IN THIS ISSUE

**Retirement planning**

Maximize your Social Security benefits

**Estate planning**

Estate planning when interest rates are low

**Tax currents**

Whistleblower limits

IRA exception not allowed

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# Trust Topics

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## Maximize your Social Security benefits

To have a successful, financially secure retirement, one must have enough income to live on. The larger one's Social Security benefit is, the easier it is to meet that need. So it's something of a puzzle that so many individuals are deciding to take their benefits early. A study last year from the Government Accountability Office (GAO) reported that 72.8% of retirees begin their benefits before reaching normal (or full) retirement age.

Early benefits are lower benefits. The table below shows just how much benefits will be reduced, based upon the year of one's birth. Note that the spousal benefit also will be reduced, creating the potential of financial insecurity for the widow or widower.

For those born in 1954, retirement with full benefits may begin next year, at age 66. The table shows the full retirement age for those born in later years. Retiring at age 62 triggers a 25% cut in benefits. Looked at another way, one can boost one's Social Security benefit by fully one-third by waiting until age 66 to begin drawing it. What's more, if one continues working from age 62 to age 66, the additional earnings record and Social Security taxes paid also will increase the eventual benefit. That larger benefit will be the basis for future inflation adjustments and so can translate into substantially higher lifetime income.

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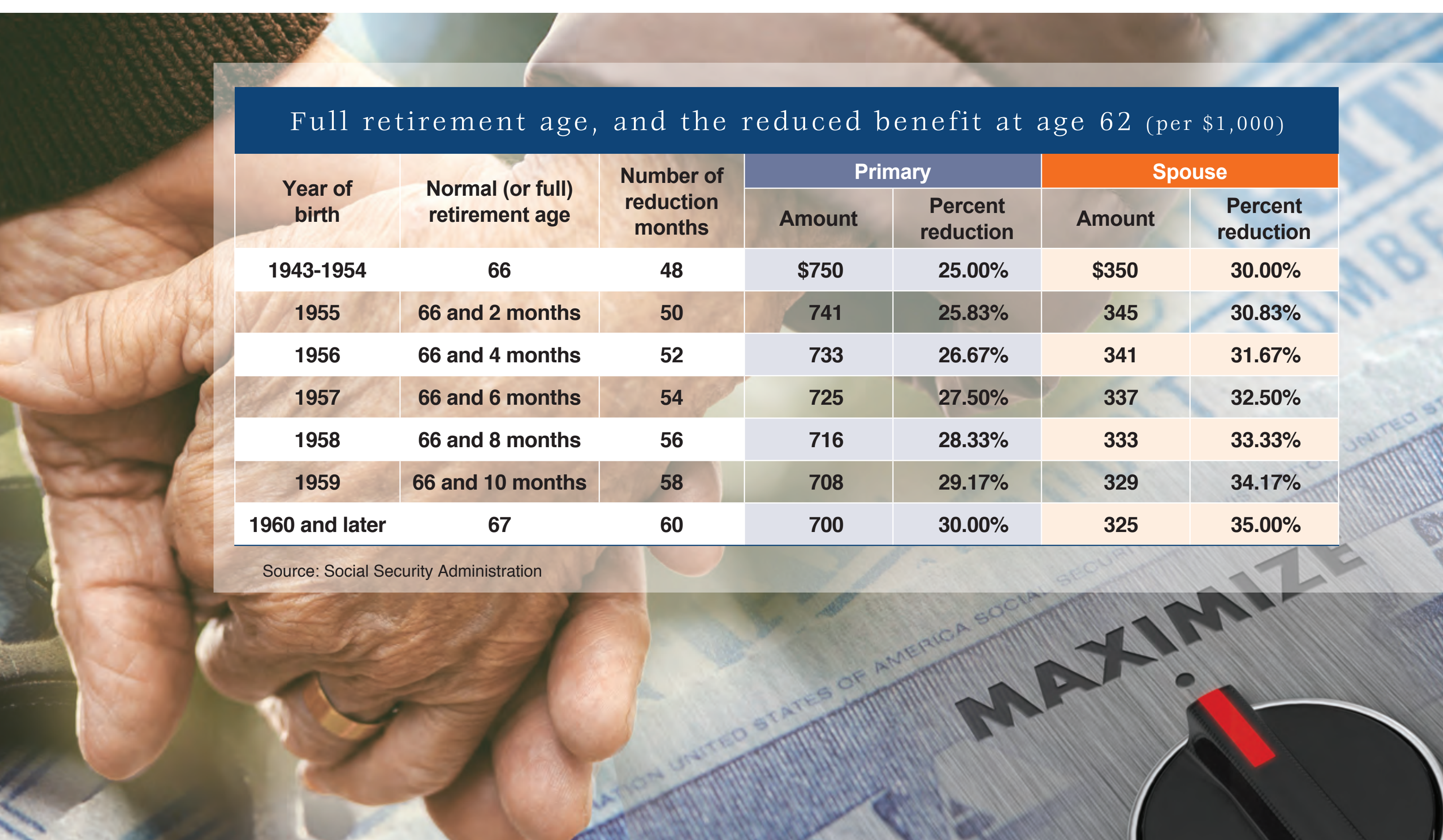

