HW FINANCIAL ADVISORS
Registered Investment Adviser
A FINANCIAL PARTNERSHIP THAT FITS

WEALTH STRATEGIES
For Financial Success

Second Quarter 2016 | (216) 595-6400

Section 529 Plans Keep Getting Better And Better

For parents saving for their children's college education, a Section 529 plan may offer several advantages. Now a new tax law—the Protecting Americans from Tax Hikes (PATH) Act of 2015—enhances those potential 529 benefits.

Section 529 plans, operated by individual states, let families set aside money to cover future education expenses of account beneficiaries. If certain requirements are met, investments in the plan grow without being eroded by current taxes, and distributions to pay "qualified" expenses—which include tuition, fees, books, supplies, equipment, and room and board for full-time students—also aren't taxed.

Now the PATH Act permanently extends a rule treating computers and related equipment as qualifying college expenses. This provision had expired after 2014, but was restored retroactive to 2015 and made permanent

There are two main types of 529s: prepaid tuition plans and college savings plans.

1. Prepaid tuition plans. This type of plan is designed to keep pace with the rising cost of college tuition. Suppose it currently costs $25,000 a year to send a child to a state university. You can spend $25,000 now to buy shares in the plan for an eight-year-old. When the child is ready to go to college in 10 years, the shares you bought will pay for an entire year of tuition—no matter what it costs at that point. (You don't have to make a single big initial deposit to a prepaid plan. Later contributions will be credited according to the costs that prevail at the time.)

A prepaid tuition plan ensures that the money you put in will grow to keep up with rising costs. And returns tend to be far higher than those on most conservative investments. You don't risk losing your principal, and your investment generally is guaranteed by the state.

2. College savings plans. In contrast to a prepaid tuition plan, a college savings plan doesn't guarantee that your returns will keep pace with rising college costs. But these plans have the potential to produce higher returns than a prepaid plan depending on the performance of the investments you choose.

Usually, these 529s offer an asset allocation strategy geared to the current age of beneficiaries or the year when they'll enter school. Such strategies may use more aggressive investments in the early years and switch to more conservative options later.

(Continued on page 4)

What Will Your Social Security Benefits Come To?

Until a few years ago, the Social Security Administration (SSA) mailed periodic estimates of retirement benefits to all workers. Not anymore. But you still can get a good idea of what your monthly benefit amount will be by using the SSA's Retirement Estimator at www.ssa.gov/retire/estimator.html.

Keep in mind that this is just an estimate based on your earnings history. It isn't written in stone. Also, Social Security rules may change in the future.

You can use the Retirement Estimator if you have enough Social Security credits to qualify for benefits and you're not (1) currently receiving benefits on your own Social Security record; or (2) waiting for a government decision about benefits or Medicare; or (3) age 62 or older and receiving benefits on another Social Security record; or (4) eligible for a pension based on work not covered by Social Security.

Note that your actual retirement benefits can differ from the estimate for several reasons:

- Your earnings may go up or down in the future.
- After benefits begin, they may be adjusted for cost-of-living increases.
- Estimated benefits are based on current law.
- Your benefit amount may be affected by military service, railroad employment, or pensions earned through work on which you did not pay Social Security tax.

Some other online estimators address those issues. But even if you don't get the estimate of your future benefits right to the penny, even a ballpark figure can help in your overall retirement planning.

Do Roth IRA Math Before Converting

The Roth IRA conversion has been one of the most popular retirement planning techniques in recent years and there's nothing to indicate that this trend will change. The main attraction is that the money you take from a Roth after the conversion is generally free from income tax and you don't have to dilute your nest egg with required minimum distributions (RMDs) as you do with traditional IRAs. For many retirement-savers, it's a good deal.

But the benefits of Roth IRAs come at a price: When you convert funds in a traditional IRA to a Roth, you must pay tax on the conversion amount, just like you would with a regular distribution from an IRA. The trick is to minimize the tax liability when you pull off this maneuver.

Normally, withdrawals from a traditional IRA are fully taxable at ordinary income tax rates, currently reaching as high as 39.6%. In addition, these distributions increase your exposure to the 3.8% surtax on net investment income, as well as other potential adverse tax consequences such as the personal exemption phaseout (PEP). Furthermore, you must begin taking RMDs from your traditional IRA accounts after you reach age 70½—no exceptions.

