



Financial Insight Quarterly

Your Source for Financial Well-Being

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April 16, 2019 was an important day for many of us. But do you know why? It was Tax Freedom Day — the day when the average American theoretically earned enough to pay his or her tax obligations for the

year. According to the Tax Foundation, Americans will pay \$3.4 trillion in federal taxes in 2019, more than they spend on food, clothing, and housing combined.* But it wasn't always this way. In fact, income taxes are a fairly new development in the overall history of America. So how did we get to this point?

In the beginning...

The United States was founded, in part, on the premise that colonists didn't want to pay taxes without representation, which led to the famous tossing of tea into the Boston Harbor and the American Revolution. However, not long after the colonies gained their freedom from England, Congress passed the Stamp Act of 1797, which essentially was our nation's first estate tax. Otherwise, from the early 1790s to 1802, the U.S. government was supported by taxes on such items as spirits (alcohol, not the ghostly kind), sugar, tobacco, and corporate bonds.

Wars played a big part in the history of taxation in this country. To fund the War of 1812, Congress taxed sales of gold, silverware, jewelry, and watches. In 1817, tariffs on imported goods provided the main source of revenue to run the government.

With the onset of the Civil War, Congress enacted the nation's first income tax law, the Revenue Act of 1861, which included a flat tax of 3% on annual incomes exceeding \$800 to help pay for the costs of the war. That tax law was repealed and replaced by the Revenue Act of 1862, which established the Office of the Commissioner of Internal Revenue (forerunner to the Internal Revenue Service), levied excise taxes on most goods and services, and replaced the flat tax with a progressive tax.

The 16th Amendment

However, it was not until 1913 with the adoption of the 16th Amendment to the Constitution, that the income tax became a permanent fixture in the American tax system. Congress now had the authority to tax income of both individuals and corporations. It didn't take the IRS long to start inundating us with forms, beginning in 1914 with the introduction of the first income tax form, the dreaded Form 1040. Enactment of the Revenue Act of 1916 introduced tax rates and income scales.

Tax rates

Here's a sobering fact: In 1913, the top federal income tax bracket was 7% on all income over \$500,000, and the lowest tax bracket was 1%. During the Great Depression, Congress raised the highest tax bracket to 63%. Wars can be expensive, as evidenced by the jump in the highest tax rate to 94% during World War II. In 2018, the highest income tax rate was lowered to 37%.

Trying to get it right

Over the years, there have been frequent attempts to reform the tax law in some manner. We've seen the adoption of the alternative minimum tax, Social Security tax, taxes on cigarettes and alcohol, gasoline taxes, aviation taxes, property taxes, telecommunication taxes, not to mention state and local taxes. To quote Will Rogers, "The difference between death and taxes is death doesn't get worse every time Congress meets."

Tax laws are always changing and will likely remain a political hot potato. Only time will tell what changes are ahead, but there is no doubt that through taxation, what the government giveth, it inevitably taketh back again.

**Tax Freedom Day 2019 was April 16, as calculated by the Tax Foundation, taxfoundation.org.*

4th Quarter 2019

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- What are continuing care retirement communities?
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Ten Year-End Tax Tips for 2019



Timing of itemized deductions and the increased standard deduction

Recent tax law changes substantially increased the standard deduction amounts and made significant changes to itemized deductions. It may now be especially useful to bunch itemized deductions in certain years; for example, when they would exceed the standard deduction.

IRA and retirement plan contributions

For 2019, you can contribute up to \$19,000 to a 401(k) plan (\$25,000 if you're age 50 or older) and up to \$6,000 to traditional and Roth IRAs combined (\$7,000 if you're age 50 or older). The window to make 2019 contributions to an employer plan generally closes at the end of the year, while you typically have until the due date of your federal income tax return (not including extensions) to make 2019 IRA contributions.

Here are 10 things to consider as you weigh potential tax moves between now and the end of the year.

1. Set aside time to plan

Effective planning requires that you have a good understanding of your current tax situation, as well as a reasonable estimate of how your circumstances might change next year. There's a real opportunity for tax savings if you'll be paying taxes at a lower rate in one year than in the other. However, the window for most tax-saving moves closes on December 31, so don't procrastinate.

2. Defer income to next year

Consider opportunities to defer income to 2020, particularly if you think you may be in a lower tax bracket then. For example, you may be able to defer a year-end bonus or delay the collection of business debts, rents, and payments for services. Doing so may enable you to postpone payment of tax on the income until next year.

