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January is a great time to evaluate your savings for retirement. We hope these articles will help guide you along this path.

If you have additional questions, please contact our office. We will be happy to work with you to help you meet your financial goals.

Happy New Year! From all of us at SmithConway

New Year's Resolution: Saving For Retirement

Key Retirement and Tax Numbers for 2017

Pretax, Roth, or After-Tax Contributions: Which Should You Choose?

Should I accept my employer's early-retirement offer?

Should I pay off my student loans early or contribute to my workplace 401(k)?



Saving for Retirement

Playing Catch-Up with Your 401(k) or IRA



A recent survey of baby boomers (ages 53 to 69) found that just 24% were confident they would have enough money to last throughout retirement. Forty-five percent had no retirement savings at all, and of those who did

have savings, 42% had saved less than \$100,000.¹

Your own savings may be on more solid ground, but regardless of your current balance, it's smart to keep it growing. If you're 50 or older, you could benefit by making catch-up contributions to tax-advantaged retirement accounts. You might be surprised by how much your nest egg could grow late in your working career.

Contribution limits

The federal contribution limit in 2016 and 2017 for all IRAs combined is \$5,500, plus a \$1,000 catch-up contribution for those 50 and older, for a total of \$6,500. An extra \$1,000 might not seem like much, but it could make a big difference by the time you're ready to retire (see table). You have until the April 18, 2017, tax filing deadline to make IRA contributions for 2016. The sooner you contribute, the more time the funds will have to pursue potential growth.

The deferral limit in 2016 and 2017 for employer-sponsored retirement plans such as 401(k), 403(b), and most 457(b) plans is \$18,000, plus a \$6,000 catch-up contribution for workers 50 and older, for a total of \$24,000. However, some employer-sponsored plans may have maximums that are lower than the federal contribution limit. Unlike the case with IRAs, contributions to employer-sponsored plans must be made by the end of the calendar year, so be sure to adjust your contributions early enough in the year to take full advantage of the catch-up opportunity.

The following table shows the amount that a 50-year-old might accrue by age 65 or 70, based on making maximum annual contributions (at current rates) to an IRA or a 401(k) plan:

Potential Savings a 50-Year-Old Could Accumulate		Without Catch-Up	With Catch-Up
IRA	By Age 65	\$128,018	\$151,294
	By Age 70	\$202,321	\$239,106
401(k)	By Age 65	\$418,697	\$558,623
	By Age 70	\$662,141	\$882,854

Example assumes a 6% average annual return. This hypothetical example of mathematical compounding is used for illustrative purposes only and does not represent any specific investment. It assumes contributions are made at end of the calendar year. Rates of return vary over time, particularly for long-term investments. Fees and expenses are not considered and would reduce the performance shown if they were included. Actual results will vary.

Special 403(b) and 457(b) plan rules

403(b) and 457(b) plans can (but aren't required to) provide their own special catch-up opportunities. The 403(b) special rule, available to participants with at least 15 years of service, may permit an additional \$3,000 annual deferral for up to five years (certain additional limits apply). A participant can use this special rule and the age 50 catch-up rule in the same year. Therefore, a participant eligible for both could contribute up to \$27,000 to his or her 403(b) plan account (the \$18,000 regular deferral limit, plus the \$3,000 special catch-up, plus the \$6,000 age 50 catch-up).

The 457(b) plan special rule allows participants who have not deferred the maximum amount in prior years to contribute up to twice the normal deferral limit (that is, up to \$36,000 in 2016 and 2017) in the three years prior to reaching the plan's normal retirement age. (However, these additional catch-up contributions can't exceed the total of the prior years' unused deferrals.) 457(b) participants who elect to use this special catch-up rule cannot also use the age 50 catch-up rule in the same year.

¹ "Boomer Expectations for Retirement 2016," Insured Retirement Institute.

Key Retirement and Tax Numbers for 2017



Every year, the Internal Revenue Service announces cost-of-living adjustments that affect contribution limits for retirement plans, thresholds for deductions and credits, and standard deduction and personal exemption amounts. Here are a few of the key adjustments for 2017.

