PERSONAL FINANCIAL PLANNING

What You Should Be Thinking About in 2016

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In January, at the 2016 AICPA Advanced Personal Financial Planning Conference, I had the opportunity to organize and moderate a "Best Ideas Panel" with four of the leading financial planning experts in the country. We explored what the attendees should be focusing on with their clients this year. Here is a summary of what we covered and things you should be thinking about throughout 2016:

Income Tax Extenders

Perhaps the two most important aspects of the tax package that Congress passed at the very end of last year were the Qualified Charitable IRA Distributions (QCD) and some changes to the 529 College Savings plans rules. Individuals who are charitably inclined and taking required minimum distributions will benefit from the ability to take up to $100,000 from their IRA and transfer it directly to charity. This allows them to avoid reporting that distribution as income. By reducing the adjusted gross income, they might be able to increase the other deductions they are allowed that were limited by their adjusted gross income, like medical and miscellaneous investment expenses. It could also limit the deductions that would otherwise be lost due to the phase out rules. This has now been made permanent in the tax law.

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The 529 plan changes were seemingly minor, but individuals are now allowed to draw from the plans with the lowest basis first in order to minimize gain should a non-qualified distribution be necessary in the future. The tax law also now allows certain computer expenses to qualify to be taken from a 529 plan. Careful planning with your clients' 529 plan assets is becoming increasingly important.

Future Tax Legislation

Unless you've been living under a rock you probably already know we are in an election year! There is growing Republican and Democratic support for potential tax legislation, and 2017 could be a tax reform year. The timing seems right as we went from 1954-1986 (32 years) and again 1986-2016 (30 years) without major reform. President Obama's budget proposals have many tax changes in them. Obviously, these will face challenges along the way, but it is good to keep an eye on what has been proposed. Broadly, these include:

- Reducing tax benefits for high-income taxpayers;
- New initiatives to bring jobs to the US;
- An increase in the estate tax;
- Closing of various perceived loopholes in the estate planning area; and
- Reduction of some of the advantageous rules related to retirement accounts.

As of this writing, Donald Trump is regarded as the presumptive Republican presidential nominee. However, the two remaining Democratic candidates are still facing off in a series of contested primaries. Each of these candidates have different tax proposals. Our current top individual income tax rate is 39.6 percent. Donald Trump would cap the top rate at 25 percent; Hillary Clinton would increase the top rate to 43.6 percent; and Bernie Sanders would push that up to 52 percent. Capital gains tax proposals vary from the current top rate of 20 percent (which Trump would retain); Clinton's proposal that includes a seven-bracket system and a top rate of 39.6 percent (depending on the asset's holding period); and Sanders' plan, which would tax capital gains as ordinary income for households with income over $250,000.

In the estate tax area, the current top rate is 40 percent and the federal exclusion is $5.45 million. While Trump would eliminate the estate tax, Clinton would raise the maximum rate to 45 percent and drop the threshold down to $3.5 million. Sanders would raise the maximum rate to 65 percent with the same threshold. Stay tuned, these will be important issues as the process unfolds this summer and through the fall.

Investments

We have seen a lot of volatility in the investment markets in 2016, from the steep decline in January and February to the strength of late. Volatility can present financial planning opportunities. Selling asset classes when they are at a loss (tax loss harvesting) can be a great way to offset gains from other areas of your clients' portfolio. Also consider suggesting strategies such as Roth IRA conversions (better done when asset values are down so they generate less taxable income), making pecuniary bequests with high basis assets to reduce gain recognition, and Generation-Skipping Transfer (GST) allocations to older non-exempt trusts.

It is also important to note that while the potential of rising interest rates may be causing volatility in the investment markets, ultimately higher rates will actually be a good thing for savers. It will also provide significant relief for insurance companies and should cause long term care insurance premiums to drop or at least stabilize.

Estate Planning

Encourage your clients to take advantage of estate planning strategies now, while they are still available. In addition to an increase in the estate tax rate to 45 percent (from the current 40 percent) and a reduction to the exclusion from the current $5.45 million down to $3.5 million, President Obama's budget proposal includes the elimination of a number of estate planning "loopholes," including the elimination of the Grantor Retained Annuity Trust (GRAT) strategy, the elimination of Dynasty Trusts by placing a maximum 90-year term on testamentary trusts, and a limitation of present interest gifts available through *Crummey* trust powers.

Retirement Planning

A lot has been written about the recent changes to Social Security benefit rules, and you need to make sure you think through the impact of these rules on your clients' unique situations and also how the benefits fit into their overall planning. Social Security planning is becoming an important piece of your clients' overall financial planning.

As you work with clients in the retirement planning area, you should also make sure you are following the new rules in the DOL Fiduciary Standard. While these rules are currently not scheduled to take effect until 2017, they should be addressed now.

Life Insurance

In the life insurance area, we talked about the popularity of Private Placement Life Insurance for the very high-net worth clients. While this is not typically an estate planning strategy, it rather reflects that the costs of the policy are less than the income tax otherwise owed.

Making sure that you are weaving together the best planning ideas from all areas of personal financial planning for your clients is more important than ever in this environment.