LENOX ADVISORS, INC

WEALTH MANAGEMENT ADVISOR

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Naming a trustee

It's one of the most important decisions of your life

Trusts are appealing for many reasons. They can enable you to hold and transfer assets for beneficiaries, avoid probate and reduce estate tax exposure. But they can be complicated to set up. One of the major decisions you'll need to make when establishing a trust is who will act as your trustee. As the name implies, this individual or financial institution must be above reproach. But that's just one quality of many that your trustee requires.

DUTIES BOTH MUNDANE AND SIGNIFICANT

Trustees have significant legal responsibilities, primarily related to administering the trust for the benefit of beneficiaries according to the terms of the trust document. But the role can require many different types of tasks. For example, even if a tax expert is engaged to prepare tax returns, the trustee is responsible for ensuring that they're completed and filed correctly and on time.

One of the more challenging trustee duties is to accurately account for investments and distributions. When funds are distributed to cover a beneficiary's education expenses, for example, the trustee should record both the distribution and the expenses covered by it. Beneficiaries are allowed to request an accounting of the transactions at any time.

The trustee needs to invest assets within the trust reasonably, prudently and for the long-term benefit of beneficiaries. And trustees must avoid conflicts of interest — that is, they can't act for personal gain when managing the trust. For instance, trustees typically can't purchase assets from the trust. The trustee probably would prefer a lower purchase price, which would run counter to the best interests of the trust's beneficiaries.

Finally, trustees must be impartial. They may need to decide between competing interests, while still acting within the terms of the trust document. An example of competing interests might be when a trust is designed to provide current income to a first beneficiary during his or her lifetime, after which the assets pass to a second beneficiary. Although the first beneficiary would probably prefer that the trust's assets be invested in income-producing securities, the second would likely prefer growth investments.

A TALL ORDER

Several qualities help make someone an effective trustee, including:

- A solid understanding of tax and trust law,
- Investment management experience,
- Bookkeeping skills,
- Integrity and honesty, and

- The ability to work with all beneficiaries objectively and impartially.

And because some trusts continue for generations, trustees may need to be available for an extended period. For this reason, many people name a financial institution or professional advisor, rather than a friend or family member, as trustee.

Naming a friend or family member as a trustee may seem appealing because it appears to be a way to reduce or avoid the fees associated with an institutional trustee. But it's important to recognize that taking on the responsibilities of a trustee requires an investment of time, energy and expertise, and that trustees deserve compensation. Even if trust documents don't provide a fee for the trustee, many states allow for a "reasonable fee." Before engaging a trustee, make sure you understand what services are included in the fee. But it's generally not a good idea to try to avoid paying a trustee fee.

ASK FOR SUGGESTIONS

If you feel that none of your friends or family members are qualified to be named your trustee, ask your Lenox Advisor for help. They may be able to serve or recommend individuals or institutions with the proper expertise and experience.

How to transition into a comfortable retirement

You've been planning and saving for decades, and now retirement is looming on the horizon. As the time to implement your retirement plan approaches, there are several steps you should take to ensure that the transition is smooth and that your money will last as long as you do.

ACTION PLAN

Ideally, you should check the following items off your task list before your last day of work.

Build an emergency cash cushion. If you haven't already done so, set aside enough to cover at least two or three months of living expenses. This is a good idea at any stage of life, but it's particularly important at retirement because there may be a time lag after you leave your job and before you begin receiving pension, Social Security or other payments.

Pay down debt. If possible, accelerate your mortgage payments and reduce your credit card debt. The less debt you have at retirement, the more manageable it will be. Plus, reducing debt will limit your need to tap tax-advantaged retirement accounts, allowing the

funds to continue growing as long as possible.

Adjust your asset allocation. At retirement, as in other stages of your life, it's a good idea to review your asset allocation in various investments. Work with a financial professional to make adjustments that reflect your changing circumstances, time horizon and risk tolerance.

