potential issues before lending friends or family a significant amount of money. ●

How To Spell Estate Tax Relief

Here's an acronym you've probably never heard of: DSUE, pronounced D-Sue, it stands for deceased spouse's unused exemption, and it could be a crucial component of your estate plan.

Frequently, a plan relies on two key tax-saving provisions—the unlimited marital deduction and the unified estate and gift tax exemption. Under the marital deduction, a spouse normally doesn't have to pay estate or gift tax on any property transferred from a spouse. The estate and gift tax exemption covers transfers to your children or other non-spouses up to \$5.49 million in 2017.

That means that a married couple together can transfer almost \$11 million to others without a penny of tax liability. Even better, the exemption is "portable" between spouses—so when the estate of the spouse who dies first doesn't exhaust all of that person's exemption, it can be used by the estate of the second spouse.

Normally, an estate tax return has to be filed only if an estate is worth more than the maximum exemption. However, a return will also have to be filed to take advantage of DSUE.

Consider this hypothetical example. A husband died early in 2017 with assets valued at \$8.49 million. He left \$5 million to his wife and the other \$3.49 million to their children. Thus, the amount of the DSUE—the \$5.49 million exemption minus the amount given to non-spouses—is \$2 million.

Now say that the wife dies late in the year with an estate valued at \$7.9 million (\$5 million from the husband and \$2 million of her own assets). Thanks to DSUE, her estate can add that \$2 million to the \$5.49 million of her own exemption to cover her entire estate. Without DSUE, her estate would owe estate

Finding The Balance For Retirement Draw-Downs

Victor and Jane Muratti, a computer analyst and schoolteacher married for more than 30 years, are nearing retirement. Over the years, they have accumulated a mosaic of investments, including stocks, corporate and municipal bonds, mutual funds, exchange-traded funds (ETFs), annuities, real estate, and master limited partnerships (MLPs). Some of these investments are in taxable accounts while others are in tax-deferred retirement plans and traditional and Roth IRAs.

Once they retire, the Murattis will begin drawing income from these various accounts, and after they reach age 70½, they'll have to start taking required minimum distributions (RMDs) from their retirement plans and IRAs. But they don't have a clue about the best way to create their retirement "paychecks."

It's a common situation and the circumstances will vary for every person or couple. However, one typical objective is to minimize federal income tax from investment transactions, while preserving as much wealth as you can for a lengthy retirement.

One way to do that is by paying attention to tax brackets. Income taxes are based on a graduated seven-bracket system, with different tax rates for each bracket. The more of your income that falls into lower brackets—and so is taxed at lower rates—the better. And to the extent that you can control how much income you receive, you could try to take just enough to fill up your current bracket without moving into the next, higher one. You can use this tax bracket management strategy throughout retirement.

But to benefit, you'll need to learn the basics for three different types of accounts you're likely to tap during retirement.

1. Taxable accounts: This category includes all of the investments you hold outside of retirement plans. You may have stocks, bonds, mutual funds and ETFs, as well as interest-bearing savings accounts and certificates of deposit (CDs). If you sell any of these at a gain, your profit will generally be taxed at the favorable rate for long-term capital gains—that is, gains on investments you've held for a year or more. The tax rate for long-term gains is 15%, or 20% if your income puts you in the top tax bracket for ordinary income. Most dividend income from stocks is also taxed at 15% or 20%. But interest from bonds and other investments is likely to be taxed at the higher rates for ordinary income.

2. Tax-deferred accounts: Within tax-deferred accounts such as 401(k) plans and traditional IRAs, capital gains and income from dividends and interest all can accumulate without being taxed. But once you start taking money out of these accounts during retirement, all or most of your withdrawals will be taxed as ordinary income. And when RMDs come along, some of the money *must* come out every year.

3. Tax-free accounts: Of course, no taxes are better than low taxes, and a Roth IRA may give you retirement income that isn't taxed at all. With a Roth IRA that you've had for at least five years, withdrawals after age 59½ are completely tax-free. Meanwhile, although interest income from most bonds is taxed at ordinary income rates, income from municipal bonds or municipal bond funds can be tax-exempt. These bonds could be a valuable part of your retirement portfolio.

