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Please contact your Stifel Financial Advisor if you have any questions about the articles or for copies of the other materials mentioned in this newsletter.

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WHEN YOU HEAR TAX CUTS, THINK ROTH CONVERSION

Roth IRAs were established by the Taxpayer Relief Act of 1997, and for roughly 20 years, individuals have taken advantage of the tax-free benefit of these accounts. Whether funding the Roth IRA by annual contributions (if eligible) or converting traditional, SEP, or SIMPLE IRA or Qualified Retirement Plan assets to a Roth, there are several ways to get valuable retirement dollars into this potentially tax-free account.

How a Roth Conversion Works

When converting your traditional, SEP, or SIMPLE IRA or Qualified Retirement Plan assets to a Roth IRA, your pre-tax balances being converted will be included as taxable ordinary income for the year of conversion. This additional ordinary income could impact Roth IRA contribution eligibility, the taxation of your Social Security benefits or Medicare premiums, as well as offsetting certain tax deductions, credits, and exemptions. That can be a significant tax hit for many individuals and may deter them from doing a Roth Conversion, but consider the significant tax benefits down the road. If you have money in a Roth IRA for over five years and are age 59 ½ or older, the distribution of all Roth IRA assets, including the earnings, are considered qualified and will be distributed tax-free. In addition, Roth IRAs do not have Required Minimum Distributions (RMDs) when the original IRA owner is living. Roth Conversions may be a really great deal if you think about all of the tax-free earnings you could accumulate.

Why a Roth Conversion Makes Sense in 2018

The Tax Cuts and Jobs Act of 2017 has lowered tax rates for many Americans starting in tax year 2018. These low rates will not be here forever, as they are set to expire in 2025 or sooner based on what happens with the next Congressional and Presidential elections. No one knows for sure what the future will bring, but with growing deficits in Social Security and other governmental programs, future tax rate hikes are a real possibility. Converting pre-tax assets to a Roth IRA now is a way to lock in today's low tax rates and avoid the uncertainty of higher taxes in the future. If tax rates were to rise, you have already paid taxes on the conversion in 2018 and future qualified Roth IRA distributions would be tax-free in times of higher tax rates.

Roth Conversion Considerations

Conversions are not one size fits all. If you are wondering if a Roth Conversion is right for you or the dollar amount you should convert, it's always recommended that you discuss the strategy with your tax preparer or a CPA. A few questions to ask would include:

1. When would you need the Roth IRA?
   If you need the money immediately, converting may not be for you.
2. What is your current tax rate?
   If your income tax rate is lower now than you expect it to be later, that may favor a conversion.
3. Do you have the money to pay the tax on the conversion from outside of the IRA?
   It is best to pay the conversion tax from non-IRA funds. Distributions from a retirement plan or IRA are generally subject to taxes as well as a 10% penalty if under age 59 ½.

Please note that, beginning in 2018, conversions are irrevocable. There is no more recharacterization or the ability to undo a conversion. This means you must be absolutely certain before you move forward with this strategy. Are you a good candidate? Is 2018 the year for your Roth Conversion? The best way to find out what is right for you is to discuss your conversion options with a knowledgeable financial and tax advisor.

OCTOBER 15 IS THE DEADLINE FOR FINAL ROTH IRA CONVERSION RECHARACTERIZATIONS

Prior to January 1, 2018, after an IRA was converted to a Roth, there may have been a situation where the individual wanted to reverse the conversion. One example would have been when a tax-filer converted a traditional IRA to a Roth and afterwards the market value of the converted securities decreased in value. In this case, the individual was permitted to recharacterize (reverse) the conversion back to a traditional IRA and do so without taxation or penalty. However, on December 22, 2017, President Trump signed into law the Tax Cuts and Jobs Act of 2017 (effective January 1, 2018), which eliminated the ability to recharacterize a Roth Conversion executed on or after January 1, 2018. Even though conversions will still be permitted, once an IRA owner, or Qualified Retirement Plan participant, converts assets into a Roth IRA, there will not be a way to reverse this action and tax will be due on all pre-tax assets that were converted.