3. Accelerate deductions

You might also look for opportunities to accelerate deductions into the current tax year. If you itemize deductions, making payments for deductible expenses such as medical expenses, qualifying interest, and state taxes before the end of the year (instead of paying them in early 2020) could make a difference on your 2019 return.

4. Factor in the AMT

If you're subject to the alternative minimum tax (AMT), traditional year-end maneuvers such as deferring income and accelerating deductions can have a negative effect. Essentially a separate federal income tax system with its own rates and rules, the AMT effectively disallows a number of itemized deductions. For example, if you're subject to the AMT in 2019, prepaying 2020 state and local taxes probably won't help your 2019 tax situation, but could hurt your 2020 bottom line. Taking the time to determine whether you may be subject to the AMT before you make any year-end moves could help you avoid a costly mistake.

5. Bump up withholding to cover a tax shortfall

If it looks as though you're going to owe federal income tax for the year, especially if you think you may be subject to an estimated tax penalty, consider asking your employer (on Form W-4) to increase your withholding for the remainder of the year to cover the shortfall. The biggest advantage in doing so is that withholding is

considered as having been paid evenly throughout the year instead of when the dollars are actually taken from your paycheck. This strategy can also be used to make up for low or missing quarterly estimated tax payments. With all the recent tax changes, it may be especially important to review your withholding in 2019.

6. Maximize retirement savings

Deductible contributions to a traditional IRA and pre-tax contributions to an employer-sponsored retirement plan such as a 401(k) can reduce your 2019 taxable income. If you haven't already contributed up to the maximum amount allowed, consider doing so by year-end.

7. Take any required distributions

Once you reach age 70½, you generally must start taking required minimum distributions (RMDs) from traditional IRAs and employer-sponsored retirement plans (an exception may apply if you're still working for the employer sponsoring the plan). Take any distributions by the date required — the end of the year for most individuals. The penalty for failing to do so is substantial: 50% of any amount that you failed to distribute as required.

8. Weigh year-end investment moves

You shouldn't let tax considerations drive your investment decisions. However, it's worth considering the tax implications of any year-end investment moves that you make. For example, if you have realized net capital gains from selling securities at a profit, you might avoid being taxed on some or all of those gains by selling losing positions. Any losses over and above the amount of your gains can be used to offset up to \$3,000 of ordinary income (\$1,500 if your filing status is married filing separately) or carried forward to reduce your taxes in future years.

9. Beware the net investment income tax

Don't forget to account for the 3.8% net investment income tax. This additional tax may apply to some or all of your net investment income if your modified adjusted gross income (AGI) exceeds \$200,000 (\$250,000 if married filing jointly, \$125,000 if married filing separately, \$200,000 if head of household).

10. Get help if you need it

There's a lot to think about when it comes to tax planning. That's why it often makes sense to talk to a tax professional who is able to evaluate your situation and help you determine if any year-end moves make sense for you.



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Key Estate Planning Documents

Estate planning is the process of managing and preserving your assets while you are alive, and conserving and controlling their distribution after your death. There are four key estate planning documents almost everyone should have regardless of age, health, or wealth. They are: a durable power of attorney, advance medical directives, a will, and a letter of instruction.

Durable power of attorney

Incapacity can happen to anyone at any time, but your risk generally increases as you grow older. You have to consider what would happen if, for example, you were unable to make decisions or conduct your own affairs. Failing to plan may mean a court would have to appoint a guardian, and the guardian might make decisions that would be different from what you would have wanted.

A durable power of attorney (DPOA) enables you to authorize a family member or other trusted individual to make financial decisions or transact business on your behalf, even if you become incapacitated. The designated individual can do things like pay everyday expenses, collect benefits, watch over your investments, and file taxes.

There are two types of DPOAs: (1) an immediate DPOA, which is effective at once (this may be appropriate, for example, if you face a serious operation or illness), and (2) a springing DPOA, which is not effective unless you become incapacitated.

Advance medical directives

Advance medical directives let others know what forms of medical treatment you prefer and enable you to designate someone to make medical decisions for you in the event you can't express your own wishes. If you don't have an advance medical directive, health-care providers could use unwanted treatments and procedures to prolong your life at any cost.

There are three types of advance medical directives. Each state allows only a certain type (or types). You may find that one, two, or all three types are necessary to carry out all of your wishes for medical treatment.

- A living will is a document that specifies the types of medical treatment you would want, or not want, under particular circumstances. In most states, a living will takes effect only under certain circumstances, such as a terminal illness or injury. Generally, one can be used only to decline medical treatment

that "serves only to postpone the moment of death."

