SARD
WEALTH MANAGEMENT GROUP, LLC

CLIENT NEWSLETTER **BY: JONATHAN SARD, CFP®**

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IMPORTANT INFORMATION

The market continues to be volatile, both to the upside and downside, but the major stock indexes are hovering near the flat line year to date. There is always headline risk in the markets so this is nothing new, and with the mid-term elections coming up soon, we can certainly expect things to heat up a bit more over the coming months.

As a reminder, we will be sending out our annual survey in August so please take a few minutes to provide your feedback so we can ensure we are providing you the advice and service you expect!

START THINKING ABOUT 2018 IRA CONTRIBUTIONS!

Consider these ideas to stay ahead of the game!

1. Make IRA Contributions Now

The best long-term strategy is to maximize IRA wealth *now*. Making contributions now for 2018 rather than waiting until April 15, 2019, earns nearly a year more of investment returns to compound until the IRA is distributed. If it turns out you were not eligible to make a contribution, excess contributions to an IRA can be withdrawn without penalty until October 15, 2019.

2. Make Gifts to Fund Children's IRAs

A child's IRA stands to earn the longest period of compound investment returns (*tax free if it is a Roth IRA)*. Moreover, Roth IRA *contributions* can be withdrawn tax free at any age. Children need earned income to contribute to an IRA, but a contribution can be made with money received as a gift or from any other source - it does not need to be paid from the child's earnings.

3. Plan a Back-Door Roth IRA Contribution

If your income is too high to contribute directly to a Roth IRA, it is still possible to contribute indirectly. There is no income limit on eligibility to either make nondeductible contributions to a traditional IRA, or to convert a traditional IRA to a Roth IRA. Thus, by making such a contribution and conversion it remains possible to effectively make a Roth contribution.

4. Correctly Project the Income Tax on a Roth IRA Conversion

Roth IRA conversions can no longer be reversed. In past years, if a Roth IRA conversion resulted in an unexpectedly high income tax bill, the conversion could be reversed by recharacterizing the Roth IRA funds back to traditional IRA status. However, starting in 2018, this is no longer allowed. To safely convert an IRA to a Roth IRA, make the conversion late in the year when tax results for the full year can be more accurately estimated, and consider making only a partial conversion to minimize tax cost. A series of annual partial conversions may convert even a large IRA without pushing income into higher tax brackets.

5. Anticipate Tax from the Pro-Rata Rule

The IRS aggregates all traditional IRAs (including SEP and SIMPLE IRAs) as one when determining tax on distributions. This can result in a surprise tax bill if unprepared, so be ready for the tax from the pro-rata rule on Roth conversions and IRA distributions. For example, to make a back-door Roth IRA contribution, Jack makes a $5,000 nondeductible contribution to a new traditional IRA and promptly converts it to a Roth IRA. All the funds in this traditional IRA are post-tax, so he expects no taxable income to result. This would be true if Jack owned *only* that one traditional IRA. However, Jack also owns another IRA holding $120,000, consisting entirely of pre-tax contributions and earnings. The IRS will aggregate the two IRAs and treat them as one with a balance of $125,000. Of that, $5,000, or 4%, consists of after-tax funds. Thus, Jack's $5,000 Roth IRA conversion will produce $4,800 of taxable income. The converted funds are 96% taxable and 4% tax free – *as will be any distribution from either IRA. Check before making any Roth IRA conversion or IRA distribution to see if the pro-rata rule will apply.*

7. Divide IRAs as Part of Beneficiary Planning

It's simplest to own just one IRA, but when estate planning becomes a priority, it may be best to divide an IRA with multiple beneficiaries into separate IRAs, each with its own beneficiary. An IRA can be divided during the year after the IRA owner's death to resolve these problems, but that creates the risk of making costly mistakes while dealing with deadlines and technical rules. For some, it may be safest to divide the IRA in advance. Another benefit of this is that each IRA may be funded with investments selected for its beneficiary, such as safe bonds for a spouse or growth stocks for a grandchild.

