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The Wealth Advisor

When Should Millennials Start Retirement Saving?

This is a true story about Jane X, who graduated from a prestigious university five years ago. She's on her third job, but she's now communications director at a private foundation and finally earning decent money.

Jane's student loans are paid off, and her good salary leaves her some money to invest. However, like many of her millennial friends, she doesn't know a lot about investments or the differences between various retirement plans. But she is thinking about her future and wonders when she should start saving for retirement.

There's a short, simple answer: NOW.

The best time to begin saving for retirement is as soon as you can. Granted, relaxing on the deck of a retirement cottage overlooking the ninth green isn't first and foremost in the minds of most 20-somethings. But you can't ignore the sheer weight of the saving numbers. Let's go back to Jane, who's 27. If she manages to save $5,000 a year in a 401(k) for the next 40 years—until she's 67, the Social Security full retirement age for her generation—and she earns an average annual return of 7%, she will end up with $1,035,632. But if she waits 10 years to start saving, when she's 37, her accumulated savings will be just $490,027.

If you're convinced that now would be a good time to get started, consider these seven steps that could help you reach your goals:

1. Budget and save. It's difficult to be diligent about setting aside money for retirement when you're young and have a million things you'd rather do with your money. But if you're able to set objectives for saving and you do your best to stick to them, it could pay off beautifully down the road. Try to train yourself to live within your means while you move ahead in your career and your personal life.

2. Take advantage of employer retirement plans. Your company probably offers a tax-deferred retirement plan—a 401(k) or a 403(b)—and your employer may provide matching contributions (for example, up to 3% of your compensation) to go alongside the pre-tax earnings you put into the plan. With all of that money invested for the long haul, it can grow and compound and you won't be taxed on the growth until you pull out funds during retirement.

3. Don't forget about IRAs. Regardless of whether you participate in an employer-sponsored retirement plan, you also can set up an IRA. With a traditional IRA, the money you put in may be partly or wholly tax-deductible, if your salary is relatively low. But here, too, you'll be taxed on withdrawals during retirement. Another option, a Roth IRA, doesn't give you a tax deduction on money going in but may provide 100% tax-free distributions in retirement.

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What's Ahead For The Markets

Every year brings new challenges. As we move forward into 2015, we do so with a strong U.S. dollar, historically low oil prices, and increased activity by central bankers. The U.S. has ended quantitative easing, which involved the Federal Reserve buying bonds in an effort to drive down interest rates and stimulate the economy.

The Federal Reserve now is expected to raise interest rates later this year. Meanwhile, European countries through the European Central Bank have just begun quantitative easing.

The above factors have contributed to recent market volatility. This has been consistent with history as volatility usually increases in the equity and bond markets prior to actual interest rate increases.

However, these issues also provide wonderful opportunities in the years ahead. Oil prices at historic lows provide excess cash flow to consumers through the gift of low fuel costs. Low oil prices and a strong dollar also help boost U.S. company profits through lower commodity prices and lower manufacturing costs. Banks are building solid balance sheets in the U.S. and are beginning to pay dividends.

Volatility in the markets can provide great buying opportunities. We are preparing our clients by investing in diversified portfolios to help balance out the unpredictability of the markets.

Donald N. Hoffman, MS, CPA

President

3 Ways To Deduct Mortgage Interest

Your home is more than an investment and a place to live—it also can be a valuable source of tax deductions. For many homeowners, one of the biggest itemized deductions on Form 1040 is the one for qualified residence interest (commonly called the "mortgage interest deduction"). In the usual situation, you can write off all, or almost all, of the mortgage interest you've paid for the year.

But this generous tax break might not stay intact forever. Recent proposals in Congress would scale back some of the tax benefits. Keep an eye out for future developments.

Under current law, you may claim deductions for three basic types of mortgage interest, up to certain limits:

1. Acquisition debt. This involves mortgage proceeds you use to buy, build, or substantially renovate a home. The loan must be secured by a qualified residence (either your principal residence or a second home such as a vacation home). Interest on such debt is deductible on amounts of up to $1 million. Acquisition debt often amounts to the lion's share of your mortgage interest deduction.

2. Home equity debt. If it's allowed by the laws of your state, you also may deduct the interest on home equity loans secured by a qualified residence, regardless of how you use the proceeds. But with home equity debt, deductions are limited to interest paid on loans of up to $100,000. In addition, the loan amount can't exceed your equity in the home.

3. Points. Although points really aren't mortgage interest, the tax law essentially treats them as if they were. These are the charges a lender may impose when you obtain a mortgage. (One point equals 1% of the amount you borrow.) You can deduct any points you paid for acquisition debt, but you'll need to deduct charges for refinancing over the term of the loan. For instance, if you refinance a $200,000 mortgage with a 10-year loan and pay two points – or $4,000 – you may deduct $400 in points ($4,000 divided by 10) annually for 10 years.

Mortgage interest deductions are claimed as itemized deductions on Schedule A of Form 1040. You can claim the deduction only if you're an owner of the home and pay the interest. Other special rules may apply, but this overview covers the basics.

