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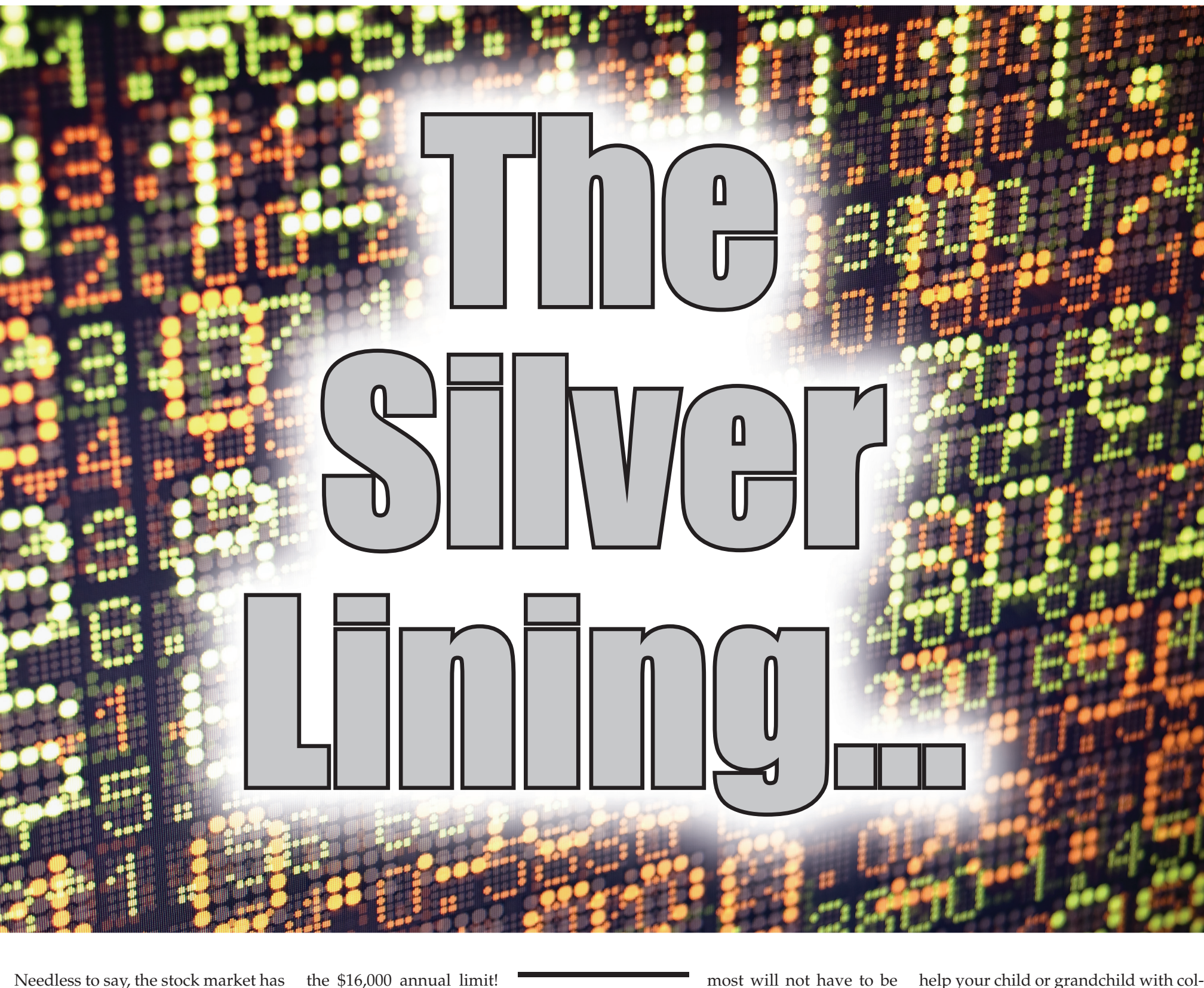

The Silver Lining...

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Needless to say, the stock market has taken us on a wild ride thus far this year.

I recall my mom always saying "look for the silver lining" in any challenging situation.

