Norman J. Politziner's
Financial Planning

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Tax Alert: Plan Now For The Demise Of Stretch IRAs

Say goodbye to the stretch IRA! That's the message from Congress, where a pending bill with bipartisan support would deep-six this tax-advantaged practice. Stretch IRAs have been a boon to non-spouse beneficiaries who inherit a retirement account because they can extend the period of tax-free growth on an inherited IRA over their expected lifetime.

Under current rules, for purposes of illustration, assume a father dies and bequeaths his 40-year-old daughter his individual retirement account. The tax code requires that she takes distributions out of the account every year. But she can extend that to over her actuarially expected lifespan codified in a table published by the IRS.

An heir can expect to live to 95, according to actuarial tables. That means a 40-year-old female heir can avoid taking the money all at once in a lump sum — and won't have to pay the IRS a big chunk of it. Instead, you can withdraw just 1/55th of the IRA amount annually, which obviously is less money than the whole of it, but also has less of a tax bite. Meanwhile, by extending the payout period, the account can grow in value over the decades, giving you more money than the sum you inherited.

Congress, however, is intent on ending this good thing. The legislation, called the Setting Every Community Up for Retirement Enhancement Act, or SECURE, passed the House of Representatives by a whopping 417 to 3. A similar version is pending in the Senate.

The law contains provisions that would be beneficial to many retirees, such as delaying required minimum distributions (RMDs) from your tax-deferred retirement plan or IRA to age 72 instead of 70½. Deferring taxes 18 more months when your account is near its all peak value is a nice boost for you, owing to the law that is widely expected to be passed by the end of 2019.

Under the House bill, a beneficiary must deplete an inherited IRA within 10 years of the owner's death. (Inheriting spouses get the money tax-free and with no RMD.) While the Senate proposal permits a lifetime stretch of the deferral on the first $450,000 of an inherited IRA, the balance is required to be withdrawn in five years. The appeal to lawmakers of squelching the stretch IRA: it would raise $15.7 billion in Government revenue over the decade through 2029.

There are ways, though, to set up an inheritance to replicate a stretch IRA. A parent or other IRA owner, who wants to pass along the money with less tax depletion and more flexibility, would want to weigh the following strategies to

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Round And Round And Up And Down We Go Again

If you like roller coasters, you must have loved the past 8 months on Wall Street.

November - December 2018 were the worst two months since 1936.

That was followed by January 2019, which was the best January since 1987.

That was followed by May 2019, which was the worst May since 2010.

And that was followed by June 2019 which was the best June since 1955.

Reading the financial papers were more exciting than a trip to Six Flags Adventure.

So what's going on?

My view; there are multiple topics of economic concern. Trade negotiations with China have been going on for months with China reneging on some of its commitments. This has negatively affected China's GDP and our farmers as well. Our farmers in the Midwest have also been negatively affected by heavy flooding which has lowered output. Europe and the underdeveloped nations have been in a slump. Germany and other country's bonds have a negative yield, resulting in more foreign purchases of US bonds. This has caused our 10-year bond yields to drop lower than the 30-day bond yields. This inverted yield curve is dangerous to continued growth and, at this writing the Federal Reserve has recently lowered the short-term rates. That, in my opinion, will be good for the economy's continued expansion.

Hold on to your hats...more to come.

Norm

The Big New Tax Break For Pre-Retired Professionals

Pre-retired dentists, doctors and lawyers as well as other independent professionals may be able to save tens of thousands of dollars in income taxes annually during their peak income years under the new federal tax regulations. The new rules are complex. Here are 10 things pre-retired business owners need to know about qualifying for a 20% reduction in qualified business income under Section 199(A) of the new Internal Revenue Code:

