The
FINANCIAL UPDATE

DAY & ENNIS, LLC
FEE-ONLY FINANCIAL PLANNING

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Passing Down IRA Assets? Clue In Family Members

Do you have substantial assets in your IRAs? It's important to be smart about beneficiary designations, and maximizing tax benefits, while avoiding potential pitfalls. But it's also essential not just to fill out all of the paperwork and forget about it. Instead, take the time to discuss your plans with family members.

Spouses who inherit traditional IRA assets have more flexibility than other beneficiaries, though non-spouses, too, can benefit from careful planning to determine the best ways to pass along money in an IRA. Here are key points to cover in your family discussions:

The first thing to do is to bring everyone up to speed on the differences between spouses and other beneficiaries.

1. Spousal beneficiaries: Spouses who are IRA beneficiaries can move the money into their own IRAs and treat it just like other assets in those accounts. They can do this without owing any tax, and if they haven't yet reached age 70½, they won't have to take the required minimum distributions (RMDs) that must begin after you reach that milestone. (But if your spouse who died already was taking RMDs, you'll need to make that withdrawal for the year of death.)

That doesn't mean a spouse can't withdraw some or all of the money in the inherited account. But any distribution will be taxed, probably as regular income. So it's generally better for tax purposes to take a series of distributions stretched over several years.

2. Non-spousal beneficiaries: If you bequeath IRA assets to your children or to anyone other than your spouse, those beneficiaries will have to follow different rules. They can't roll over the money tax-free into IRAs of their own. Instead, they must arrange to receive a series of distributions based on their life expectancies or empty out the inherited accounts within five years. Because beneficiaries tend to be younger than the deceased IRA owner, they often can use the strategy of withdrawing funds gradually over their life expectancies, an approach often referred to as a "stretch IRA."

But those non-spouse beneficiaries *will* have to take annual RMDs regardless of how old they are. Because the amount of those yearly withdrawals depends on the inheritor's age, younger beneficiaries will be able to take smaller RMDs than those who are older. But if they fail to take an RMD in any year they'll be hit by a penalty of 50% of the amount that should have been withdrawn. They'll also owe regular tax.

The amount of these RMDs will be based on the account balances on

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We Have Always Been Fiduciaries

A new rule requiring financial advisors to uphold "fiduciary standards" became partially effective June 9, 2017. The Department of Labor has scheduled it to be fully implemented by January 1, 2018.

So how does it affect investors? It means that anyone compensated for investment advice on retirement accounts such as 401(k)s and IRAs must put the best interests of clients before their own.

Many stock brokerage firms and insurance companies are fighting the new rule and want it to be revised. They do not like the rule because it prohibits them from receiving commissions on investments and products they sell. Labor Secretary Alexander Acosta has made it clear that he intends to revise the rule before 2018.

While the final fate of the rule is uncertain, it is good to know that we have always been fiduciaries at Day and Ennis. As fee-only financial planners, we have no vested interest in selling you anything. Clients seek us out for unbiased, independent financial advice. Please give us a call if you have any questions about the rule or if we can help you with your financial plans.

Sincerely,
Day & Ennis, LLC

How You Can Manage Risk Aversion

During the first two months of 2017, the stock market was rolling merrily along, with the Dow Jones Industrial Average (DJIA) breaking through the 20,000-point barrier for the first time. But the "Trump bump" won't last forever and some prognosticators are forecasting eventual doom and gloom. In all likelihood, the stock market will continue to experience ups and downs, just like it has throughout its history.

Regardless of whether the market is going up or down, or staying relatively stable, your portfolio should reflect your personal aversion to risk. Primarily, there are three types of risk to address in this overall philosophy:

1. Risk of loss of principal: This is the risk of losing the money you initially invested. Say you buy a stock for $1,000 that jumps to $1,200 before it falls back to $900. If you sell the stock at that point, you will have lost $100 of principal.

2. Risk of loss of purchasing power: You may be willing to limp along with modest returns, but you're losing money if the inflation rate exceeds your rate of return. For instance, if you acquire a bank CD paying a 2% annual rate and inflation rises to 3.5%, you're losing 1.5% in the purchasing power of that investment.

3. Risk of outliving your savings: Is your investment plan overly conservative? Remember that the stock market historically has outperformed most comparable investments over long periods, although there are no absolute guarantees. Therefore, you're likely to fare better with a well-devised investment plan than you would if you stuffed your money under a mattress. Otherwise, you might outlive your savings, especially given recent increases in life expectancies.

Risk assessment surveys can provide some insights. Typically, an analysis will reveal that you tend to be either a conservative, moderate, or aggressive investor, within certain ranges. Your portfolio should reflect this characterization.

If you indicate a more conservative bent, you may want to fine-tune your investments accordingly, taking into account asset allocation and diversification methods. Again, these strategies do not offer any guarantees, nor do they protect against losses in declining markets, but they remain fundamentally sound.