**Full retirement age, and the reduced benefit at age 62** (per $1,000)

| Year of birth | Normal (or full) retirement age | Number of reduction months | Primary | | Spouse | |
|---|---|---|---|---|---|---|
| | | | Amount | Percent reduction | Amount | Percent reduction |
| 1943-1954 | 66 | 48 | $750 | 25.00% | $350 | 30.00% |
| 1955 | 66 and 2 months | 50 | 741 | 25.83% | 345 | 30.83% |
| 1956 | 66 and 4 months | 52 | 733 | 26.67% | 341 | 31.67% |
| 1957 | 66 and 6 months | 54 | 725 | 27.50% | 337 | 32.50% |
| 1958 | 66 and 8 months | 56 | 716 | 28.33% | 333 | 33.33% |
| 1959 | 66 and 10 months | 58 | 708 | 29.17% | 329 | 34.17% |
| 1960 and later | 67 | 60 | 700 | 30.00% | 325 | 35.00% |

Source: Social Security Administration

Still, the thought process of someone who is 62 might go something like this: If I don't take my early benefits, how much am I leaving on the table? How many years of collecting "full" benefits will it take to offset the four years of taking no benefits at all? The answer is 12 years, if full retirement age is 66. One needs to live to age 78 to "break even" on the decision to wait for the full retirement age. At age 62, that's pretty far off on the horizon. Perhaps the early retirees are not being so irrational after all.

What about the additional credit for delaying retirement to age 70? Each month of delay past full retirement age boosts the benefit by 2/3 of 1%, or 8% per year.

### Another perspective

Some people are under the impression that Social Security is not a good investment. Not true. Imagine that Don's annual benefit at normal retirement age would be $16,000 per year, and he chooses to begin an early benefit of $12,000 per year at age 62. When he reaches age 66, Don realizes that he really will need $16,000 per year after all. To achieve that, he buys a single-life annuity of $4,000 per year. Could he buy that with the $48,000 in early benefits he's collected? No, he could not, not even close. According to a recent study, the commercial cost of an inflation-adjusted single-life $4,000 annuity for a male would be $71,000 (higher for females, who have long life expectancies).

As a group, retirees are living longer and longer. Most people will live to "break even" on a decision to delay their retirement. *Money* magazine also reported that life expectancy for 65-year-old men is 84, and for women it's 86.5. For a retired couple, there's a 50% chance that one partner will be alive at age 92!

### Planning for couples

When a husband and wife each have earnings records, the choices are more complicated, and more important to understand. Each partner has a basic benefit plus a spousal benefit, but may only collect the larger benefit. They don't have to claim at the same time. For example, one spouse might begin benefits early, while the other waits until age 66 or later to begin.

