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Hello,

I'm Looking forward to a great 2016!

Please feel free to contact me anytime to review your investments and plan for the future.

Mike

Issue 16

Don't Forget About Year-End Investment Planning

When 401(k) Plans Go Bad--Avoiding Disqualification

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Don't Forget About Year-End Investment Planning

As the year draws to a close, there might be a slew of tasks on your to-do list. One task to consider is setting up a meeting with your financial professional to review your investments. If you take the time to get organized now, it may help you accomplish your long-term goals more efficiently. Here are some steps that might help.

Evaluate your investment portfolio

During the meeting with your financial professional, review how your overall investment portfolio fared over the past year and determine whether adjustments are needed to keep it on track.

Here are some questions to consider:

- How did your investments perform during the year? Did they outperform, match, or underperform your expectations?
- What caused your portfolio to perform the way it did? Was it due to one or multiple factors?
- Were there any consistencies or anomalies compared to past performance?
- Does money need to be redirected in order to pursue your short-term and long-term goals?
- Is your portfolio adequately diversified, and does your existing asset allocation still make sense?

Addressing these issues might help you determine whether your investment strategy needs to change in the coming year.

Aim for balance

During the portfolio review process, look at your current asset allocation among stocks, bonds, and cash alternatives. You might determine that one asset class has outperformed the others and now represents a larger proportion of your portfolio than desired. In this situation, you might want to rebalance your portfolio.

The process of rebalancing typically involves buying and selling securities to restore your portfolio to your targeted asset allocation based on your risk tolerance, investment objectives, and time frame. For example, you might sell some securities in an overweighted asset class and use the proceeds to purchase assets in an underweighted asset class; of course, this could result in a tax liability.

If you own taxable investments that have lost money, consider selling shares of losing securities before the end of the year to recognize a tax loss on your tax return. Tax losses, in turn, could be used to offset any tax gains. When attempting to realize a tax loss, remember the wash sale rule, which applies when you sell a security at a loss and repurchase the same security within 30 days of the sale. When this happens, the loss is disallowed for tax purposes.

If you don't want to sell any of your current investments but want to change your asset allocation over time, you might adjust future investment contributions so that more money is directed to the asset class you want to grow. Once your portfolio's asset allocation reaches your desired balance, you can revert back to your previous strategy, if desired. Keep in mind that asset allocation and diversification do not guarantee a profit or protect against loss; they are methods used to help manage investment risk.

Your financial professional can help you understand how your investments may be affected by capital gains and other taxes. You can learn more about current tax laws and rates by visiting www.irs.gov.

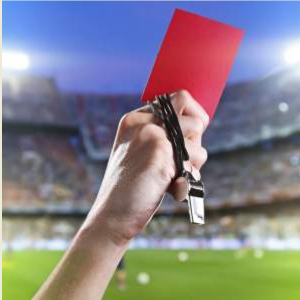
Set goals for the coming year

After your year-end investment review, you might resolve to increase contributions to an IRA, an employer-sponsored retirement plan, or a college fund next year. With a fresh perspective on where you stand, you may be able to make better choices next year, which could potentially benefit your investment portfolio over the long term.

Note: *There is no assurance that working with a financial professional will improve investment results. All investing involves risk, including the potential loss of principal, and there can be no guarantee that any investing strategy will be successful.*

See disclaimer on final page

When 401(k) Plans Go Bad--Avoiding Disqualification



The IRS correction programs--SCP, VCP, and Audit CAP--are components of the IRS Employee Plans Compliance Resolution System (EPCRS), currently described in Revenue Procedure 2013-12. The Rev. Proc. contains general guidance on how failures should be corrected and describes correction methods already approved by the IRS for many common plan failures.

As a small-business owner, you probably either have, or have considered adopting, a 401(k) plan. 401(k) plans have assumed their starry status in the retirement universe because of the favorable tax benefits they provide to both employers and employees.

Most importantly, employers get an immediate tax deduction for contributions they make to their plans, and employees benefit from pre-tax contributions and tax-deferred, or in some cases tax-free, accumulation of investment earnings. But these tax benefits come at a cost. Employers must follow strict and often complicated laws in the Internal Revenue Code, and regulations promulgated by the government agencies charged with interpreting those laws--primarily the Internal Revenue Service and the Department of Labor.

