2nd Quarter 2017

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Financial Insights

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Roth IRA Conversions: The Time May Be Right

Perhaps you've thought about converting part of your traditional IRAs to a Roth IRA in the past, but you didn't pull the trigger. For instance, you might not have had the money available to pay the tax on a conversion without diluting your retirement assets. Or you may not have wanted pay that tax in a year in which you were in a high tax bracket.

Now, however, with the possibility that Congress will soon pass significant tax cuts, the time may be right to convert to a Roth this year or next.

With a traditional IRA, contributions may be deductible from your taxable income, but not if you also participate in a retirement plan at work or earn too much to qualify for a deductible IRA. When you take distributions from a traditional IRA, usually during retirement, you're taxed at the rates for ordinary income on the portion representing tax-deductible contributions and earnings. Under current law, the top ordinary income tax rate is 39.6%. In addition, if you withdraw from an IRA before you reach age 59½, you must pay a 10% penalty tax unless you qualify for a special exception.

Suppose you're age 55 and you take a fully taxable distribution of $100,000 from your traditional IRA. If you're in the top 39.6% bracket, you'll owe tax of $39,600, plus a penalty of $10,000, for a total tax bill of $49,600. Withdrawing that money also could have other adverse tax consequences, such as making you liable for a 3.8% surtax on net investment income.

Contributions to a Roth IRA, meanwhile, are never tax-deductible, but when you take a distribution from a Roth you've had for at least five years that income is completely tax-free and also exempt from the 10% tax penalty. The lure of future tax-free payouts is usually the driving force behind converting a traditional IRA to a Roth.

The downside of a conversion is that you're taxed on maybe all or at least a part of the amount you convert, just as if it were a distribution from a traditional IRA. If you're in the peak of your earning years and in the top 39.6% tax bracket, or close to it, you may owe a hefty tax for the conversion. Even if you spread out the conversion over several years, the cost may be too high to stomach. (If most of your contributions to the traditional IRA were not deductible, however, the tax hit of a conversion could be reduced considerably.)

But if tax rates indeed are reduced soon, a conversion might become more palatable. For example, if a previously proposed three-tier structure of 12%, 25%, and 33% were adopted, someone

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Federal Estate Tax Reduced, But What About State Taxes?

The IRS has increased the federal estate tax exemption, which is indexed annually for inflation, to $5.49 million for 2017, up from $5.45 million in 2016. That lets couples now shield as much as $10.98 million from federal estate tax.

Depending on where you live, you still might have to worry about estate and inheritance taxes on the state level. But there's more good news: Nine states have enacted changes in these taxes to reduce the tax bite for some families in 2017.

In New Jersey, which long has had only a $675,000 exemption from state estate tax, the amount will increase to $2 million in 2017 before the tax goes away in 2018. But a state inheritance tax for heirs who aren't direct descendants still applies. In Maryland, meanwhile, the state exemption rises to $3 million; in Minnesota, to $1.7 million; and in New York, to $5.25 million (effective April 1, 2017). Rhode Island and Washington are indexing their exemptions for inflation. Finally, Delaware, Hawaii, and Maine will match the federal exemption amount.

Residents of some states may need to amend their wills to reflect the changes and to avoid any unintended results—such as giving more than you'd planned to a particular heir. An estate-planning professional can help you with your situation.

5 'Other' Retirement Saving Ideas

Usually, experts will tell you that the best way to save for retirement is by putting money into a 401(k) plan, an IRA, or another well-known retirement saving vehicle. And they're usually right. But you may not have access to a 401(k), and the contribution limits for IRAs are relatively low. Or those options may not appeal to you for other reasons.

That doesn't mean you can't save for retirement. Here are five other possibilities you might consider:

1. Brokerage accounts: Unlike when you sell a holding from inside a tax-deferred retirement plan, the sale of stocks, bonds, or mutual funds in a brokerage account may result in current taxes. But the maximum tax bite for assets held longer than one year is only 15% or 20% for investors in the top ordinary income tax bracket. That's much better than the taxes you'll rack up when you eventually withdraw money from your retirement plans. Those distributions will be taxed at rates as high as 39.6%.

2. Annuities: An annuity is a contract with a financial institution that provides you with income for a term of years or for your lifetime. There are many kinds of annuities, and the amount you receive may be fixed or variable, perhaps depending on the performance of investments. You'll be taxed only when payments are made, but annuity income is taxed at ordinary income rates.

