Investment News April 2017

Building an Emergency Fund

Everyone should aim to have a cash reserve.

We all would love to have a little extra cash on hand for emergencies. Saving up that cash can be a challenge – but with a little effort, that challenge can be met.

Imagine a 30-year-old couple with no real savings. Let's call them Kurt and Diana. Together, they earn about $8,000 a month, but their household finances are being squeezed by education debt, rent, and the high cost of living in an affluent metro area. They have about $300 in the bank between them, and they just learned they have a baby on the way. Their need to save has never been greater. How can they do it?

They have many options for building their fund, more than they first assume. Kurt has an old dirt bike gathering dust in his dad's garage, and he is no longer into off-road motorcycling. Even in its dusty condition, it could easily be sold for more than $1,500. They each have gym memberships; Kurt drops his and Diana switches to a cheaper gym, leading to a 12-month savings of $500.

Kurt also explores the possibility of working weekends or evenings as a barista in addition to his full-time job, a move that could bring in a couple of thousand dollars in the next few months. The pair sense they have a federal tax refund coming – and the average I.R.S. refund for the 2015 tax year was $2,860. They could put some or all of a four-figure refund toward their emergency fund, rather than toward paying down their student loans.[1]

Ideally, Kurt and Diana's emergency fund should be $25,000 or more (the equivalent of 3 or more months of living expenses). No, they are not going to come close to that this year. Or next year. They have started, though, and it looks as if they will soon have a few thousand dollars set aside for emergencies. Even having $1,000 could ease many acute financial pains.

There are numerous potential ways to boost your emergency fund. Some are simple: save $5 or $10 a week and deposit it, eat out less, drop those memberships and subscriptions, sell something, save the money the I.R.S. hands back to you. Some require more ingenuity and energy: getting a part-time job for supplemental income, renting out a room.

Perhaps the easiest way of all is to create an automatic transfer of a small portion of your paycheck into a dedicated emergency savings account each month. Saving will seem painless this way, and when you pay off a debt, you can direct the money you used each month to reduce it into your emergency fund instead.

Citations.

1 - fool.com/retirement/2017/02/26/how-big-is-the-average-americans-tax-refund.aspx [2/26/17]

Horwitz & Associates
1650 Lake Cook Road, Suite 190
Deerfield, IL 60015

Phone: 224-632-4600
Fax: 224-632-4590

Www.HorwitzAdvisors.com
Ed Horwitz — Ed@HorwitzAdvisors.com
Gerald Horwitz — GAH@HorwitzAdvisors.com

2017 Market Performance 01/01/2017 to 03/31/2017

DJIA ^DJI Up 4.56%
S&P 500 ^GSPC Up 5.53%
NASDAQ ^IXIC Up 9.82%
Russell 2000 ^ RUT Up 2.12%

* Index performance does NOT include any fees (Gross of fees)

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When Someone Dies Without a Will

Where do things proceed from that point?

Every day, people die intestate. In legalese, that means without a will. This opens the door for the courts to decide what happens with their estates.

When no valid will exists, state intestacy laws dictate how assets are distributed. These laws divide an estate evenly (or equitably) among heirs. Any assets held in joint tenancy go to the joint owner. Assets held in a trust transfer to the trust beneficiaries (with spouses getting a share of those assets in some states). Community property goes to a spouse or partner in community property states.[1]

Simple, right? Unfortunately, the way assets transfer under these laws may not correspond to the wishes of the deceased person. Did the decedent want some of his or her estate to go to a charity or a person close to them? These laws will not allow that. State law will also decide who the executor of the estate is, since the decedent never named one.[2]

If the deceased person designated beneficiaries for his or her retirement accounts and life insurance policy, those retirement accounts and insurance proceeds should transfer to those beneficiaries without dispute, even when no will exists. When life insurance policies and retirement accounts lack designated beneficiaries, then those assets are lumped into the decedent's estate and subject to intestacy laws.[2]

Most people have specific ideas about who should inherit what from their estates. To articulate those ideas, they should write a will – or better yet, they should draft one with the help of an attorney. Anyone who cares about the destiny of his or her wealth should take this basic estate planning step.

For a last will & testament to be valid, it must meet three important tests. It must be created by a person of sound mind. It must express that person's free will – that is, it cannot be written or drafted under coercion or duress. Lastly, it must be signed and dated in the presence of two or more unrelated people who stand to inherit nothing from that person's estate.[1]

Many wills are signed in the presence of notaries; although, a will does not have to be notarized to be legally valid. Some wills are self-proving – they have an attached, notarized affidavit, which acknowledges that all three tests noted in the preceding paragraph have been met. When this affidavit accompanies a will, there is no need to track down the parties who witnessed the signing and dating of the document years before.[1]

A last will and testament should be formatted and printed using a computer and printer; at the very least, it should be typed. Handwritten wills may not pass muster in some probate courts.[1]

When an individual dies intestate, the future of his or her estate is largely up to the courts. A basic, valid will stating his or her wishes may prevent that fate.

