April 18, 2018

BLUME CAPITAL MANAGEMENT
A Few Financial Tips Following Tax Season

With the deadline for filing your 2017 tax return (or filing an extension) behind us, you may find yourself wondering if there are other things you should be doing for tax planning purposes or more generally for your financial health. After you finish organizing your records from 2017, it is a good time to learn about or refresh your memory about some financial considerations that may be relevant to you or your loved ones.

This is certainly not an exhaustive list and, as always, you should consult with your accountant for specific tax guidance and other specialists as appropriate. Nevertheless, we thought some of the points described herein may be useful for you. Read on to learn more about 529 education savings plans, tax-free gifting, health savings accounts, IRMAA Medicare surcharges, Social Security claiming strategies, and Qualified Charitable Distribution from an IRA (applicable at age 70 ½).

529 Plans

As you may know, a 529 plan is an investment account that can provide tax savings if the funds are used to pay for certain educational expenses. These "qualified tuition programs" are offered by all 50 states, and most 529 plans are open to residents of any state. While California does not, many states offer additional benefits to residents who invest in their own state's plans.

The advantage of putting money into a 529 plan is the opportunity to let the funds grow and be withdrawn tax free to pay for education. Therefore, the longer the time horizon, the greater the potential tax savings. These accounts were designed to help pay for college, but the funds can be used for a wider range of expenses than many people realize and there are some strategies that can boost the savings.

So how do 529 plans work exactly? Contributions to 529 plans are made with after-tax dollars; in other words, there are no federal tax savings when you set aside money in a 529 plan, although some states do offer state tax deductions or credits. The funds must be used to pay for qualified educational expenses in order to avoid a 10% penalty on any gains in the account. If the money is used to pay for qualified educational expenses, the distributions are tax free and penalty free.

For college expenses, 529 funds can be used for tuition, fees, books, supplies, and even room and board if the student is enrolled at least half time. Money in 529 plans can also be used at a wide range of

eligible institutions including traditional four-year colleges and universities, local community colleges, theological seminaries, vocational or trade schools, and international schools.

A major change starting in 2018 is an expanded definition of "qualified" expenses. Money in 529 plans can now be used for up to $10,000 of tuition per year for private primary and secondary education. Qualified K-12 educational expenses can only include tuition and neither all states nor all plans have changed their rules to align with the new federal law. Consequently, it is important to check with one's state and one's plan before using 529 funds for K-12 tuition.

Another benefit of 529 plans is that one can take advantage of a special funding rule to "front-load" contributions. In general, one can contribute up to the annual gift tax exclusion amount ($15,000 per recipient in 2018) to each beneficiary's 529 plan without incurring gift taxes. The lump-sum contribution gift tax averaging rule allows one to give of up to five times the annual gift tax exclusion amount in a single year.

For example, a married couple could accelerate five years of gifting and contribute $150,000 in 2018 to a 529 plan using gift tax averaging (each spouse gifting $75,000 or five times $15,000). They would avoid federal gift tax provided that no other gifts are made to the same beneficiary during that five-year period.

While one would not want to over fund a 529 plan, they are quite flexible. There are no age limits on contributions or distributions. In addition, the beneficiary may be changed or funds transferred to another family member (e.g., cousin) of the current beneficiary.

Tax-Free Gifting

If one would like to help a family member or friend with current bills, there is an unlimited tax-free gifting option for medical or educational expenses. With the federal gift and estate tax exemption now up to $11.2 million for an individual, one may not be subject to gift tax under any circumstance, but laws can change and some states impose estate or inheritance taxes.

In general, gifts must be reported on one's tax return if more than the annual gift tax exclusion amount ($15,000 per recipient in 2018) is given in a calendar year to a non-spouse beneficiary. While the gift may not be taxable, IRS Form 709 typically needs to be filed to track use of one's lifetime exemption from gift and estate tax.

To avoid the need to file IRS Form 709 and still support non-spouse beneficiaries, one can directly pay certain medical or educational expenses. To qualify for the medical expense exclusion, funds must be paid directly to the health care provider, medical facility, or even insurance company (to cover health insurance premiums). The educational expense exclusion is limited to tuition only and payments must be made directly to the educational institution (primary through graduate school is eligible).

Health Savings Accounts (HSAs)

One must be covered by a HSA-qualified health care plan in order to take advantage of the tax saving, but if eligible, these accounts offer significant tax advantages. The primary purpose is to allow people to fund their out-of-pocket medical costs with pre-tax dollars. Health savings accounts, compared to other types of flexible spending accounts for health care, have an added benefit that the money can be used in future years (i.e., the funds do not need to be spent in the year contributed).

HSA-qualified health care plans are also referred to as "high-deductible" health insurance. In 2018, to be eligible to contribute to a health savings account, one must be covered by a plan with a minimum deductible of $1,350 for an individual or $2,600 for a family; although the plan can offer free preventative care. There are additional details with regards to eligibility and qualified expenses that we will not attempt to cover here.

HSAs are the only investment vehicles that have a triple tax benefit. Contributions are federally tax deductible (or withdrawn pretax from paychecks by one's employer), as they are in most states except for California, New Jersey, and Alabama. The money can be invested and earnings are tax deferred; no taxes are due on the growth in the account. And, if used for qualified medical expenses, the money can be withdrawn tax free.

