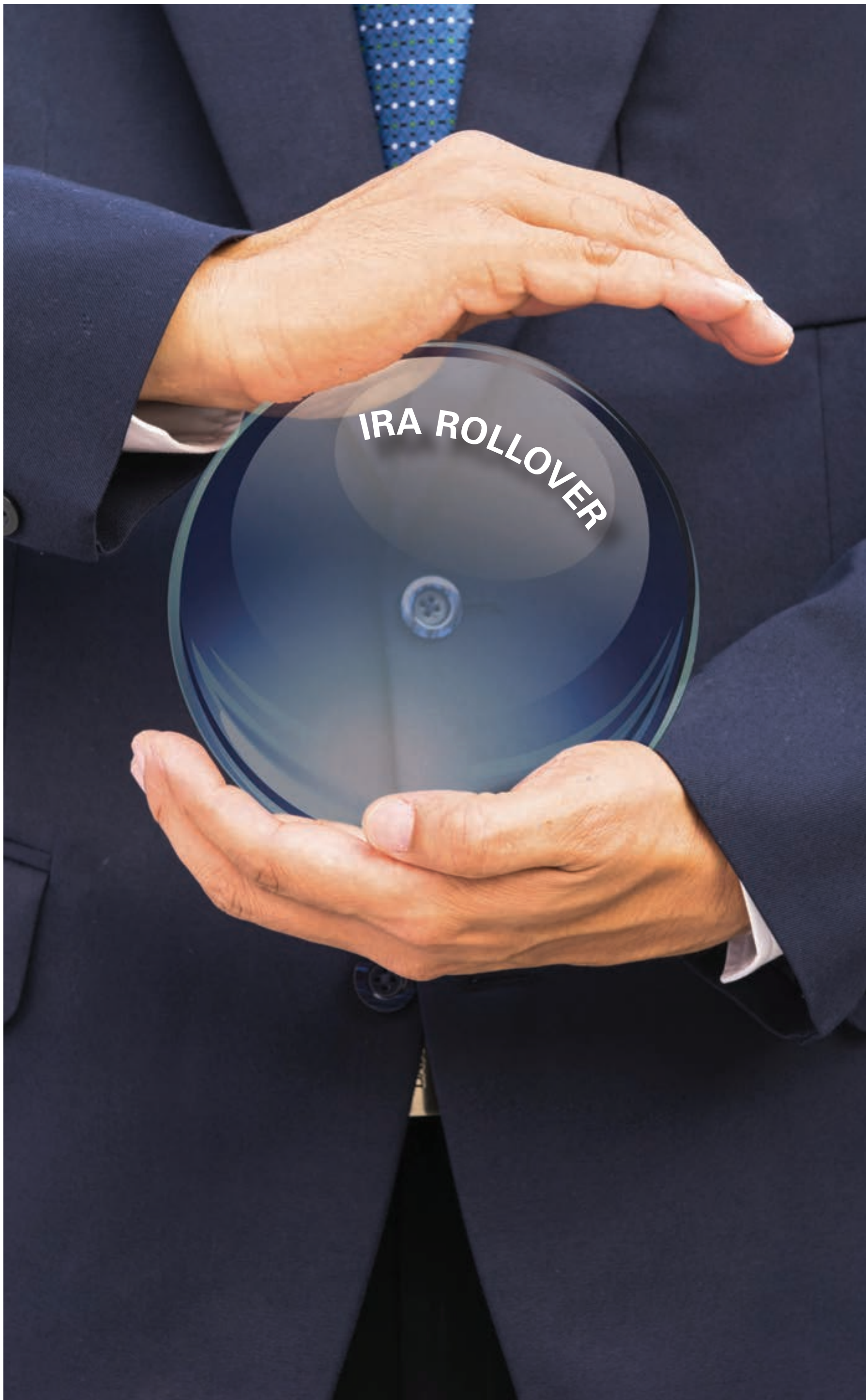
IN THIS ISSUE

Trust UPDATE

Stillman BANK

Q&A on IRA rollovers



A recent report from the Government Accountability Office suggests that IRAs are becoming an increasingly important element of retirement security. An estimated 43 million taxpayers have IRAs, worth an estimated $5.2 trillion. Some 42.3 million of these IRAs are worth less than $1 million, and 800,000 are worth more. Some 314 taxpayers have IRAs worth $25 million or more.

