



Your Financial Future

Flourney Wealth Management

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I hope this newsletter finds you well, relieved that once again tax time came and hopefully went without too many surprises, and looking forward to summer!

Each of us has a financial picture, some of which is common to our friends and family, but we always have our unique goals, timeframes, and concerns. This is what I enjoy about working with each of my clients. What is the right answer and or points to consider to their individual questions and circumstances? It is not always the most obvious solution. This is why, I have chosen to use this newsletter format to showcase educational information which covers different aspects of people's financial lives.

I would love some feedback about it. Would you like to receive this newsletter in paper form by snail mail? Would you like it monthly or quarterly? Is there other information that you'd like in a newsletter? How can I make it more valuable to you?

Look forward to hearing from you!

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WEALTH MANAGEMENT

Six Potential 401(k) Rollover Pitfalls



You're about to receive a distribution from your 401(k) plan, and you're considering a rollover to a traditional IRA. While these transactions are normally straightforward and trouble free, there are some pitfalls you'll want to avoid.

1. Consider the pros and cons of a rollover. The first mistake some people make is failing to consider the pros and cons of a rollover to an IRA in the first place. You can leave your money in the 401(k) plan if your balance is over \$5,000. And if you're changing jobs, you may also be able to roll your distribution over to your new employer's 401(k) plan.

- Though IRAs typically offer significantly more investment opportunities and withdrawal flexibility, your 401(k) plan may offer investments that can't be replicated in an IRA (or can't be replicated at an equivalent cost).
- 401(k) plans offer virtually unlimited protection from your creditors under federal law (assuming the plan is covered by ERISA; solo 401(k)s are not), whereas federal law protects your IRAs from creditors only if you declare bankruptcy. Any IRA creditor protection outside of bankruptcy depends on your particular state's law.
- 401(k) plans may allow employee loans.
- And most 401(k) plans don't provide an annuity payout option, while some IRAs do.

2. Not every distribution can be rolled over to an IRA. For example, required minimum distributions can't be rolled over. Neither can hardship withdrawals or certain periodic payments. Do so and you may have an excess contribution to deal with.

3. Use direct rollovers and avoid 60-day rollovers. While it may be tempting to give yourself a free 60-day loan, it's generally a mistake to use 60-day rollovers rather than direct (trustee to trustee) rollovers. If the plan sends the money to you, it's required to withhold 20% of the taxable amount. If you later want to roll the entire amount of the original distribution over to an IRA, you'll need to use other sources to make up the 20% the plan withheld. In addition, there's no need to taunt

the rollover gods by risking inadvertent violation of the 60-day limit.

4. Remember the 10% penalty tax. Taxable distributions you receive from a 401(k) plan before age 59½ are normally subject to a 10% early distribution penalty, but a special rule lets you avoid the tax if you receive your distribution as a result of leaving your job during or after the year you turn age 55 (age 50 for qualified public safety employees). But this special rule doesn't carry over to IRAs. If you roll your distribution over to an IRA, you'll need to wait until age 59½ before you can withdraw those dollars from the IRA without the 10% penalty (unless another exception applies). So if you think you may need to use the funds before age 59½, a rollover to an IRA could be a costly mistake.

5. Learn about net unrealized appreciation (NUA). If your 401(k) plan distribution includes employer stock that's appreciated over the years, rolling that stock over into an IRA could be a serious mistake. Normally, distributions from 401(k) plans are subject to ordinary income taxes. But a special rule applies when you receive a distribution of employer stock from your plan: You pay ordinary income tax only on the cost of the stock at the time it was purchased for you by the plan. Any appreciation in the stock generally receives more favorable long-term capital gains treatment, regardless of how long you've owned the stock. (Any additional appreciation after the stock is distributed to you is either long-term or short-term capital gains, depending on your holding period.) These special NUA rules don't apply if you roll the stock over to an IRA.

