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Your Wealth Management Partner

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the IRA account holder already was taking RMDs at the time of death, inheritors will need to make sure that the RMD is withdrawn for the year in which the account holder died. Failing to meet this requirement triggers a penalty equal to 50% of the amount that should have been withdrawn.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

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Spotlight On... Carrie Wildfong

Greetings. My name is Carrie Wildfong and I joined the team at Mosaic Financial Group in January, 2016. Previously I have worked as a paralegal in a variety practice areas including: Trust and Estate Administration, Elder Law, Medicaid Planning and Corporate Restructuring. I also worked for one year as a Circuit Court Clerk in Muskegon County, Michigan, and spent time serving as a Peace Corps Volunteer in Ghana, West Africa in 2015.

The team at Mosaic is full of outstanding mentors and working amongst them has been a great experience. I am fortunate that my role allows me to exercise my existing skill sets while affording me time to learn and develop as an accounting paraprofessional. Mosaic's support and encouragement toward their employees to engage in continuing education is one of the things that makes Mosaic a remarkable place to work.

I grew up in a small town in West Michigan and therefore love the beach and all things related to the Lake Michigan shoreline. I spend as much time outdoors as I can and enjoy hiking, camping, kayaking, swimming and yoga. I hold B.S. in Marketing and Communications from Grand Valley State University, and a Certificate in Paralegal Studies from Loyola University Chicago.

Tax Rules For Collectible Donations

Do you collect art, jewelry, coins, or stamps? Or maybe your passion is action figures or sports memorabilia. Whatever the focus, your collection could be valuable—and donating all or part of it to a museum or another nonprofit organization could earn you a substantial tax deduction. If you play your cards right, you may be able to write off the full value of your donation immediately.

The basic rule is that you can deduct the fair market value (FMV) of a collectible item you give to charity if selling it would have produced a long-term capital gain. So if you've owned the property for more than one year, the amount you deduct can include the item's appreciation in value since you acquired it. And you never will be taxed on that gain.

On the other hand, for a collectible you've owned for a year or less, your deduction is limited to your "basis" in the property (usually, your initial cost). These are essentially the same rules that apply to donations of securities.

Suppose you acquired a sculpture for $10,000 eleven months ago and it's now worth $15,000. If you donate it to a museum now, you can deduct $10,000 as a charitable contribution. However, if you wait just over a month longer, the full $15,000 is deductible.

Is there a catch? Yes, just one. When you donate "tangible personal property," such as collectibles, you can take a deduction based on FMV only if the property is used in a manner relating to the charity's tax-exempt function.

Let's go back to our example of the sculpture. If you give the artwork to a museum after you've owned it for more than a year and it is displayed for the public to see, you still can write off $15,000. However, if the nonprofit is your alma mater and school officials shove it into a storeroom, you can deduct only your basis, or $10,000.

In some cases, the higher deduction easily can be salvaged. For instance, if you give it to your college but insist the sculpture be displayed in a building where art majors can study it, you should qualify for the full deduction.

The other thing that's important is to have your item or collection appraised by an independent expert in the field to establish its value. This is an IRS requirement and will come in handy if the agency ever challenges the deduction amount. But here's a bonus—you may be able to deduct the cost of the appraisal as a miscellaneous expense, subject to the usual threshold for such write-offs.

Other tax rules, including limitations on itemized deductions, may come into play. But this is the way to get the most bang for your buck under current law. ●

Should You Move To A Different State?

Are you happy where you're living now? You may be comfortable in your location because it's close to where you work, it's a great place to raise your kids, and it's close to your friends and family. But it doesn't have to be forever. In fact, you might contemplate a move in the near future, especially if you're nearing retirement or are already retired.

Why would you move? For starters, there could be personal issues. You might enjoy living in a warmer climate, getting away from congestion, and living closer to a golf course or by water. But economic considerations, especially with regard to taxes, also may be part of the equation. Depending on your situation, it may be far less costly for you to live somewhere else when you take state and local taxes into account. Consider the following:

- You may be living in a state with high income tax rates. When you add state and local taxes to your federal tax load (including a top income tax rate of 39.6% and a 3.8% Medicare surtax), your top tax rate could exceed 50%. You could save money by moving to a state with lower rates. A few—Alaska, Florida, Nevada, South Dakota, Texas, Washington, and Wyoming—don't have an income tax.
- You may be living in a state with high taxes on retirement income. The tax treatment of retirement income varies widely around the country. For example, some states don't tax any income from retirement plans and Social Security benefits, some provide a partial exemption, and some tax all retirement income.
- You may be living in a state with high sales taxes. Almost all states impose sales and use taxes, but there's wide variation in the rates. Only five states—Alaska, Delaware, Montana, New Hampshire, and Oregon—don't have a sales tax. This could be a prime consideration if you expect to

Take 7 Financial Steps In A Second Marriage

Marrying again after divorce or the death of a spouse may offer great personal benefits. But it also can lead to financial complications, especially if you have children from your first time around.

However, the blessed event doesn't have to be ruined by family squabbles. Discussing matters openly and deploying a range of estate planning strategies can help you develop a plan that meets your needs. Here are seven steps to help move you along:

1. Open the lines of communication. Before you tie the knot, be up-front about your concerns and preferences. Talk to each other about your intentions and how you expect to pass along assets to other family members, including any children and grandchildren. You might find it helpful to include an impartial person, such as your financial advisor, to "broker" the talks.