Tax effects of plan disqualification

Plans that comply with the tax rules are said to be "qualified" and therefore entitled to their favorable tax status. But plans that run afoul of the rules (for example, by improperly excluding participants, missing contributions, or failing discrimination tests) can become "disqualified." The potential consequences of disqualification are severe:

- Employees are taxed on their pretax contributions in the year those contributions are made to the plan, rather than the year the contributions are paid from the plan.
- In general, employees are taxed on employer contributions, and plan investment earnings, in the year they vest, rather than the year benefits are paid; in certain cases, highly paid employees are taxed on the entire value of their accounts (to the extent not already taxed).
- Employers take deductions for plan contributions in the year their employees vest in that contribution, rather than the year the employer made the contributions to the plan.
- The plan trust must pay taxes on its earnings.
- Distributions from the plan are ineligible for special tax treatment and cannot be rolled over tax free to IRAs or other qualified employer plans.

Even worse, a plan may be disqualified *retroactively* if the plan defect occurred in a prior year. This means that employers and employees would likely need to file amended returns to reflect the tax effects of disqualification for those prior years. Penalties for underreporting income in those prior years could also be imposed. And while the IRS generally can't go back more than three years (six years if there was a substantial underreporting of income) to collect taxes for any earlier year, the IRS might require correction of those closed years if an employer seeks to requalify its plan.

IRS to the rescue

Luckily, the IRS has adopted several programs that may help you avoid the potentially disastrous consequences of disqualification.

The Self-Correction Program, or SCP, is generally the program of choice if you're eligible. This program allows you to self-correct many plan errors--and preserve the tax-favored status of your plan--without contacting the IRS or paying a fee, and there are no application or reporting requirements. "Correction" generally means that the plan and participants must be placed in the same position they would have been if the failure had not occurred. The program is available for any errors that occur when you don't follow the written terms of your plan. You can correct insignificant errors at any time. And you can even self-correct significant operational errors if you act promptly. ("Egregious" errors can't be corrected using SCP.)

If you're not eligible for SCP (or if you'd like the comfort of IRS approval of your corrections), the next step is the Voluntary Correction Program (VCP). This program is available only if your plan is not being audited. You must submit an application to the IRS describing the plan failure(s), describe how you intend to correct those failures, and detail the administrative changes you intend to adopt to avoid those failures occurring in the future. You must also pay a compliance fee, ranging from a few hundred dollars to $25,000, depending on the nature of the failure and the number of plan participants. If your application is approved, the IRS will generally agree not to disqualify your plan because of the disclosed failures if you complete the approved corrections within 150 days.

If you don't use SCP or VCP to voluntarily correct plan errors, and the IRS discovers the failures itself (for example, during a plan audit), you may still be able to preserve your plan's tax benefits by using the Audit Closing Agreement Program (Audit CAP). Under this program, you must correct the plan failures, enter into a "Closing Agreement" with the IRS, and pay a penalty equal to a negotiated percentage of the additional taxes that would have been payable had the plan been disqualified.

The qualified plan rules are complicated. Working with a retirement plan professional can help you avoid mistakes that could lead to the ultimate penalty of disqualification.

What to Know About Buying a Fixer-Upper

If you install certain energy-efficient equipment in your home, you may be eligible for a tax credit.

The residential energy efficient property credit (available through 2016) can be claimed for 30% of the cost of specific energy-efficient equipment that you install in your home. This equipment includes solar electric items, solar water heaters, wind turbines, geothermal heat pumps, and fuel cell property.

See IRS Tax Tip 2015-38 for more information.

Buying a fixer-upper property has become popularized thanks to home improvement shows. But buying a fixer-upper--either to keep or resell--isn't just for TV.

Why purchase a fixer-upper?

There are many reasons to consider purchasing a fixer-upper, such as:

- Profit potential--If you choose to rent or sell the home, you have an opportunity to earn an income or make a profit.
- Build equity--If you plan to occupy the home, you can build equity over time and eventually pass the home to family members.
- Reduced competition--Buyers may be reluctant to purchase properties that require extensive renovations. A smaller competition pool may increase your chances of acquiring the property at a lower cost.

Because there are many potential benefits to buying a fixer-upper, it's important to understand the process and the potential problems that can come with it.

Location, location, location

Location is key when purchasing any piece of real estate. Look for properties in desirable areas or where property values are on the rise. The renovations needed could elevate the home to the level of the neighboring houses. Updating a home in an undesirable neighborhood may leave you with a property that costs more to renovate than you would make by reselling it.

What about foreclosures?

Purchasing foreclosed properties has become increasingly popular for those looking to profit from real estate; however, buying bank-owned property can come with many possible drawbacks. In many instances, homes owned by a bank cannot be fully inspected prior to purchase, and the bank may be unable to provide information on the condition of the home. This can lead to some unwelcome surprises when you finally get to see the property you've purchased. When purchasing a foreclosed home, anticipate some setbacks and create a contingency reserve for unforeseen costs.

Easy vs. expensive fixes

Whether you're planning to do the work yourself or hire an expert, you need to know how difficult, time-consuming, and expensive the improvements will be.