Review health insurance options. This is critical, since health care will likely be a major expense as you get older. Once you reach age 65, Medicare will cover most of your routine expenses, but you'll probably need supplemental coverage for nonroutine expenses and separately to cover long-term care.

Create a budget. Carefully analyze your expected retirement expenses and make adjustments to your preliminary budget if necessary. Developing a realistic budget is the best way to minimize the chances that you'll outlive your savings.

Make a Social Security plan. You have a lot of flexibility in determining when to begin Social Security payments. For example, you can start collecting as early as age 62 or as late as age 70. But remember that the timing can substantially affect your financial plan. The later you start receiving benefits, the greater the monthly benefit. So it's generally best to wait as long as possible.

However, you may need to start sooner if you have health issues or require funds for living expenses. It's particularly important to delay Social Security if you continue working. If you collect Social Security benefits before you reach full retirement age and your earnings exceed certain thresholds, your benefits will be reduced.

Develop a retirement income timeline. Determine the timing of your income during retirement and the sources from which it will come, factoring in expected retirement expenses. If you have traditional IRAs or other retirement accounts, you'll need to take required minimum distributions (RMDs) from these accounts starting when you reach age 70½, whether you need the money or not. If RMDs don't cover your expenses, it's generally best to withdraw funds from other sources in this order:

1. Taxable investment accounts,
2. Tax-deferred accounts, such as traditional IRAs or 401(k) accounts, and
3. Tax-free accounts, such as Roth IRAs or Roth 401(k) accounts.

Withdrawals from taxable accounts generate mostly capital gains, which are taxed at a lower rate. This withdrawal plan allows funds in tax-advantaged accounts to continue growing as long as possible.

START NOW

It's best to begin working on the transition several years before your planned retirement date. The sooner you begin, the more time you'll have to make necessary adjustments. But if you get a late start or are unexpectedly forced to retire, a financial planning expert can be particularly helpful in getting you on track to a secure postwork life.

Should you convert your balance to a Roth IRA?

If you've accumulated a big balance in a traditional IRA, now may be an ideal time to convert some or all of it to a Roth IRA. The recently enacted Tax Cuts and Jobs Act (TCJA) reduces individual income tax rates through 2025, lowering the cost of conversion. When you do a Roth conversion, you're subject to tax on some or all of the amount you convert, so it could be cheaper to do it now, while tax rates are more favorable.

But why choose a Roth in the first place?

PRIMARY BENEFITS

Roth IRAs are advantageous if you expect your tax rate to go up in the future — or at least not go down. That's because Roth IRA contributions get no deduction up front, while qualified withdrawals of contributions and earnings are tax-free. Given the TCJA's temporary reduction of tax rates, your tax rate may go up in 2026 (assuming your income remains about the same and Congress doesn't take action).

Contributions to traditional IRAs, on the other hand, are taxed later: They're deductible (up to an annual limit) if you're eligible, but withdrawals of deductible contributions, plus earnings, are taxable. If you expect your tax rate to be lower when you withdraw the funds, such as in retirement, you may be better off deferring taxes with a traditional IRA.

Second, regardless of your expected tax rate, you may benefit from a Roth IRA conversion if your other assets are sufficient to meet your living expenses in retirement. With a traditional IRA, you must begin taking required minimum distributions (RMDs) — and pay taxes on those distributions — every year once you reach age 70½. But a Roth IRA imposes no such requirement, so you can allow the funds to continue growing tax-free as long as you wish.

And if you hold a Roth IRA for life, you can leave it to your spouse, children or other loved ones free of income taxes. In contrast, an inherited traditional IRA can come with a substantial income tax bill.

WATCH OUT FOR THE PRO-RATA RULE

Nondeductible contributions to a traditional IRA aren't taxable when those amounts are converted to a Roth IRA. But that doesn't mean you can choose to convert only those amounts in an attempt to avoid taxes. The "pro-rata" rule treats all of your traditional IRA funds as a single account and allocates the converted amount among deductible contributions, nondeductible contributions and earnings on a pro-rata basis.