Keep in mind, though, that the "Pease rule" may reduce your itemized deductions, including mortgage interest deductions, if your income is sufficiently high. The reduction equals 3% of the excess adjusted gross income (AGI) over an indexed threshold (but not by more than 80% overall). For 2015, the AGI threshold is $258,250 for single filers and $309,900 for joint filers. ●

Can You Avoid Estate And Gift Tax?

Are you hoping to pass investment assets to your heirs without any tax damage? Under the current rules, you have plenty of leeway to avoid estate and gift taxes on the federal level, although state taxes may be another story. However, keep in mind that your investment returns may outpace the inflation adjustments to the personal gift and estate tax exemption—and this could mean that your wealth will grow enough to be subject to taxes when you die.

There are two main estate and gift tax breaks: the annual gift tax exclusion and the unified estate and gift tax credit.

1. Annual gift tax exclusion. You can give each recipient, such as a younger family member, assets valued up to $14,000 a year without paying any gift tax (or even having to file a gift tax return). The exclusion is doubled to $28,000 for joint gifts made by a married couple. So, if you and your spouse each give the maximum $14,000 to five other family members, you can reduce your taxable estate by $140,000. And you can do this year after year.

The annual gift tax exclusion is indexed for inflation but rises only when the cost of living increases enough to result in a $1,000 bump to the exempt amount. With inflation very low in recent years, increases have slowed to a crawl. The last adjustment was made in 2013, from $13,000 to the current $14,000.

2. Unified estate and gift tax credit. This generous credit can wipe out either estate taxes, gift taxes, or a combination of the two.

After a decade of gradual increases, Congress permanently locked in the exemption amount at an inflation-adjusted $5 million. For 2015, the exemption is $5.43 million (up from $5.34 million in 2014). That means a couple easily can shelter more than $10 million in assets from estate tax, although any lifetime gifts exceeding the annual gift tax exclusion will reduce the amount available to help an estate avoid estate taxes.

But you can't simply take this tax shelter for granted. Remember that your assets may appreciate in value at a rate

7 Steps To Take After A Spouse's Sudden Death

The funeral is over, the mourners are gone, and now you're left with the rest of your life after the unexpected death of your beloved spouse. What's a devastated widow or widower to do? For starters, DON'T do anything rash, such as selling the homestead or cashing in all of your stock holdings right away. It may be difficult, especially from an emotional standpoint, but you can pick up the pieces slowly and get your finances in order. Here are seven steps for moving forward:

1. Meet with your professional advisors. One of the first steps – if not the absolute first – should be to contact your attorney, accountant, and financial advisor. These professionals can provide guidance for handling all of the legal, tax, and financial matters relating to you and your deceased spouse. Their counsel will be valuable as you work your way through the remaining six steps on this list.

2. Get the will probated. Assuming your spouse had a valid will and you're the executor—typically the case with married couples—you must begin to probate the will by filing a petition with the appropriate county office. Depending on the particulars, it can take as little as a few weeks or as long as a few years for the process to be completed. Keep your attorney in the loop the entire way.

3. Apply for benefits. Normally, you'll be entitled to Social Security benefits, including a one-time death benefit, plus Veteran's Administration (VA) benefits if your spouse was a military veteran. A surviving spouse over age 60 at the time of the other spouse's death may claim survivor benefits from Social Security. But don't continue to cash Social Security checks for a deceased spouse; you'll likely have to pay those back. It may be necessary to visit the local Social Security office and to contact the VA when appropriate. Also, don't forget to inquire about benefits from your spouse's employer if your spouse was still working.

4. Collect life insurance proceeds. Once reality sets in, you have to go about the regular business of making payments on the mortgage, the car loan, and other debts. Life insurance proceeds could be needed sooner rather than later. Examine your records to determine what you're entitled to receive through any private and employment-based policies. Your insurance agent can help, and your financial advisor can consult with you on how best to deploy any insurance benefit.

5. Review the books. Once you've had a chance to catch your breath, make a comprehensive review of your financial affairs. Go over your checkbooks, files, and online ledgers covering living expenses, loans, and other financial obligations. Separate accounts according to whether they're in your spouse's name, your name, or were held jointly. Then let banks, insurance companies, and other entities know about your spouse's death. And keep copies of these communications and verifications.

6. Change account titles. Begin the tedious process of re-titling accounts at banks, brokerage houses, and the like. Generally, you automatically will be granted a change on accounts owned as joint tenants with rights of survivorship (JTWROS), but the financial institution may require documentation. Contact each institution and comply with its procedures. Make sure you have enough death certificates to meet all of the obligations.

7. Start planning for the long term. Last, but not least, after you've addressed all of the issues requiring prompt attention, look to the future. It's time to circle back to the advisors who helped you at the outset. Reevaluate your investment portfolio, taking your evolving circumstances into account. Update your estate plan with an emphasis on passing wealth to your heirs, such as children and grandchildren, with minimum tax erosion. An estate tax return generally has to be filed within nine months of death. Finally, make those lifestyle choices – perhaps selling a home, heading off on extended travel, or both – that suit your changing needs.

