Financial *focus*

ACP
Alliance of Comprehensive Planners

FALL 2019

In This Issue

Consider the Downsides of Early Retirement

By Jane Young CFP®, EA, MBA
Colorado Springs, CO

Early retirement can be a great opportunity to spend more time with family, travel, and pursue hobbies, but it's not without significant drawbacks. At retirement, there is a significant financial adjustment. As a retiree, you shift from contributing to your retirement portfolio to steadily pulling money from your nest egg. The typical retirement age is around 65, and the average life expectancy is 85. According to the Social Security Administration, a quarter of those who reach 65 will live beyond age 90. If you retire at 65, your retirement nest egg will need to cover expenses for at least 20 to 25 years, increasing to 30–35 years if you retire at 55.

Understandably, one of the biggest concerns in retirement is outliving your money. Before considering early retirement, calculate how much will be needed to meet your desired lifestyle, including inflation and unexpected expenses. Keep in mind that early retirement results in a double whammy—you both start drawing from your portfolio and stop saving and contributing sooner.

In addition, when you retire early, you will need to purchase health insurance, and you won't be eligible for Medicare until age 65. The cost of medical insurance and additional out-of-pocket medical expenses can be significant. Be sure you include estimated health insurance costs in your retirement expense projections.

For very early retirees, if you take distributions from your IRA or 401k plan before age 59½ you may owe early withdrawal penalties of 10% (there are a few exceptions that allow penalty-free withdrawals at age 55). A tax penalty of 10% of IRA/401k withdrawals in addition to ordinary income taxes will have a significant impact on your portfolio. If you plan to retire before age 59 ½, it would be wise to build up a non-retirement account to avoid the 10% penalty on IRA and 401k plan withdrawals in the early years of retirement.

Many who retire early choose to take Social Security benefits at age 62. This has a significant negative impact on future Social Security benefits. At age 62, you will experience a 25% reduction in benefits from what you would receive if you waited to start drawing Social Security benefits until you reach your full retirement age (around age 66 for most people). Additionally, when you stop working, you stop increasing the average income on which Social Security is calculated. Early retirement also usually reduces income from a private pension, if taken before age 65.

Aside from the financial impact of retiring early, there are the social and emotional consequences of retirement. Initially, you may enjoy the extra free time and flexibility to travel and enjoy your hobbies but after a few years you may find that you need more substance. Working provides a sense of purpose, accomplishment, pride, and social stimulation. Plan out your retirement to engage in challenging and meaningful activities. It is common for retirees to experience a lack of fulfillment, loss of identity, social isolation, and insecurity when they no longer have their work identity and social contacts. This can be especially true for early retirees because their friends and colleagues are still working. Think about and plan to engage in activities that provide purpose, meaning, and self-esteem in retirement.

To gain some of the benefits of early retirement without as many drawbacks, alternatives include seeking out a job with greater flexibility or transitioning into retirement gradually. Some employers will allow valued employees to phase into part-time roles over a few years before they fully retire.

Whom Should I Name as Trustee?

By Steve Martin CFP®, CPA, JD
Nashville, TN

Choosing a trustee may be one of the most important decisions in your estate planning. Unfortunately, it is also one of the hardest decisions to make. Before we look at options for naming a trustee, here is a brief overview of trustees and their duties.

Who is a trustee?
A trustee is an individual or institution named in the trust document (or in a trust created in a will) charged with carrying out the terms of the trust—usually by following the explicit terms in the trust or by adhering to applicable laws.

A trust can come into play either during life or death of the person who creates the trust (the grantor). Trusts are often created to hold assets for one's heirs or beneficiaries for a variety of reasons (e.g., asset preservation, estate taxes, divorce protection, or protection of minor children). The trust specifies how long the trust is to last and when trust assets are required or allowed to be distributed to beneficiaries (e.g., at the attainment of specific ages, or discretionary based on a certain standard specified in the trust).

For purposes of this brief article we will focus on naming a trustee for an irrevocable trust. Revocable trusts created while living become irrevocable (i.e., terms of the trust cannot be changed) after the grantor dies. Trusts created within a will for minor children are irrevocable because they are only created after the death of the person writing the will.

What does a trustee do?
A trustee is first and foremost a fiduciary who must act in the best interests of the beneficiaries of the trust. The trustee manages the assets for the beneficiaries and must act in accordance to this high legal standard.

A trustee's obligations fall into three broad areas:
- Administrative function: trust accounting (keeping track of the assets, income, and distributions), communications, and tax compliance
- Investment function: managing the investments in accordance with trust law
- Distribution function: determine when and how much to distribute from the trust assets to the beneficiaries

Thus, the trustee has relatively big duties, and this can be a time-consuming chore that may last for many years. Choosing a trustee is obviously quite important.

