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I wrote this month's article prior to my brief return to WNY. Over the past month, we've lost a couple wonderful friends and clients. Life is so fragile. Each time I see things like this happen, I remember why I started in this business so many years ago. This is why we are in the business of helping people.

Sometimes when I write, I feel the influence of my childhood Pastor, Reverend Nelson. He was always looking for the good in people and he was always encouraging people to live their lives to the fullest. No matter what stage of life you are in, it makes sense to take full advantage of your life and talent.

During my career, I was always interested in goals and goal achievement. The more I focused, the more I accomplished. It was not easy, but it worked. Then, as I went through my illness, operation and recovery, my goals changed. They had to. But as my recovery progressed, I realized that focusing on goals not only helped me survive, they would be the key to returning to a life I would be happy with.

Everyone has an obligation to make the most of their opportunities. The first step in your planning is "Cleaning Up Financial Messes". The next step is organizing your planning priorities. As a firm, each of our members are here to help.

The fall is a great time to take the next step in improving your Financial Planning. If some aspect of your planning needs attention, make it one of your goals. Write it down, and when the time is right, resolve those issues that concern you.

Have a wonderful Thanksgiving!

Richard Moldenhauer

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UNDERSTANDING INHERITED IRAS

What beneficiaries need to know and consider.

At first glance, the rules surrounding inherited IRAs are complex.

Here are some questions (and potential answers) to consider if you have inherited one or may in the future.

Who was the original IRA owner?

If the original owner was your spouse, you have a fundamental choice to make. You can roll over your late spouse's IRA into an IRA you own, or you can treat it as an inherited IRA. If the original owner was not your spouse, you must treat the IRA for which you are named beneficiary as an inherited IRA.[1,2]

What kind of IRA is it?

It will either be a traditional IRA funded with pre-tax contributions or a Roth IRA funded with post-tax contributions.

Do you want to let the money grow and take RMDs or cash it all out now?

In the case of a small IRA, many heirs just want to cash out – it seems bothersome to schedule tiny withdrawals out of the IRA across the remainder of their lifetimes. Money coming out of an inherited traditional IRA is taxable income, however – and if a lump sum is taken, the tax impact could be notable.[1]

If the IRA is substantial, there is real merit in scheduling Required Minimum Distributions (RMDs) instead. This gives some of the still-invested IRA balance additional years to grow and compound. Any future growth will be tax deferred (traditional IRA) or tax free (Roth IRA).[1]

Internal Revenue Service rules say that RMDs from inherited IRAs must begin by the end of the year following the year in which the original IRA owner died. These RMDs are required even for inherited Roth IRAs. Each RMD is considered regular, taxable income.[1,2]

One asterisk is worth noting regarding inherited traditional IRAs. If the original IRA owner died on or after the date at which RMDs are required for that IRA, then you can schedule RMDs during the remainder of your lifetime using tables in I.R.S. Publication 590 as a guide. If the original IRA owner died before that date, you have a choice of scheduling RMDs over a lifetime or withdrawing the whole IRA balance by the end of the 5th year following the year of the original owner's death.[2,3]

What is the IRA's basis?

In other words, what is the amount on which the original IRA owner paid taxes? For an inherited traditional IRA, the basis equals the amount of all non-deductible contributions that the original IRA owner made. For an inherited Roth IRA, the basis equals the amount of total contributions made by the original owner.[4]

When you know the basis, you can figure out the percentage of an RMD from an inherited traditional IRA that is subject to tax. RMDs out of inherited Roth IRAs are not normally taxed, but if the inherited Roth IRA is less than five years old, you must determine the basis. The Roth IRA's basis will be distributed to you first, then the Roth IRA's earnings, and only the earnings will be taxed. Earnings can be withdrawn tax free from an inherited Roth IRA starting on the first day of the fifth taxable year after the year the Roth IRA was first created.[1,4]

Can you withdraw more than the RMD amount from an inherited IRA each year?

Certainly, but keep in mind that a large, lump-sum payout could leave you in a higher tax bracket.[1]

What happens when you inherit an inherited IRA?

As a secondary beneficiary to that IRA, you assume the RMD schedule of the person who was the primary beneficiary.[1]

Can you convert an inherited traditional IRA into a Roth IRA?

The I.R.S. forbids this – with one exception. A spousal IRA heir who rolls over an inherited IRA balance into their own traditional IRA can arrange a Roth conversion.[3]

If you have inherited an IRA, talk with a financial professional.

That conversation may help you determine a tax-efficient way to manage and withdraw these assets.

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Citations.

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WILL DEBT SPOIL TOO MANY RETIREMENTS?

What pre-retirees owe could compromise their future quality of life.

The key points of retirement planning are easily stated. Start saving and investing early in life. Save and invest consistently. Avoid drawing down your savings along the way. Another possible point for that list: pay off as much debt as you can before your "second act" begins.

Some baby boomers risk paying themselves last.

Thanks to lingering mortgage, credit card, and student loan debt, they are challenged to make financial progress in the years before and after retiring.

More than 40% of households headed by people 65-74 shoulder home loan debt.

That figure comes from the Federal Reserve's Survey of Consumer Finances; the 2013 edition is the latest available. In 1992, less than 20% of Americans in this age group owed money on a mortgage. Some seniors see no real disadvantage in assuming and retiring with a mortgage; tax breaks are available, interest rates are low, and rather than pay cash for a home, they can arrange a loan and use their savings on other things. Money owed is still money owed, though, and owning a home free and clear in retirement is a great feeling.[1]

Paying with plastic too often can also exert a drag on retirement.

Personal finance website ValuePenguin notes that the average U.S. household headed by 55- to 64-year-olds now carries $8,158 in credit card debt. As for households headed by those aged 65-69, they owe an average of $6,876 on credit cards.[2]

According to the latest Weekly Rate Report at CreditCards.com, the average APR on a credit card right now is 16.15%. How many investments regularly return 16% a year? What bank account earns that kind of interest? If a retiree's consumer debt is increasing at a rate that his or her investments and deposit accounts cannot match, financial pain could be in the cards.[3]

Education debt is increasing.

Older Americans are dealing with student loans – their own and those of their adult children – to alarming degree. In all 50 states, the population of people 60 and older with student debt has grown by at least 20% since 2012. That finding from the Consumer Financial Protection Bureau may be understating the depth of the crisis, which may have its roots in the Great Recession. Fair Isaac Corporation (FICO) says that between 2006-16, the number of Americans aged 65 and older with outstanding education loans has tripled.[4,5]

Just what kind of financial burden are these loans imposing? According to FICO, the average 65-or-older student loan borrower is dealing with a balance of $28,268. That is up 40% from the average balance in 2006.[5]

How can pre-retirees and retirees address such debts?

One way might be to reduce household expenses and apply the money not spent to debt. Financial assistance for adult children may need to end. Retiring later could also be a good move – income is the primary resource for fighting debt, and the more income earned, the more financial power a senior has to pay debts off.
Servicing debt in retirement can become very difficult. Large recurring debts can drain off a retiree's cash flow and increase overall household financial risk. Retiring without major debt is a comparative relief.

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