Suppose, for example, that you have two traditional IRAs: One has $60,000 in deductible contributions and earnings and the other has $30,000 in nondeductible contributions, but no earnings. You might think you can convert the $30,000 nondeductible IRA into a Roth IRA and avoid taxes. But under the pro-rata rule, the $30,000 is treated as if it had come from one big $90,000 IRA comprising two-thirds deductible contributions and earnings and one-third nondeductible contributions. As a result, two-thirds of the conversion amount, or $20,000, is taxable, and only the remaining $10,000 is nontaxable.

Keep in mind that a Roth IRA conversion can potentially push you into higher tax brackets, depending on your income level and the amount you're converting. To avoid this result, consider doing the conversion gradually between now and 2025. This allows you to spread the tax liability over several years and avoid a bracket-busting increase to your taxable income in a single tax year.

IRREVOCABLE CHOICE

If you believe a Roth IRA conversion is right for you, thoroughly review the relative costs and benefits. Careful planning is particularly important now that the TCJA has eliminated a tax code provision that had allowed taxpayers to "undo" a Roth IRA conversion up until the extended tax return due date for the year in which the conversion is made.

But, starting in 2018, Roth IRA conversions are irrevocable. Talk with your Lenox Advisor before you pull the trigger.

MAKING THE SWITCH

If you decide to convert your traditional IRA to a Roth IRA, be sure you understand the tax implications. You'll be subject to federal income taxes on the amount you convert, if the funds are attributable to deductible contributions and earnings.

Amounts attributable to nondeductible contributions aren't taxable, since they were made with after-tax dollars. Unfortunately, you can't reduce or eliminate taxes on a Roth IRA conversion by converting only nondeductible amounts. (See "Watch out for the pro-rata rule.")

Dollar cost averaging has an unexpected price attached

Many investors use dollar cost averaging (DCA) to reduce their average cost per share and lower the risk that they'll make a substantial investment just before the market plummets. But while DCA offers some peace of mind, it comes at a price.

WHAT IS DCA?

DCA simply means investing an available lump sum of money in equal installments over time. For example, if you receive a $50,000 after-tax bonus at work but are uncomfortable investing it all at once, you might invest $10,000 per month for five

months or $5,000 per month for 10 months.

As asset prices fluctuate, investing the same dollar amount each period ensures that you buy more shares when prices are low and fewer shares when prices are high. In other words, you reduce your average cost per share over time. And if you're risk-averse, DCA tends to minimize the odds that you'll invest a large amount just before a market drop. DCA also helps remove emotions from your investment strategy. By investing the same amount each period, you'll be less tempted to try to "time" it.

WHAT'S THE DOWNSIDE?

Although DCA can lower your risk, it may also cause you to miss out on potentially higher returns. That's because your money is held in cash or cash equivalents for a longer period while you wait to invest it. Not only do you risk losing the potential gains you might have earned had you invested in higher-returning securities sooner, but there's the risk that cash investments won't keep pace with inflation. This can erode your returns even further.

The alternative is lump sum investing (LSI), or investing the entire amount immediately — typically in a mix of stocks and bonds. The volatility of these investments increases your risk when purchased all at once, but they outperform the DCA approach more often than not. According to a study by investment company Vanguard, LSI historically outperforms DCA about two-thirds of the time (using a 12-month DCA period). And that advantage increases as the time frame increases.

There's another potential disadvantage of DCA. Depending on the type of investment, it may involve higher brokerage fees than LSI.

WHAT'S YOUR TIME HORIZON?

If your investment time horizon is longer, LSI may be more effective than DCA (although it's important to note that you can lose money using either strategy). But if you're uncomfortable with the risk of LSI, another potential approach is to ensure that your portfolio's target asset allocation is appropriate given your risk tolerance. Talk with your Lenox Advisor about the best strategy for your specific situation.

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