RYAN POAGE & CO.
INVESTMENTS | WEALTH MANAGEMENT

TAKING STOCK

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816-531-4555

Learn The Ins And Outs Of Education Tax Breaks

If you have one or more children in college, or your offspring will be heading to college or university soon, you already know about the ever-rising cost of higher education. It's not unusual for a year at an elite university to cost $50,000 or even more. Suppose you have three children who have the grades to get into top-notch colleges and each one spends four years at such a school. That's a total cost of at least $600,000!

Although federal tax laws provide some relief to parents in the form of two higher education credits and a tuition deduction, those tax breaks are phased out for upper-income taxpayers. What's more, you can claim only one of those tax benefits in a year. Here's what's available:

1. American Opportunity Tax Credit (AOTC). The AOTC, formerly known as the Hope Scholarship credit, recently was extended by Congress through 2017. The credit equals the sum of 100% of the first $2,000 of qualified tuition and related expenses and 25% of the next $2,000 of such expenses, for a maximum annual credit of $2,500. But you could claim the credit for each child who's in college, so if you have three kids in school at the same time, you could claim a maximum credit of $7,500 in that year.

Under another recent tax law change, the AOTC now applies to the first four years of a student's higher education. Previously, it was limited to just two years. Furthermore, you're allowed to receive up to 40% of the value of the AOTC as a tax refund, up to a maximum of $1,000, in the unlikely event that you have zero tax liability.

But the AOTC is phased out based on a family's modified adjusted gross income (MAGI). For 2015, the phaseout range is between $80,000 to $90,000 of MAGI for single filers and $160,000 to $180,000 for joint filers. Once you exceed the higher threshold, you can't claim the AOTC at all.

2. Lifetime Learning Credit (LLC). Unlike the AOTC, the LLC is on the books permanently, but it is generally not as beneficial as its close cousin. It is equal to 20% of the first $10,000 of qualified expenses, for a maximum of $2,000. And that limit applies to each taxpayer, not each student. So for those parents with three children in school at the same time, the maximum credit remains $2,000. What's more, unlike the AOTC , the LLC can't result in a tax refund.

Finally, the MAGI phaseout levels for the LLC are even lower than they are for the AOTC. For 2015, the range is between $55,000 to $65,000 for single filers and $110,000 to $130,000 for joint filers.

3. Tuition deduction. Finally, you may be able to deduct tuition and related fees that you pay to a college on behalf of your dependent children. The allowable deduction is either $4,000 or $2,000 depending on your MAGI for the year. For single filers, the deduction is $4,000 for a MAGI of up to $65,000 and $2,000 if your MAGI is between $65,000 and $80,000. Joint filers can deduct $4,000 for a MAGI of up to $130,000 and $2,000 if your MAGI is between $130,000 and $160,000. Exceed those upper thresholds and you don't get the deduction.

The tuition deduction officially expired after 2013. However, after much debate in Congress, it was extended retroactively one year for 2014.

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Nasdaq Milestone Brings Humorous Reflection

At the time of this writing, the Nasdaq Index is close to finally hitting a new high, 15 years after its tech-bubble peak. It's been a long and interesting journey and reminds me of a now-funny conversation I had as a newly licensed financial advisor intern when I was a college senior.

The son of the firm's founder and I were talking about the unbelievable growth in the markets and he said "Can you imagine that when my dad got started in the business (in the 1960s) the market didn't go anywhere for 15 years . . . can you imagine that?" I responded, "Oh no, that would be crazy. Thank goodness that era is over . . . ."

Well, three years later I opened a branch of a major brokerage firm. The week it opened the Dow peaked, and two months later the Nasdaq hit its now 15 year old record.

Let that be one more example of the investing relevance of the Mark Twain quote about history not repeating itself but often rhyming. I'm all for the next phase rhyming like the 1980s & 90s.

Ryan

Go Back In Time On Roth Conversion

Who says you can't go home again? If you recently converted funds in a traditional IRA into a Roth and the value of the account has declined, or you have other reasons for regretting the move, you can "recharacterize" the conversion. In effect, it's like it never happened. But a "return home" isn't automatically allowed. You must meet an IRS deadline.

Why would you convert in the first place? If you're in a high tax bracket and actively participate in an employer retirement plan, your contributions to a traditional IRA aren't tax deductible, and though you won't be taxed when you withdraw those contributions during retirement, you will owe taxes, at your ordinary income rate, on distributions of investment earnings from the account. The top current tax bracket is 39.6%, plus you may owe an extra 3.8% surtax on net investment income (NII). And, under the rules for required minimum distributions (RMDs), you must begin emptying your IRA in annual increments after age 70½.

In contrast, qualified distributions from a Roth that's at least five years old are 100% tax-free. The 3.8% surtax also doesn't apply. ("Qualified" means that the distribution was (1) made after age 59½, (2) made on account of death or disability, or (3) used for first-time homebuyer expenses, with a lifetime limit of $10,000.) Moreover, RMD rules don't apply to a Roth IRA during your lifetime. You can keep your account intact and pass it along to your heirs, who will be able to take lifelong, tax-free distributions. The only catch is that to make a conversion to a Roth IRA, you must pay tax on the amount you transfer, just as you would on a regular IRA distribution.