6. And if you're rolling over Roth 401(k) dollars to a Roth IRA... If your Roth 401(k) distribution isn't qualified (tax-free) because you haven't yet satisfied the five-year holding period, be aware that when you roll those dollars into your Roth IRA, they'll now be subject to the Roth IRA's five-year holding period, no matter how long those dollars were in the 401(k) plan. So, for example, if you establish your first Roth IRA to accept your rollover, you'll have to wait five more years until your distribution from the Roth IRA will be qualified and tax-free.

Nearing Retirement? Time to Get Focused



A financial professional can help you estimate how much your retirement accounts may provide on a monthly basis. Your employer may also offer tools to help. Keep in mind, however, that neither working with a financial professional nor using employer-sponsored tools can guarantee financial success.

If you're within 10 years of retirement, you've probably spent some time thinking about this major life change. The transition to retirement can seem a bit daunting, even overwhelming. If you find yourself wondering where to begin, the following points may help you focus.

Reassess your living expenses

A step you will probably take several times between now and retirement--and maybe several more times thereafter--is thinking about how your living expenses could or should change. For example, while commuting and dry cleaning costs may decrease, other budget items such as travel and health care may rise. Try to estimate what your monthly expense budget will look like in the first few years after you stop working. And then continue to reassess this budget as your vision of retirement becomes reality.

Consider all your income sources

Next, review all your possible sources of income. Chances are you have an employer-sponsored retirement plan and maybe an IRA or two. Try to estimate how much they could provide on a monthly basis. If you are married, be sure to include your spouse's retirement accounts as well. If your employer provides a traditional pension plan, contact the plan administrator for an estimate of your monthly benefit amount.

Do you have rental income? Be sure to include that in your calculations. Is there a chance you may continue working in some capacity? Often retirees find that they are able to consult, turn a hobby into an income source, or work part-time. Such income can provide a valuable cushion that helps retirees postpone tapping their investment accounts, giving them more time to potentially grow.

Finally, don't forget Social Security. You can get an estimate of your retirement benefit at the Social Security Administration's website, ssa.gov. You can also sign up for a *my* Social Security account to view your online Social Security Statement, which contains a detailed record of your earnings and estimates of retirement, survivor, and disability benefits.

Manage taxes

As you think about your income strategy, also consider ways to help minimize taxes in retirement. Would it be better to tap taxable or tax-deferred accounts first? Would part-time work result in taxable Social Security benefits? What about state and local taxes? A qualified tax professional can help you develop an appropriate strategy.

Pay off debt, power up your savings

Once you have an idea of what your possible expenses and income look like, it's time to bring your attention back to the here and now. Draw up a plan to pay off debt and power up your retirement savings before you retire.

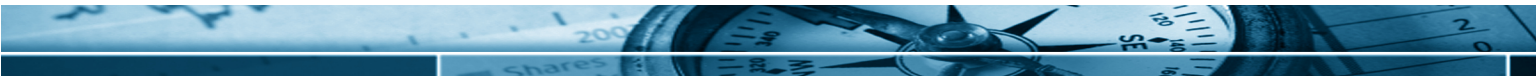
- **Why pay off debt?** Entering retirement debt-free--including paying off your mortgage--will put you in a position to modify your monthly expenses in retirement if the need arises. On the other hand, entering retirement with mortgage, loan, and credit card balances will put you at the mercy of those monthly payments. You'll have less of an opportunity to scale back your spending if necessary.
- **Why power up your savings?** In these final few years before retirement, you're likely to be earning the highest salary of your career. Why not save and invest as much as you can in your employer-sponsored retirement savings plan and/or your IRAs? Aim for the maximum allowable contributions. And remember, if you're 50 or older, you can take advantage of catch-up contributions, which allow you to contribute an additional \$6,000 to your employer-sponsored plan and an extra \$1,000 to your IRA in 2016.