Conversions in 2017 May Still Be Recharacterized

As stated in the previous paragraph, the effective date to no longer allow recharacterizations was January 1, 2018. The IRS clarified that conversions that occurred in 2017 may still be recharacterized and the deadline to complete the reversal is Monday, October 15, 2018.

Contributions May Still Be Recharacterized

The IRS allows taxpayers that contribute to either a traditional or Roth IRA the opportunity to recharacterize that contribution (plus earnings or less the loss) to the other type of IRA. This may be a good strategy for those who discover their traditional IRA contribution is not deductible and therefore elect to make it a Roth IRA contribution or that they exceeded the income limit for Roth contribution eligibility and therefore elect to make it a non-deductible traditional IRA. Note that in order to move a traditional IRA contribution to a Roth IRA, the taxpayer's Modified Adjusted Gross Income (MAGI) must be under the allowable limits for the year the contribution is intended ($133,000 for a single filer and $196,000 for married couples filing a joint return for 2017). However, there are no MAGI limits for non-deductible contributions to traditional IRAs, and therefore, taxpayers may recharacterize Roth contributions to a traditional IRA if the IRA owner is under the age of 70½ for the intended contribution year.

EXTENSION DEADLINE FOR EMPLOYER CONTRIBUTIONS

Employers may wait until the company's tax filing due date plus extensions to make company contributions to Qualified Retirement Plans, SEP, and SIMPLE IRAs.

For fiscal year business owners, the standard tax filing date is the 15th day of the third month after the end of the corporation's tax year. Extensions can stretch the employer funding and filing deadline an additional six months following the normal filing deadline.

For calendar year filers, March 15, 2018, was the 2017 tax filing deadline for corporations including S-Corps. The 2017 tax filing deadline for self-employed individuals was April 17, 2018 (April 15 fell on a Sunday and Emancipation Day was observed on Monday, April 16, 2018).

Extension Deadlines

Business owners may request automatic extensions for tax filing, which includes plan contributions, by submitting appropriate forms to the IRS before their normal filing date.

If an extension was granted, September 17, 2018 (September 15 falls on a Saturday) is the final day a corporation may make company contributions. For self-employed individuals, October 15, 2018, is the final day employer contributions may be accepted and tax returns filed for 2017.

WAIVER OF 60-DAY ROLLOVER REQUIREMENT

Distributions from employer-sponsored plans and IRAs are generally excluded from an individual's income if the amount is rolled over into an eligible retirement plan within 60 days from the distribution. The IRS has issued guidance for individuals who have received IRA distributions and have missed their 60-day deadline. The guidance allows for IRA holders to self-certify that they satisfy certain requirements and are allowed an exception to the 60-day rollover limitation.

The Self-Certification Process

Under this guidance, IRA holders may certify that a rollover contribution satisfies certain conditions by completing the model letter included in the appendix of Revenue Procedure 2016-47 (or a substantially similar letter). The IRA holder must present this to the plan administrator or financial institution that received the rollover. In addition to the letter, the following conditions must be met:

- The IRS has not previously denied a rollover waiver request related to the rollover contribution.
- The contribution must be made to the plan or IRA as soon as practicable after the reason(s) for the delay no longer prevent the taxpayer from making the contribution. Rollovers made within 30 days of this date are deemed as satisfactory.
- The rollover contribution satisfies all requirements for a valid rollover (except for the 60-day limitation).

Reasons for Waiving the 60-Day Rollover Requirement

In order to self-certify for the 60-day rollover exception, one or more of the following situations must have occurred:

- Financial institution error
- Misplaced and uncashed the distribution check
- Mistakenly believing that the rollover was placed in an eligible plan
- Severe damage to the individual's principal residence
- Death of a family member
- Serious illness of the individual or a family member
- Incarceration of the individual
- Restrictions imposed by a foreign country
- Postal errors
- IRS levy proceeds returned to the taxpayer
- Delays by the distributing financial institution in providing information required to complete the rollover

Although the certification is not a waiver by the IRS of the 60-day rollover limitation, the IRS will ordinarily honor certifications that individuals qualify for, as a waiver of the 60-day rule. Individuals using the certification process must keep detailed records and be aware that if the IRS later determines during the course of an audit or examination that the requirements for the waiver were not met, they may be subject to additional taxes and penalties.