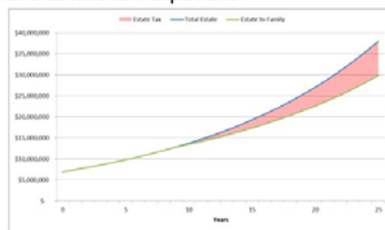
Also make cancellation notices. Your review may reveal gym and club memberships and magazine and journal subscriptions that you can cancel right away. Re-titling your financial accounts will take precedence over this type of bookkeeping, but try not to let this linger, either. Usually, a phone call or a quick note will be enough to take care of things. ●

greater than the annual inflation adjustments for the estate tax exemption. (Of course, assets also might decline in value.) This is especially true if the recent trend in low inflation persists. For example, suppose a couple has $7 million in assets and earns an annual average return of 7%. If the inflation rate remains at 2%, it will only take nine years for the couple to face federal estate tax exposure.

Wealth Preservation & Transfer

In General

Example. Consider a couple with $7,000,000 in assets. If inflation is 2% and their assets grow at 7%, within nine years the couple will have estate tax exposure:



For those in the danger zone, tax-sheltered trusts and other techniques could help safeguard assets from estate tax. In addition, making annual tax-exempt gifts for several years can help reduce the eventual size of the estate. ●

View All Tax Angles On Dividends

What's the tax deal with dividends? At first glance, it looks to be cut and dried. You receive dividends during the year and you pay tax on the amount reported to you on your Form 1099s. End of story, right?

Not exactly. First, many dividends are eligible for preferential tax treatment, much like long-term capital gains. Second, some astute timing on your part can minimize the tax you owe on dividends. Third, you need to be aware of a common tax mishap that befalls investors.

Here's a quick overview:

1. Qualified dividends. Generally, dividends issued by domestic companies are "qualified" when paid to stockholders and mutual fund owners, and that normally means special tax treatment. In some cases, qualified dividends also may be paid by foreign corporations, including shares represented by publicly traded American Depositary Receipts (ADRs) and shares that are otherwise readily tradable on an established U.S. securities market.

As for long-term capital gains, the maximum tax rate on qualified dividends is 15%, or 20% for investors in the top ordinary income tax bracket of 39.6%. Investors in the two lowest brackets of 10% and 15% may benefit from a 0% rate on qualified dividends.

To qualify for the reduced tax rates, shareholders of common stock and mutual funds must own the stock for more than 60 days, including the "ex-dividend" date (when dividends are paid). The holding period is 90 days for preferred stock. Being sure to meet these requirements could affect the timing of your transactions.

2. Tax timing. Although investors usually aren't concerned with corporate mechanisms, it's important to know the ex-dividend date. After this date, buyers of the securities no longer are entitled to receive dividends. However, as long as you buy a stock before its ex-dividend date, you then can sell the stock at any time, even after the ex-dividend date, and still receive the dividends.

One common tax planning strategy is to arrange to sell mutual fund shares before the ex-dividend date and buy shares after the date dividends are declared. If instead you buy shares just before the ex-dividend date, you will have additional tax liability for the current tax year, even if the value of your shares declines.

3. Reinvested dividends. Most investors choose to have dividends in an investment automatically reinvested. That way, your money keeps earning more money for you. Just be aware that you're paying tax on dividends each year and your tax basis for the investment should be adjusted upward. Otherwise, if you're not careful, you could end up paying tax again when you sell the shares – in effect, a double tax.

As you can see, there are more tax angles to dividends than first meets the eye. Makes sure you understand all of the rules, and act accordingly. ●

Millennials Retirement

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4. Invest wisely. This is good advice not only for money in tax-advantaged retirement accounts but also for money you invest in taxable brokerage accounts. We can help you find the investment balance that best suits your personal needs, objectives, risk tolerance, and other circumstances. Although there's no foolproof method, you should have more leeway to be aggressive now than you would when you're nearing retirement or already retired. Of course, past performance is no guarantee of future results, but you can use historical stock market trends to help shape your investment strategies.

5. Expect the unexpected. Even the best-laid plans of retirement saving can be derailed by an emergency such as a hospital stay or the loss of a job. Try to leave enough wiggle room within your budget to account for some unforeseen financial trouble. Rather than put yourself in a position to have to skip or slash retirement plan contributions, remember to put aside cash in a "rainy day" fund. Most experts recommend building up enough to sustain you for at least half a year during which you may have no other income.

6. Avoid debt like the plague. One of the biggest impediments to retirement saving is a crushing debt load. You're not doing yourself any favor by deferring part of your salary to an employer plan at the same time that you're charging luxury items on a credit card with sky-high interest rates. That's not to say that borrowing isn't warranted at times—perhaps to help buy a home or car—but make sure it fits into your overall plan.

7. Educate yourself. Finally, you can improve the chances for a secure, comfortable retirement by learning all of the rules of the road, including the nuances of investments and the tax differences between various accounts. Knowledge is your friend. Rely on us to give you a solid foundation for going forward. ●

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