Account for health care

Finally, health care should get special attention as you plan the transition to retirement. As you age, the portion of your budget consumed by health-related costs will likely increase. Although Medicare will cover a portion of your medical costs, you'll still have deductibles, copayments, and coinsurance. Unless you're prepared to pay for these costs out of pocket, you may want to purchase a supplemental insurance policy.

In 2015, the Employee Benefit Research Institute reported that the average 65-year-old married couple would need \$213,000 in savings to have at least a 75% chance of meeting their insurance premiums and out-of-pocket health care costs in retirement. And that doesn't include the cost of long-term care, which Medicare does not cover and can vary substantially depending on where you live. For this reason, you might consider a long-term care insurance policy.

These are just some of the factors to consider as you prepare to transition into retirement. Breaking the bigger picture into smaller categories may help the process seem a little less daunting.



Tools for students

The Department of Education and the Consumer Financial Protection Bureau have launched the "Know Before You Owe" campaign, which includes a standard financial aid award letter for colleges to use so that students can better understand the type and amount of aid they qualify for and more easily compare aid packages from different colleges. In addition, to help students search for and select suitable colleges, the Department has launched its College Scorecard online tool at collegescorecard.ed.gov.

Sources

- ¹ College Board, *Trends in College Pricing 2015*
- ² The Institute for College Access and Success, *Student Debt and the Class of 2014*, October 2015
- ³ Federal Reserve Bank of New York, *Quarterly Report on Household Debt and Credit*, November 2015

What's New in the World of Higher Education?

If you're a parent or grandparent of a college student or soon-to-be college student, you might be interested to learn what's new in the world of higher education.

Higher college costs

Total average costs for the 2015/2016 school year increased about 3% from the previous year: \$24,061 for public colleges (in-state), \$38,855 for public colleges (out-of-state), and \$47,831 for private colleges.¹

Total average costs include direct billed costs for tuition, fees, room, and board; and indirect costs for books, transportation, and personal expenses. Together, these items are officially referred to as the "total cost of attendance." Note that the cost figure for private colleges cited by the College Board is an average; many private colleges cost substantially more--over \$60,000 per year.

Higher student debt

Seven in 10 college seniors who graduated in 2014 (the most recent year for which figures are available) had student loan debt, and the average amount was \$28,950 per borrower.² It's likely this amount will be higher for the classes of 2015 and 2016.

Student loan debt is the only type of consumer debt that has grown since the peak of consumer debt in 2008; balances have eclipsed both auto loans and credit cards, making student loan debt the largest category of consumer debt after mortgages. As of September 2015, total outstanding student loan debt was over \$1.2 trillion.³

Reduced asset protection allowance

Behind the scenes, a stealth change in the federal government's formula for determining financial aid eligibility has been quietly (and negatively) impacting families everywhere. You may not have heard of the asset protection allowance before. But this figure, which allows parents to shield a certain amount of their nonretirement assets from the federal aid formula, has been steadily declining for years, resulting in higher expected family contributions for families. For the 2012/2013 year, the asset protection allowance for a 47-year-old married parent was \$43,400. Today, for the 2016/2017 year, that same asset protection allowance is \$18,300--a drop of \$25,100. The result is a \$1,415 decrease in a student's aid eligibility (\$25,100 x 5.64%, the federal contribution percentage required from parent assets).

New FAFSA timeline

Beginning with the 2017/2018 school year, families will be able to file the government's

financial aid application, the FAFSA, as early as October 1, 2016, rather than having to wait until after January 1, 2017. The intent behind the change is to better align the financial aid and college admission timelines and to provide families with information about aid eligibility earlier in the process.

One result of the earlier timeline is that your 2015 federal income tax return will do double duty as a reference point for your child's federal aid eligibility--it will be the basis for the FAFSA for *both* the 2016/2017 and 2017/2018 years.