But what if the value of the converted account declines significantly? Suppose you converted $500,000 in an IRA to a Roth on January 1. If you're in the 39.6% tax bracket this year, the conversion tax is $198,000 (39.6% of $500,000). However, if the account value falls to $450,000, you've paid $19,800 more in tax (39.6% of the $50,000 difference) than you would have owed if you had waited to convert.

The tax law permits you to recharacterize a Roth back to a traditional IRA. You just have to meet the deadline for a recharacterization—the due date for your tax return for the year of the conversion, plus any extensions. So you'll be able to reverse a 2014 Roth conversion as late as October 15, 2015.

And if circumstances dictate that you change your mind again? You can reconvert your account back to a Roth, but you'll have to wait until the later of (1) the beginning of the tax year following the tax year of the conversion and (2) the end of the 30-day period beginning on the day of the recharacterization. ●

Straight Talk About Living Trusts

Ask two financial experts about the benefits of using a revocable living trust and you might well get precisely opposite reactions, especially on a regional basis. One might say that it's the greatest thing since sliced bread, while the other could argue that it should be avoided like the plague. The truth probably lies somewhere in between.

How does a living trust work? You set up the trust, transfer assets to it, and name a trustee to handle matters. If you designate yourself as the "initial beneficiary," you're entitled to receive income from the trust for the rest of your life. At the same time, you designate "secondary beneficiaries"—perhaps your spouse, your children, or both spouse and kids—who will receive the remaining assets when the trust terminates.

Significantly, you can still retain some control of assets in a living trust while you're alive. For instance, depending on the trust terms, you may be able to sell assets and keep the proceeds, amend terms of the trust (for example, change secondary beneficiaries), or revoke it entirely. The assets in the trust become irrevocable upon your death.

The main advantage is that assets in a living trust are exempt from probate, a process that may be required for assets bequeathed through a will. Proponents of living trusts note that the probate process can be costly and time-consuming. Also, if you face physical or mental limitations in your old age, with a living trust, a trustee for your assets is already in place.

However, detractors point out there are less expensive ways of avoiding probate, such as acquiring property jointly with rights of survivorship (although this may not be the best option in community property states). Also, the cost and complexity of probate is often exaggerated and can vary greatly from state to state. Finally, despite a common perception to the contrary, there's no estate tax advantage to using a living

The Energy Boost To The Economy

If gasoline prices in 2015 stay at the current level, the American economy could literally experience a major energy boost.

In 2013, Americans spent an amount equal to 2.4% of gross domestic product (GDP) on motor fuels and home heating oil. In late 2014, gasoline prices were down about 18% from $3.75 per gallon in 2013 to $3.08. If the 2.4% share of GDP spent on gasoline and diesel fuel in 2013 were reduced by 18%, it would mean that Americans would get an additional 0.43% of GDP (18% X 2.4%) to spend on all other retail categories.

Of course, consumers might choose to bank some of the savings they're getting from lower gas prices, and you can't assume that the GDP will get a.43% boost from energy savings in 2015. But, even if the boost to the economy were half of that amount, say .20% instead of .43%, it's a material plus looking ahead.

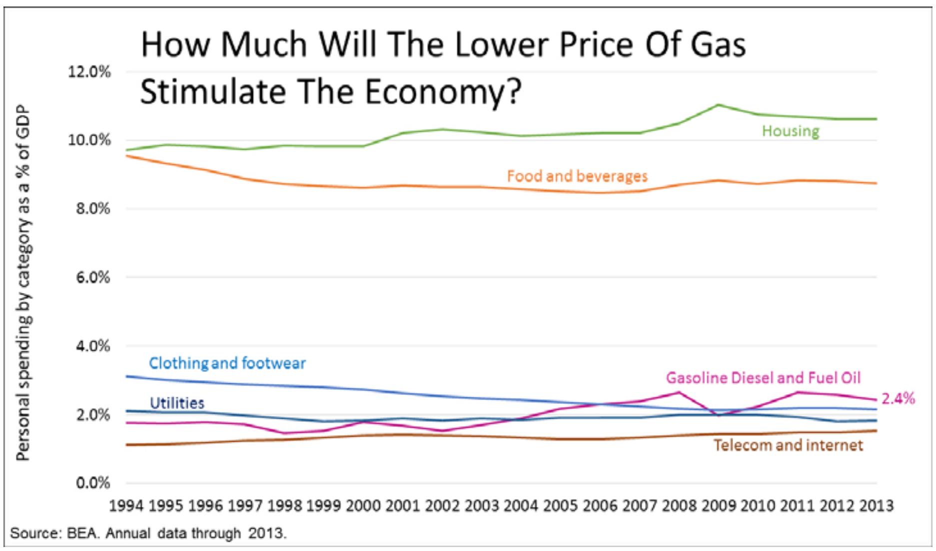
Even if consumers don't turn around and spend every dollar saved on lower gasoline prices, the stimulus to GDP provided by the energy boost is likely to have a noticeable effect on the economy. A three-tenth of 1% boost to GDP tacks on an additional 10% to GDP growth. That money stays in the U.S., and will help create jobs and trickle down through the system.