NEW SIMPLE IRA PLANS FOR 2018 MUST BE ESTABLISHED BY OCTOBER 1

SIMPLE IRAs are a great, low-cost option for employers with fewer than 100 eligible employees to offer a retirement savings benefit and help retain quality employees. They allow eligible employees to make pre-tax salary deferrals up to $12,500 ($15,500 if age 50 or older) per year and generally requires the employer to make annual contributions for each eligible employee. With SIMPLE IRA plans, each eligible employee or participant maintains his or her own SIMPLE IRA account for contributions and investing. Within a 60-day period preceding a plan year, the employer sponsoring the SIMPLE IRA must allow eligible employees to make salary-deferral elections for the upcoming plan year or, in other words, tell the employer how much to withhold from each paycheck to be deposited into the SIMPLE IRA. November 2 is the deadline for employers sponsoring existing SIMPLE IRA plans to provide plan information and a salary-deferral election to eligible employees for the following plan year.

For new SIMPLE IRA plans, October 1 is an important date, as the IRS requires all new SIMPLE IRA plans to be established by October 1 of the year in which deferrals will be made. The initial 60-day election period for new plans must begin by October 1, 2018, in order to contribute for 2018.

If you are an employee of a company currently not offering a retirement plan, consider discussing the SIMPLE IRA with your employer. Or, if you are an owner of a small business looking for a low-maintenance, cost-effective retirement plan, think about the benefits of the SIMPLE IRA, but don't forget the SIMPLE IRA Adoption Agreement or Plan establishment document must be signed by October 1, 2018, to contribute for 2018.

THE IMPORTANCE OF RETIREMENT PLAN EDUCATION

Having a great retirement plan is not enough. Everyone plans to retire; having a plan for retirement is a different story. Participants need to feel empowered to save and plan for retirement. Helping participants feel confident in their decision to save starts with education. Participants need to understand the fundamentals of saving, the benefits of starting early, and the importance those decisions will have on future ones.

The National Institute on Retirement Security shows that the median retirement account balance is $3,000 for working-age households and $12,000 for near-retirement households (U.S. News & World Report, 2018). The 2018 Retirement Confidence Survey found that only 17 percent of American workers feel very confident about having enough money for a secure retirement (Employee Benefits Research Institute (EBRI), 2018). Furthermore, the survey shows that about eight in ten workers expect their workplace retirement savings plan to be a source of retirement income, with about half saying it will be a major source (EBRI, 2018).

Employees undoubtedly are looking to their employer-sponsored retirement plans for retirement income. For most, their retirement plan may be their only source of income in retirement outside of Social Security. The lack of savings points to a lack of understanding and education about finances. Today, the Employee Retirement Income Security Act (ERISA) doesn't mandate that plan sponsors concern themselves with participant education at all. Failure to provide it doesn't constitute a breach of fiduciary obligation. However, the reasons for providing participant education are clear. Research shows employees are failing to take adequate advantage of their retirement plan options. That trend defeats the purpose of offering them in the first place. If an organization is willing to invest in providing the plan, make the investment in making it work for participants.

For the average participant, investing can be intimidating. Plan Sponsors can help demystify their retirement plan by offering a variety of avenues for their employees to get access to the information they need to make informed decisions regarding their retirement.

Teaching participants how to weigh their own situation is the most important step in making their retirement plan work for them. Everyone's situation is unique, and it is important for the plan participant to really think about how they envision their retirement, even if it is 30 or more years from now. Plan participants need to be thinking about the end result to make sure they are saving enough to reach their individual goals.

A PricewaterhouseCoopers/AonHewitt survey found that more than half of workers surveyed were under financial stress, and further reported that "the financially stressed survey respondents were significantly more likely to become ill, miss work, or be distracted at work because of personal financial matters ... "

Helping participants with the basics of investing and saving for retirement will not only help them be retirement ready but more efficient in their daily role. Stifel is here to provide guidance and help educate participants. Your Stifel Financial Advisor can help find the right solutions to manage a retirement plan communications program and help plan participants take a step towards being retirement ready.