Retirement plans

- Employees who participate in 401(k), 403(b), and most 457 plans can defer up to \$18,000 in compensation in 2017 (the same as in 2016); employees age 50 and older can defer up to an additional \$6,000 in 2017 (the same as in 2016).
- Employees participating in a SIMPLE retirement plan can defer up to \$12,500 in 2017 (the same as in 2016), and employees age 50 and older will be able to defer up to an additional \$3,000 in 2017 (the same as in 2016).

IRAs

The limit on annual contributions to an IRA remains unchanged at \$5,500 in 2017, with individuals age 50 and older able to contribute an additional \$1,000. For individuals who are covered by a workplace retirement plan, the deduction for contributions to a traditional IRA is phased out for the following modified adjusted gross income (AGI) ranges:

	2016	2017
Single/head of household (HOH)	\$61,000 - \$71,000	\$62,000 - \$72,000
Married filing jointly (MFJ)	\$98,000 - \$118,000	\$99,000 - \$119,000
Married filing separately (MFS)	\$0 - \$10,000	\$0 - \$10,000

Note: The 2017 phaseout range is \$186,000 - \$196,000 (up from \$184,000 - \$194,000 in 2016) when the individual making the IRA contribution is not covered by a workplace retirement plan but is filing jointly with a spouse who is covered.

The modified AGI phaseout ranges for individuals making contributions to a Roth IRA are:

	2016	2017
Single/HOH	\$117,000 - \$132,000	\$118,000 - \$133,000
MFJ	\$184,000 - \$194,000	\$186,000 - \$196,000
MFS	\$0 - \$10,000	\$0 - \$10,000

Estate and gift tax

- The annual gift tax exclusion remains at \$14,000.
- The gift and estate tax basic exclusion amount for 2017 is \$5,490,000, up from \$5,450,000 in 2016.

Personal exemption

The personal exemption amount remains at \$4,050. For 2017, personal exemptions begin to phase out once AGI exceeds \$261,500 (single), \$287,650 (HOH), \$313,800 (MFJ), or \$156,900 (MFS).

Note: These same AGI thresholds apply in determining if itemized deductions may be limited. The corresponding 2016 threshold amounts were \$259,400 (single), \$285,350 (HOH), \$311,300 (MFJ), and \$155,650 (MFS).

Standard deduction

These amounts have been adjusted as follows:

	2016	2017
Single	\$6,300	\$6,350
HOH	\$9,300	\$9,350
MFJ	\$12,600	\$12,700
MFS	\$6,300	\$6,350

Note: The 2016 and 2017 additional standard deduction amount (age 65 or older, or blind) is \$1,550 for single/HOH or \$1,250 for all other filing statuses. Special rules apply if you can be claimed as a dependent by another taxpayer.

Alternative minimum tax (AMT)

AMT amounts have been adjusted as follows:

	2016	2017
Maximum AMT exemption amount		
Single/HOH	\$53,900	\$54,300
MFJ	\$83,800	\$84,500
MFS	\$41,900	\$42,250
Exemption phaseout threshold		
Single/HOH	\$119,700	\$120,700
MFJ	\$159,700	\$160,900
MFS	\$79,850	\$80,450
26% on AMTI* up to this amount, 28% on AMTI above this amount		
MFS	\$93,150	\$93,900
All others	\$186,300	\$187,800

*Alternative minimum taxable income



When choosing between pretax and Roth contributions, the general rule is to consider whether you think you will benefit more from the tax break today than you would from a tax break in retirement. Specifically, if you think you'll be in a higher tax bracket in retirement, Roth contributions may be more beneficial in the long run.

Generally, non-Roth after-tax contributions should be considered after reaching the maximum contribution amount for pretax and Roth options.

