REFLECTIONS

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WINDGATE
WEALTH MANAGEMENT

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SUPERCHARGE YOUR ROTH IRA

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Financial Planner

Don't let Roth IRA income limits prevent you from gaining tax-free growth

"It's the best motivation to save for retirement that we've seen in America. Everybody should be in the Roth game if they can."
-IRA expert and financial-industry speaker, Ed Slott.

The Roth IRA is perhaps the most attractive retirement savings vehicle for investors. Unlike traditional IRAs which provide tax-deferred growth (you pay the tax eventually), Roth IRA assets grow tax-free. Assets with this favorable tax characteristic can provide desirable flexibility in retirement years, where the future state of tax rates is very uncertain. The Roth IRA protects you from paying future income taxes, and this protection also continues for your heirs.

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If you have any questions or comments, or if you know of any friends or family that might benefit from our services, please give us a call at 844.377.4963

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High-income earners can sidestep the Roth income limitations by contributing to an IRA and then converting it to a Roth.

While everyone should get in the Roth game, as Mr. Slott proposes, for high-income earners it hasn't always been so easy. Roth IRA contributions are not allowed once a married couple has an AGI over $196K (or $133K for an individual). IRA conversions – changing an account from an IRA into a Roth IRA – were not possible for high-income earners until recent changes in the tax law removed income limitations. Here, the "backdoor IRA" strategy was born.

Backdoor IRA: How it Works

The Backdoor Roth IRA strategy allows those who earn more than the Roth limitations contribute to a Roth IRA anyway, with one small workaround. While contributing to a Roth IRA is prohibited for high-income earners, anyone can make contributions to a Traditional IRA. In addition, anyone who has funds in an IRA can "convert" the assets into a Roth IRA. Put together, high-income earners can sidestep the Roth income limitations by contributing to an IRA and then converting it to a Roth. IRA limits are currently $5,500 ($6,500 for those aged 50 and over), and the strategy can be repeated every year.

The main obstacle to making a “backdoor” Roth contribution is the *pro-rata* rule, which can limit the effectiveness of the strategy. The pro-rata rule forces all IRAs to be counted as one account, so a $5,500 Roth conversion will be considered as a partial conversion of all existing IRA assets, not as a standalone transaction. The downside here is the tax benefits are issued on a pro-rata basis, meaning if $5,500 represents 5% of all your combined IRAs, only 5% of the $5,500 can be converted tax-free into a Roth (the remainder will be considered a taxable distribution – not the desired outcome). Note the rule only aggregates IRA accounts, so 401(k)'s, spouse's accounts, or other Roth accounts are not counted (SIMPLE and SEP IRA assets are included).

Roth Supercharge Strategy: Unlock Extra Savings From Your 401(k)

Investors can save $5,500 per year in a Roth via the backdoor strategy; this a good start, but high-income earners may want to do more. If your 401(k) allows for both after-tax contributions and in-service distributions, you can quickly accumulate significant Roth IRA assets by using this supercharged strategy.

Many people are familiar with the $18,000 limit for 401(k) contributions ($24,000 for those over 50). But there is a lesser-known overall limit of $53,000; this includes employee contributions, employer match and profit sharing. If a 401(k) plan allows for after-tax contributions, an employee can make additional contributions above and beyond the standard $18,000 limit. Here's an example of how it works:

William is age 49 and maxing out his 401(k) salary deferrals	**$18,000**
The company matches at 50%	**$ 9,000**
Amount under overall $53K limit William can contribute “after-tax”	**$26,000**

If the 401(k) also allows for “in-service distributions,” William can then rollover the $26,000 after-tax 401(k) contribution into his Roth IRA, regardless of his income level. Combined with the $5,500 backdoor Roth strategy, William can now put away $31,500 into a Roth IRA every year!

Not everyone will have this opportunity as it depends largely on your 401(k) plan’s flexibility and design. But for those eligible, it can be an outstanding way to accumulate assets into a Roth IRA. Ask your 401(k) administrator if your plan allows for: 1.) after tax contributions and 2.) in-service withdrawals. If so, call or email and we can discuss how a supercharged Roth IRA strategy can advance your retirement planning.