What are some options for naming a trustee?
One can choose individual persons as trustees or corporate trustees (or both). An individual can be a family member, friend, or advisor while the corporate trustee can be a stand-alone trust firm or a trust department within a larger financial services organization. Choice of trustee depends on a variety of factors, including skillset, availability, complexity of the trust and situation, and cost.

Advantages of naming an individual (family member or trusted friend)
- Potentially lower costs
- Potentially more knowledge and empathy towards the beneficiaries (especially if a family member)
- More flexibility
- More privacy

Advantages of a corporate trustee
- Potential for greater continuity compared to an individual that may pass away or otherwise become unavailable to serve
- Expertise and an experienced trust dept team
- Avoid inter-family conflicts if naming an individual family member
- Family members are not inconvenienced

Other options
- Name both individual and corporate trustee as co-trustees
- Individual with hired assistance of a fee-only financial advisor and boutique trust firm

An alternative to the full-service corporate trustee while obtaining professional expertise is to use an individual trustee who hires out the expertise. The pricing is generally more flexible and may save significant sums over the life of the trust.

Flexibility and long-term thinking are key.
Regardless of who you name in the trust document, it is important to look beyond the initial naming of a trustee. Terms of the trust should provide language naming successor trustees and how a trustee can be removed and replaced. State law may also come into play in making changes to the trustee.

Most important: Action is needed.
The biggest risk is not choosing a trustee because you can't decide. You cannot create an estate plan after you pass away, but you can make changes down the road. Your ACP financial advisor can help you evaluate the pros and cons of possible trustees before you spend time with an attorney to draft and execute estate planning documents.

If You Outlive Your Term Life Insurance, *Did You Waste Your Money?*

By Michelle Morris CFP®, EA
Quincy, MA

Later this year, the first of my husband's and my term life insurance policies expire. Twenty years ago, I found out I was pregnant. In between waves of nausea I remember thinking, "We should get life insurance."

We chose 20-year term life insurance policies. Term life insurance pays a benefit in the event of the death of the insured during a specified term. It is especially important for people with young children. We chose level premium term insurance for the 20 years we expected we would need to replace income in order to support the surviving spouse as our children grew.

In the event of an untimely death, life insurance proceeds help the surviving spouse and children maintain their lifestyle. It's important for anyone with earnings the family depends on, but also for stay-at-home caregiving spouses. If the caregiver spouse dies, how much would it cost to hire out all the tasks the caregiver did? (Answer: a lot)

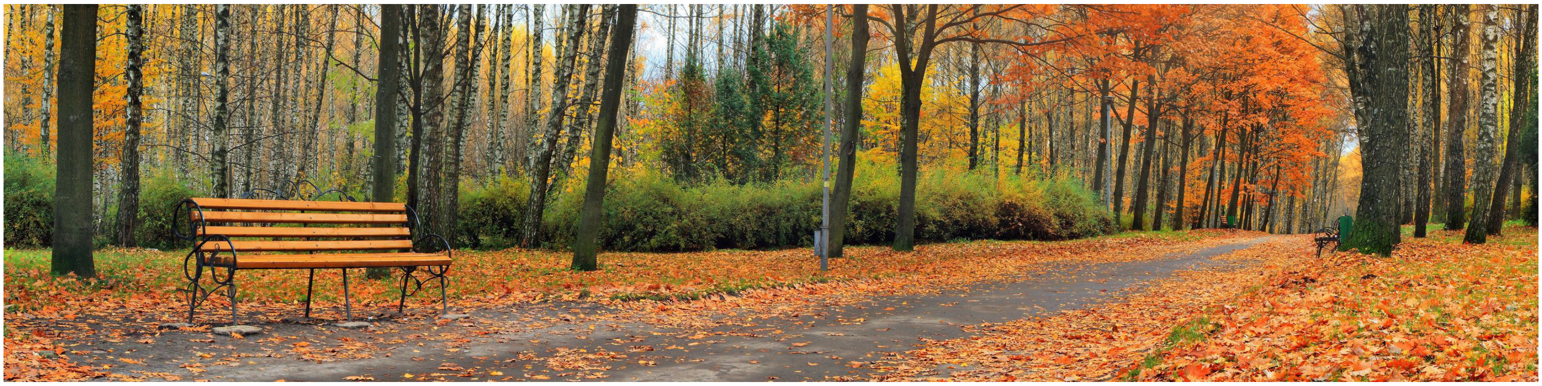
So, for nearly 20 years, two auto-debits to Banner Life Insurance have gone out of our checking account on the 26th of every month. Though paying the life insurance premiums annually works out to be a little less expensive than paying it monthly, an annual payment can't be on auto-debit. I love the convenience of monthly auto-debit of our premiums. I never have to think about it. I never have to worry that the policy will lapse because I missed a payment.