3. Real estate: There are no guarantees, but real estate investments may appreciate in value and provide steady income. If you own investment real estate (for example, a commercial building or an apartment complex), you can rent it to tenants and receive regular income. You also may be able to deduct certain expenses, including depreciation, to offset the tax due on that rental income. When you finally sell the property, any appreciation will be taxed at the rates for capital gains.

4. Small businesses: You might start a business and run the company yourself, or you could invest in someone else's enterprise. The tax law provides a special exclusion for investments in "qualified small business stock" (QSBS) if you meet certain requirements. Such investments bring the chance of a big payoff, but they also can be risky. Many small businesses fail within their first years of operation.

5. Life insurance: Although life insurance technically isn't an investment for retirement, it could provide benefits that help fund your retirement. Typically, a policy offers protection for your spouse in retirement if you should die, and you can borrow against the cash value of some kinds of insurance. An added benefit is that life insurance proceeds are completely exempt from income tax. You may also be able to take withdrawals or arrange a tax-free exchange to an annuity or a long-term care insurance policy.

These are a few ways to think outside the box in deciding how to fund your retirement. Talk with your advisor about the ideas that will work best for you. ●

Annuities and real estate investments are income-generating investments that may offer attractive yields and distribution growth rates, but they are complex investments with unique tax characteristics and significant risks. As a result, annuities and real estate investments may not be suitable for all clients. It is important to understand all the features, characteristics and risks of any particular investment offering under consideration. Consult with a tax advisor before investing in annuities and real estate.

Sticking With The Fundamentals

When financial advisors explain the reasons to invest in, or not invest in, particular stocks, they often refer to the "fundamentals" of the companies in question. Media pundits also may cite "fundamentals" in their stock prognostications. And corporate officers may brag about their companies' "fundamentals."

But what does it all mean? They're generally referring to fundamental analysis, a traditional school of thought in looking at companies' basic numbers as a way to evaluate profitability.

Unlike technical analysis of a company, which focuses on the recent trading and pricing history of the company's stock, fundamental analysis paints a broad picture of a company. This process identifies the fundamental value of the shares and leads to decisions to buy or sell the stock.

With technical analysis, you're trying to spot patterns that will help predict whether the fortunes of a company will rise or fall. In contrast, fundamental analysis involves profit margins, management decisions, growth potential, balance sheets, a company's role in a specific industry or sector, and political and other events, domestically and globally, that might affect its performance.

But fundamental analysis isn't limited to figuring out which stocks to buy and when to buy them. It is also about analyzing the timing of possible sales or purchases.

For example, when the stock market is booming, as it was at the start of 2017, investors are quick to jump on the bandwagon, while during times of stock market decline, the same investors often flee in a panic. That's what happened in 2008 and 2009, when the economy contracted and share prices fell by more than half. Of course, there are times when it makes sense to sell stocks, but it is best not to base such decisions based on fear.

A better idea is to take a closer look at the fundamentals. In doing so, you might

5 Steps To Realize An Early Retirement Dream

Have you dreamed about getting out of the rat race and retiring early? You could live a simpler life, pursue personal passions such as travel or recreation, and reduce your stress level. But you might think an early retirement is just for multimillionaires and out of your reach.

Think again. Early retirement doesn't have to be a pipe dream. It could become a reality through some diligent planning and dedication to your goals. These five steps may push you along the way:

Step 1: Plan on spending less. Don't give up if retirement planning calculators show you'll need much more than what you believe you conceivably can set aside. You can put a sizable dent in the "nut" you have to crack by significantly reducing your spending habits.

Remember that you won't be incurring commuting costs and a high-priced wardrobe for your job once you leave work. Furthermore, if you're hoping to travel around the world, you may be able to do it on a tighter budget than you thought. And simplifying your lifestyle—for example, maintaining just one car (or not even having one) instead of two —will provide savings.

Of course, life likely will throw you some curveballs, so be prepared for that, too. Build a cushion into your plan.

Step 2: Downsize your home. Part and parcel of the first step to early retirement is a reduction in housing costs. For most people, this is the single largest drain on savings. Do you really need that rambling colonial in the suburbs if your kids are grown and out of the house? This can be especially beneficial if the mortgage is paid off. You can sell the home at a sizable gain, move to a less expensive place, and pocket the difference.

Consider a retirement community if you're age 55 or older. If that's not the right fit, look for housing that's affordable but gives you the flexibility you want. For some early retirees, it's an apartment in a city with easy access to restaurants and stores.