Keep in mind that distributions of earnings on non-Roth after-tax contributions will be subject to regular income taxes and possibly penalty taxes if not rolled over to a traditional IRA. IRS Notice 2014-54 clarifies the rules regarding rollovers of non-Roth after-tax plan contributions to a Roth IRA.

For more information specific to your situation, consult a qualified tax professional. (Working with a tax or financial professional cannot guarantee financial success.)

Pretax, Roth, or After-Tax Contributions: Which Should You Choose?

If your employer-sponsored retirement savings plan allows pretax, after-tax, and/or Roth contributions, which should you choose?

Pretax: Tax benefits now

With pretax contributions, the money is deducted from your paycheck before taxes, which helps reduce your taxable income and the amount of taxes you pay now. Consider the following example, which is hypothetical and has been simplified for illustrative purposes.

Example(s): Mark earns \$2,000 every two weeks before taxes. If he contributes nothing to his retirement plan on a pretax basis, the amount of his pay that will be subject to income taxes would be the full \$2,000. If he was in the 25% federal tax bracket, he would pay \$500 in federal income taxes, reducing his take-home pay to \$1,500. On the other hand, if he contributes 10% of his income to the plan on a pretax basis--or \$200--he would reduce the amount of his taxable pay to \$1,800. That would reduce the amount of taxes due to \$450. After accounting for both federal taxes and his plan contribution, Mark's take-home pay would be \$1,350. The bottom line? Mark would be able to invest \$200 toward his future but reduce his take-home pay by just \$150. That's the benefit of pretax contributions.

In addition, any earnings made on pretax contributions grow on a tax-deferred basis. That means you don't have to pay taxes on any gains each year, as you would in a taxable investment account. However, those tax benefits won't go on forever. Any money withdrawn from a tax-deferred account is subject to ordinary income taxes, and if the withdrawal takes place prior to age 59½ (or in some cases, 55 or 50, depending on your plan's rules), you may be subject to an additional 10% penalty on the total amount of the distribution.

Roth: Tax benefits down the road

On the other hand, contributing to an employer-sponsored Roth account offers different benefits. Roth contributions are considered "after-tax," so you won't reduce the amount of current income subject to taxes. But qualified distributions down the road will be tax-free.

A qualified Roth distribution is one that occurs:

- After a five-year holding period and
- Upon death, disability, or reaching age 59½

Nonqualified distributions are subject to regular income taxes and a possible 10% penalty tax. However, because Roth contributions are made with after-tax dollars, a distinction is made

between the portion of the distribution that represents contributions versus earnings on those contributions. If at some point you need to take a nonqualified withdrawal from a Roth 401(k)--due to an unexpected emergency, for example--only the proportion of the total amount representing earnings will be taxable.

Example(s): In order to meet an unexpected financial need of \$8,000, Tina decides to take a nonqualified hardship distribution from her Roth 401(k) account. Of the \$20,000 total value of the account, \$18,400 represents after-tax Roth contributions and \$1,600 is attributed to investment earnings. Because earnings represent 8% of the total account value ($\$1,600 \div \$20,000 = 0.08$), this same proportion of Tina's \$8,000 distribution--or \$640 ($\$8,000 \times .08$)--will be considered earnings subject to both income taxes and a 10% penalty tax.

However, keep in mind that tapping your account before retirement defeats its purpose. If you need money in a pinch, try to exhaust all other possibilities before taking a distribution. Always bear in mind that the most important benefit of a Roth account is the opportunity to build a nest egg of tax-free income for retirement.

After-tax: For those who are able to exceed the limits

Some plans allow participants to make additional after-tax contributions. This plan feature helps those who want to make contributions exceeding the annual total limit on pretax and Roth accounts (in 2016, the limit is \$18,000; \$24,000 for those age 50 or older). As with a traditional pretax account, earnings on after-tax contributions grow on a tax-deferred basis.

If this option is offered (check your plan documents), keep in mind that total employee and employer contributions cannot exceed \$53,000, or \$59,000 for those 50 and older (2016 limits).