The baby is now in college. We are older and grayer. Fortunately, we are still healthy. When the policies expire, instead of lamenting loss of those policies and all the premiums paid, we will celebrate our good health. And, we have had twenty years to sock away retirement savings while paying low premiums for insurance protection.

Term insurance doesn't cost a lot—especially if you're in good health. Today a 34-year-old woman who does not smoke and has the highest health rating can buy a thirty-year million-dollar policy for ≈$30/month. Why is it so cheap? Because very few term policies pay out.

A healthy nonsmoking 34-year-old woman is not very likely to die by the time she is 64. But an unlucky few do. Of one hundred 34-year-old women who buy and keep their 30-year term policies, the premiums paid by the 97 or so women who outlive their term policies are the source of funds for death benefit payouts to the beneficiaries of the three who don't make it.

There are lots of ways to waste your money: Lottery tickets, cheap plastic crap, expensive coats requiring all new accessories. But term life insurance isn't one of them.



Tax Tips for the Fall

By Steve Cruice, CFP®, CPA
Highlands Ranch, CO
Alicia Klein, CFP®, EA
Tucson, AZ
Jacob D. Kuebler, CFP®, EA
Champaign, IL

Thanks to tax reform legislation passed in 2017 and the complexity of the tax code, most taxpayers are left unsure about how to plan for taxes in the coming years. The 2017 law altered the federal income tax brackets, doubled the standard deduction, and changed many other tax credits and deductions, such as for pass-through businesses. Three members of the Alliance of Comprehensive Planners (ACP) came together to provide tips for taxpayers to reduce confusion as they plan to minimize their tax footprint moving forward for 2019.

ACP certified member, Steve Cruice, CFP®, CPA, Lead Advisor, Simply Steward, LLC, offers this advice:

Identify opportunities to bunch deductions. With the higher standard deduction enacted from the 2017 Tax Cuts and Jobs Act, it may make sense for some people to bunch deductions such as medical expenses, charitable contributions, and certain taxes in one year and take the standard deduction the next, or vice versa. This strategy can allow people to raise their itemized deductions above the standard deduction in certain years to avoid losing out on these itemized deductions. For a married couple, aged 50, filing jointly in 2019, the standard deduction for this couple is $24,400. Let's also assume that this couple is in the 24% federal income tax bracket with income of $125,000 per year and they pay approximately 6% state income tax. They anticipate the following itemized deductions for 2019: State income taxes and property taxes of: $10,000 (note, there is a cap of $10,000 of itemized taxes under the new tax law); Mortgage interest: $7,000; Charitable contributions: $6,250.

Based on the above, this couple expects to have itemized deductions of $23,250, which is below the standard deduction of $24,400. Since they will not have itemized deductions that exceed the standard deduction in 2019, what if, instead of making their charitable contributions in 2019, they wait and make their 2018 contributions on January 1, 2020? Assuming they also give $6,250 in 2020 (on top of the delayed 2019 contribution), they would have itemized deductions in 2020 of $29,500 (taxes of $10,000+mortgage interest of $7,000+charitable contributions of $12,500). By taking the standard deduction in 2019 and shifting, or bunching, two years' charitable contributions into 2020 they will save approximately $1,530 in federal and state taxes over taking the standard deduction in both years.

ACP certified member, Jacob D. Kuebler, CFP®, EA, Bluestem Financial Advisors, LLC, suggests the following:

Reconsider using Roth-type retirement savings. Many employer 401(k) and other retirement plans allow for Roth contributions, which means funds go in after-tax (no tax savings now), but grow tax-free and can be spent tax-free in retirement. The newest tax legislation temporarily reduces tax rates for most taxpayers through 2025, at which point rates will revert back to the higher rates. As a result, it might be beneficial to pay tax now through Roth savings and enjoy the growth and use of these funds tax-free later. This may be especially true for business owners who saw a reduction in tax under the new Qualified Business Income (QBI) deduction. Retirement savings by a business owner made into pre-tax (non-Roth) savings may actually reduce the QBI deduction and result in less tax savings.

ACP certified member, Alicia Klein, CFP®, EA, Senior Advisor, Cambridge Financial Group, suggests the following:

Max out your Health Savings Account. This is a triple tax-free benefit. Health Savings Accounts (HSAs) allow you to put money into a savings account to be used for health costs. One, the savings are not subject to payroll taxes (7.65% for those making under $132,900). Two, the savings are not subject to income tax. Three, the distributions are not subject to tax if used for qualified health costs. Most HSA plans allow for a portion of the money to be invested, as well.

Navigating the new tax laws can be confusing, but by using an experienced guide, such as a member of ACP, taxpayers can prepare for the coming tax year with confidence.

All content provided by members of:

ACP
Alliance of Comprehensive Planners
www.acplanners.org