Citations.
1 - legalzoom.com/knowledge/last-will/topic/wills-intestate [3/20/17]
2 - money.cnn.com/2016/04/28/pf/dying-without-a-will-prince/ [4/28/16]

Key Estate Planning Mistakes to Avoid

Too many people make these common errors.

Many affluent professionals and business owners put estate planning on hold. Only the courts and lawyers stand to benefit from their procrastination. While inaction is the biggest estate planning error, several other major mistakes can occur. The following blunders can lead to major problems.

Failing to revise an estate plan after a spouse or child dies. This is truly a devastating event, and the grief that follows may be so deep and prolonged that attention may not be paid to this. A death in the family commonly requires a change in the terms of how family assets will be distributed. Without an update, questions (and squabbles) may emerge later.

Going years without updating beneficiaries. Beneficiary designations on qualified retirement plans and life insurance policies usually override bequests made in wills or trusts. Many people never review beneficiary designations over time, and the estate planning consequences of this inattention can be serious. For example, a woman can leave an IRA to her granddaughter in a will, but if her ex-husband is listed as the primary beneficiary of that IRA, those IRA assets will go to him per the beneficiary form. Beneficiary designations have an advantage – they allow assets to transfer to heirs without going through probate. If beneficiary designations are outdated, that advantage matters little.[1,2]

Thinking of a will as a shield against probate. Having a will in place does not automatically prevent assets from being probated. A living trust is designed to provide that kind of protection for assets; a will is not. An individual can clearly express "who gets what" in a will, yet end up having the courts determine the distribution of his or her assets.[2]

Supposing minor heirs will handle money well when they become young adults. There are multimillionaires who go no further than a will when it comes to estate planning. When a will is the only estate planning tool directing the transfer of assets at death, assets can transfer to heirs aged 18 or older in many states without prohibitions. Imagine an 18-year-old inheriting several million dollars in liquid or illiquid assets. How many 18-year-olds (or 25-year-olds, for that matter) have the skill set to manage that kind of inheritance? If a trust exists and a trustee can control the distribution of assets to heirs, then situations such as these may be averted. A well-written trust may also help to prevent arguments among young heirs about who was meant to receive this or that asset.[3]

Too many people do too little estate planning. Avoid joining their ranks, and plan thoroughly to avoid these all-too-frequent mistakes.

Citations.
1 - thebalance.com/why-beneficiary-designations-override-your-will-2388824 [10/8/16]
2 - fool.com/retirement/2017/03/03/3-ways-to-keep-your-estate-out-of-probate.aspx [3/3/17]
3 - info.legalzoom.com/legal-age-inherit-21002.html [3/16/17]

The 60-Day IRA Rollover Rule

Will it apply to your retirement savings distribution?

If you receive a distribution from your IRA or workplace retirement plan, what will you do with it? You will probably want to arrange an IRA rollover – a common and useful financial move designed to take these invested assets from one retirement account to another, without tax consequences. The I.R.S. may give you just 60 days to do it, however.

The clock starts ticking on the day you receive the distribution. If assets from your employee retirement plan account or your IRA are paid directly to you, you have 60 calendar days to transfer those funds into an IRA or workplace retirement plan. If you fail to do that, the I.R.S. will characterize the entire distribution as taxable income. (It may also tack on a 10% early withdrawal penalty if you take possession of such funds before age 59½.)[1]

Your goal is to make this indirect rollover by the deadline. It is called an indirect rollover because its mechanics can be a bit involved. If the assets are coming out of an employee retirement plan, your employer may withhold 20% of them in accordance with tax laws. Unfortunately, you do not have the option of depositing only 80% of the distribution into an IRA or another employee retirement plan – you must deposit 100% of it by the deadline. You have to come up with the remaining 20%, yourself, from your own savings. The withheld 20% should be returned to you at tax time if the rollover completes smoothly.[2]

Can you make multiple IRA rollovers using funds from a single IRA? You can, but the I.R.S. says the rollovers must occur at least 12 months apart. Additionally, the I.R.S. prohibits you from making a rollover out of the "new" IRA that receives the transferred assets for a year following that transfer.[1]

This 12-month limit does not apply to every kind of retirement plan rollover. Trustee-to-trustee transfers, where the investment company (acting as custodian of your IRA or retirement plan account) simply sends a check for the assets to the brokerage firm that will eventually receive them, are exempt from the 60-day deadline. So are rollovers between workplace retirement plans, IRA-to-plan rollovers, and plan-to-IRA rollovers. If you are converting a traditional IRA to a Roth IRA, the 60-day rule is also irrelevant.[1,2]

Some retirement savers simply opt for a trustee-to-trustee transfer – a direct rollover – rather than an indirect one. A direct rollover of retirement assets is routine, and it can be coordinated with the help of a financial professional. If you do prefer to perform an indirect rollover on your own, be mindful of the 60-day rule and the potential ramifications of missing the deadline.

Citations.

1 - irs.gov/retirement-plans/plan-participant-employee/rollovers-of-retirement-plan-and-ira-distributions [2/8/17]

2 - fool.com/retirement/2017/03/08/what-to-do-with-your-old-401k-when-switching-jobs.aspx [3/8/17]