1. Sole proprietors, LLCs, S corps, partnerships and other pass-through entities qualify.

2. Real estate and rental business income — including self-rentals — may qualify.

3. Some businesses are specified as ineligible and you may need a professional to determine if you qualify.

4. Service-business owners could get a deduction on 20% of their income, subject to income limitations.

5. A business owner with $315,000 in taxable income owes tax on only $252,000 — saving more than $12,000 of income tax.

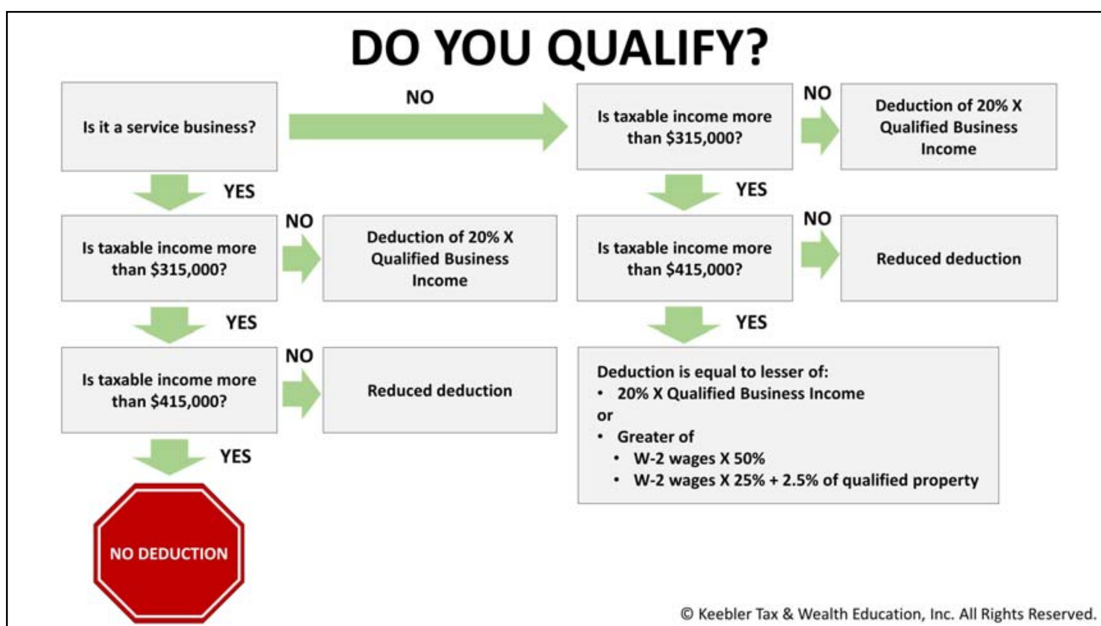
6. If you are married filing jointly and have more than $315,000 of income, the 20% deduction is subject to a phase-out. The phase-out begins at $157,500 for single filers.

7. If you have more than $415,000 of income from the service business, the 20% deduction is eliminated ($207,500 for single filers).

8. To keep your income below these thresholds, consider contributions to a defined benefit (DB) plan.

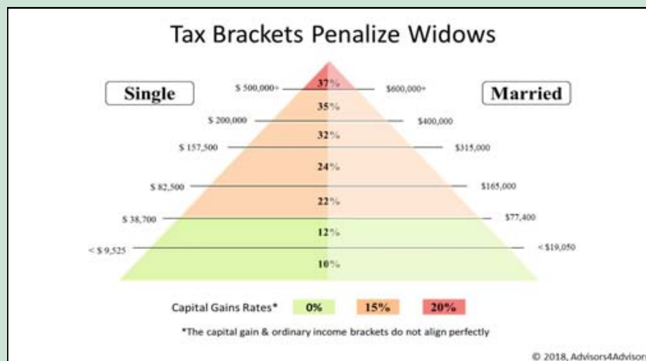
9. DB plans require you to commit to funding a defined benefit plan instead of a defined contribution plan, making them more complex.

10. A DB plan can supercharge retirement savings while minimizing your taxable income to enable you to qualify for the 20% deduction for business owners. ●



Reduce Your Widow's Tax Bill Materially Annually

This is a good time to consider converting a traditional individual retirement account into a Roth IRA. Tax rates are low but unlikely to stay that way. Here's a long-term strategy that takes advantage of the current tax policy and economic fundamentals — a tax-efficient retirement investment and avoids a new twist in the Tax Cut And Jobs Act that penalizes widows.



The Rules. With a traditional individual retirement account (IRA), taxes on gains reinvested are deferred. An IRA grows with no taxes owed. When you retire, withdrawals are taxed as income. A Roth IRA is different. You pay income tax upfront and Uncle Sam promises tax-free withdrawals when you're retired.

The Math. According to data from the non-partisan Congressional Budget Office, math will drive a surge in the $21 trillion U.S. debt starting in 2023, when interest owed on the debt accelerates, as does the risk of default. As 2023 nears, running trillion-dollar budget deficits annually becomes an increasingly untenable policy and tax rates are likely to rise.

Inflation, too. Inflation has been low for many years. While it is not expected to rise sharply, the real cost of the federal debt would be reduced if inflation rises. Inflation is unlikely to work against those converting to a Roth IRA in 2018.