- A health-care proxy lets one or more family members or other trusted individuals make medical decisions for you. You decide how much power your representative will or won't have.
- A do-not-resuscitate (DNR) order is a legal form, signed by both you and your doctor, that gives health-care professionals permission to carry out your wishes.

Will

A will is quite often the cornerstone of an estate plan. It is a formal, legal document that directs how your property is to be distributed when you die. If you don't leave a will, disbursements will be made according to state law, which might not be what you would want.

There are a couple of other important purposes for a will. It allows you to name an executor to carry out your wishes, as specified in the will, and a guardian for your minor children.

The will should be written, signed by you, and witnessed.

Most wills have to be probated. The will is filed with the probate court. The executor collects assets, pays debts and taxes owed, and distributes any remaining property to the rightful heirs. The rules vary from state to state, but in some states smaller estates are exempt from probate or qualify for an expedited process.

Letter of instruction

A letter of instruction is an informal, nonlegal document that generally accompanies your will and is used to express your personal thoughts and directions regarding what is in the will (or about other things, such as your burial wishes or where to locate other documents). This can be the most helpful document you leave for your family members and your executor.

Unlike your will, a letter of instruction remains private. Therefore, it is an opportunity to say the things you would rather not make public.

A letter of instruction is not a substitute for a will. Any directions you include in the letter are only suggestions and are not binding. The people to whom you address the letter may follow or disregard any instructions.

Take steps now

Life is unpredictable. So take steps now, while you can, to have the proper documents in place to ensure that your wishes are carried out.

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What are continuing care retirement communities?

Continuing care retirement communities (CCRCs) are living arrangements that combine independent living, assisted living, and nursing home care on a single campus. CCRCs offer residents a continuum of care throughout their lives.

Typically, you enter a CCRC as a resident of an independent housing unit, which may be a condominium, apartment, or single-family home. When you need more care or are unable to live independently, you can move to the assisted living facility on campus. Should you need the next level of care, you can move into the on-site nursing home.

While specific services and benefits may differ, communities generally offer dining facilities, transportation, lawn care, housekeeping, social activities, laundry, emergency call monitoring, and security. As needs arise, additional services may include preparation of meals, health services such as medical care, and personal care such as assistance with toileting, bathing, and personal hygiene.

The fee arrangements for CCRCs vary and generally include both a monthly fee and an

entrance fee. These fees can be quite substantial depending on the location of the community, the services offered and chosen, and the living arrangements desired. The entry fee may be fully or partially refundable, and monthly fees may increase over time. Medicare and/or health insurance may pay for some of the services provided.

There are three basic types of residential arrangements for CCRCs:

- **Life care or extended contract.** This option offers unlimited assisted living, medical treatment, and skilled nursing care. This alternative is often the priciest because there are typically no additional fees or charges.
- **Modified contract.** This contract is similar to the life care option, except that only certain defined services are included for a predetermined price and/or for a specified length of time. Extra charges will apply if you need additional services or are able to extend the contract's time frame.
- **Fee-for-service contract.** While the initial enrollment fee may be lower, assisted-living and skilled-care services are paid for at their market rates.



Do independent living communities differ from CCRCs?

Independent living communities, also known as rental retirement communities, offer housing options for active seniors and retirees who require little or no assistance with daily activities. Most independent living residents desire an environment where they don't have to be concerned about safety, maintenance, and homeownership responsibilities.

One of the major offshoots of the burgeoning number of baby boomers retiring every day is the growing retirement living industry. More and more communities dedicated to senior living are opening each year. Two popular options are continuing care retirement communities (CCRCs) and independent living communities. While there are similarities between the two, there are important differences as well.

Both CCRCs and independent living communities may offer amenities such as a clubhouse, lounge, dining rooms, fitness centers, swimming pools, housekeeping services, and transportation. CCRCs usually offer a higher level of amenities and services than independent living communities.

The main difference between CCRCs and

independent living communities is the extent of health-related, or continuing care, services offered by CCRCs, which include assisted living services, memory care, and long-term care. Independent living communities typically do not offer continuing care services. Instead, the resident may arrange for such services through an outside agency. Generally, independent living communities do not offer assisted living services or long-term care.

Another difference between CCRCs and independent living communities relates to the costs. Most CCRCs require a substantial entry fee plus a monthly fee. Typically, independent living communities charge a monthly fee, similar to rent. Independent living fees are usually not covered by any type of insurance, including Medicare and long-term care insurance. However, health-related services and care that a resident receives (which are not offered by the independent resident community) may be covered by insurance or Medicare.

Determining which type of community is the best choice depends on a number of factors including the services needed or desired and the costs associated with each type of residential community.