Another benefit of making after-tax contributions is that when you leave your job or retire, they can be rolled over tax-free to a Roth IRA, which also allows for potential tax-free growth from that point forward. Some higher-income individuals may welcome this potential benefit if their income affects their ability to directly fund a Roth IRA.¹

¹ In addition to rolling the proceeds to a Roth IRA, participants may also (1) leave the assets in the original plan, (2) transfer assets to a new employer's plan, or (3) withdraw the funds (which in some cases could trigger a taxable event).

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Should I accept my employer's early-retirement offer?

The right answer for you will depend on your situation. First of all, don't underestimate the psychological impact of early retirement. The adjustment from full-time work to a more leisurely pace may be difficult. So consider whether you're ready to retire yet. Next, look at what you're being offered. Most early-retirement offers share certain basic features that need to be evaluated. To determine whether your employer's offer is worth taking, you'll want to break it down.

Does the offer include a severance package? If so, how does the package compare with your projected job earnings (including future salary increases and bonuses) if you remain employed? Can you live on that amount (and for how long) without tapping into your retirement savings? If not, is your retirement fund large enough that you can start drawing it down early? Will you be penalized for withdrawing from your retirement savings?

Does the offer include post-retirement medical insurance? If so, make sure it's affordable and provides adequate coverage. Also, since Medicare doesn't start until you're 65, make

sure your employer's coverage lasts until you reach that age. If your employer's offer doesn't include medical insurance, you may have to look into COBRA or a private individual policy.

How will accepting the offer affect your retirement plan benefits? If your employer has a traditional pension plan, leaving the company before normal retirement age (usually 65) may greatly reduce the final payout you receive from the plan. If you participate in a 401(k) plan, what price will you pay for retiring early? You could end up forfeiting employer contributions if you're not fully vested. You'll also be missing out on the opportunity to make additional contributions to the plan.

Finally, will you need to start Social Security benefits early if you accept the offer? For example, at age 62 each monthly benefit check will be 25% to 30% less than it would be at full retirement age (66 to 67, depending on your year of birth). Conversely, you receive a higher payout by delaying the start of benefits past your full retirement age--your benefit would increase by about 8% for each year you delay benefits, up to age 70.



Should I pay off my student loans early or contribute to my workplace 401(k)?

For young adults with college debt, deciding whether to pay off student loans early or contribute to a 401(k) can be tough. It's a financial tug-of-war between digging out from debt today and saving for the future, both of which are very important goals. Unfortunately, this dilemma affects many people in the workplace today. According to a student debt [report](#) by The Institute for College Access and Success, nearly 70% of college grads in the class of 2014 had student debt, and their average debt was nearly \$29,000. This equates to a monthly payment of \$294, assuming a 4% interest rate and a standard 10-year repayment term.

Let's assume you have a \$300 monthly student loan payment. You have to pay it each month--that's non-negotiable. But should you pay more toward your loans each month to pay them off faster? Or should you contribute any extra funds to your 401(k)? The answer boils down to how your money can best be put to work for you.

The first question you should ask is whether your employer offers a 401(k) match. If yes, you

shouldn't leave this free money on the table. For example, let's assume your employer matches \$1 for every dollar you save in your 401(k), up to 6% of your pay. If you make \$50,000 a year, 6% of your pay is \$3,000. So at a minimum, you should consider contributing \$3,000 per year to your 401(k)--or \$250 per month--to get the full \$3,000 match. That's potentially a 100% return on your investment.

Even if your employer doesn't offer a 401(k) match, it can still be a good idea to contribute to your 401(k). When you make extra payments on a specific debt, you are essentially earning a return equal to the interest rate on that debt. If the interest rate on your student loans is relatively low, the potential long-term returns earned on your 401(k) may outweigh the benefits of shaving a year or two off your student loans. In addition, young adults have time on their side when saving for retirement, so the long-term growth potential of even small investment amounts can make contributing to your 401(k) a smart financial move.

All investing involves risk, including the possible loss of principal, and there can be no guarantee that any investing strategy will be successful.

