STRATEGIC Wealth Advisors

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The Tax Impact of a 529 Rollover

Thirty-four states offer some sort of tax deduction or tax credit for contributions made to a 529 plan. But in 29 of those 34 states, the tax break is available only for contributions made to an in-state plan. Only Arizona, Kansas, Maine, Missouri, and Pennsylvania give residents a tax break for contributing to any state's plan. If you own an out-of-state 529 plan, you may be missing out on this tax break advantage, and it may be worthwhile to do some research and consider rolling your out-of-state plan to an in-state one.

The tax break can be a real plus, but the quality of the 529 plan (its investment options and fees, in particular) is important, too. If you've already opened an out-of-state 529 plan a while ago, you may want to revisit that decision because 529 plans can change over time. If your state now offers a better plan, check with the plan or a tax professional to see if there are tax advantages to rolling funds over. Many states do not provide a tax break for inbound 529 rollovers, but some do. States that do may limit deductions to just the contribution portion of the out-of-state 529 or let you deduct the entire amount including earnings.

529 plans are tax-deferred college savings vehicles. Any unqualified distribution of earnings will be subject to ordinary income tax and subject to a 10% federal penalty tax. An investor should consider the investment objectives, risks, and charges and expenses associated with municipal fund securities before investing. More information about municipal fund securities is available in the issuer's official statement, and the official statement should be read carefully before investing. Tax law is ever-changing and can be quite complex. It is highly recommended that you consult with a legal, tax, or financial professional with any questions or concerns.

What's Happening at SWA

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April 15th marked the official "end" of tax season. With that behind us (at least for those of us who didn't extend), The SWA Team kindly requests that all of our advisory clients send us a copy of their 2012 Federal and state income tax returns (including all schedules). We use your returns to monitor a number of parameters such as taxable income, deductions, marginal and average income tax brackets, capital loss carry forwards, net operating losses, taxable Social Security benefits, and more. This information, in turn, may be used to update financial projections and make investment and financial planning decisions. We prefer electronic copies of returns but hard copies will work as well. Please contact us with any questions.

Monthly Market Commentary

Recovery, full steam ahead? It would appear so. The stock market returned 11.02% during the first quarter of 2013, and the U.S. economy continues to grow at a slow but steady pace, despite apparent volatility and instability displayed by most major economic indicators.

GDP: For starters, real GDP growth rates have been highly volatile from quarter to quarter; for example, from 3.1% in Q3 2012 to only 0.1% in Q4 2012. However, it's important to keep in mind that the data includes some measurement and seasonal-adjustment issues that may blur the big picture a little bit. Morningstar economists forecast that GDP will grow at a slow, but sustainable 2.0%–2.5% rate in 2013, very similar to 2011 and 2012.

Employment: The private sector added only 95,000 jobs in March (compared with 254,000 in February). At first glance, this number is discouraging, and the lowest in nine months. However, similar to the case for GDP above, month-to-month data is volatile, influenced by weather and other seasonal factors, and often subject to revisions. Three-month average employment growth (YOY), a more reliable data point, does show slow erosion, but no catastrophic decline (2.1% in December, 2.0% in January, and 1.9% in February and March).

The Big Four: Given all the fiscal scares, Hurricane Sandy, volatile gasoline prices, and new taxes, the U.S. economy is doing surprisingly well, according to the Big Four economic indicators (private employment growth, retail sales, manufacturing, and real disposable income). Private sector year-over-year employment growth has been steady at 2% for almost two years, while retail sales growth (adjusted for inflation and excluding autos and gasoline) has been in the 2%–3% range for almost as long. Even U.S. manufacturing data hasn't been particularly volatile, especially if weather events are removed. Of the Big Four, only real disposable income has been very volatile, and most of that volatility is due to ever-shifting inflation rates (with food and energy showing the most volatility) and changes in government tax policy, not changes in wages.

Consumer: Consumer spending continues to drive the economy, constituting about 70% of GDP. Unfortunately, consumers were severely hit early in 2013 with soaring gasoline prices, a higher payroll tax, and delayed tax refunds. On the other hand, they also have a lot going for them, including lower inflation in many categories, better employment prospects, increasing home prices and related construction activity, and a much higher stock market and related wealth effects. While consumer spending is not as robust as it once was, it is clearly not falling apart in the middle of all the economic headwinds, either.