If your 401(k) allows for both after-tax contributions and in-service distributions, you can quickly accumulate significant Roth IRA assets by using this supercharged strategy.

GRADUATION GIFTS FOR LIFE LESSONS

Graduation season is underway, and that means proud parents across the country are ready to celebrate their sons and daughters. Sure, you could give the graduate in your life another Target gift card stuffed inside a generic card. Or you could aim higher by trying to slip in a life lesson along with that tangible reward. Instead of cash, consider a way to give them a reward that also introduces financial or cultural literacy.

Read below for the best graduation gifts for your child or graduate you know that could empower them for the rest of their lives.

Starting a Roth IRA

A college graduate saddled with student loans or a low salary might not think about starting their own retirement account, no matter how much you talk about compound interest. So you can start an account for them. Gifting a Roth IRA to a child, is an outstanding way to introduce them to the concept of savings and investment.

Let them know you're starting an account, as it will only be possible to create an account together with their signature. However, most brokerage firms allow you to send in checks and deposit money into someone else's IRA – motivation enough for them to sign the application. You can only contribute what they have earned in a year, up to the limit of $5,500.

Assuming your graduate learns to properly care for their Roth IRA and does not make unqualified withdrawals, over time these accounts can become significant assets. After all, the law of compound interest demonstrates the simple fact that the benefit of when you start saving outweighs how much you save. Hopefully they can become devoted to the idea of letting their savings work for them during their earliest working years.

Gift Appreciated Stock

Instead of a standard cash gift, you can reward your child while helping yourself with a lower tax bill if you give your child stock that has appreciated. Otherwise, you'll eventually have to pay long-term capital gains tax (15% to 23.9%, depending on your income) on any amount your investments have appreciated. Gifting appreciated stock is a better alternative than giving cash because it removes this future tax burden from your portfolio.

Gifting a Roth IRA to a child, is an outstanding way to introduce them to the concept of savings and investment.

When you give appreciated stock to your child and they sell the security, capital gains tax is paid at their rate – which is likely lower than yours. Children who are working and not dependent on their parents will even pay zero tax if their income is below $37K. If you gift to a child who is still dependent on you, any portion of the gift over $2,100 will be taxed at your rate (this is also known as the kiddie tax). Your child can also choose to keep the stock if they don't need the cash or only sell partial shares, a great way to introduce them to having an investment account of their own.

Professional Resume

Parents want the best for their children - a good job with a high salary and great benefits. Unless they have strong connections, they usually can't influence if their children get hired. But they can give them a great resume.

Gift them a professional resume when they graduate college, so they have the best chance at landing a job and moving out of your basement.

You can hire someone through Fiverr or purchase a creative template through Etsy. Make sure your student has the requisite software needed to update the resume themselves, so they won't have to hire someone every time they get a new gig.

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Cook Book

It's a typical scenario: broke college student lives on Ramen because they don't know how to cook. If this describes your child, don't despair. Every great cook had to start from somewhere. Here are the best cookbooks for novice chefs:

- Leanne Brown's "Good and Cheap" was designed for those living on food stamps, but is perfect for the recent grad who wants to eat cheap and healthy.
- Mark Bittman's "How to Cook Everything: The Basics" is a how-to encyclopedia that will show the best way to cook everything from vegetables to seafood.
- Alton Brown's "I'm Just Here for the Food" is a masterpiece from a chef who explains why certain flavors work well together and how beginner chefs can develop their own recipes.

Happy Graduation to the Class of 2017!

MAXIMIZE YOUR TAX SAVINGS - DEDUCT OUR COSTS

April 15th is behind us, and depending on the size of your bill, it may have been a good reminder that you should maximize all available tax deductions. Fortunately, the IRS does allow a tax deduction for certain investment related expenses, including our management costs. Each year we provide a summary of our costs reported on your custodian 1099 tax form. What may be lesser known is that you can also deduct costs from your IRAs, provided it is planned for correctly. Read on to make sure you are taking full advantage of the investment advisory cost tax deduction.

