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21st century retirement

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Tax and Retirement Planning for Families with a Stay-at-Home Spouse

In many families, one of the spouses stays home, often to care for children and the household. This may be hard work, but for tax purposes the contributions of the stay-at-home spouse are not recognized in the same way as they are for individuals with earned income. If your wife or husband does not have paid employment, your family may have to do some additional planning to minimize your tax bill, while ensuring that you are saving enough for retirement to cover the needs of both partners.

Even if your husband or wife has not earned a significant amount of income through paid employment, he or she may be entitled to a Social Security spousal benefit. Based on the working spouse's earnings record, the spousal benefit can be claimed after the working partner has filed for benefits and the nonworking partner has reached retirement age. The spousal benefit generally amounts to 50% of the monthly Social Security payment received by the spouse who worked regularly, or less if claimed early.

But Social Security benefits alone are unlikely to cover the needs of most couples in retirement. Thus, your family's retirement strategy should include a plan for both partners, even if you are the sole earner. If you have not done so already, consider making the maximum contribution to your employer-sponsored 401(k) plan. While your nonworking partner is not permitted to contribute to your workplace retirement plan, the annual contribution limit in 2019 is $19,000, or $25,000 for individuals age 50 and over. The funds in the account will be held in your name, but can be inherited by your spouse, and are typically divided between the spouses in the event of a divorce.

Another option for tax-advantaged retirement savings is a spousal IRA, which is simply a regular IRA designed specifically for spouses who are not employed or are working too little to contribute to a qualified retirement account. While it is a fundamental rule that individuals need to have earned income, or wages, in order to contribute to an IRA, a nonworking spouse is permitted to open an account to which the working spouse may contribute. Provided you file a joint return, you are permitted to contribute up to $6,000 (or $7,000 for those age 50 and older) in 2019 to an account in your partner's name, while also contributing the same amount in your own IRA. Thus, your household may be eligible to contribute up to a total of $12,000 or $14,000 to two separate IRA accounts.

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Should Retirement Be Hard Work?

Ah, retirement! Finally, there will be time to relax, free from financial worry. Many people think of retirement as a time to travel or pursue special interests—a welcome break from the 40-hour workweek. But without careful retirement planning, you may actually need to work harder and longer than you imagined during your so-called retirement years. It may be safe to say that, when it comes to retirement, the best-laid plans are made well before the traditional retirement age of 65.

Know Your Resources

How many times have you said, "I'll do that when I retire," expecting plenty of free time to pursue your passions after liberation from the 9-5 work schedule? But, have you considered the cost of not working? A general rule of thumb is that you may need 60% to 80% of your pre-retirement income to maintain your lifestyle during retirement. Careful planning now can help you maintain your desired lifestyle during retirement, as well as help ensure that you have the resources in which to do so.

For many, Social Security, employer-sponsored retirement plans, and personal savings are the primary sources of retirement income. It is important to recognize that Social Security was designed not to be the sole source of income for retirees, but merely one component in the overall retirement income package. Therefore, many workers rely on an employer-sponsored retirement plan to provide substantial income. However, both of these sources may need to be supplemented with personal savings to help provide enough income to meet your retirement goals.

Put Time on Your Side

Early retirement planning puts time on your side. It is never too early to begin saving and never too late to start. In fact, one advantage of early retirement planning is that you have a longer period of time before retirement, which allows a great opportunity to increase your savings through potential growth.

An equally important consideration for retirement planning is the reality of inflation, which can affect even substantial savings. For example, a modest 4% inflation rate, maintained over 15 years, reduces the purchasing power of $250,000 to $138,816. Starting early may allow your savings to outpace inflation.

Although it can be difficult to imagine a time when you will not have to be at the office or worksite each morning, the day may arrive sooner than you think. Therefore, begin preparing for retirement *now*—even if it seems a long way off. With time on your side, the best-laid plans may help ensure future financial well-being for you and your family. ■

Protect Your Estate with an Irrevocable Life Insurance Trust

Many estate planning practitioners view the **irrevocable life insurance trust (ILIT)** as a flexible and useful tool that can provide a number of benefits to their clients. Because the question of where the ILIT fits into the overall estate planning process can be somewhat confusing, a closer look at its potential advantages may prove helpful.

Inheritance Comes with a Price

Typically, the amount of estate planning necessary is dictated by the size of your assets. For instance, if you are married, a properly drafted and executed **will** and **inter vivos (living) trust** for you and your spouse—coupled with proper asset ownership—ensures that the first $22.8 million in 2019 (annually adjusted for inflation) of your estate passes to heirs free of Federal estate taxes. In 2019, the top tax rate remains at 40%.

Thus, estates exceeding $22.8 million for married individuals in 2019 (or $11.4 million per individual) are subject to Federal estate taxes. For this reason, the ILIT has become a popular technique to help fund the payment of estate taxes and to help ensure that assets are passed to your family in full.

Opportunity Knocks

The proceeds of a life insurance policy that is purchased and owned by an ILIT, if correctly structured and administered, are not included in your estate. Instead, they may be payable to the ILIT's *beneficiaries* (often children or grandchildren) without incurring estate tax consequences.