The bigger long-term upside comes into play for people who are able to fund their HSA and can afford to pay for medical expenses out of pocket with after-tax dollars. In 2018, the maximum annual contribution is $3,450 for an individual or $6,900 for a family, those over age 55 can contribute an additional $1,000 annually. If one can maximize contributions for several years and let the funds grow, the money can be withdrawn tax free in retirement to cover qualified medical expenses. It is even feasible to maintain records of medical expenses from pre-retirement years (paid with after-tax dollars) and then take a tax-free withdrawal in retirement to cover living expenses. In summary, if you have access to a HSA-qualified health care plan, it is worth evaluating the retirement saving option.

Medicare Surcharge -- Income-Related Monthly Adjustment Amount (IRMAA)

Many people are not aware that high-income Medicare enrollees are required to pay an Income-Related Monthly Adjustment Amount surcharge on their Medicare Part B and Part D premiums. In essence, high earners pay larger Medicare premiums. The surcharge is based on one's Modified Adjusted Gross Income (MAGI) from two years prior. There are four tiers of increasing surcharges based on income thresholds. The applicable MAGI for 2018 is one's Adjusted Gross Income plus any tax-exempt bond interest from the 2016 tax year (using the return filed in 2017).

In 2018, the top tier of these IRMAA surcharges applies at lower income thresholds. The top income tier for 2018 is "only" $160,000/year for individuals or $320,000 for married couples filing jointly, down from $214,000 and $428,000, respectively, in 2017.

The IRMAA premium surcharges in 2018 range from $798 to $4,433 total for the year, therefore not a tremendous expense, but it is beneficial to recognize if any proactive planning may be applicable. For example, new Medicare enrollees who are retiring should request an adjustment to avoid having their

pre-retirement wages treated as part of their income. Alternatively, one can consider the timing of a transition from private health insurance if still working past age 65.

Social Security Claiming Strategies

The earliest that one can start receiving Social Security retirement benefits is age 62. It is, however, rarely advisable to begin claiming benefits before one's "full retirement age" and frequently, it is better to wait until age 70 based on expected longevity.

Your full retirement age (FRA) is based on your year of birth. People born in 1937 or earlier have a FRA of age 65. Those born from 1943 to 1954 have a FRA of age 66. The FRA is age 67 for anyone born in 1960 or later. For the interim years, those born 1938 to 1943 and 1955 to 1959, the FRA increases by two months for each subsequent year of birth.

One's benefit amount is permanently reduced for each month before the applicable FRA that one claims Social Security retirement benefits. Conversely, earnings are permanently increased for each month after the applicable FRA that one waits, up until age 70. For example, the following table illustrates the impact of different filing dates for someone with a FRA of age 66:

If you start getting benefits at age ...	And you are the: Wage Earner, the Retirement Benefit you will receive is ...	Sample annual Wage Earner Retirement Benefit amount (for illustrative purposes)
62	**reduced to 75.0%**	**$18,750**
64	reduced to 86.7%	$21,675
65 + 6 months	reduced to 96.7%	$24,175
65 + 11 months	reduced to 99.4%	$24,850
66 = FRA	**100.0%**	**$25,000**
68	increased to 116.0%	$29,000
69 + 6 months	increased to 128.0%	$32,000
69 + 11 months	increased to 131.3%	$32,833
70	**increased to 132.0%**	**$33,000**

Of course, there are many other considerations to take into account when determining when to claim Social Security retirement benefits, including eligibility for spousal or survivors benefits, the existence of any non-covered pensions, and expected longevity. In general, we recommend that people wait until age 70, but each situation should be analyzed individually.

Qualified Charitable Distributions

Utilizing Required Minimum Distributions (RMDs) from retirement accounts is gaining popularity as a way to fund charitable contributions. One is typically required to begin taking RMDs from tax-deferred retirement accounts starting at age 70 ½. These RMDs are taxed as ordinary income.

In certain circumstances, it may be beneficial to use one's RMD (versus a gift of appreciated stock) for tax-favored charitable giving. Donating a portion or all of one's RMD by means of a Qualified Charitable Distribution (QCD) reduces one's taxable ordinary income and therefore reduces Adjusted Gross Income (which, as discussed above, can impact Medicare premiums).

A typical scenario when a QCD makes sense is where one has a large annual RMD combined with substantial earned income past age 70 ½. Certainly, there can be other considerations that impact the merit of using a QCD for charitable giving, so each circumstance must be evaluated annually.

Questions?

Please let us know if you would like to further discuss any of the topics described herein or if there are other financial topics about which we may be of assistance.

Sincerely,

Amy S. Thacher, CFP®

*Please Note: Blume Capital Management is neither a law firm nor a certified public accounting firm and no portion of its services should be construed as legal or accounting advice. Moreover, you should not assume that any discussion or information contained above serves as the receipt of, or as a substitute for, personalized investment advice from Blume Capital Management. Please remember that it remains your responsibility to advise Blume Capital Management, **in writing**, if there are any changes in your personal/financial situation or investment objectives for the purpose of reviewing/evaluating/revising our previous recommendations and/or services, or if you would like to impose, add, or to modify any reasonable restrictions to our investment advisory services. A copy of our current written disclosure statement discussing our advisory services and fees is available upon request.*