So, let's take my mom's advice and dive into two areas that I feel may qualify as the "silver lining" in this volatile stock market. From a tax planning perspective, when your investments go down in value, it might, and I stress *might*, make sense to convert a portion of your traditional IRA into a ROTH IRA. You could do the same with a pre-tax retirement account, such as a 401k, 403B, etc. and convert to a ROTH account within the retirement plan, if available.

Why do I say that it "might" be a good idea versus stating that it is a good idea? What are the considerations? The most obvious consideration is converting pre-tax money into a ROTH account creates a taxable event. So, the first consideration is how you will pay the tax. The preferred method is to use your bank money that has been taxed already. To clarify, if you converted, as an example, $50,000 into a ROTH IRA, that $50,000 is now income taxable. If you are in the 22% tax bracket, the federal income tax due would be $11,000 (plus your state income tax). It is much better to use after-tax bank money to pay that tax.

Consider the alternative of not using bank money: you convert $50,000 of traditional IRA money into a ROTH IRA. The federal tax bill is $11,000, but you would have to withdraw an additional $11,000 to pay the income tax bill on the $50,000. That creates an additional federal tax bill of $2,420 on that $11,000. This becomes too expensive and inefficient. As you can see, typically that math doesn't work in your best interest!

Another consideration pertains to gifting. The annual gifting amount has been raised up to $16,000. If you gift more than $16,000, you will have to file a gift tax form with the IRS -- Form 709. There is no gift tax due on this type of gift ($16,000) and there is a lot of confusion around gifting, which I will explain shortly. (IRS, n.d.)

Why can gifting of shares of highly appreciated stock be significant? Well, let's say that you have some highly appreciated shares of a stock. The current reduced value of that stock allows you to gift more shares of that stock and stay under the $16,000 annual gift limit. So, when the share value recovers, your gift is worth more than the $16,000 annual limit! Keep in mind that the value of the stock is determined on the date of the transfer.

There is a lot of confusion around the gifting rules. When you make gifts during your lifetime, theoretically, you reduce the amount that you can pass at your death without your estate being taxable at the federal level. The $16,000 gift amount will not reduce the amount that you can pass on when you die without a federal estate tax.

Now that the federal exemption amount is a smidge (I know that's a technical term) over $12 million, most will not have to be concerned about gifting much larger amounts over the $16,000 figure. If a gift is greater than $16,000, you would file the gift tax form with the IRS; no tax would be due as long as the gift is under $12 million. (IRS, n.d.) As you can see, most people could make some very generous gifts way above the $16,000 amount without being concerned with a federal estate tax. Always work with a professional to help ensure that any gifting will not trigger a tax.

Here is another potentially great idea when gifting highly appreciated shares of stock. Let's say you want to help your child or grandchild with college tuition. Your options are -- write a check or use some highly appreciated stock as a gift. You may be wondering what the big difference would be.

Here is the big difference. Instead of selling the stock and paying a capital gains tax of 15% and possibly the "Medicare surcharge of 3.8% or 20% capital gains tax plus the surcharge, you may be able to gift the shares of stock to a college age child, let them sell the stock and if they are in the lower two tax brackets, they would be able to sell the stock shares and pay zero tax! Yes, you read that correctly, zero capital gains tax! (IRS, n.d.)

There are many advantages of working with a financial planning team versus investment brokers. As financial planners, we focus on the entire financial picture, not just the investments.

We have other tax-efficient strategies. The larger your IRA/retirement plan balance, the more valuable these strategies can be, in most cases. Everyone's financial situation is different, so it's important to work through yours to help maximize your tax savings!

Investing involves risk, including the potential loss of principal. Any references to protection benefits, safety, security, lifetime income, etc., generally refer to fixed insurance products, never securities or investment products. Insurance and annuity products guarantees are backed by the financial strength and claims-paying ability of the issuing insurance company. Please remember that converting an employer plan account to a Roth IRA is a taxable event. Increased taxable income from the Roth IRA conversion may have several consequences including (but not limited to) a need for additional tax withholding or estimated tax payments, the loss of certain tax deductions and credits, and higher taxes on Social Security benefits and higher Medicare premiums. Be sure to consult with a qualified tax advisor before making any decisions regarding your IRA.

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