Another factor to be considered is that a divorced spouse whose marriage lasted at least ten years and who is currently not married may apply for spousal benefits. If the ex-spouse is collecting benefits, the spousal benefit is available at age 62. If both parties are 62 or older and the divorce occurred at least two years ago, spousal benefits may be available whether or not the primary earner has begun to claim them.

### How we can help you

We've worked with a broad spectrum of business owners, executives, and professionals to solve the problems—and maximize the opportunities—associated with stepping onto the retirement road. Our experience is yours to draw on. Whether you're retiring early, retiring late, or regrouping to start a new career, we stand ready to propose realistic strategies, geared to your personal requirements.

To learn more, make an appointment with one of our asset-management specialists. ☐

## Popular baby names

The Social Security Administration has compiled the frequency of baby names going back to 1919, based upon applications for Social Security cards. In 2018 the five most popular names for girls were Emma, Olivia, Ava, Isabella, and Sophia. For boys, the top five were Liam, Noah, William, James, and Oliver.

Name popularity varies considerably over time, and the variability is greater for girls than boys. The table here shows the all-time top ten names for 1919-2018.

On the Social Security Administration's Web site, one may search for the most popular names by state, by year, by decades, and more.

| Rank | Name | Number | Name | Number |
|---|---|---|---|---|
| 1 | James | 4,764,644 | Mary | 3,328,565 |
| 2 | John | 4,546,819 | Patricia | 1,562,727 |
| 3 | Robert | 4,535,897 | Jennifer | 1,466,854 |
| 4 | Michael | 4,323,074 | Linda | 1,448,194 |
| 5 | William | 3,631,876 | Elizabeth | 1,436,232 |
| 6 | David | 3,560,660 | Barbara | 1,406,173 |
| 7 | Richard | 2,477,879 | Susan | 1,105,188 |
| 8 | Joseph | 2,367,801 | Jessica | 1,044,492 |
| 9 | Thomas | 2,167,014 | Sarah | 995,436 |
| 10 | Charles | 2,124,748 | Karen | 985,261 |

Source: www.ssa.gov/OACT/babynames/decades/century.html

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# Estate planning when interest rates are low

Some estate planning strategies divide property into current and future interests. Each interest is valued separately. The value of each interest will be affected by current interest rates as published monthly by the IRS. One key rate that affects the deduction for gifts to charity or the gift tax on transfers to family members is referred to as the "7520 rate," as that is the Internal Revenue Code section where it is defined.

Back in the late 1990s, the 7520 rate was in the neighborhood of 5% to 7%. In 2000 it was 8% or higher for part of the year. More recently, the 7520 rate has been far lower—1.8% in October, 2.0% in November of 2019. The manner in which low interest rates affect the attractiveness of various split-interest planning techniques was recently reviewed by attorney Larry Katzenstein for Leimberg Information Services, an internet resource for estate planners.

### *Bad ideas*

Low interest rates boost the value of an annuity, because future payments are discounted less for the time value of money. At a 0% interest rate, for example, the right to receive $10,000 per year for ten years is $100,000.

A charitable remainder annuity trust (CRAT) is one in which a fixed-dollar amount is paid by a trust for a term of years or for the life of a private beneficiary. A CRAT created when interest rates are low will generate a lower deduction for the future charitable interest. Mr. Katzenstein points out that when rates are as low as they are now, and depending upon the age of the income beneficiary, there is a good chance that the probability of the exhaustion of the trust will exceed 5%, which would eliminate any charitable deduction entirely.

A Qualified Personal Residence Trust QPRT is a mechanism for transferring a home to one's children at a future moment, typically ten years. According to Mr. Katzenstein, if a ten-year QPRT were created by a 70-year old for a $1 million residence, the taxable value of the gift to the children would be $314,710 when the interest rate is 8%. But if the interest rate of 1.8% were used, as it would have been in October of this year, the taxable value zooms to $568,430. On the other hand, if there is no QPRT, the estate tax value of the home would be $1 million, so the strategy still may be a good one for some families.