Quarter-end insights: A lot of fiscal issues were at least temporarily "settled" this quarter, helping to reassure both consumers and businesses. The fiscal cliff negotiations and the March sequestration resulted in a total deficit reduction of about $300 billion slated for 2013. The Fed plans on maintaining a relatively loose monetary policy, assuring investors that low interest rates and bond buybacks would continue to fuel further growth. As slow as this growth may be, the U.S. economy is better positioned and growing faster than many other developed economies. Some of the factors providing a longer-term advantage include newfound supplies of oil and gas, low electricity prices, more available land for building, and an improving auto industry.

In Europe, however, the situation isn't getting better, even when excluding the effects of the Cyprus situation. The Chinese economy seems to have bottomed, and future Chinese growth (if any) will likely be lower than previous peaks, and more likely to be consumption based than focused on infrastructure. Last, but not least, U.S. corporations are starting to invest for growth again (capital spending and acquisitions), which could prove to be an effective engine for further stock market appreciation.

Financial Preparations for a Natural Disaster

As residents of areas affected by Hurricane Sandy found out, a natural disaster can bring about not only emotional hardship, but financial hardship, as well. From keeping important documents safe and accessible to having enough cash on hand to get by until things return to normal, being prepared for a disaster is an important part of protecting your home and your family. It could be a natural disaster like a hurricane, tornado, flood, fire, mudslide, or earthquake. Or it could be something on a more limited scale like a power outage. Whatever the crisis, taking the steps below will help you better handle whatever might come your way.

Get Organized Before a Disaster Strikes: Chances are that's not at the top of your to-do list for the weekend, so it's very easy to procrastinate. But think of it this way: You buy insurance to protect you from catastrophes; disaster preparedness is just another kind of insurance that you prepare yourself. It doesn't have to cost a lot, but it could really save time and added frustration should something happen to you. Once you've got a plan, you only need to update it periodically.

Keep Important Papers and Documents Safe and Easily Accessible: You might need to gather your most important papers in a hurry. Do you know where they are? Can you grab them quickly and leave the house immediately if you need to? Here are some of the documents to which you may need access: IDs (driver's license, Social Security card, passport, birth certificate), financial documents (checkbooks, investment account numbers, passwords, and phone numbers, retirement account information, estate documents, insurance policies), and medical records. Most importantly, you'll need cash (at least enough to cover one to two weeks' emergency expenses).

You might also want to have a list of key contacts/phone numbers, which may include family cell-phone numbers and e-mail addresses, police, fire, and ambulance numbers, Red Cross and emergency response center local numbers, as well as your company's human resources department number.

Keep all these important papers in a plastic bag in your home safe, or in any safe place from where you can grab them quickly if you need to leave your home in a hurry. Also, it may be a good idea to leave copies of everything with your attorney and/or financial advisor, in case the original documents get lost or damaged.

Prepare for a Medical Emergency: What if you or a family member suffer an injury (or worse) when disaster strikes? Check your health-insurance coverage to determine out-of-pocket costs in case surgery or emergency treatment is needed, and try to set aside enough money to cover these costs. Designate a family member or close friend as your primary contact, and prepare a living will and power of attorney for health care (documents that specify your wishes in case you're incapacitated).

Create an Emergency Fund: Most experts recommend setting aside enough money to cover about six months of living expenses. But it is equally important that this money be easily accessible. It may be a good idea to keep about half in cash, ready to use (what if it's impossible to get to a bank in the aftermath of the disaster?), and the other half in liquid investments that you can cash out easily.

What to Do if Disaster Strikes: If your house has been damaged, you may need emergency shelter. The Red Cross or your local emergency response center should be able to help. Your property insurance agent can help you file a claim on your homeowners or other types of insurance policies. If your area has been declared a federal disaster area, you may qualify for financial relief. If you have been injured, you might need to file for disability benefits. If you are healthy but a family member needs your care, you may be able to take as many as 12 weeks of unpaid leave under the Family and Medical Leave Act without losing your job.

