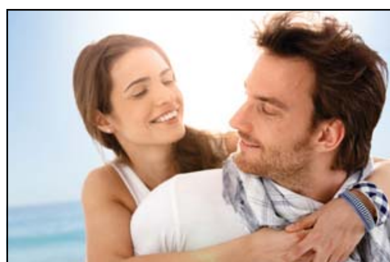
PARTNERS
WEALTH MANAGEMENT
Third Quarter 2017 (630) 778-8088/info@partnerswealth.com

When Should Millennials Start Retirement Saving?

This is a true story about Jane X, who graduated from a prestigious university five years ago. She's on her third job, but she's now communications director at a private foundation and finally earning decent money.

Jane's student loans are paid off, and her good salary leaves her some money to invest. However, like many of her millennial friends, she doesn't know a lot about investments or the differences between various retirement plans. But she is thinking about her future and wonders when she should start saving for retirement.



There's a short, simple answer: NOW.

The best time to begin saving for retirement is as soon as you can. Granted, relaxing on the deck of a retirement cottage overlooking the ninth green isn't first and foremost in the minds of most 20-somethings. But you can't ignore the sheer weight of the saving numbers. Let's go back to Jane, who's 27. If she manages to save $5,000 a year in a 401(k) for the next 40 years—until she's 67, the Social Security full retirement age for her generation—and she earns an average annual return of 7%, she will end up with $1,035,632. But if she waits 10 years to start saving, when she's 37, her accumulated savings will be just $490,027.

If you're convinced that now would be a good time to get started, consider these seven steps that could help you reach your goals:

1. Budget and save. It's difficult to be diligent about setting aside money for retirement when you're young and have a million things you'd rather do with your money. But if you're able to set objectives for saving and you do your best to stick to them, it could pay off beautifully down the road. Try to train yourself to live within your means while you move ahead in your career and your personal life.

2. Take advantage of employer retirement plans. Your company probably offers a tax-deferred retirement plan—a 401(k) or a 403(b)—and your employer may provide matching contributions (for example, up to 3% of your compensation) to go alongside the pre-tax earnings you put into the plan. With all of that money invested for the long haul, it can grow and compound and you won't be taxed on the growth until you pull out funds during retirement.

3. Don't forget about IRAs. Regardless of whether you participate in an employer-sponsored retirement plan, you also can set up an IRA. With a traditional IRA, the money you put in may be partly or wholly tax-deductible, if your salary is relatively low. But here, too, you'll be taxed on withdrawals during retirement. Another option, a Roth IRA, doesn't give you a tax deduction on money going in but may provide 100% tax-free

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Thank You

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For those of you recently joining our firm, allow us to illustrate how our commitment to service and a comprehensive wealth management process can clarify your long-term goals. We're here to help develop, articulate and implement plans while providing clients with the confidence needed to achieve them. Partners Wealth Management strives to bring order to our clients' finances and manage risk, while building and protecting their assets. To explore opportunities within your wealth management plan, contact our offices at (630) 778-8088 to schedule a review.

John

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One Last Shot At A Tax Exemption

Did your child graduate from college or graduate school this spring? If that's the case, this may be the last year you will be able to claim a dependency exemption for that son or daughter. But even then, you need to be careful to observe all of the tax rules covering such exemptions.

For starters, your dependency exemption for each qualifying child in 2017 is $4,050, the same as the personal exemption you and your spouse may claim. But you may lose some of the tax benefit of these exemptions under the personal exemption phase-out (PEP) rule. It kicks in at $261,500 of modified adjusted gross income (MAGI) for single filers and $313,800 of MAGI for joint filers.

To qualify for dependency exemptions, you must meet a two-part test. First, you have to provide more than half of your child's annual support for the year. Second, your dependent can't have earned more than the personal exemption amount in gross taxable income for the year. It's the second part of the test that often jeopardizes an exemption.

However, you may be in line for a special tax break. If your child is under age 19 or is a full-time student and under age 24, the second part of the test doesn't apply. That means you often still can claim a dependency exemption for a child in the year he or she graduates from college as long as you provide half of your son's or daughter's support.

Of course, if your kid is lucky enough to land a high-paying job right out of school, it may be a stretch to reach that half-support level. You might have to be extra-generous at the end of the year to secure the exemption one last time.

Consider this hypothetical example: Suppose your daughter graduates in May and starts working full-time in July. She earns $4,000 a month at her new job and contributes $800 of that amount to a 401(k). The retirement plan contribution doesn't count as support, but the other $3,200 a month does, and for six months that adds up to $19,200.

If you provided $1,500 in monthly support to your daughter while she was in school and after she graduated, you will have given her $18,000 for the year. But that's less than half of her total support.

