TACONIC VIEWS

Financial Insights for Secure Retirements and Life's Transitions

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Consider the Downsides of Early Retirement

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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

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The SECURE Act – A First Glance

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At the end of 2019, President Trump signed the SECURE Act as part of the government's spending bill. The SECURE legislation — which stands for "Setting Every Community Up for Retirement Enhancement" — puts into place many provisions intended to strengthen retirement security across the country. It is the most sweeping update to the laws governing retirement accounts since the Pension Protection Act in 2006.

This article will attempt to highlight some of the changes that affect most retirement savers. A section by section summary in fairly readable language can be found at: https://waysandmeans.house.gov/sites/democrats.waysandmeans.house.gov/files/documents/SECURE%20Act%20section%20by%20section.pdf

Retirement Accounts - Required Minimum Distributions (RMD) from retirement accounts now start at age 72 rather than 70.5. You can also continue to make traditional IRA contributions (including spousal contributions) after age 70.5. These *may* be deductible and you still need to have earned income.

You can continue making qualified charitable distributions (QCD) from your IRA after age 70.5, however, these may be reduced if you keep making IRA contributions. Tax preparers will have

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Transitions…

Financial Planning for Life's Transitions

Whom Should I Name as Trustee?

By Steve Martin, CFP® ,CPA, JD
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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 at death of the grantor (the person who creates the trust). 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?
You 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. Here are some plusses and minuses to consider:

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

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*Naming a Trustee…**Continued from preceding page*

Advantages of a corporate trustee

- Potential for greater continuity; an individual 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 send time with an attorney to draft and execute estate planning documents.

*Early Retirement …**Continued from page one*

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. Other alternatives might 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. By considering your financial and emotional needs carefully, you will be able to determine whether retiring early is truly in your best interest.

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to keep a running tally of both (a new accounting headache). The government is trying to prevent people who already have sufficient savings from simply trying to get two deductions. In my opinion, the QCD will still be the best option for charitable individuals who take the standard deduction.

Death of the "stretch" - changes in the stretch provision is the issue that has most fiduciary financial planners on their toes. Note that there is no such thing as an IRA account that is called a "stretch." It is a concept.

Let's refresh ourselves on this one. In the simplest case, let's say you are married, same age, each with an IRA. At some point you have to take the money out (now, at age 72). This required minimum distribution (RMD) is calculated over your respective lifetimes. If you live to 95, that's over 20 years. If you die at age 80, and your spouse is the beneficiary, he/she gets to keep the distribution going over his/her lifetime. But if you leave your IRA to a named non-spouse (son, John), he also gets to take the money out based on a lifetime calculation. That's the "stretch." Life calculations are generally l-o-n-g-e-r, and you can dribble out the money and the taxes that accompany the distribution. If you do not name a beneficiary, it goes to your estate, and the money and tax payments have to come out within 5 years, pushing the taxes forward.

Under the new law, you can still leave money to your spouse to obtain the longer lifetime calculation. But any non-spouse (with certain exceptions) now has to take all of the money out within 10 years. OK, you say. Sounds good. It's still pretty long and the time frame is twice that of the 5-year rule. However, a number of people name their *grandchildren* as secondary beneficiaries behind the spouse. If the grandchild inherits at age 40, they could have obtained 50 years of stretch!

The government is now saying that the benefit of retirement accounts should, for the most part, stay with the original account owner (a/k/a the "worker"). The original intent was not to benefit younger heirs. So this will certainly mess up some established estate planning. Your reaction to it will depend on your personal money philosophy….do you want to relieve future heirs from income tax burdens, or do you just want to worry about your own income taxes during your lifetime and let kids handle their own tax problems? If you don't mind leaving taxes with your heirs, you can suggest that they go see a financial planner to review the impact of new inherited IRA rules.

One thing to note, if you have either living or testamentary trusts that include language about retirement accounts, it's important to have those reviewed under the new law because there can be future unanticipated consequences.

Other matters, highlighted by taxpayer type:

Graduate students or post-doctoral individuals – certain fellowships may count as compensation for IRA purposes. Thus, you can contribute and start saving earlier.

Birth or Adoption of a child - permits withdrawals of up to $5,000 to be taken from an IRA or qualified retirement plan without incurring the 10% early distribution penalty.

College students – parents can use their 529 Plan to cover certain expenses for participation in an apprenticeship program certified and registered with the Secretary of Labor.

SECURE Act – continued from previous page

Student Loans - Section 529 plan distributions can be used to repay education loans up to a $10,000 lifetime maximum, per student. This includes education loans for the taxpayer OR a sibling. Each student has one $10,000 maximum. Careful record keeping will be required.

Kids with investment income - Kiddie tax computation reverts back to the old method, requiring information about the parents' and siblings' returns instead of the simplified method the TCJA gave of using the trust tax rates.

Part-time Workers – in a nod to the "gig" economy, long-term part-time job workers (more than 500 hours/year) must be allowed to participate in the 401K plan (used to be 1,000 hours/year).

Tax filing Scofflaws - The minimum penalty for not filing income taxes found in Section 6651(a) is increased from $330 to $435, effective for returns DUE AFTER December 31, 2019.

Finally, in an early valentine to the lobbying efforts of the insurance industry, The SECURE Act opens the gates for more employers to offer annuities as investment options within 401(k) plans so that "lifetime guaranteed income" products become more available. Previously, employers held fiduciary responsibility to ensure these products are appropriate for employee portfolios. Under the new rules, the onus falls on insurance companies, which sell annuities, to offer proper investment choices (ahem). So fiduciary responsibility has been lessened. To this we say, "*caveat emptor.*" Let the buyer beware. Be careful and be sure to obtain independent advice before proceeding.

There are many other provisions that provide specific benefits to various parties to incentivize retirement saving. UNLESS OTHERWISE NOTED IN THE ACT, ALL OF THESE PROVISIONS ARE EFFECTIVE FOR TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 2019.

You can be quite sure that questions will arise over time as the implications of the Act flow through the retirement planning and income tax landscape. Hopefully, I have given you a taste of what is to come. Be sure to ask your own financial or tax advisor about the impact on your current and future planning. The best way to feel secure about the SECURE Act is through education.

News!

Keeping up with Taconic Advisors...

Chip's study group visited the Hudson Valley in September and toured the FDR Home in Hyde Park, traipsed trails at Mohonk and had a 'rockin' great Sunday Brunch at 'The Falcon' in Marlboro. Oh yes, they also studied and shared management knowledge while visiting our Poughkeepsie and Saugerties offices.

Meredith and John recently taught financial basics to a class of entrepreneur students at Ulster BOCES. They got rave reviews!

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

By Michelle Morris, CFP®, EA
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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 non-smoking female with 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 non-smoking 34-year-old female is not very likely to die by the time she is 64. But an unlucky few do. Of one hundred 34-year old females 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.