A Beginner's Guide to Credit Cards

Credit cards are magic little pieces of plastic that allow you to use money without having it, right? Wrong. The reality is that credit cards are magic little pieces of plastic designed to make money for the credit-card companies. Not being aware of your full responsibilities as a credit card holder can bury you deep in debt and significantly limit your access to credit in the future. Therefore, it is crucial for you, the consumer, to be aware of all the little details of credit-card transactions.

A credit card is a valuable convenience, since it means you don't have to carry cash around anymore. But it definitely does not mean that you can make unlimited purchases and not pay for them, as some people may think. With a credit card, all the purchases you make during a certain period of time are allowed to accumulate, and you receive a bill (statement) for the total amount spent at the end of that time period (usually a month). Once you get the bill, you have a grace period—normally 20 to 25 days—until the due date.

When you receive the bill, you'll notice you can make a minimum payment, or you can pay the balance in full. In other words, you owe $3,000, but you can make only a minimum payment of $1,000 and keep the other $2,000 for yourself. This is great, right? Wrong again. If you do not pay your balance in full, your credit card company will make money by charging you fees.

Finance charges and late fees: If you have an outstanding balance (money that was not paid on time) on your credit card, you will pay interest on that balance. There are various methods for calculating your outstanding balance (adjusted balance, average daily balance, previous balance, ending balance), so try to understand which method your credit card issuer uses. Credit-card issuers have to disclose the interest rate they charge, so make sure you know what your APR (annual percentage rate) is. If you are billed monthly, the interest rate used to calculate your finance charges will generally be your APR divided by 12. Also, credit -card rates can be fixed or variable, so if yours is variable make sure you understand why it varies and how.

If you pay your balance in full every time, you will manage to avoid finance charges, but it is still important for you to know what they are, just in case. Before you sign up for the card (not after!), read the payment rules carefully (they differ from one issuer to another). If you pay by check, mail the payment early or, even better, pay online. Be aware that paying late may result in an increase of your interest rate in the future.

In addition to finance charges, every time you delay payment you will have to pay a late fee, which can be substantial. It is obviously in your best interest to pay your balance in full every time and as early as possible. Also, when deciding which credit card to choose, look for a card with a low APR. It may have fewer bells and whistles, but it will save you money in the long run. A useful source of information on credit card rates is the website www.bankrate.com.

Annual fees, credit limit fees, cash advance fees, and balance transfer fees: Some credit card issuers charge an annual fee per card, usually assessed on your first statement. Fortunately, avoiding this one is simple: Choose a card without an annual fee. You can also be charged if your outstanding balance exceeds your credit limit. You can probably avoid this fee by requesting a credit limit increase, but this is tricky because then you'll be tempted to spend more. Card companies generally charge a fee for cash advances, which can be calculated as a flat charge per transaction or as a percentage of the total. You can also be assessed a fee for balance transfers. The point should be clear by now: It is in the credit card company's best interest to charge you all these fees, and it is in your best interest to avoid them. Make sure you know all the rules, and make all your payments on time.

Social Security for the Self-Employed

If you thought that running a successful business on your own was hard enough already, think again. As a self-employed individual, defined by the IRS as someone who operates a trade, business or profession, (either by yourself or as a partner), you are required to pay self-employment tax as well as income tax. Self-employment tax consists of Social Security and Medicare taxes, similar to those withheld from the pay of most wage earners. Failure to comply with IRS regulations may result in your business operations being jeopardized. The following are a few key facts to keep in mind:

1. The Social Security tax rate for 2013 is 15.3% on self-employment income up to $113,700. Should your net earnings exceed $113,700, you continue to pay only the Medicare portion of the Social Security tax, which is 2.9%. Starting this year, the Medicare tax rate for net earnings in excess of $200,000 ($250,000 for joint filers) is increased to 3.8%.

2. You need to have worked and paid Social Security taxes for a certain length of time to get Social Security benefits (no more than 10 years of work, which is equivalent to 40 credits). In 2013, if your net earnings are $4,640 or more, you earn the yearly maximum of four credits. If your net earnings are less than $4,640, you could still earn credit (depending on how you report your earnings).

3. Certain income does not count for Social Security and should not be included in figuring your net earnings. These include dividends from shares of stocks and interest on bonds, interest from loans, rentals from real estate, and income received from limited partnerships.

Tax law is ever-changing and can be quite complex. It is highly recommended that you consult with a financial or tax professional with any tax-related questions or concerns.

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