Mission Coast Financial
Kimberly Hankins
80 Garden Court
Suite 210
Monterey, CA 93940
831-717-4235
khankins@royalaa.com

Mission Coast Financial Times

Summer 2018

Mid-Year Planning: Tax Changes to Factor In

The Tax Cuts and Jobs Act, passed in December of last year, fundamentally changes the federal tax landscape for both individuals and businesses. Many of the provisions in the legislation are permanent, others (including most of the tax cuts that apply to individuals) expire at the end of 2025. Here are some of the significant changes you should factor in to any mid-year tax planning. You should also consider reviewing your situation with a tax professional.

New lower marginal income tax rates

In 2018, there remain seven marginal income tax brackets, but most of the rates have dropped from last year. The new rates are 10%, 12%, 22%, 24%, 32%, 35%, and 37%. Most, but not all, will benefit to some degree from the lower rates. For example, all other things being equal, those filing as single with taxable incomes between approximately $157,000 and $400,000 may actually end up paying tax at a higher top marginal rate than they would have last year. Consider how the new rates will affect you based on your filing status and estimated taxable income.

Higher standard deduction amounts

Standard deduction amounts are nearly double what they were last year, but personal exemptions (the amount, $4,050 in 2017, that you could deduct for yourself, and potentially your spouse and your dependents) are no longer available. Additional standard deduction amounts allowed for the elderly and the blind remain available for those who qualify. If you're single or married without children, the increase in the standard deduction more than makes up for the loss of personal exemption deductions. If you're a family of four or more, though, the math doesn't work out in your favor.

Itemized deductions — good and bad

The overall limit on itemized deductions that applied to higher-income taxpayers is repealed, the income threshold for deducting medical expenses is reduced for 2018, and the income limitations on charitable deductions are eased. That's the good news. The bad news is that the deduction for personal casualty and theft losses is eliminated, except for casualty losses suffered in a federal disaster area, and miscellaneous itemized deductions that would be subject to the 2% AGI threshold, including tax-preparation expenses and unreimbursed employee business expenses, are no longer deductible. Other deductions affected include:

- **State and local taxes** — Individuals are only able to claim an itemized deduction of up to $10,000 ($5,000 if married filing a separate return) for state and local property taxes and state and local income taxes (or sales taxes in lieu of income).
- **Home mortgage interest deduction** — Individuals can deduct mortgage interest on no more than $750,000 ($375,000 for married individuals filing separately) of qualifying mortgage debt. For mortgage debt incurred prior to December 16, 2017, the prior $1 million limit will continue to apply. No deduction is allowed for interest on home equity loans or lines of credit unless the debt is used to buy, build or substantially improve a principal residence or a second home.

Other important changes

- **Child tax credit** — The credit has been doubled to $2,000 per qualifying child, refundability has been expanded, and the credit will now be available to many who didn't qualify in the past based on income; there's also a new nonrefundable $500 credit for dependents who aren't qualified children for purposes of the credit.
- **Alternative minimum tax (AMT)** — The Tax Cuts and Jobs Act significantly narrowed the reach of the AMT by increasing AMT exemption amounts and dramatically increasing the income threshold at which the exemptions begin to phase out.
- **Roth conversion recharacterizations** — In a permanent change that starts this year, Roth conversions can't be "undone" by recharacterizing the conversion as a traditional IRA contribution by the return due date.

Building Confidence in Your Strategy for Retirement

In 2018, 64% of workers surveyed were either somewhat or very confident in their ability to afford retirement, up from 60% in 2017. Among retirees surveyed in 2018, 75% were confident, down from 79% in 2017.

Source: 2018 Retirement Confidence Survey, EBRI

[1] Guarantees are contingent on the claims-paying ability and financial strength of the annuity issuer. Generally, annuity contracts have fees and expenses, limitations, exclusions, holding periods, termination provisions, and terms for keeping the annuity in force. Most annuities have surrender charges that are assessed if the contract owner surrenders the annuity. Withdrawals of annuity earnings are taxed as ordinary income. Withdrawals prior to age 59½ may be subject to a 10% federal income tax penalty.

Each year, the Employee Benefit Research Institute (EBRI) conducts its Retirement Confidence Survey to assess both worker and retiree confidence in financial aspects of retirement. In 2018, as in years past, retirees expressed a higher level of confidence than today's workers (perhaps because "retirement" is less of an abstract concept to those actually living it). However, worker confidence seems to be on the rise, while retiree confidence is on the decline. A deeper dive into the research reveals lessons and tips that can help you build your own retirement planning confidence.