Once you convert to a Roth, "qualified" distributions after five years are completely exempt from income tax. Qualified distributions, for this purpose, include withdrawals you take after age 59½, that are made because of death or disability, or are used for a first-time home purchase (up to a lifetime limit of $10,000). And you don't have to take RMDs during your lifetime no matter how long you live.

You may be able to contribute directly to a Roth IRA, but that option is phased out for upper-income taxpayers. A conversion may be your only viable route.

If you're thinking about a Roth conversion this year, you might consider limiting the amount you convert to the maximum you can add to your income without moving into a higher tax bracket. For example, if you expect to be in the 25% bracket and have another $50,000 to spare before crossing into the 28% bracket, you could take this opportunity to convert $50,000 from your traditional IRA to a Roth. Not only is that amount below the thresholds for the 3.8% surtax and PEP, the tax rate is limited to 25%. You then could repeat this strategy over multiple years to keep your tax liability at a reasonable level.

Finally, you're holding another tax card up your sleeve: If it suits your needs, you might decide to "recharacterize" part of the converted amount back into a traditional IRA. This could be a good idea if the value of the account declines significantly after the conversion. You have until the tax return due date for the year of the conversion plus extensions to recharacterize, giving you plenty of time to make an informed decision. ●

Women Save More For Retirement Than Men But Have Less

Question: Are men or women more likely to invest in retirement savings plans at work?

Answer: 73 percent of women employees participate in such plans while only 66 percent of men do.

Question: Do men or women put more of their employment income into retirement savings accounts?

Answer: Women put 7 percent of their salary into retirement savings while men stash away 6.8 percent.

Question: Are men or women more likely to invest their retirement savings in the stock market?

Answer: Women are just as aggressive as men when it comes to investing their money for retirement, with women investing 73 percent of their savings in equities compared to 74 by men.

Despite these statistics – compiled and reported by the research department at Vanguard – women still come up short in the all-important area of account balances.

Jean Young, senior research analyst at Vanguard and author of the report, says that in March 2015, women held an average of $79,572 in defined contribution retirement plans as compared to an average of $123,262 held by men. The median balances, for women and men, were $24,446 and $36,875, Young says.

"Women seem to be a bit better at (retirement saving) than men. They're more likely to save, and when they save, they save more," she adds.

Then what is behind these discrepancies? The glass ceiling is partly responsible. To this day, women still make less money on average than men even when they're doing the same kind of work.

In addition, because men make more money than women, it tends to be easier for them to save more money over time. Young says that when the Vanguard researchers adjusted their

IRS Issues Its Dirty Dozen Tax Scams For '16

Despite recent budget cuts, the IRS is ramping up its efforts to root out scam artists who perpetrate tax frauds. The agency recently issued this list of "Dirty Dozen Tax Scams" to watch out for in 2016:

1. Identity theft: This remains the number one concern of IRS officials. Typically, someone steals your Social Security number and uses it to file a tax return, claiming a fraudulent refund.

2. Phone scams: Crooks may make aggressive phone calls when impersonating IRS agents. They might threaten you with police arrest, deportation, license revocation, or some other action—which legitimate agency employees wouldn't do.

3. Phishing: A scammer may pose as a representative of an organization you know and trust, perhaps sending mass emails under another person's name or purporting to be a bank, credit card company, tax software provider, or government agency. The goal is to get you to provide personal information.

4. Tax preparer fraud: The vast majority of tax professionals provide honest, high-quality service. But some dishonest preparers perpetrate refund fraud, identity theft, and other scams. "Choose your tax return preparer carefully because you entrust them with your private financial information that needs to be protected," says IRS Commissioner John Koskinen.

5. Offshore accounts: Numerous people have evaded U.S. taxes by hiding income in offshore banks, brokerage accounts, or nominee entities and then using debit cards, credit cards, or wire transfers to get access to the funds. Others employ foreign trusts, employee-leasing schemes, private annuities, or insurance plans.

6. Inflated refund claims: Scam artists routinely pose as tax preparers during tax-return time and attract victims by promising large federal tax refunds. They might use flyers, advertisements, phony storefronts, and word of mouth to spread the word—even using community groups or churches where trust is high. They often target low-income people, the elderly or non-English speakers.