School Year	Tax Return Required	FAFSA Earliest Submission
2016/2017	2015	January 1, 2016
2017/2018	2015	October 1, 2016
2018/2019	2016	October 1, 2017

American Opportunity Tax Credit now permanent

The American Opportunity Tax Credit was made permanent by the Protecting Americans from Tax Hikes Act of 2015. It is a partially refundable tax credit (meaning you may be able to get some of the credit even if you don't owe any tax) worth up to \$2,500 per year for qualified tuition and related expenses paid during your child's first four years of college. To qualify for the full credit, single filers must have a modified adjusted gross income (MAGI) of \$80,000 or less, and joint filers must have a MAGI of \$160,000 or less. A partial credit is available for single filers with a MAGI over \$80,000 but less than \$90,000, and for joint filers with a MAGI over \$160,000 but less than \$180,000.

New REPAYE plan for federal loans

The pool of borrowers eligible for the government's Pay As You Earn (PAYE) plan for student loans has been expanded as of December 2015. The new plan, called REPAYE (Revised Pay As You Earn), is available to *all* borrowers with federal Direct Loans, regardless of when the loans were obtained (the original PAYE plan is available only to borrowers who took out loans after 2007).

Under REPAYE, monthly student loan payments are capped at 10% of a borrower's discretionary income, with any remaining debt forgiven after 20 years of on-time payments for undergraduate loans and 25 years of on-time payments for graduate loans. To learn more about REPAYE or income-driven repayment options in general, visit the federal student aid website at studentaid.gov.

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How long should I keep financial records?

There's a fine line between keeping financial records for a reasonable period of time and becoming a pack rat. A general rule of thumb is to keep financial records only as long as necessary. For example, you may want to keep ATM receipts only temporarily, until you've reconciled them with your bank statement. But if a document provides legal support and/or is hard to replace, you'll want to keep it for a longer period or even indefinitely. It's ultimately up to you to determine which records you should keep on hand and for how long, but here's a suggested timetable for some common documents.

One year or less	More than one year	Indefinitely
Bank or credit union statements	Tax returns and documentation*	Birth, death, and marriage certificates
Credit card statements	Mortgage contracts and documentation	Adoption papers
Utility bills	Property appraisals	Citizenship papers
Annual insurance policies	Annual retirement and investment statements	Military discharge papers
Paycheck stubs	Receipts for major purchases and home improvements	Social Security card

*The IRS requires taxpayers to keep records that support income, deductions, and credits shown on their income tax returns until the period of limitations for that return runs out--generally three to seven years, depending on the circumstances. Visit irs.gov or consult your tax professional for information related to your specific situation.



Should I loan my child money for a down payment on a house?

For a lot of young people today, it's difficult to purchase a home without at least some financial assistance. As a result, many young adults turn to their parents or other family members for help with a down payment.

If you plan on lending your child money for a down payment on a house, you should try to assume the role of a commercial lender. Setting the terms of the loan in writing will demonstrate to your child that you take both your responsibility as lender and your child's responsibility as borrower seriously.

While having an actual loan contract may seem too businesslike to some parents, doing so can help set expectations between you and your child. The loan contract should spell out the exact loan amount, the interest rate and a repayment schedule. To avoid the uncomfortable situation of having to remind your child that a payment is due, consider asking him or her to set up automatic monthly transfers from his or her bank account to yours.

This type of loan documentation is also important for IRS purposes because there may be potential income and gift tax issues with these types of loans. For example, interest paid by your child will be considered taxable income, and if adequate interest is not charged for the loan, special imputed interest rules may apply.

If you don't feel comfortable lending your child money, you may want to consider making a smaller, no-strings-attached gift that doesn't have to be repaid. Currently, you can gift up to \$14,000 annually per person under the gift tax exclusion. However, if you do gift money for a down payment, your child's lender may still require him or her to put up some of his or her own money, depending on the type of mortgage chosen.

Keep in mind that lending money to family members can be a tricky proposition. Before entering into this type of financial arrangement, you should take the time to carefully weigh both the financial and emotional costs.