Create a foundation of predictable sources of income

Workers surveyed expect to rely less on traditional sources of guaranteed income — a defined benefit pension plan and Social Security — than today's retirees. More than 40% of retirees say that a traditional pension plan provides them with a major source of income, and 66% say that Social Security is a primary source. Yet just one-third of today's workers expect either a pension or Social Security to play a big role.

Understand how Social Security works. Although nearly half of today's workers say they have considered how their Social Security claiming age could affect their benefit amount, the median age at which they plan to claim benefits is 65. Moreover, less than a quarter of respondents say they determined their future claiming age with benefit maximization in mind. Why does this matter? It's because the vast majority of today's workers won't be able to collect their full Social Security retirement benefit until sometime between age 66 and 67, depending on their year of birth. Claiming earlier than that results in a permanently reduced benefit amount. To help ensure you make the most of your Social Security benefits, take the time to understand the ramifications of different claiming ages and strategies before making any final decisions.

Consider creating your own "pension" income. Eight in 10 workers in the EBRI survey hope to use their defined contribution plan assets [e.g., 401(k) or 403(b)] to purchase a product that will provide a guaranteed stream of income during retirement. Depending on individual circumstances, this could be a wise move. To help provide yourself with a steady stream of income, you might consider annuitizing a portion of your retirement plan assets or purchasing an immediate annuity, a contract that promises to pay you a steady stream of income for a fixed period of time or for life in exchange for a lump-sum payment.[1]

When combined with your Social Security benefits, the payments received from an immediate annuity can help ensure that your everyday "fixed" expenses are covered. Any additional assets can then be earmarked for future growth potental and "extras," such as travel and entertainment.

Pay attention to your health — and health-care costs

Health. The EBRI survey revealed a correlation between health and retirement planning confidence. For example, 60% of today's workers who are confident in their retirement prospects also report being in good or excellent health, while only a little more than a quarter of those who are not confident report similar levels of health. Moreover, 46% of retirees who say they are confident also say they are in good health, compared with just 14% of those who are not confident.

The lesson here is pretty straightforward: Healthy habits may pay off in healthy levels of confidence. Eat plenty of fruits and vegetables, exercise, get enough sleep, and take steps to minimize stress. And don't skip important preventive checkups and lab tests. Keep in mind that even the most diligent savings strategies can be thrown off track by unexpected medical costs.

Health-care costs. The percentage of retirees who are at least somewhat confident that they will have enough money to cover medical expenses in retirement has dropped from 77% in 2017 to 70% in 2018. And four out of 10 retirees say that health-care expenses are at least somewhat higher than they expected. However, retirees who have estimated their health-care costs (39% of respondents) are more likely to say their expenses are about what they expected them to be. On the other hand, just 19% of workers have calculated how much they will need to cover their health expenses in retirement.

If you have not yet thought about how much of your retirement income may be consumed by health-care costs, now may be the time to start doing so. Having at least a general idea of what your medical expenses might be will help you more accurately project your overall retirement savings goal.

Did you know that 94% of all workers are covered under Social Security?

Source: Social Security Fact Sheet on the Old-Age, Survivors and Disability Insurance Program, July 2017

Quiz: Can You Answer These Social Security Benefit Questions?

Most people will receive Social Security benefits at some point in their lifetimes, but how much do you know about this important source of income? Take this quiz to learn more.

Questions

1. Can you receive retirement and disability benefits from Social Security at the same time?

a. Yes

b. No

2. If your ex-spouse receives benefits based on your earnings record, your benefit will be reduced by how much?

a. Reduced by 30%

b. Reduced by 40%

c. Reduced by 50%

d. Your benefit will not be reduced

3. For each year you wait past your full retirement age to collect Social Security, how much will your retirement benefit increase?

a. 6%

b. 7%

c. 8%

4. Monthly Social Security benefits are required to be paid by which of the following methods?

a. Paper check only

b. Paper check, direct deposit, or debit card

c. Direct deposit or debit card

5. Are Social Security benefits subject to income tax withholding?

a. Yes

b. No

6. Once you've begun receiving Social Security retirement benefits, you can withdraw your claim if how much time has elapsed?

a. Less than 12 months since you've been receiving benefits

b. Less than 18 months since you've been receiving benefits

c. Less than 24 months since you've been receiving benefits

Answers

1. b. No. If you receive a disability benefit, it will automatically convert to a retirement benefit once you reach full retirement age.

2. d. Your benefit will not be reduced if your ex-spouse receives Social Security benefits based on your earnings record.

3. c. Starting at full retirement age, you will earn delayed retirement credits that will increase your benefit by 8% per year up to age 70. For example, if your full retirement age is 66, you can earn credits for a maximum of four years. At age 70, your benefit will then be 32% higher than it would have been at full retirement age.