Widow Penalty. Many surviving spouses will face a tax penalty after losing

As A Final Act of Love, Plan Thoughtfully

"Everybody wants to go to heaven," according to a classic blues song, "but nobody wants to die." Nor does anyone like to think about dying. And that must be why some people don't put much thought into estate planning, much less in drawing a schematic for distributing one's earthly possessions to those you love the most.

But this is important. It's something you want to do diligently. It's something you want to get right.

Your heirs and the executor of your estate — the person you choose to oversee that your wishes are carried out — will remember you kindly for your clarity of purpose; it's good for all involved. Otherwise, you risk setting off a family feud. Resolving not to leave your property open to legal dispute, here are three key rules for further planning your estate:

Name Beneficiaries Correctly. Putting someone's name in your will may not be enough, of course. It's wise to name who gets what in documents filed with your insurer, annuity provider and retirement fund sponsor, usually for individual retirement accounts. To be clear, if you want your daughter to get your ABC Stock 500 fund, naming her in the will does no good. It must be on file with a custodian. Moreover, listing multiple beneficiaries of real estate often is an invitation to a quarrel. What if you give your home to your three children? Maybe one wants to keep it for old time's sake, and the other two want to unload it and pocket the money. Or perhaps they all want to sell but can't agree on a broker or a fair selling price. In the meantime, they would need to chip in to maintain the house, which can cause further disputes.

Keep Estate Plans Current. Years or decades may pass between when an estate plan is devised and your death. Lots can change. Like spouses. If you divorced and never updated your will afterward, your ex could end up inheriting your worldly possessions. And what about your nephew, who was so delightful as a kid but grew up to be someone you don't really want to help financially. What's more, the tax laws could have changed, and old plans may be totally out of sync with current rules. Reviewing your will annually makes sense.

Provide Vital Information. Another problem is not furnishing your executor and heirs with a thorough up-to-date list of accounts and how to get access to them. Account titles, user names, and passwords — along with security questions — must be stored. Encrypting and saving this information is best. Writing it down and storing it in a safe deposit box is next best. However, not everything should be stored digitally. Mortgage documents, the deed to your home, your last mortgage payment and paperwork on your car are best kept in a safety deposit box, which requires a key and a photo I.D. to access. So, remember to arrange access for your executor with the bank. In leaving an item of sentimental value, consider who among your heirs would most appreciate its significance. Your Facebook, Instagram and Amazon account can be managed from the grave using online services such as Mylennium. It's wise to have a master list with all user names and passwords for financial holdings. This can be in your safe deposit box or in a secure place in your home. Trouble is, keys tend to get lost. Encrypting it and storing it online or on secure media you keep in your home is better.

Nobody wants to die but if you want to go to heaven, making your final wishes easy on loved ones is a thoughtful final act to help get you there. ●

a mate under the new tax brackets enacted by the Tax Cuts And Jobs Act. For example, a couple with $170,000 of adjusted gross income is in the 24% top bracket, but after one spouse dies, the survivor would fall into the 32% bracket.

Avoiding The Widow Penalty. Retired married couples converting from a traditional IRA to a Roth account can avert the widow penalty with proper planning. Since Roth accounts generate tax-free income, converting to a Roth places a surviving spouse in a lower tax bracket. For example, a couple with $170,000 of adjusted gross income (AGI) would convert from a traditional IRA to a Roth IRA, lowering their AGI to less than $157,500. If one spouse dies, the survivor would be in the 24% bracket applied to singles with up to $157,500 of adjusted gross income.

Not For Everyone. Converting makes no sense unless you have cash on hand to pay the income tax on withdrawals from your traditional IRA. Paying taxes owed on a conversion by withdrawing larger amounts from a traditional IRA usually limits a nest egg's growth potential and is unwise.

Tax-sensitive investing is complicated, and this simplified version of the rules and examples are only intended to encourage to plan properly because a move like this can reduce a tax bill materially and annually for a widow.

We evaluate tax planning opportunities for clients. Please contact our office to talk about your personal situation or if you have any questions about this strategy. ●

Asset allocation cannot eliminate the risk of fluctuating prices or uncertain returns. Diversification does not assure a profit or guarantee against loss.