To get over that hump and save your exemption for your daughter, you might give her a cash gift, say $2,000, around the holidays, maybe to help her buy a car. Now you're providing more than half of her support for the year — $20,000 ($18,000 + $2,000) compared with $19,200. The $2,000 gift allows you to claim a $4,050 exemption.

Of course, Congress could revise these tax rules, but it's unlikely that any changes involving dependency exemptions would be retroactive to the beginning of the year. Keep one eye on the progress of tax reform talks in Washington and the other eye on your child's support totals for the year. ●

Do Robo Advisors Have Glitches?

Robots already do serious work in manufacturing, construction, and an increasing number of other fields. And now, "robo advisors" are invading financial services. Within the next decade, these automated portfolio managers are expected to be handling trillions of dollars in assets.

But are robo advisors an upgrade over their human counterparts? The jury is still out on that question, so let's take a closer look.

How do robo advisors work? It's not like R2-D2 sets up a face-to-face meeting at his office and devises a financial plan for your future. Instead, you input critical data—including your age, risk tolerance, assets, and goals—into a software package, which then spits out an investment "asset allocation" based on an algorithm. So, the technology does all of the grunt work.

Typically, the allocation will rely heavily on exchange-traded funds (ETFs) holding a mix of domestic and international stocks and bonds. Although robo advisors vary, normally the algorithms that determine which ETFs to hold are based on modern portfolio theory or a version of it.

Although you may be attracted by the idea of a portfolio automatically tailored to your needs, robo advisors have certain shortcomings. For one thing, they haven't been sufficiently tested during a range of market conditions such as the sustained downturn that began in 2008-2009.

In addition, there's the fact that a faceless, mechanical robo advisor won't react in the same way as a human advisor. Who is responsible if your investments go south? You can't consult with the tech experts who provided the coding for the software (nor are they likely to know much about managing your investments). In some cases, there is an 800 number you can call, but the software still drives the final decisions.

Should You Fly Solo In Your Own 401(k) Plan?

Do you own and operate a small business? Although your equity in the company could help finance your retirement someday, it's also important to put money in a retirement account, just as you would if you worked for someone else. There are several kinds of tax-advantaged accounts for you to consider.

One plan that has been popular recently is the solo 401(k). In the past, high administrative fees often discouraged business owners from using these plans, but costs have come down. Plus, a solo 401(k) may offer distinct advantages.

The solo 401(k) also goes by various other names, including the solo-k, the uni-k, and the one-participant-k. It closely resembles a traditional 401(k) for larger businesses, but this one covers only a business owner with no employees (or just that person and his or her spouse). Solo 401(k)s generally have the same rules and requirements as other 401(k)s.

With a solo 401(k), a business owner wears two hats: one as employee and one as employer. Contributions can be made in both capacities.

1. As an employee, you can make elective deferrals equal to 100% of compensation (or "earned income" if you're self-employed), with an annual limit in 2017 of $18,000, or $24,000 if you're age 50 or older.

2. As an employer, you can contribute up to 25% of your compensation. (Special rules apply if you're self-employed.) For 2017, your total contributions—as employer and employee—to an account for you and your spouse can't exceed those specified limits and are capped at a maximum of $54,000.

To see how this might work, consider Ben, age 55, who earns $100,000 from his S corporation in 2017. As an employee, Ben chooses to defer the maximum $24,000 to his solo 401(k), and he adds an employer contribution of $25,000. That lets Ben make a total contribution of $49,000 for 2017. That's almost half his salary.

This unique one-two punch can enable a business owner to save a sizable amount for retirement even if contributions begin relatively late in life.

If a small business owner also is employed by a second company and participates in that company's 401(k) plan, the annual limit for that owner's deferrals is the total that goes to both plans. Thus, in our example above, Ben could defer a total of only $24,000 for the year, not $49,000.

What if you're self-employed? You'll have to make a special computation to figure the maximum amount of elective deferrals and nonelective contributions for yourself. When figuring the contributions, compensation is your "earned income," defined as net earnings from self-employment after deducting both:

- One-half of your self-employment tax and
- Contributions for yourself.

The IRS provides worksheets in Publication 560, Retirement Plans for Small Business, for figuring the allowable contribution rate and tax deduction for your 401(k) plan contributions.

But with a solo 401(k), you won't have to pass strict nondiscrimination testing requirements that can be the bane of existence for traditional 401(k) plans. A business owner with no other employees doesn't need to perform testing for the plan, because there are no other employees who could have received lesser benefits.

Finally, an owner with a solo 401(k) plan generally is required to file an annual report with the IRS if the plan has $250,000 or more in assets at the end of the year.