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A spousal IRA can be a traditional IRA or a Roth IRA. The traditional IRA is tax-deferred, which means that you won't pay income taxes on current contributions, but you will owe taxes on distributions in retirement. By contrast, Roth IRA contributions are made with after-tax dollars, but the funds in the account grow on a tax-deferred basis and can be withdrawn tax free in retirement.* Thus, a Roth IRA may be an attractive option if you expect to be paying higher tax rates in retirement or wish to leave an IRA to beneficiaries. However, in 2019 the eligibility for contributing to a Roth account starts to phase out for married couples with a modified adjusted gross income (AGI) of $193,000, and is capped at $203,000.

It is also important to keep in mind that the deduction for taxpayers making contributions to a traditional IRA is phased out for married couples filing jointly when the spouse who makes the IRA contributions is covered by a workplace retirement plan. While the modified AGI phase-out range is $103,000 to $123,000 in 2019 for the spouse who is employed, it is raised to $193,000 to $203,000 for an IRA contributor who is not covered by a workplace retirement plan and is married to an individual who is covered.

Married couples in which one partner owns a business or is self-employed have additional options for saving for a stay-at-home spouse's retirement. For example, if you own a business, your partner may be able to provide services to your company, such as bookkeeping or answering calls, while still remaining primarily at home. If you pay your partner as an employee, he or she can qualify to participate in the company's retirement plan. This approach can lower your family's current income tax bill, while helping to secure your financial future as a couple. ■

*Unless certain criteria are met, Roth IRA owners must be 59 ½ or older and have held the IRA for five years before tax-free withdrawals are permitted.

protect your estate with an irrevocable life insurance trust

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An ILIT can purchase a life insurance policy on your (the donor's) life, with the policy premiums funded by annual gifts you make to the ILIT. Consequently, your **annual gift tax exclusion** ($15,000 annually per donee and $30,000 for gifts made by husband and wife) can be used to maximize gifts to the ILIT.

As a more advanced strategy, an ILIT can help ensure continuity in a **closely held business**. For instance, passing a family-owned business of substantial value to heirs may be hampered by potentially large estate taxes. These taxes, in some instances, may require a forced sale of the business to raise the necessary cash to pay them. However, an ILIT can purchase a life insurance policy on the owner, with the death benefit providing the cash needed to help meet estate tax obligations and keep the business in the family.

Preparing for Your Future

Estate planning is an *ongoing* process that requires a personal commitment to help ensure your desired intentions are fulfilled. An ILIT can be an integral part of your overall plan. Be sure to consult your estate planning team, including your insurance, legal, and tax professionals, about your unique circumstances. ■

New Retirement Savings Plans Are Needed to Ensure Financial Security for More Workers

While the vast majority of Americans who save for retirement do so through a 401(k) or similar plan provided by their employer, additional types of saving plans may be needed to help the millions of workers who are not adequately saving in workplace plans build a financially secure retirement, according to an article published on March 14 by The Pew Charitable Trusts.

The article, "3 Ways People May Save for Retirement in the Future," was written by John Scott, director of Pew's retirement savings project. Scott observed that "we may have reached the limit of what our employer-sponsored system can do to support a secure retirement," as currently only about half of private sector businesses offer retirement benefits, and even though around 140 million people participate in retirement plans, the proportion of the employed workforce covered by these plans has never exceeded 70%.

Scott argued that while Congress could increase incentives to encourage more employers to sponsor plans, he noted that previous research has shown that small employers are often reluctant to offer retirement benefits because of the plan startup costs and administrative burdens, and that is not clear that offering them a new tax break would overcome these concerns.

Given that is unlikely that many more employers will start voluntarily offering retirement benefits or that many more employees will start saving on their own, Scott said, new approaches that build on the elements that are known to work in the current system should be considered. Specifically, he recommended the development of a low-cost, portable, individual-based system, managed by a third party, that allows workers to automatically contribute to their own retirement account with each paycheck, and that gives employers the option to add to those accounts through a matching contribution.

While acknowledging that no current initiative fully captures these ideas, Scott noted that recent actions at the state and Federal levels point to the outlines of a system that could cover more workers, without relying solely on individual employers to sponsor their own retirement plan.

Among these initiatives, Scott said, are state-level retirement savings programs for employees without a workplace plan. He reported that California, Connecticut, Illinois, Maryland, and Oregon are implementing programs in which workers are automatically enrolled at a default rate of contribution, typically around 5% of pay, and with the ability to opt out at any time.

In these programs, employers facilitate worker contributions through their payroll systems, but otherwise are not involved.

Scott also mentioned that a new approach may come from Congress, as the Retirement Security Act, which would allow any group of employers to share plan costs in group plans known as multiple employer plans, or MEPs, was recently introduced in the Senate. He observed that these plans could be especially helpful to smaller employers wary of the administrative costs of offering a stand-alone plan.

Finally, Scott pointed out that there are more than 10 million independent or contingent workers in the U.S. who have very low rates of retirement benefit coverage. To help these workers save in a changing economy, he recommended the development of retirement savings models that expand coverage options, possibly using new entities affiliated with associations, unions, or industry sectors. ■

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