In addition to the energy boost resulting from lower gas prices, car sales and housing starts also are brightening the economic forecast for the U.S.

Car sales collapsed during the last recession but have recovered fully. We're running at about a rate of 17 million car sales per year, but the average car in the U.S. fleet is 11 years old, and that is old by historical standards. As a result, it is likely that car sales will be robust for the foreseeable future as we replace old cars with new ones.

Housing starts also are experiencing a tailwind because of demographic factors. The U.S. population grows by three million annually, which requires adding about 1.5 million housing units a year to accommodate our growing population. At the rate the U.S. was building new housing at the end of 2014, we were set to build one million new housing units in 2015. To keep up with population growth, the rate at which new housing units are built in 2015 is likely to increase to the 1.5 million historical norm, further adding to the likelihood of a "Goldilocks economy" -- not too hot, not too cold, but just right.

Of course, the world and personal circumstances can impose a new reality on you at any moment. Factors unknown to us currently can overtake economic fundamentals temporarily at any time. Still, the tailwind to economic growth is undeniable and perhaps explains why U.S. stocks, as measured by major broad stock indexes, have broken through to new all-time highs. ●



Source: BEA. Annual data through 2013.

trust if you retain the right to revoke it, as is typically provided. And even die-hard supporters of living trusts acknowledge you'll still need a will to tie up the loose ends of your estate.

So when does a living trust make sense? Consider these four key factors:

1. Age. Younger people in good health have less incentive to use a living trust than do retirees. Remember, a living trust will provide little benefit during your life.

2. Financial status. The more wealth you have, the more you're likely to benefit from a living trust. It will make things easier on your heirs if some or all of your assets bypass probate.

3. Marital status. If you're married and you own a house or other main assets jointly with your spouse, there's less need for a living trust. Furthermore, many states allow surviving spouses to use expedited probate procedures.

4. Confidentiality. One of the main arguments for a living trust is that your testamentary disposition remains confidential. This could be important for some families.

Don't be swayed by the hype of either point of view. Make an assessment of whether a living trust is right for you. ●

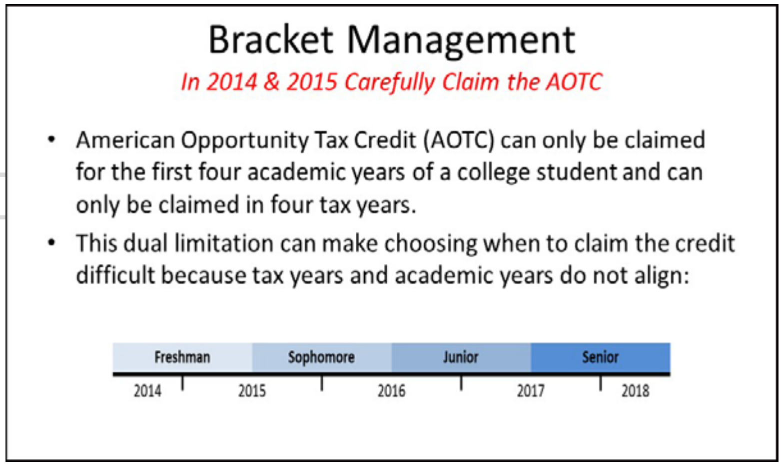
Education Tax Breaks

(Continued from page 1)

Remember that you can claim only one of these three tax breaks in a given year, even if you don't exceed the phaseout limits. Because those cutoffs are relatively low, and because the tax relief they offer won't make much of a dent in the overall cost of sending a child to college, most parents will need to look elsewhere for tax benefits. Consider the advantages of college saving devices such as Section 529 plans and Coverdell Education Savings Accounts (CESAs).

Section 529 plans can prove to be especially valuable because they have very high contribution limits and the money you contribute to a plan is invested and can compound over time. You aren't taxed on investment earnings in a plan and distributions for most college expenses also aren't taxed. And if there's money left over after one child finishes school, you can transfer the account to a sibling.

CESAs aren't as attractive as 529 plans because CESAs have an annual contribution limit of $2,000, although if you begin putting in money when a child is very young it could add up to a decent amount of education savings, and the assets in these accounts also can grow without any current tax. Moreover, a CESA can be tapped to pay for private school education before a child enters college. That's not allowed with Section 529 plans. ●



Ryan Poage & Co.
Investments | Wealth Management
Plaza Corporate Centre
800 W. 47th St., Ste. 700
Kansas City, MO 64112
816-531-4555
877-531-4555
www.ryanpoage.com