HOW TO TAKE ADVANTAGE OF THE NEW TAX LAW THROUGH QUALIFIED RETIREMENT PLANS

Business owners encounter situations where the tax deductions afforded through traditional defined contribution plans are not significant enough to lower their tax liability to an impactful level. As a result, a defined benefit or cash balance plan might be a consideration to further reduce the business owner's taxable income and adjusted gross income (AGI). Cash balance plans are a form of defined benefit plan often created to accompany an existing defined contribution plan to gain access to high contribution limits and greater tax deductions.

The new tax law, signed into law on December 22, 2017, includes a key change to the tax treatment of pass-through entities, which creates a significant financial incentive for certain service businesses to sponsor a qualified retirement plan. This additional incentive has created a buzz in the defined benefit/cash balance plan space as an opportunity to further enhance tax deductions.

Which Business Types Are Classified as Pass-through Entities and Why?

Pass-through entities, for tax purposes, are sole proprietorships, partnerships, LLCs, and S-corporations because their profits are passed through to the owners and taxed at individual rates. Pass-through income can be taxed at individual rates as high as 39.6% effective 2018. The new tax law lowers the top individual rate to 37%, allowing many pass-through entities to deduct 20% of their business income.

Considerations to Qualify for the Deduction

Here are a few limitations and phase-outs to consider when determining if business owners qualify for the new deductions:

- The 20% deduction of Qualified Business Income (QBI) cannot exceed 20% of total taxable income, minus net capital gains.
- Pass-through entities can only take advantage of the full 20% deduction when the owners' total taxable income doesn't exceed a threshold amount of $315,000 for joint filers and $157,500 for single filers.
- If taxable income exceeds the threshold, the 20% deduction amount may be reduced on a capital and wage limitation.
  - The limitation is calculated as the greater of 50% of the owner's share of W-2 wages paid by the business, or 25% of the W-2 wages plus 2.5% of the capital asset used in the creation of income.
- If taxable income exceeds $415,000 for joint filers, or $207,500 for single filers, the pass-through deduction can't exceed the lesser of 20% of QBI, or the wage and capital limitation.

Who Doesn't Qualify?

The new tax law has placed specific guidelines on which pass-through entities do not qualify for the 20% deduction:

- Pass-through entities that are considered a "specified service business" with taxable income above $315,000 for joint filers ($157,500 for single filers) are phased out.
  - "Specified service business" is defined as "Any trade or business involving the performance of services in the fields of health, law, consulting, athletics, financial services, brokerage services, or any trade or business where the principal asset of such trade or business is the reputation or skill of one or more of its employees or owners, or which involves the performance of services that consist of investing and investment management trading, or dealing securities, partnership interests, or commodities. The definition is modified to exclude engineering and architecture service."
- No pass-through deduction is available for owners with taxable income above $415,000 ($207,500 for single filers).

How Do Qualified Plans Significantly Benefit Specified Service Businesses?

Since most specified service businesses are phased out for the new 20% pass-through deduction when joint income exceeds $315,000 (eliminated above $415,000), contributions to a qualified plan can afford a major financial incentive. Considering that contributions to a qualified retirement plan can reduce the owners' taxable income below the threshold outlined in the qualifications detail above, it is possible to take full advantage of the new 20% deduction.

Practical application (excerpt from Kravitz Information Release January 2018): A doctor is filing joint returns and has taxable income of $450,000 and makes a cash balance contribution of $135,000.

- Taxable income after cash balance contribution: $315,000 ($450,000 – 135,000)
- 20% pass-through deduction for $315,000: $63,000 (20% X $315,000)
- Taxable income reported: $252,000 ($315,000 – $63,000)
- Tax liability from new tax brackets: $49,059 ($28,179 + ($87,000 X 24%))
- Effective tax rate (tax liability/taxable income): 19.5% ($49,059/$252,000)

Not all businesses are suitable for a cash balance plan arrangement, but it can be a powerful solution to consider for the right business structure. As a result, business owners should consult with their tax advisors to fully understand the impact that the new tax law has on their tax liability.

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Deadline to establish a new

SIMPLE IRA PLAN TO CONTRIBUTE FOR 2018

October 1, 2018