One doesn't accumulate IRA balances that large by making a maximum contribution each year and getting lucky with investments. Larger IRAs are nearly always the result of a rollover from an employer's qualified retirement plan, one that has long had much higher contribution caps than IRAs.

The IRA rollover is a critical tool for preserving retirement capital. Here are some questions that we've heard in this area.

Mixed distribution

Q. I've made both pre-tax and after-tax contributions to my employer's retirement plan. Are there special considerations for my IRA rollover?

A. In October the IRS provided helpful guidance for taxpayers who have both pre-tax and after-tax balances in their employer-provided retirement plans *(Notice 2014-54)*. In most cases the taxpayer will have the flexibility to achieve an optimum tax result.

The IRS provided the following fact pattern. Taxpayer's 401(k) account consists of $200,000 of pre-tax money and $50,000 of after-tax contributions. Upon a separation from service, Taxpayer has requested a distribution of $100,000. Those funds must come proportionately from each pot, so the distribution will be $80,000 pre-tax, $20,000 after-tax.

From this setup, the IRS explores several scenarios for the Taxpayer. First, he may order that the money be paid directly to IRAs, the pre-tax money to a traditional IRA and the balance to a Roth IRA.

Continued on next page

That approach preserves all the favorable tax attributes of the distribution for the future.

Next, the Service assumes that Taxpayer wants to roll $70,000 of his distribution into a successor employer plan. Because that amount is less than the pre-tax portion of the distribution, the entire amount will be assumed to be of pre-tax money. If the new employer plan allows for separate accounting of after-tax contributions, Taxpayer has the option of so designating a portion of the rollover. However, he does not have that choice if the new plan does not provide for separate accounting, the IRS warned.

Missed deadline

Q. I received a big retirement plan distribution that I meant to roll over to an IRA, but I didn't get to it within 60 days. What can I do now?

A. The best way to handle a rollover is a trustee-to-trustee transfer. Are you certain that you received a distribution? That is, if the distribution check is made out to the recipient plan, instead of to you, this still may be a trustee-to-trustee transfer. Such a check may be delivered to the payee plan after the 60-day deadline has passed, even after the death of the participant.

If that solution is not available, the next question is whether an exception to the 60-day rule might apply. These exceptions are:

First-time homebuyer. Let's say that your withdrawal was a "first-time homebuyer" distribution. If there is a delay or cancellation of the purchase or construction of the home, the amount withdrawn may be recontributed back into the IRA without penalty. The time limit on this is 120 days, instead of 60 days.

Disaster-based extensions. If a federal disaster has been declared in your area, the IRS may issue a pronouncement on the availability of automatic extensions for various filings, which may include your rollover.

Financial institution errors. If you took action within 60 days, but the deposit to the IRA happened after 60 days solely because of an error by your financial institution, you can get an automatic waiver of the 60-day rule. This works, provided that the funds are deposited in the eligible plan within a year of the original distribution.

Frozen deposits. If a bank becomes insolvent, so that a participant can't get money out in time to meet the 60-day rule, the rule is suspended. The time during which the money has been frozen doesn't count toward the 60 days, and the participant has 10 days after the assets are unfrozen to complete the rollover.

Inherited IRAs

Q. I've inherited a substantial IRA from my parent. What are my choices? Can I roll over the money into my own IRA? What I'd really like to do is convert the inherited IRA to a Roth IRA.

A. Those approaches are not available to you. Because you are not the spouse of the decedent, you only are permitted to arrange a trustee-to-trustee transfer of the money to another IRA in the name of the decedent and yourself. A death triggers the process of exposure of the IRA accumulation to taxation. Although that taxation can be extended over your actuarial lifetime, it can't be delayed beyond that, which is why the decedent's name always must appear on the IRA.

If you attempt to convert an inherited IRA into a Roth IRA, the conversion will be treated as a complete and taxable distribution of the IRA followed by an excess contribution to the Roth IRA. Similarly, if you attempt a trustee-to-trustee transfer from the inherited IRA to one in your own name, it will be treated as a complete distribution followed by a regular contribution to your IRA (not a rollover contribution).