8. Plan for RMDs

Check your Required Minimum Distribution obligations and be sure they are met – *remember there is a 50% penalty for missing one!* Under the aggregation rules, if you have multiple traditional IRAs, the year's entire RMD can be taken from any one of those IRA accounts. This can be a way to adjust the amounts left to different beneficiaries or, if the IRAs invest in different kinds of assets, to liquidate particular assets first. People who inherit IRAs as non-spouse beneficiaries must take RMDs starting in the year after the death of the IRA owner. This is regardless of the beneficiary's age, and even if a Roth IRA is inherited. For someone who reaches age 70½ during 2018, the first RMD must be taken by April 1, 2019. For others, RMDs must be taken by year-end.

9. Plan a Qualified Charitable Distribution

Those who are at least age 70½ and wish to make charitable contributions can do so advantageously by doing a qualified charitable distribution (QCD). This is a direct transfer from an IRA to a charity. A QCD may be as large as $100,000 and can be used to satisfy RMD requirements. A QCD is not included in income as a distribution. Tax-wise, this is better than taking a taxable IRA distribution and trying to offset it with a charitable contribution deduction, because there is no need to file an itemized tax return (which fewer people

may be doing under the Tax Cuts and Jobs Act). Also, a QCD does not increase adjusted gross income (AGI) as a taxable IRA distribution does. Higher AGI can be costly in several ways, for instance by increasing income tax on Social Security benefits and increasing Medicare premiums. When nearing age 70½, it may make sense to delay making charitable contributions until you become eligible to make use of QCDs.

Given all of these options, we always stress how important it is to plan. Be sure you are sitting down with us on a regular basis to discuss your entire financial situation. Each quarter we want to remind you to alert us to changes in your financial situation or investment objectives to ensure that we are aware of any situation that might require changes in the management of your accounts. Please remember to contact us to discuss how these changes impact your investment accounts!

Financial Tip of the Month

How to lock down the home sale exclusion

Good news if you're selling your home: The home sale exclusion wasn't touched by the massive tax law changes. Arguably one of the biggest tax breaks to be left intact, it allows you to exclude capital gains tax on the first $250,000 in profit from a sale of a home. The maximum home sale exclusion is doubled to $500,000 if you're married and file jointly.

How the exclusion works

The basic requirements are relatively simple. To qualify, you must have owned and used the home as your principal residence at least two of the previous five years. For example, if you live in a home for two years and then move full-time to a vacation home for three years, you can still qualify for the exclusion on the sale of the first home.

Consider these factors if you're determining whether or not you can take advantage of the home sale exclusion:

- The years you own and use your principal home don't have to be consecutive. For instance, you might live in a principal residence for one year, switch to another home in the second year and then move back to the first home in the third year.
- Joint filers can claim the maximum exclusion if either spouse owned the home for at least two out of the last five years leading up to the sale date, both spouses have lived in the home for two out of the five years and neither spouse has elected the exclusion within the last two years. This could be crucial for recently divorced or remarried taxpayers.
- Generally, a short temporary absence won't count against you. A college professor on sabbatical or snowbirds spending winters in Florida should be OK.
- If you split time between two homes during the year, the place where you stay most often is generally treated as the principal residence. Therefore, to claim the exclusion for a home, make sure you reside there more than half the year for at least two years.

You may qualify for a partial exclusion if you sell a home before you meet the two year requirement due to an employment change, health issue or some other unforeseen event. In this case, then exclusion is prorated based on your use.

Please keep in mind that this tip is designed to be of help for you, but is not to be relied upon as advice. It is merely a reminder that there are many choices you have available to you, and that planning may be the only way to find the right answers for your situation. As with any financial issues, make sure you get the right information before making a decision. If you have any questions, we'll be glad to help you!

Client Quiz

Question: What is the top marginal income tax bracket for 2018?

A. 25%

B. 28%

C. 36%

D. 37%

E. 39.6%

We wanted to thank those of you who have participated in our Client Introduction program. As you know, marketing for new clients takes a great deal of money, time, and energy and we would much rather spend our resources improving your financial health. We, like most businesses are looking to grow; however, for the benefit of our existing clients we are only able to take on a limited number of new clients each year. Over the years, we have learned that encouraging you to introduce us to people you know works well for all of us…we help you, and you help us. If you aren't familiar with our friends helping friends program, please call our office or be sure to ask us at your next meeting. The few minutes it takes to learn about how it works will be well worth your time and energy!

Answer: **D**. The top marginal income tax bracket is 37%.

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