Other potential ideas are to weight your portfolio more heavily to bonds than you did in your younger days. The technique of "bond laddering," with bonds maturing at different dates, is a variation on this theme. Similarly, conservative investors may emphasize dividend-paying stocks and blue chips, as well as mutual funds and exchange traded funds (ETFs) offering diversification.

Every situation is different. Reach out to us to address your specific concerns. ●

Trust As IRA Beneficiary: Not Crazy

You may have heard that you can't name a trust as a beneficiary of your IRA—but in fact that is a perfectly legal option for IRA owners. But whether you should do it is a completely different story and requires further analysis.

IRAs can be complicated enough on their own without bringing a trust into the equation. And if you do name a trust as a beneficiary and then make a mistake with your account, the tax consequences could be devastating—so proceed with extreme caution. You'll need to work with an attorney experienced in these matters.

Why would you want to name a trust as your IRA beneficiary? It's not a tax-saving move and indeed could increase your tax bill. Still, there are valid reasons for using this planning technique. The primary benefit is protection against the IRA assets being squandered or attached by creditors. For example, you might want to pass money in an IRA to someone who is under age 21 and may not have much experience handling financial affairs or to a family member who is known to be a spendthrift. Having the account pass into a trust could enable a trustee to control how the money is distributed.

In a similar vein, you might intend to provide IRA funds to your spouse in a second or third marriage, but without shortchanging your children from an earlier marriage. In that case, you might leave the assets to a trust that pays out income to support a surviving spouse for life, with the remainder going to the children.

In any of these cases, naming a trust as your IRA beneficiary could be helpful—though, again, you'll need to work with an attorney with specialized knowledge of trusts and estate planning. Having the proper language in documents for the IRA and the trust is crucial.

Avoid These 6 Mistakes In Stretch IRA Planning

As talk of the possibility of tax reform continues in Washington, there's an increased focus on the rules for "stretch IRAs." This retirement planning technique, which enables you to preserve assets in an inherited IRA for an extended period, could be targeted in a larger tax reform package. For the time being, however, stretch IRA planning remains a viable option for many people.

But to use a stretch IRA successfully, you'll need to follow a number of important rules and avoid common mistakes made by those who inherit IRA assets.

If you own an IRA, you must take required minimum distributions (RMDs) annually beginning the year after you reach age 70½. Otherwise, you'll be hit with a stiff IRS penalty. Those distributions are taxed at your rate for ordinary income—which could be as high as 39.6%—and are based on a calculation that considers the account balance at the end of the previous year and your life expectancy (or your joint life expectancies with your spouse).

However, beneficiaries who inherit your IRA can arrange for RMDs based on their own life own expectancies, unless they choose to empty the account more quickly. Stretching out the IRA in this fashion can help preserve wealth for younger generations.

With those basics in mind, consider these six common mistakes in stretch IRA planning:

Mistake #1: Your account is titled improperly. When someone dies and IRA assets are inherited, it's crucial to ensure that the account name is titled correctly. For example, if someone other than your spouse inherits your IRA, your name should remain on the inherited IRA account title and it must be indicated that it is an inherited IRA by using the words "beneficiary" or "beneficiary IRA" or "inherited IRA."

Mistake #2: You fail to take RMDs. If the IRA account holder already was taking RMDs at the time of death, inheritors will need to make sure that the RMD is withdrawn for the year in which the account holder died. Failing to meet this requirement triggers a penalty equal to 50% of the amount that should have been withdrawn.

Mistake #3: You, as the primary beneficiary, fail to utilize a disclaimer when appropriate. A qualified disclaimer is a legal document that effectively says you choose not to receive the IRA assets, which then will pass to the contingent beneficiaries listed on the IRA paperwork. This strategy may be preferable if you don't need the money and you intend to pass along the inherited assets to younger beneficiaries eventually. Doing it now means RMDs will be based on the new owner's longer life expectancy.

Mistake #4: You fail to analyze contingent beneficiaries when using a disclaimer. It's important to consider all relevant financial and tax factors before agreeing to pass up inherited IRA assets through a disclaimer. This is not a casual decision. Consider whether the contingent beneficiaries in fact will be able to stretch out the IRA longer under their life expectancies and look at their tax consequences. Younger contingent beneficiaries may be in a lower tax bracket than you are, and if they pay the taxes that could reduce the overall tax bite.

Mistake #5: You take a lump-sum distribution. Some people think they're required to take a lump-sum distribution from an inherited IRA to empty the account immediately. That's simply not true. If you need the money, go ahead and take it. But if you don't have a pressing need, going the stretch IRA route could enable you to preserve wealth longer and generally will reduce tax liability.

A large lump-sum distribution could rocket you into a higher tax bracket and force you to lose more of the inheritance in taxes.