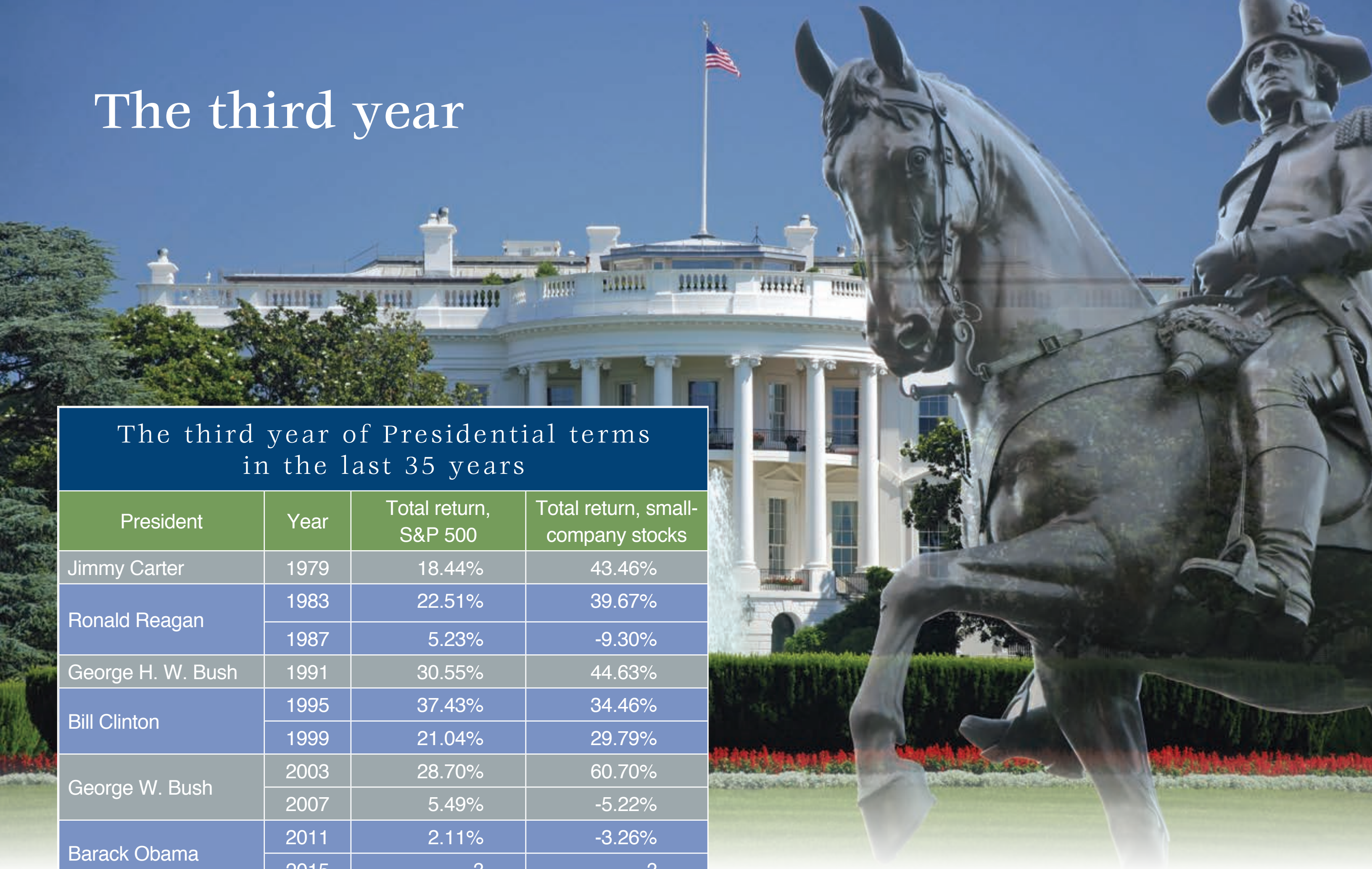
Do you have a question?