Ten Things About 10-Year U.S. Stock Market Performance

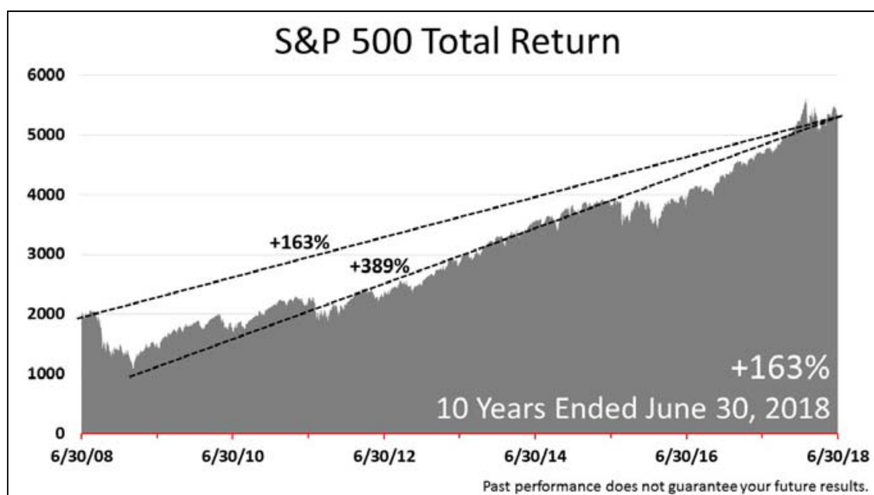
Although a picture is said to be worth a thousand words, out of respect for your time, here are 290 words about this chart of U.S. stock market performance over an amazing decade.

1. Over the 10-year period ended June 30, 2018, the S&P 500 total return index gained +163%, an average annual return of 16.3%, compared to the average annually since 1926 of 10%.

2. From the financial crisis bottom on March 9, 2009, the S&P 500 total return index through June 2018 gained +389% — an average return in those nine years of 43.2%.

3. In the nine-year bull run, stocks "corrected" — market-speak for a decline of 10% to 20% — four times, and each double-digit setback came in the last five years.

4. An investor with perfect timing predicted the March 9, 2009 low during the bottom of the 40% drop in prices in the bear market of 2008-9, which no one could, and then held for the next nine years, despite four corrections.



5. An investor with the worst possible timing, who put their retirement nest egg in stocks at market peak a decade ago, just before values plunged by 40%, in the decade, averaged a return of 16.3% annually.

6. The Great Recession decline of 40% was one of the worst bear markets in modern U.S. history.

7. Those within five years of retiring are at the greatest risk to bad timing and can be mitigated by strategically allocating assets, which is crucial to pre-retirees.

8. America's 500 largest publicly held companies more than fulfilled their role as the engine of growth in a broadly diversified retirement portfolio.

9. Understanding 10 years of stock market performance requires knowing statistics, but mostly depends on knowing the history of domestic and global financial assets, along with economic fundamentals driving growth.

10. No one can predict the end of a bear or bull market or the stock market's next big move. ●

The Demise Of Stretch IRAs

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maximize your impact on the next generation:

Convert the IRA to a Roth. Before an IRA holder passes, it might be wise to convert the account to a Roth. The giver will have to pay taxes on the money up front. But a Roth requires no minimum distributions annually; your heirs will owe the IRS zilch and can withdraw at his or her own schedule.

Insure payment of the conversion tax. One way to pay the Roth conversion taxes is to take out a life insurance policy on the donor — the proceeds from which are tax-free. At the IRA donor's death, the policy's proceeds pay the taxes for the Roth conversion. Otherwise, the up-front taxes may (and often do) come from the IRA itself, thus shrinking it. An insurance product's cost must be considered as well as the creditworthiness of the insurer.

Set up an irrevocable trust with a life insurance policy. This is a variant on the previous strategy. Here, the donor takes a distribution from the IRA long before death and uses the money to fund the trust. The trust is called "irrevocable" because the terms of the trust can't be altered without the approval of its beneficiaries. Although the trust can't grow tax-free, like a stretch IRA, its distribution is also at the discretion of the recipient.

Create a charitable remainder trust. For those of a philanthropic bent, this arrangement serves a double purpose. At death, the IRA owner funds the trust, which pays the beneficiary for a specified period or for the person's lifetime. The trust establishes a set amount or percentage that goes to the inheritor. (The estate receives a charitable deduction for the gift.) The other big win: what's left over goes to a designated charity.

Implementing these tax strategies requires the advice of an experienced tax professional, who understands your personal situation. This article is not tax or legal advice, but it is an alert to IRA owners and their beneficiaries to watch the proposal now wending its way through Congress and prepare to act on a strategy. U.S. tax laws historically are usually not signed until the end of the year but waiting on this tax reform to be signed may not leave you enough time to formulate the best strategy for minimizing taxes owed on an inherited IRA under the SECURE Act and optimizing your impact on the next generation of your family. Please contact us with questions. ●

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