FINANCIAL TID-BITTS

Information to chew on...

Tibbitts Financial Consulting
Steven Tibbitts, CFP®, CRC®
231 Hubbard Street
Allegan, MI 49010
269-673-4600
877-510-4648
steve@tibbittsfinancial.com
www.tibbittsfinancial.com

Hi Everyone,

Spring is just around the corner! Winter wasn't nearly as tough as it has been the previous two years, so hopefully we will have a longer warm season to enjoy outside activities.

Hopefully these articles will provide some insight, or maybe raise a few questions. If you have questions or concerns regarding your situation, please don't hesitate to call. As always, if I can be of help to you or anyone you care about, please let me know.

Thank you!

Steve

March 2016

TIBBITTS

FINANCIAL CONSULTING

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.

See disclaimer on final page

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.](studentaid.gov)

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.](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

TIBBITTS

FINANCIAL CONSULTING

Pros and Cons of Working from Home

Telecommuting, or working from home, is offered by many employers to their employees. Find out whether the financial advantages and disadvantages of working from home make it a viable option for you.

Imagine that your employer gives you the choice between either working from home or commuting to the office throughout your work week. You might think the obvious choice is to work from the comfort of your own home; after all, staying in your pajamas all day and avoiding stressful commutes sound appealing. But there are some considerations to think about before you decide that telecommuting is right for you.

Advantages

Working from home could end up saving you a considerable amount of money. It eliminates the cost of commuting by cutting down what you spend on gas, public transportation and parking fees, and car maintenance. And depending on your company's dress code, you could save what you might spend on expensive work-related clothes.

Besides reducing some of your daily expenses, working from home could provide you with more opportunities and increased productivity. Telecommuting might mean you are no longer tied to a single location, which could allow you to explore more flexible work opportunities within the company. Working from home may also motivate you to use your time more effectively and accomplish more for your company because you'll save time commuting.

Balancing work and family life could be easier when you work from home, as well. Time that you might spend traveling to work, appointments, and family obligations will be saved when you no longer have to schedule around a daily drive to and from the office. Depending on your company's flexibility and the demands of your job, working from home may even eliminate or reduce child-care needs for your children, giving you more time to spend with your loved ones in addition to saving you money.

It's possible that you could be healthier by working from home. Your exposure to co-workers who come to work with a cold or the flu is reduced, which prevents you from having to take a sick day to visit your doctor. You may also wind up feeling less stressed when you don't have to worry about commuting or potential work-life issues.

Disadvantages

Before you get too excited about the appeals of working from home, consider the drawbacks. For instance, telecommuting could affect your work performance. Isolation from the office may result in your professional achievements being overlooked, which could potentially delay a promotion or raise.

Less opportunity to interact regularly with co-workers might mean missing out on important information, as well as feeling lonely. Plus, distractions around your home can interfere with your daily responsibilities and could result in a negative response from your employer.

Another financial downside of working from home is the prospect of providing your own office materials. Does your company provide you with supplies such as a computer, printer, and fax machine? Will you need to pay for office setup, postage services, or scanners, among other items?

You might think that a home office tax deduction could alleviate the cost of home office expenses, but you'll need to be careful with your home office use in order to qualify. The space you claim a deduction for must be used for business-only purposes. Any use of this space not related to your work may prevent you from taking this tax break. For more information, review IRS Publication 587, Business Use of Your Home.

You'll also need to think about how your increased presence at home may result in an increase in your home utility usage. Specifically, you'll probably spend much of your time using energy-consuming technology to perform your job. In turn, this could cause your electric bill to spike. Practicing energy efficiency may help reduce the bill, but you still might have to pay more than you'd like each month as the cost of working from home.

What works for you?

If your employer allows you to work from home, think about a few other things besides how it would affect your wallet:

- Consider whether your home has appropriate space to accommodate a home office.
- Understand that you may need to seek remote tech support on occasion to perform your job.
- Think about whether you're self-directed and able to work well independently in a home setting.
- Set expectations for yourself.
- Be familiar with any company policies that may apply to remote employees.

It's possible that you can strike a balance and choose to work from home one or two days a week, thereby reaping more of the telecommuting positives than negatives. You could also ask to undergo a trial period to make sure that working from home is truly what works best for both you and your employer.

TIBBITTS

FINANCIAL CONSULTING

Tibbitts Financial Consulting
Steven Tibbitts, CFP®, CRC®
231 Hubbard Street
Allegan, MI 49010

TIBBITTS

FINANCIAL CONSULTING

What is the federal funds rate?

In December 2015, the Federal Open Market Committee (FOMC) raised the federal funds target rate to a range of 0.25% to 0.50%, the first shift from the rock-bottom 0% to 0.25% level where it had remained since December 2008.

The federal funds rate is the interest rate at which banks lend funds to each other from their deposits at the Federal Reserve, usually overnight, in order to meet reserve requirements. The Fed also raised a number of other rates related to funds moving between Federal Reserve banks and other banks. The Fed does not directly control consumer savings or credit rates, but the federal funds rate serves as a benchmark for many short-term rates, such as savings accounts, money market accounts, and short-term bonds.

The prime rate, which commercial banks charge their best customers, is typically about 3% above the federal funds rate. Other forms of business and consumer credit--such as small-business loans, adjustable-rate mortgages, auto loans, and credit cards--are often directly linked to the prime rate. Actual rates can vary widely. Fixed-rate home mortgages and other long-term loans are generally not linked directly to the prime rate, but may be indirectly affected by it

The FOMC expects economic conditions to "warrant only gradual increases" in the federal funds rate. Most Committee members projected a target range between 0.75% and 1.75% by the end of 2016, so you can probably expect a series of small increases this year. Although rising interest rates make it more expensive for consumers to borrow, higher rates could be good for retirees and savers who seek current income from bank accounts, CDs, bonds, and other fixed-interest investments.

The FDIC insures CDs and bank savings accounts, which generally provide a fixed rate of return, up to $250,000 per depositor, per insured institution. The principal value of bonds may fluctuate with market conditions. Bonds redeemed prior to maturity may be worth more or less than their original cost. Investments seeking to achieve higher yields also involve a higher degree of risk.

Source: *Federal Reserve, 2015*