We specialize in two very important areas of personal financial management:

- Helping clients to *achieve* financial independence, using tax-sensitive techniques as appropriate.
- Helping clients to *maintain* financial independence by providing unbiased investment advice and trusteeship.

For specifics on how we might help you, see our asset-management specialists. ☐

The third year



The third year of Presidential terms in the last 35 years

President	Year	Total return, S&P 500	Total return, small-company stocks
Jimmy Carter	1979	18.44%	43.46%
Ronald Reagan	1983	22.51%	39.67%
	1987	5.23%	-9.30%
George H. W. Bush	1991	30.55%	44.63%
Bill Clinton	1995	37.43%	34.46%
	1999	21.04%	29.79%
George W. Bush	2003	28.70%	60.70%
	2007	5.49%	-5.22%
Barack Obama	2011	2.11%	-3.26%
	2015	?	?

Source: M.A. Co.

An interesting phenomenon was noticed by market watchers during the last century. The stock markets generally did best in the third year of a Presidential term. Writing in *The New York Times* in 2010 about the 65 years since World War II, Floyd Norris observed that third years have had positive returns 94% of the time, with an inflation-adjusted median change in the S&P 500 of 18.0%. That's nearly three times better than the median for the fourth year of 6.7%.

The Wall Street Journal recently provided an update covering a longer time frame. Since 1900 the S&P 500 has grown an average of 10.7% in Presidential third years, and it has been in positive territory in 75% of those years. In contrast, the study showed average gains of just over 4% in the first two years of a term, and 7.8% in the fourth year. One suggested explanation for the pattern is that Presidents push through their toughest legislation in the first two years, then pull back to focus on economic growth before the next election.

The Presidency of Barack Obama has rather decisively broken this mold. During his first two years in office, the S&P 500 total return was 26.46% in 2009 and 15.06% in 2010. In his third year there was no change in the S&P 500; the 2.11% total return came entirely from dividends. That was followed up with a 16.00% return in his fourth year and a stunning 32.39% total return in the first year of his second term.

One reason for the strong early market performance during the Obama administration may be that the market indices were unusually severely depressed as he came into office. Another contributing factor may be the unprecedented spell of low interest rates, which has given investors fewer good alternatives to investing in stocks.

Develop your own plan

Of course, the real driver of stock market returns is the economy, but economic growth can be affected by politics. Congress might take up corporate tax reform, or it could take up pro-growth regulatory reform. On the other hand, many economic factors are beyond the control of governments, such as the drop in the world price of oil that contributed to the collapse of the ruble in December. The fallout from that development is unknown at this writing.

If investing were easy, everyone would be good at it. The record suggests that such is not the case. If you would like an independent review of your portfolio management strategies, we will be pleased to be of service. ☐

Data bank

Planning for a financially secure retirement is more important than ever. Some people are taking the challenge seriously. Reference points from 2014, and looking ahead to 2015.

CENSUS BUREAU	
Poverty rate for men 65 and older	6.8%
Poverty rate for women 65 and older	11.6%
Social Security Administration	
Maximum taxable earnings for Social Security taxes	$118,500
Maximum monthly benefit for workers retiring in 2015 at full retirement age	$2,663
Earnings test for early retirees	$15,720
Earnings test in the year that one reaches full retirement age	$41,880
Value of Social Security trust fund	$2.783 trillion
IRS	
IRA contribution limit	$5,500
IRA "catch-up" limit	$1,000
401(k) contribution limit	$18,000
401(k) "catch-up" limit	$6,000
Pension maximum	$210,000
PLAN SPONSOR COUNCIL OF AMERICA SURVEY	
Participation rate, small plans	85.4%
Average salary deferral, small plans	9.0%
Participation rate, large plans	77.0%
Average salary deferral, large plans	6.9%
INVESTMENT COMPANY INSTITUTE	
Households with a traditional IRA	29.4%
Households with a Roth IRA	15.6%
Total IRA money market investments	$230 billion
Total IRA bond fund investment	$465 billion
Total IRA domestic equity fund investment	$1.244 trillion
Total of IRA and defined contribution retirement plan investments in domestic equity funds	$2.885 trillion

Sources: As noted and M.A. Co.