7. Fraudulent charities: "Fake charities set up by scam artists to steal your money or personal information (create) a recurring problem," says Koskinen. Following major disasters, scammers representing bogus charities will reach out to people by telephone or email to solicit money or financial information. They may even directly contact disaster victims in an effort to obtain personal information.

8. Falsely padding deductions: The IRS has warned taxpayers to avoid the temptation to falsely inflate deductions or expenses on their returns in order to underpay taxes and possibly receive larger refunds. Although most taxpayers file honest and accurate tax returns on time, some fudge the information. Think twice before overstating deductions for charitable contributions and business expenses or claiming invalid personal credits.

9. Excessive claims for business credits: Promoters have perpetrated various scams involving business credits. For example, although the fuel tax credit is limited to off-highway business use or use in farming, the IRS often finds unscrupulous preparers have enticed groups of taxpayers to claim the credit erroneously. The IRS also routinely sees misuse of the research credit.

10. Falsifying income: Some people falsely increase the income they report to the IRS. This scam involves inflating or including income on a tax return that was never earned, either as wages or as self-employment income, to maximize refundable credits. Taxpayers may be encouraged to do this by unscrupulous tax return preparers.

11. Abusive tax shelters: Tax schemes have evolved from abusive domestic and foreign trust arrangements into even more sophisticated strategies. These scams often take advantage of the financial secrecy laws of some foreign jurisdictions and the availability of credit or debit cards issued from offshore financial institutions.

12. Frivolous tax arguments: The IRS also describes common frivolous tax arguments made by those who refuse to comply with federal tax laws. Frequently, taxpayers refuse to pay taxes on religious or moral grounds by invoking their First Amendment rights. Those efforts inevitably fail.

The message to taxpayers in this list of Dirty Dozen Tax Scams is clear: Stay vigilant against thieves and adhere to the letter of the tax law. ●

data to account for disparities in income, the savings balance differences almost vanished, except for workers at the very top end of the income picture.

Why do differences persist at the top of the income scale? Young believes that may be because men are likely to have spent more of their careers in high-paying jobs compared with women. That may give the well-paid men more years to put away substantial retirement savings.

Another reason women may lag behind overall is access to retirement savings plans. Lower-paid workers and part-time employees—and women are likely to fall into both categories—frequently can't participate in such plans.

Another study, by the Employee Benefits Research Institute, found that the gender pay gap also can be explained by the kinds of jobs men and women gravitate to. Women in the past have frequently applied for jobs at the bottom end of the employment spectrum, and often chose part-time work because of their other responsibilities.

Young says these findings are a reminder that women need to negotiate for better salaries when applying for jobs or promotions. ●

HW FINANCIAL ADVISORS
Registered Investment Adviser
A FINANCIAL PARTNERSHIP THAT FITS

Registered Investment Adviser
Four Commerce Park Square
23240 Chagrin Boulevard, Suite 880
Cleveland, OH 44122-5450
P: (216) 595-6400
F: (216) 292-4258
(877) 367-4926
www.hwfa.com

Cleveland — Columbus — Mentor

Section 529 Plans

(Continued from page 1)

You're not obligated to use a Section 529 college savings plan for a college in your state, and you're free to use another state's plan if you like its features. Keep in mind, though, that in-state plans may offer state income tax deductions or other benefits for residents.

These plans also offer flexibility if an intended beneficiary doesn't go to college or if there's money left over after graduation. In either case, you can switch to a different beneficiary. Typically, a plan will allow one such change a year.

The PATH Act includes a couple of other significant changes in this area. For one thing, it adjusts a rule relating to taxable distributions for *non-qualified* expenses. Under the new law, each such distribution will be taxable based on the amount only in that particular account, rather than in all the Section 529 accounts you've established. In addition, if a Section 529 plan distribution is used to pay for tuition and subsequently is refunded—for example, if your child leaves school—the new law permits you to contribute that amount to another 529 plan within 60 days.

Finally, a Section 529 plan also offers gift-tax advantages. Normally, you can give anyone up to a specified amount—$14,000 in 2016—without owing gift tax. That amount is doubled to $28,000 for joint gifts from a married couple. But with 529s, you can contribute an amount equal to five years' worth of gifts if a proper gift tax return is filed. That means you could put $70,000 in an account for one beneficiary—or $140,000 if you give with your spouse—completely free of gift tax. ●