What may be lesser known is that you can also deduct costs from your IRAs, provided it is planned for correctly.

How It Works

Any expenses associated with investment and financial management during the taxable year qualify for tax deductions. However, costs are claimed as a miscellaneous itemized deduction, which means the deduction is subject to a 2% AGI floor (AGI is your income after "above the line" deductions, such as 401(k) contributions). Only costs that you pay which are over and above 2% of your AGI can qualify for a deduction. For example, if you have an AGI of $100,000, only investment costs above $2,000 can be deducted. There is also an AMT (Alternative Minimum Tax) adjustment for investment costs, so AMT taxpayers will not be able to claim the deduction.

What About IRA Costs?

While the deduction for investment costs is rather straightforward – they are reported on your 1099 and almost surely picked up by your accountant each year – the matter is more complicated for IRAs. According to the IRS, for costs to be deductible they have to be related to the production of income. Because IRAs are tax-deferred and do not create ongoing income, investment costs directly paid from assets in an IRA cannot be deducted on your tax return. The IRS leaves room for one big and important caveat however: Investment advisory costs for IRAs can be paid with outside taxable dollars and still be deducted as a miscellaneous expense. So, if you take all IRA costs and simply pay them from assets held in a non-IRA account, you can still get the deduction.

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What Can I Do?

We can easily arrange for you to pay any IRA investment costs from your taxable accounts. For the strategy to make sense, ensure that your fee will be deductible in the first place. Again, costs will only be deductible if they add up to over 2% of your AGI. You will also want to verify with your accountant that you are not exposed to the AMT. In summary:

1. Make sure you are deducting any investment costs for non-IRA accounts above and beyond 2% of your AGI every year.

2. Determine if IRA costs would be deductible. If so, consider paying all IRA costs using funds in taxable accounts.

3. Consider using "outside" funds to pay for investment costs on Roth IRAs. It's better to pay with after-tax dollars than using the future-tax-free-growth dollars inside the Roth itself.

If you wish to start a conversation with us and your tax advisor about changing the way your investment costs might be deducted, give us a call 844-377-4963.

WINDGATE SUPPORTS LITTLE ANGELS

Windgate Wealth Management is proud to continue our support of the Little Angels Pledge Run. This year marked the 30th annual bike run, and we celebrated by becoming a Diamond sponsor.

On May 21, 2017, former Chicago Bear Roland Harper led the way for 575 motorcycles and 750 riders on an 87 mile excursion to support the Little Angels, a loving home for children and young adults with severe disabilities and complex medical needs. Over 150 volunteers ensured yet another hugely successful event.

Final numbers are coming, but the organization estimates over $100,000 in proceeds from this year's event. The annual bike run has raised over $4.3 million in its 30 year history. Windgate Wealth Management topped the list of fourteen corporate sponsors this year. Hundreds of private donors and raffle ticket buyers contributed the rest.

Marklund Wasmund Center at Little Angels, a residential facility, opened its doors in 1958. Located in Elgin, Illinois, the home provides children and young adults with complex medical and developmental needs a lifetime of loving care and professional support in a place that feels like home. It is a state-of-the-art facility offering round-the-clock skilled nursing, therapeutic, and habilitation services in a warm, caring environment. In addition to the loving medical and personal care the staff provides, educational and developmental programs also help residents progress and live fulfilling lives. In 2016, Little Angels merged with Marklund to capitalize on synergies and efficiencies that will help ensure the best care possible into the future.