When considering which account to draw from and in what order, a common strategy is to take RMDs first—because you must make those withdrawals—then tap your taxable accounts next, leaving assets in tax-deferred accounts to grow without being eroded by taxes for as long as possible. Finally, make tax-free withdrawals from your Roth IRA, which offers the additional advantage of not requiring distributions during your lifetime.

In addition, to the extent you can, you might practice tax bracket management, capping your taxable income at a level that will let you avoid moving into a higher bracket. So that even if you can't avoid taxes entirely during retirement, you may be able to keep them under control.

Everyone's distribution strategy in retirement is unique to their situation. Feel free to reach out to us for help developing your own strategy for creating your retirement "paycheck." ●

tax of 40% of $2 million, for an estate tax bill of $800,000.

Even if a surviving spouse remarries, he or she maintains the DSUE from the previous spouse. However, you can't use a DSUE from more than one spouse.

Finally, keep in mind that the $5.49 million exemption gets higher every year to account for inflation, but the DSUE remains locked into the amount that was available when the first spouse died.

If you are concerned about estate taxes, we are happy to work with you and your attorney to develop a plan that fits your situation. ●

This Tax-Free Rollover Goes Right To Charity

The tax law provides a unique planning opportunity for retirees who have to take required minimum distributions (RMDs). You're allowed to transfer funds directly from your traditional IRA to a qualified charitable organization without paying any federal income tax on the distribution. Although the contribution isn't tax deductible, it does count toward your RMD for the year.

This tax break—sometimes called a "charitable rollover"—had expired and been reinstated several times. Thanks to the Protecting Americans from Tax Hikes (PATH) Act of 2015, however, the tax provision is now permanent.

Under the PATH Act, someone who's at least age 70½—the age at which RMDs must begin—can instruct an IRA custodian to move up to $100,000 of funds from that person's IRA to a favorite charity. A married couple can transfer up to $200,000, assuming they're both old enough to begin taking RMDs.

Can't you accomplish the same result by taking a taxable IRA distribution and then donating that amount to charity? Not exactly. There are several other factors to consider, including annual limits on deductions for donations to charity, plus potential tax return complications. What's more, the direct rollover is valuable to non-itemizers who aren't eligible to deduct charitable contributions. And this method is simpler.

There are, however, a few more details to attend to with this approach. To qualify for the tax exclusion, the distribution must be made directly from the IRA trustee to a qualified charitable organization. You're not allowed to use the funds temporarily before transferring them to the charity's coffers.

In addition, the contribution must otherwise qualify as a charitable donation. If the deductible amount decreases because of a benefit received in return — for example, the value of a dinner at a fundraiser — or the deduction would not be allowed due to inadequate substantiation, you can't take the exclusion.

A bonus is that you're required to start taking RMDs in the year after the year in which you turn age 70½. If you take a charitable rollover, you can meet this obligation without paying the usual tax on an IRA distribution.

This tax law provision also applies to Roth IRAs, though it may not be advisable to take this approach with a Roth. Roth IRA distributions to account holders over age 59½ are usually tax-free, and it doesn't make sense to use money that isn't taxed to make a donation that isn't deductible. If your are considering using your funds from a retirement account to donate to your favorite charity, give us a call to discuss whether or not this strategy is the best way to accomplish your goals. ●

Prosper In Your Golden Years

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4. Slow down RMDs. After you reach age 70½, you normally have to take required minimum distributions (RMDs) from traditional retirement plans such as 401(k)s and IRAs. The minimum amount you must withdraw is based on your life expectancy and the account balance on December 31 of the prior year. If you can resist the temptation to take more than you're legally required to you'll preserve more of your assets for retirement.

5. Consider the tax implications. When you need to start withdrawing funds for retirement, where should you turn first? This is a complex decision that requires careful thought as far as taxes are concerned. For example, if you anticipate being in a higher tax bracket during retirement than you are now, you might withdraw funds from taxable accounts first and Roth IRAs last, so the Roth funds can keep growing tax-free. If you expect your tax bracket to plummet, you might do the opposite. Financial and tax advisors can help you devise a strategy that works for you.

6. Work for a longer time. If you still think your retirement is underfunded, you might postpone retirement by working full-time for an extra few years, or you could use the earnings from a part-time job to supplement your retirement income. Call us to put together a plan that works for you. ●