Of course, a solo 401(k) isn't the only tax-advantaged retirement plan option if you're self-employed or own a small business. Other types of plans—including the Simplified Employee Pension (SEP) and the Savings Incentive Match Plan for Employees (SIMPLE)—provide similar benefits within generous limits. But a solo 401(k) may offer extra flexibility by allowing both employee and employer contributions. ●

Furthermore, a robo advisor operates in a virtual vacuum. It doesn't have a complete financial picture or know you personally. If there's a call center for a particular robo advisor, you'll likely speak to a different person every time you call. In other words, the methodology behind these technological marvels won't take into account all of the factors influencing your life.

Finally, proponents of robo advisors claim that they are less expensive than human advisors, but that's not always the case. In any event, you may find that the services of a trusted personal advisor are well worth the cost in the long run. Despite the latest technological advancements, humans can still play a valuable role in guiding your investment decisions. ●

New Opportunity For Stand-Alone HRAs

The 21st Century Cures Act, signed into law in the waning days of the Obama administration, provides funding for cutting-edge medical research and other improvements in the health care system. But it also allows small businesses to offer stand-alone "health reimbursement arrangements" (HRAs) to their employees.

An HRA provides special accounts for health care expenses, much like health care flexible spending accounts (FSAs). Unlike FSAs, however, HRAs are funded solely by employer contributions, rather than by payroll deductions from employees. Contributions are exempt from taxes, as are distributions for qualifying health care expenses.

Funds in an HRA may be used for co-payments, deductibles, and co-insurance, as well as for regular doctor and hospital visits. Frequently, an employer will pair an HRA with a high-deductible health insurance plan.

The rules for HRAs were complicated by the 2010 Affordable Care Act (ACA), which soon might be changed substantially or repealed. Under the ACA, employers with 50 or more full-time or full-time equivalent employees (FTEs) must provide minimal essential health insurance to employees or face substantial penalties. Other ACA provisions involving limits and restrictions for "group health plans" effectively barred stand-alone HRAs for smaller businesses.

But now the Cures Act authorizes the use of stand-alone HRAs if five key requirements are met:

1. The plan is maintained by an "eligible employer" that has fewer than 50 employees. The employer can't offer another group health plan to any of its employees.

2. The plan is funded solely by employer contributions. Salary reductions aren't permitted.

3. The HRA is available to all eligible employees under the same basic terms. But certain workers may be excluded, including those with less than 90 days of service and part-time and seasonal employees. Also, reimbursements may vary in different geographic areas, within certain parameters.

4. The maximum annual contribution is $4,950 per year for an HRA covering only the employee and $10,000 for an HRA covering a worker's family. These amounts will be indexed for inflation.

5. The plan must provide payment or reimbursement for medical care expenses, including premiums for individual health insurance. Employees must provide documentation of services to receive payments.

The new law also coordinates these new rules for HRAs with other parts of the ACA. For instance, it prevents employees from claiming a tax credit for a health insurance premium in an exchange for any month in which they are provided HRAs with affordable coverage. Finally, the law specifies reporting and notification requirements for employers. ●

Millennials Retirement

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distributions in retirement.

4. Invest wisely. This is good advice not only for money in tax-advantaged retirement accounts but also for money you invest in taxable brokerage accounts. We can help you find the investment balance that best suits your personal needs, objectives, risk tolerance, and other circumstances. Although there's no foolproof method, you should have more leeway to be aggressive now than you would when you're nearing retirement or already retired. Of course, past performance is no guarantee of future results, but you can use historical stock market trends to help shape your investment strategies.

5. Expect the unexpected. Even the best-laid plans of retirement saving can be derailed by an emergency such as a hospital stay or the loss of a job. Try to leave enough wiggle room within your budget to account for some unforeseen financial trouble. Rather than put yourself in a position to have to skip or slash retirement plan contributions, remember to put aside cash in a "rainy day" fund. Most experts recommend building up enough to sustain you for at least half a year during which you may have no other income.

6. Avoid debt like the plague. One of the biggest impediments to retirement saving is a crushing debt load. You're not doing yourself any favor by deferring part of your salary to an employer plan at the same time that you're charging luxury items on a credit card with sky-high interest rates. That's not to say that borrowing isn't warranted at times—perhaps to help buy a home or car—but make sure it fits into your overall plan.

7. Educate yourself. Finally, you can improve the chances for a secure, comfortable retirement by learning all of the rules of the road, including the nuances of investments and the tax differences between various accounts. Knowledge is your friend. Rely on us to give you a solid foundation for going forward. ●

Partners Wealth Management | 1700 Park Street, Suite 200, Naperville, IL 60563 | 630-778-8088 | Fax: 630-778-8049 | www.partnerswealth.com | info@www.partnerswealth.com

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