Step 3: Secure adequate health insurance. One of those curveballs could be your health. Even if you're in reasonably good shape as you enter early retirement, there's no way to predict what will follow. And your retirement could last longer than you initially expected.

Medicare kicks in at age 65 and you can supplement it with another policy. Prior to that age, the Affordable Care Act (ACA) has made it easier for some people to retire early, but the future of the ACA, in this current climate, is in jeopardy. Conduct in-depth research to find health insurance policies that provide the necessary coverage at a cost you can handle. Depending on your situation, you might opt for a high-deductible plan. In any event, you can't go without health insurance!

If you expect to be traveling extensively, include this in your health insurance considerations. For instance, you may decide to obtain temporary travel insurance, based on your destinations.

Step 4: Maximize your investments. Saving more for retirement—and that includes how you invest your funds—may enable you to call it quits early.

Of course, everyone's situation is different. Put together a diversified portfolio that is aimed at your objectives while taking into account your personal risk tolerance. Frequently, your assets will involve a mix of stocks, bonds, mutual funds, and perhaps other investments such as real estate and exchange-traded funds (ETFs).

International investments, too, may be part of that mix, though such holdings bring special risks, including the potential that economic and political turmoil and currency fluctuations could affect the value of your investments.

Step 5: Count on taxes. Finally, don't dismiss taxes as a factor. Even if tax rates fall soon, they could rise again, and taxes always will erode your retirement savings to some degree. One strategy that may help is to move to a state with lower state tax rates.

Cashing in stocks during your retirement will result in capital gains, currently taxed at favorable rates, while distributions from retirement plans such as 401(k)s and traditional IRAs are taxed at higher rates for ordinary income. Also, payouts you take before age 59½ may be hit with a 10% tax penalty. (Roth IRA distributions can be tax-free, but you still may be penalized if you withdraw funds too early.) Remember that you must begin taking required minimum distributions (RMDs) from most retirement plans and traditional IRAs after age 70½. In addition, Social Security benefits may be subject to tax.

These and other steps can help take you closer to your dream of early retirement. ●

Income-generating investments such as stocks, bonds, mutual funds, ETFs and real estate may offer attractive yields and other benefits, but they are complex investments with unique tax characteristics and significant risks. As a result, these investments may not be suitable for all clients. It is important to understand all the features, characteristics and risks of any particular investment offering under consideration. Consult with a tax advisor before investing in such income-generating investments.

ask—and get answers to—these questions after a market decline has pushed down the price of a particular holding:

- Is the business model still solid?
- Have profit margins remained consistent?
- Is the company financially sound?
- Is the company likely to thrive over time?

If the answers are "yes," you may be well-served to retain your shares in the company for the long term. However, if the firm appears to be heading in the wrong direction, has shrinking profit margins, and sports a business model that is out of touch with changes in the industry, you probably should sell sooner rather than later.

Of course, you don't have to pour through financial reports and other documents to guide your decisions. If you invest in mutual funds, their professional managers are doing this work for you, analyzing company fundamentals to help them decide what to buy or sell to maximize their funds' performance. And we routinely help clients investigate stock fundamentals as they shape their portfolios. Please give us a call if you'd like to discuss your current and potential holdings. ●

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Roth IRA Conversions

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who had been in the 39.6% bracket might save tens of thousands of dollars in taxes on a large conversion. This may be enough to convince you to convert should tax rates be cut, especially if you believe that the rates might rise again in the future.

Of course, there's no guarantee that a tax cut will be enacted, and if you made a conversion assuming taxes would go down, you could be disappointed. In that case, though, you could decide to "recharacterize" your new Roth IRA back into a traditional IRA. With this technique you simply undo the conversion. As far as the IRS is concerned, it's as if it never had occurred.

What's more, you have plenty of time to decide if you want to recharacterize. The deadline is the tax return due date for the year of the conversion plus extensions. In other words, if you convert in 2017, you have until October 15, 2018, to complete a recharacterization.

And there's nothing that says you couldn't choose to convert to a Roth IRA all over again. But the earliest you could do that is the beginning of the tax year following the tax year of the conversion or the end of a 30-day period beginning on the day of the recharacterization, whichever is later.

Yet while it's possible to undo a Roth conversion—and then to reconvert back to a Roth—it's better not to proceed based just on what you think is going to happen in Washington. We can help you weigh the factors of your situation as you weigh the pros and cons of a Roth conversion now or later. ●

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