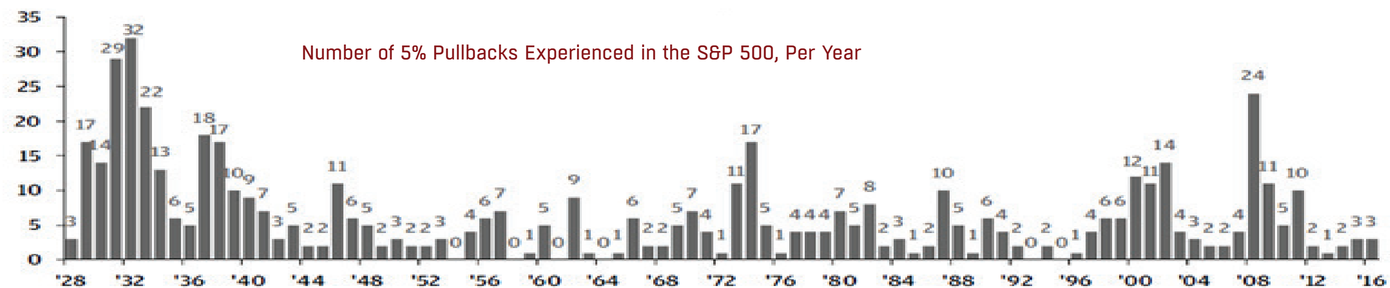
We at Windgate Wealth Management are proud to support wonderful organizations like Little Angels in our community. For more information on this facility or to contribute to the efforts, please contact Little Angels through their website, www.marklund.org or by phone at (630) 593-5464.

VOLATILITY IS NORMAL - Pullbacks happen very frequently, even in normal times

It seems like investors and headlines both have one question on their minds lately... Trump? Of course, we have no idea if events in Washington grow into future scandal or are washed away into the never-ending news cycle. However, what we do know is that market volatility had been at a record low until recently. As of this writing, investors do appear to be getting nervous, but the S&P 500 has yet to experience a single 5% pullback in 2017.

Forget politics for a moment and remember that volatility in the market is normal. The table below shows that pullbacks of 5% or more occur about once every three months. Pullbacks of 10% are likely to occur once per year, while large declines greater than 20% typically occur just once per market cycle. Confident investors realize that volatility is just the nature of the market. Investors need to determine the cause of the volatility before reacting to it.

It is our belief that presidents and governments only have limited influence on the long-term prospects of the economy and stock prices. Ultimately, investments are driven by earnings and economic growth, both of which continue to be strong. While it's possible, even likely, that political events will cause significant short-term market swings throughout this summer, remember that volatility is a normal part of investing.



Source: Standard & Poor's, FactSet, J. P. Morgan Asset Management. For illustrative purposes only. Returns are based on price index only and do not include dividends. Data are as of December 31, 2016.

QUOTES ON MONEY, WORK AND HUMOR

Money can buy happiness, but words are free. Here are a few of our favorite quotes and comics regarding money, work and humor.

- "'Price is what you pay; value is what you get.' Whether we're talking about socks or stocks, I like buying quality merchandise when marked down." - Warren Buffett
- "I'd like to live as a poor man with lots of money." - Pablo Picasso
- "People often say that motivation doesn't last. Well, neither does bathing – that's why we recommend it daily." – Zig Ziglar
- "Wealth is not his that has it, but his that enjoys it." - Benjamin Franklin
- "Dogs have no money. Isn't that amazing? They're broke their entire lives. But they get through. You know why dogs have no money? … No Pockets." - Jerry Seinfeld

"And now I'll set my retirement savings to simmer for 15-20 years."

"Budget: a mathematical confirmation of your suspicions." - A. A. Latimer

"All I ask is the chance to prove that money can't make me happy."- Spike Milligan

"I'm tired of hearing about money, money, money, money, money. I just want to play the game, drink Pepsi, wear Reebok." - Shaquille O'Neal

"I put a dollar in one of those change machines. Nothing changed." - George Carlin

"It would be so easy to flip this house."

Any opinions expressed in this article are general in nature and cannot be guaranteed to be suitable for every individual. Individual needs and situations vary. Talk to your financial advisor to help you consider what options might be right for you.

The information provided herein represents the opinion of Windgate Wealth Management and is not intended to be a forecast of future events, a guarantee of future results, nor investment advice. The information is neither a recommendation to buy or sell a security or invest in a specific sector. Past performance is not indicative of future results.

Perritt Capital Management, Inc. is the registered investment advisor for Windgate Wealth Management accounts.

CELEBRATING 25 YEARS

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