### *Good ideas*

With a Grantor Retained Annuity Trust (GRAT), the grantor keeps the annuity for himself or herself, and the remainder passes to the children at a future date. The value of that remainder falls as the value of the retained annuity rises, so the gift tax exposure of the GRAT is reduced.

The usual strategy when creating a GRAT is to set the annuity interest high enough to bring the taxable gift down to zero. That is easier to do in the low interest rate environment that we have today. Mr. Katzenstein calculates that when the interest rate is 8%, and a ten-year GRAT starts out at $1 million, the retained annuity must be $149,029 to zero out the gift. With a 1.8% interest rate, only $110,165 need be retained. If the assets placed in the GRAT can earn more than 1.8%, the annuity can be paid for the term without diminishing trust principal, so the entire $1 million passes to heirs tax free.

The Charitable Lead Annuity Trust (CLAT) also produces favorable results when interest rates are low. In this approach the charity receives a fixed-dollar amount from the trust for a specific number of years, and the trust principal passes to private beneficiaries in the future.

Mr. Katzenstein also recommends looking into a charitable gift of the remainder interest in a personal residence or farm. Deductions for such commitments are maximized now. The donor may occupy the property for life, and the donor doesn't have to part with any liquid assets.

### *Neutral idea*

The Charitable Remainder Unitrust (CRUT) is generally not affected by changes in interest rates. In this trust the private interest is defined as a percentage of the value of the assets, as determined every year.

Have you reviewed your estate plans recently? Are you satisfied that your planning is optimum for your family? We would be pleased to share our thoughts with you on this important subject. ☐

## Whistleblower limits

Vincent J. Apruzzese made a claim against a Florida decedent's estate. The decedent was unnamed in the court reports; call him "Mr. X." Evidently, Apruzzese was not satisfied with the progress on the claim. In any event, hoping to be rewarded for "blowing the whistle" on a tax cheat, he alerted the IRS to the fact that the estate had drastically underpaid its federal estate taxes.

As it happened, the estate tax return already was being audited, and the agent in charge was nearly ready to issue a "no change" order. Based upon the new information from Apruzzese, he took another look at the valuations that were used in four federal gift tax returns. The values were found to be too low, and so additional taxes, interest, and penalties of some $424,000 were assessed. That amount was paid promptly by the estate.

For his valuable information, the IRS offered Apruzzese $43,000. He was not satisfied with that award, because he apparently felt that the IRS recovery should have run into the millions of dollars. He filed suit in Tax Court, asking that the estate tax return for Mr. X's estate be reopened and reexamined.

The Tax Court does have jurisdiction over the determination of whistleblower awards. However, the Court held, it does not have the authority to order the IRS to restart an audit.

## IRA exception not allowed

When Lily and Bahman Amadi bought their first home, they came up short on the money needed for a down payment. Lily worked for the State of New York, and she had been setting money aside in her 401(k) plan for retirement. She asked for and received $6,686 from the plan, which went toward purchasing the house.

When they filed their joint tax return, the Amadis did not report the 401(k) distribution. IRS caught the omission, and it assessed income tax as well as a 10% penalty for the premature distribution. Acting as her own attorney, Lily took the matter to the Tax Court. Her petition read, in part:

"The money that I had to cash out went to purchasing a house that we are paying very high taxes for. I wouldn't use my retirement money, if I could. I used it toward something that we needed for our growing family. I don't think we should pay tax on top of what we are paying, since we are paying taxes on our house."

There is no question that distributions from the pretax portion of a 401(k) plan must be included in taxable income. The harder problem is whether the 10% penalty should apply. IRC §72(t) waives the penalty for distributions used for first time home purchases, but only for distributions from "individual retirement plans." The Court declined to stretch this language to include an individual account plan, such as a 401(k) plan, although there is no policy justification for the distinction. ☐

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