Mistake #6: You fail to analyze spousal rollovers. Current tax law offers greater flexibility to spouses who inherit an IRA. They can roll over inherited assets into their own IRA accounts and set up payouts calculated on their own life expectancies. However, a rollover isn't always the optimal approach for spouses. For instance, if a surviving spouse is under age 59½, payouts from the IRA will trigger the 10% penalty tax for early withdrawals, on top of the regular income tax owed. ●

One key aspect of such an arrangement is that the trust you name as IRA beneficiary should have people—and not an institution or your estate—as its beneficiaries. That could enable those beneficiaries to use "stretch IRA" planning techniques to lengthen the amount of time that assets can utilize an IRA's tax advantages. Although required minimum distributions (RMDs) still will have to happen, they'll be based on the life expectancies of the ultimate beneficiaries. The younger they are, the longer the money can be shielded from taxes. If more than one nonspouse beneficiary is named in a trust, the age of the oldest living beneficiary must be used. Consider separate trusts for each nonspouse beneficiary.

A variation on this theme calls for naming your spouse as the primary beneficiary and the trust as the contingent beneficiary. Such a setup provides greater flexibility because the surviving spouse may roll over the inherited IRA assets into his or her own IRA as part of post-mortem estate planning. ●

5 Retirement Mistakes You Can Fix

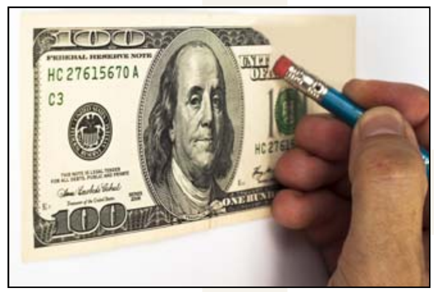
To err is human, but some mistakes are worse than others, and slip-ups that occur while you're planning for retirement can come back to haunt you financially.

But it may not be too late for you to fix some common mistakes. Here are five prime examples:

1. Saving too little. It seems obvious, but not setting aside enough money could become a big problem if you underestimate the amount you'll need to live on—all the more likely as life expectancies continue to rise. So if your employer offers a 401(k) plan with matching contributions, try to take full advantage of it, even though your take-home pay will be reduced by deferrals. And you can supplement these savings with IRA contributions.

2. Starting too late. From the start of your career there are many financial priorities competing for a share of your salary. You may be saving to buy a home or to put your kids through school. Yet while early contributions to a retirement plan can produce outsized benefits, you may be able to make up for lost time if you put as much as the law allows into your retirement savings. For 2017, the maximum 401(k) deferral is $18,000 or $24,000 if you're age 50 or over. The IRA limit is $5,500 or $6,500 if age 50 or over. You also might decide to work a few years longer than you'd originally planned. That can boost your savings while reducing the length of your retirement.

3. Ignoring taxes. Taxes are an essential part of the retirement planning equation. When you take money out of your retirement plans you'll likely owe federal and state income tax on those distributions. Part of your Social Security benefits also is subject to taxation. And your tax rate during retirement might be higher than you expect if you don't get some of the deductions you were able to claim while you were working. Factoring in taxes when you plan for retirement will help you create a more realistic scenario.



4. Not diversifying your investments. While you've undoubtedly heard about the benefits of spreading your investment dollars across many kinds of holdings, it's often tempting to stick with investments that have been doing well for you. But there's no guarantee that gains on a particular stock or fund will continue, and creating a diversified portfolio can help reduce the risk that you'll be hurt by losses in one or two investments. Just keep in mind that diversification doesn't provide guaranteed protection, especially in declining markets.

5. Ending retirement planning when you retire. Even after you retire you'll have important decisions to make. You'll need to make sure your portfolio stays diversified, and you'll likely need to allocate some money to stocks or other investments that may help you keep pace with rising costs.

Maybe the biggest overall mistake you can make is assuming you know it all. Reach out for expert assistance to avoid the common traps. ●

Passing Down IRA Assets?

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December 31 of the prior year and a factor based on the beneficiary's projected life expectancy in IRS-prescribed tables. You have until December 31 of the current year to receive your RMDs, which generally will be calculated and paid out by the custodian of your IRA.

Of course, non-spousal beneficiaries, too, can choose to withdraw more than the required amount or to take a lump-sum distribution of everything in the account.

With these basic rules in place, there can be several strategies to maximize tax and other benefits. For example, naming younger beneficiaries could extend the life of a stretch IRA and reduce the amount that is lost to taxes. One way to do that, if your children don't need the funds, is to designate your grandchildren as beneficiaries. Or you could name a child as a primary beneficiary and a grandchild as a contingent beneficiary. When you pass away, the child would have the option to "disclaim" the inheritance, passing it along to the contingent beneficiary and thus lengthening the payout schedule. As long as assets remain within the IRA they won't be subject to current taxes.

The family members who inherit IRA assets then can make their own beneficiary designations immediately, selecting a spouse or a child to inherit the account. Your beneficiaries also will be able to avail themselves of strategies for extending the life of the IRA.

These rules cover assets in traditional IRAs. There are different requirements for Roth IRAs, from which most distributions, even by beneficiaries, are tax-free. The original account holders don't have to take RMDs, although beneficiaries are required to withdraw money each year according to schedules based on their life expectancies. ●

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