Easy fixes include painting walls, removing wallpaper, replacing light fixtures and fans, and refinishing floors. More expensive fixes include replacing a roof, plumbing, electrical, or windows; an extensive kitchen or bath remodel; and replacing HVAC systems or adding central air.

Some renovations add more value to the home than others. When making renovation decisions, consider both the estimated cost and the home's projected resale value. Less expensive renovations may generate a higher profit margin, while more expensive renovations might leave you with a minimum return on the money you spent.

Tax consequences

While renovations are one of the most important (and exciting) aspects of owning a fixer-upper, also consider the potential tax consequences that come with buying any piece of real estate. The tax implications will vary depending on whether you live in the home, rent it out, sell it right away, or hold on to it for a while for resale. Talk to your tax professional to learn more about the tax consequences for your specific situation.

Financing your fixer-upper

Both the Federal Housing Administration (FHA) and Fannie Mae offer loan programs specifically for people renovating a home.

The FHA 203(k) Rehab Loan is a government-funded loan that can help you finance both the purchase of the home and the projected cost of renovations in one mortgage. This loan program is limited to the rehabilitation of homes that will be owner occupied, and therefore might be a good option if you want to invest in a fixer-upper that will stay in your family. (Source: U.S. Department of Housing and Urban Development, 203(k) Rehab Mortgage Insurance)

Unlike 203(k) loans, the Fannie Mae HomeStyle Loan is not limited to the renovation of homes that will be owner occupied; therefore, this loan program can be used by homebuyers who wish to renovate a fixer-upper into a vacation home or rental property. There are no restrictions on the types of repairs allowed except that all repairs must be on the property and must add value to the home. (Source: Fannie Mae HomeStyle Renovation Mortgage Fact Sheet, August 2014)

For more information on both loans, visit hud.gov and fanniemae.com.

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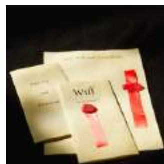

What do I need to do to create a will?

A will is a legal document that is generally used to describe how you want your estate to be distributed after your death. It might also be used to name an executor for your estate or a guardian for your minor children. It is generally a good practice to name backup beneficiaries, executors, and guardians just in case they are needed. Even though it's not a legal requirement, a will should generally be drafted by an attorney.

In order to make a will, you must be of legal age (18 in most states). You must also understand what property you own, who the family members or friends it would seem natural to leave property to are, and who gets what under your will.

Generally, a will is a written document that must be executed with appropriate formalities. You should sign the document (or direct someone else to sign for you in your presence). The will should also be signed by at least two witnesses who are of legal age and understand what they are witnessing; some states require three witnesses. The witnesses should not benefit from any provisions in the will. Some states also require that a will be notarized.

Some states allow a will that is entirely in your handwriting, known as a "holographic" will. Some states allow a "nuncupative" will, which is an oral will you dictate during your last illness, before witnesses, that is later converted to writing.

Note that certain property is not transferred by a will. For example, property you hold in joint tenancy or tenancy by the entirety passes to the surviving joint owner(s) at your death. Also, certain property (e.g., life insurance, qualified retirement plans, IRAs, Totten Trust accounts, Payable on Death accounts, Transferrable on Death accounts) passes directly to the designated beneficiary at your death, bypassing the probate process.

Your will does not take effect until you die. You can create a new will or revoke or amend an existing will up until your death.

How do I change or revoke a will?

Your will does not take effect until you die. You can create a new will or revoke or amend an existing will up until your death.

A will remains valid until properly revoked or superseded. Revoking your will must be done very carefully. Most state laws require that the will be revoked by a subsequent instrument (a new will) or by a physical act (e.g., destroying or defacing it). This means the will must either be burned, torn, or canceled with the intent to revoke. You might, for example, write REVOKED across the will and sign and date the revocation.

You can amend (change) your will by executing a codicil. A codicil is a separate, written, and formally executed document that becomes part of your will. More specifically, a codicil is a supplement or addition to a will that explains, modifies, or revokes a previous will provision or that adds an additional provision. A codicil generally should be used only for minor changes to your will. You should execute a new will if there are many changes or a major change.

A codicil should generally be executed with the same formalities as required for a will. In general, the codicil must be signed, dated, and witnessed in accordance with the laws of the appropriate state.

The codicil should be attached to the will it is amending. Be sure to draft, execute, and attach a copy of the codicil to each copy of your will.

Although a new will usually must be contested in its entirety, some states will allow a codicil to be contested on its own. If it is found to be invalid, only the changes contained in the codicil will be voided and the remaining will provisions remain valid.

Some states provide that provisions in a will may be revoked automatically upon marriage or divorce. It is generally a good practice to review your will and make changes as needed upon marriage or divorce, or for any other major changes in your life.

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