4. c. Since 2013, the Treasury Department has required electronic payment of federal benefits, including Social Security. You can sign up for direct deposit of your benefits into your current bank account or open a low-cost Electronic Transfer Account (ETA) at a participating financial institution. Another option is to sign up for a Direct Express® prepaid debit card. Under this option, your Social Security benefits are deposited directly into your card account, and you can use the card to make purchases, pay expenses, or get cash.

5. b. No. Withholding isn't mandatory, but you may voluntarily ask the Social Security Administration to withhold federal income tax from your benefits when you apply, or later, if you determine you will owe taxes on your Social Security benefits (not everyone does). You may choose to have 7%, 10%, 15%, or 25% of your benefit payment withheld. Ask a tax professional for help with your situation.

6. a. If something unexpected happens and you've been receiving Social Security benefits for less than 12 months after signing up, you can change your mind and withdraw your claim (and reapply at a later date). You're limited to one withdrawal per lifetime, and there are also financial consequences. You must repay all benefits already paid to you or your family members based on your application (anyone affected must consent in writing to the withdrawal), and repay any money previously withheld, including Medicare premiums or income taxes.

Mission Coast Financial
Kimberly Hankins
80 Garden Court
Suite 210
Monterey, CA 93940
831-717-4235
khankins@royalaa.com

Mission Coast Financial

What are some tips for creating a budget and sticking to it?

It's a common problem for many individuals — wondering exactly where your paycheck goes each month. After paying expenses, such as your mortgage, utilities, and credit card bills, you may find little left to put toward anything else.

Creating a budget is the first key to successfully manage your finances. Knowing exactly how you are spending your money each month can set you on a more clear path to pursue your financial goals. If you become sidetracked when it comes to your finances, consider these tips for creating a budget and staying on the right path.

Examine your financial goals. Start out by making a list of your short-term goals (e.g., new car, vacation) and long-term goals (e.g, your child's college education, retirement) and prioritize them. Consider how much you will need to save and how long it will take to reach each goal.

Identify your current monthly income and expenses. Add up all of your income. In addition to your regular salary and wages, be sure to include other types of income, such as dividends, interest, and child support. Next, add up all of your expenses. Sometimes it helps to divide expenses into two categories: fixed (e.g., housing, food, transportation) and discretionary (e.g., entertainment, vacations). Don't forget to factor in any financial goals you would like to pursue.

Evaluate your budget. Once you've added your income and expenses, compare the two totals. Ideally, you should be spending less than you earn. If this is the case, you're on the right track, and you'll need to look at how well you use your extra income toward achieving your financial goals. On the other hand, if you are spending more than you earn, you should make some adjustments to your budget. Look for ways to increase your income or reduce your expenses, or both.

Monitor your budget. Finally, you should monitor your budget periodically and make changes when necessary. Keep in mind that any budget that is too rigid is likely to fail. Keep your budget flexible as your changing circumstances demand.

What are some strategies for paying off credit card debt?

Nowadays, it's easier than ever to get caught up in the cycle of credit card debt. In fact, it's become a growing problem for many Americans. According to the Federal Reserve, total U.S. credit card payments reached 111.1 billion in 2016, up 7.4% from 2015.[1]

If you find that you are struggling to pay down a credit card debt balance, here are some strategies that can help eliminate your credit card debt altogether:

Pay off cards with the highest interest rate first. If you have more than one card that carries an outstanding balance, prioritize your payments according to their interest rates. Send as large a payment as you can to the card with the highest interest rate and continue making payments on the other cards until the card with the highest interest rate is paid off. You can then focus your repayment efforts on the card with the next highest interest rate, and so on, until they're all paid off.

Apply for a balance transfer with another card. Many credit card companies offer highly competitive balance transfer offers (e.g., 0% interest for 12 months). Transferring your credit card balance to a card with a lower interest rate can enable you to reduce interest fees and pay more against your existing balance. Most balance transfer offers charge a fee (usually a percentage of the balance transferred), so be sure to do the calculations to make sure it's cost-effective before you apply.

Pay more than the minimum. If you only pay the minimum payment due on a credit card, you'll continue to carry the bulk of your balance forward without reducing your overall balance. As a result, try to make payments that exceed the minimum amount due. For more detailed information on the impact that making just the minimum payment will have on your overall balance, you can refer to your monthly statement.

Look for available funds to make a lump-sum payment. Are you expecting an employment bonus or other financial windfall in the near future? If so, consider using those funds to make a lump-sum payment to eliminate or pay down your credit card balance.

[1] Federal Reserve, 2017