Consider this checklist of points to discuss:

- Existing financial obligations (for example, a promise to pay for a grandchild's education);
- Plans for future support and funding for retirement;
- Guardianship of any minor children; and
- A prenuptial agreement protecting your personal interests.

2. Conduct an inventory. Now is a good time to compile a list of your assets. This may include: stocks, bonds, mutual funds, and other investments; amounts that you've transferred to trusts; retirement plan and IRA funds; and proceeds that will be available from life insurance policies. Also, review any agreements made during the course of your first marriage. For instance, if you were required to name your then-spouse as the beneficiary of your retirement plan accounts, you may have less flexibility than you thought.

3. Consider the variables. Not everything is cut and dried. It's up to you to decide which assets, if any, you will comingle with your new spouse's. Keep in mind, though, that the laws of your state also may come into play. For instance, in community property states, the law presumes that assets will be owned jointly. But most states mandate "equitable distribution," calling for property to be distributed fairly, but not necessarily equally. Also, you'll want to factor in your age and health status, as well as those of your spouse.

4. Pay attention to titles. The way that property is titled, both prior to marriage and after, can have a profound effect. For example, setting up accounts as joint tenants with rights of survivorship (JTWROS) will make it clear that assets will go directly to the other named person, such as your spouse, when you die. But if a title names you as the sole legal owner of assets, they'll pass to your estate and not directly to your spouse.

5. Name your beneficiaries. If you're entering a new marriage you'll likely need to amend your existing will or replace it entirely. In particular, it's important to review the beneficiaries you've named for various assets in the will. Also, take a look at the beneficiary designations in documents for all of your retirement plans, IRAs, and life insurance policies. Those beneficiary designations take precedence over whatever may be in your will.

6. Show some trust. Your estate plan may include one or more trusts, which can be useful in transferring wealth to children of an earlier marriage while imposing some constraints on the recipients. Here are a few possibilities:

Bypass trust: This vehicle could be designed to provide income to a surviving spouse, with the remainder of trust assets going to other designated family members.

Q-tip trust: With a qualified terminable interest property (Q-tip) trust, a surviving spouse may receive income, but not principal, when the owner dies, with children receiving the remainder from the surviving spouse's estate.

Spendthrift trust: As the name implies, this trust can be helpful in restricting beneficiaries' access to assets until they reach a specified age or meet other requirements.

7. Don't forget about taxes. Last, but not least, it makes sense for both of you to consider how to minimize estate tax on the federal and state levels. That likely means use of the generous estate tax exemption ($5.49 million in 2017) as well as the "portability" provision allowing a surviving spouse's estate to benefit from the unused portion of a deceased spouse's exemption. Such provisions could be included in trust documents or other estate planning devices.

The second time around, it's more important than ever to seek expert assistance from your estate planning advisors. Don't hesitate to contact us. ●

make substantial taxable expenditures during retirement.

- You may be living in a state with high property taxes. Although the real estate market generally has been soft recently, there has been little relief from property taxes for homeowners. And that town whose high property taxes may have seemed worthwhile when you were sending your kids to its great schools could be less appealing when your nest is empty.

- You may be living in a state with high inheritance taxes. This is a final factor that could influence where you choose to retire. The rules differ from state to state, and in several states the laws deviate from federal estate tax law.

All of these tax considerations could affect what you'll spend during retirement. With a little homework, you may be able to find a place with low taxes and one that appeals to you for other reasons. ●

What Would Estate Tax Repeal Mean?

If President Trump and the Republican-led Congress get their way, the federal estate tax will be repealed. This could be good news for wealthy families that were facing a hefty estate tax bill in the near future. However, if certain changes accompanying the estate tax repeal also are enacted, other families may encounter an unpleasant income tax surprise.

Normally, an unlimited marital deduction shields transfers between spouses from federal estate and gift taxes, while a separate, finite exemption shelters gifts and bequests to other beneficiaries, including your children. The current exempt amount, which is indexed for inflation, is $5.49 million in 2017. The top tax rate on additional amounts is 40%.

In addition, heirs can benefit from a "step-up" in basis when they inherit investment assets—they're valued on the date of death rather than what was paid for them. So if someone acquired securities for $1 million and it was worth $5 million when that person died, the beneficiary's adjusted basis for income tax purposes is $5 million. The $4 million of appreciation that occurred before the death remains untaxed forever.

Assuming the estate tax is repealed effective for 2017, there would be no more federal estate tax worries for families inheriting an estate worth more than $5.49 million. However, under the latest proposals, Congress also would eliminate the step-up in basis (with an $10 million exception for farms and small business interests), and that could result in income tax problems for many families.

Returning to the example of giving $5 million of assets with a basis of $1 million to non-spouse beneficiaries, no estate tax would be due under the current law, thanks to the $5.49 million exemption. But under the proposed reforms (and barring any exemptions), if beneficiaries carry over the basis on those shares and sell the assets for $5 million, they will have a taxable gain of $4 million, subject to the prevailing tax rates for capital gains.

Of course, this is just a hypothetical example and other rules (e.g., a $1 million exemption) could apply, but the potential for major income tax liability is real. Also, state estate taxes may still be a factor. Once it becomes clear whether estate tax reform will be enacted, and what shape it will take, meet with your financial and tax advisors to map out a strategy. ●

Avoid These 6 Mistakes

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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. ●

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