Outlook

A Quarterly Newsletter from Roffman Miller Associates

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The More Things Change…

As the previous tenant of this front page, Peter Miller, once said, “Good market, short letter.” For those of you who know me well, I’m not usually capable of a short letter (or conversation). But I promise to do my best.

There’s plenty to talk about – the stock market had strong returns in 2017. Can it happen again? Interest rates remained low, but where will they go from here? How will the new tax law affect us? How will it affect the economy as a whole? Sometimes I think what Peter meant was that the ‘good market’ we’re speaking of is already in the past and we shouldn’t spend too much rehashing it. But in his ‘short letter’ he pointed out that although we can’t accurately predict the future we should always look ahead: we should continue to focus on our guiding principles like finding high-quality companies with good potential for growth; allocating assets according to our individual tolerances for risk; and reviewing financial plans frequently to build and reinforce our trust in the process. And, of course, using common sense.

All of us will be affected by the new tax law, some in a negative way and some in a positive way. I can remember back to 2013 when the provisions of the 2003 Tax Reconciliation Act were going to sunset and dividends were going to be taxed at the maximum rate of 39.6%. If you paid any attention to the news media, it was the beginning of the end for investors. Fortunately, our clients ignored the hype and stayed invested. Ultimately Congress intervened and we still have favorable rates on dividends and capital gains today, proving that we should only worry about what we can control. Susan summarizes the most impactful elements of the new law on page three.

I can’t remember what exactly was the last thing to generate as many investor questions as Bitcoin. It might have been gold, or maybe Florida real estate back in 2006. I hesitate to draw the comparison because gold and land are as old as history itself, and Bitcoin is brand new. Unfortunately, if Bitcoin is actually a permanent, useful tool for global markets, it comes at a bad time. This is a classic period in the market cycle where some investors become bored with the past 9 years of market gains, and they need something with more pizzazz. No one wants to miss out. The speculation and hype surrounding bitcoin is beginning to look like just another mania. Bob has penned his thoughts on the back page.

I don’t know if it’s true that the more things change, the more they stay the same. But I do know that the majority of Americans are still employed by small businesses. And throughout every change in the tax code over the course of my career, entrepreneurs and business owners have been able to access some type of tax-advantaged retirement plan. The rules often change on us, but in the end these plans get the job done. Kevin covers some ideas for small business owners on the next page.

We hope you find this edition of our newsletter informative. All of us here are Roffman Miller wish you the best for a healthy and fulfilling new year in 2018. As always, we welcome you to call and schedule some time to review your plans and investments.

Mark Frombach
Chief Investment Officer

SEP-IRA, Individual 401(k), SIMPLE IRA – Which is Best for the Self-Employed?

By Kevin Cooke

If you're self-employed, take advantage of the great retirement plan options available to you. Three popular small business retirement plans that you'll want to consider are the SEP-IRA, Individual 401(k), and the SIMPLE IRA. Contributions to any of these plans reduce your taxable income while allowing your investments to grow tax-deferred. Below is a quick look to give you a better understanding of these three options.

SEP-IRA (Simplified Employee Pension Plan)
SEP-IRAs provide business owners a simplified method to contribute towards their retirement and their employees' retirement. Employer contributions are made to a SEP-IRA account which is opened for each plan participant. Employee contributions are not permitted.

<u>Contribution Limits</u>: Contributions to your SEP can't exceed the lessor of: 1) 20% of net self-employment earnings, or 2) $54,000 for 2017 ($55,000 for 2018).

I primarily think of the SEP as a vehicle for the self-employed with no employees. Why? Because you're required to contribute the same percentage of compensation to your employees as your defer for yourself. Furthermore, even if your employees are part-time you may have to contribute. Employees must be allowed to participate if they're over age 21, earn at least $600 annually, and have worked for you in at least three of the last five years.

Individual 401(k) Plan
One-participant 401(k) plans may also be referred to as: Solo 401(k), Solo-k, or Uni-k. Regardless of the name, they cover business owners with no employees, or the owner and his/her spouse if working in the business.

<u>Contribution Limits</u>: Your *employee* contributions are limited to $18,000 for 2017 ($18,500 for 2018) plus an additional $6,000 if you're age 50 or more. In no case can this amount exceed 100% of your compensation. You can also make *employer* contributions up to 20% of net self-employment earnings. For 2017, your total contributions as both employer and employee are limited to a maximum of $54,000 ($60,000 once you reach age 50). For 2018, the maximum total contribution is $55,000 ($61,000 once age 50).

SIMPLE IRA (Savings Incentive Match Plan for Employees)
Simple IRAs function like traditional IRAs while providing higher contribution limits than traditional IRAs. The SIMPLE IRA has lower contribution limits than both the SEP and Individual-k.

<u>Contribution Limits</u>: Your *employee* contributions are limited to $12,500 for 2017 and 2018 plus a smaller catch-up contribution for those over 50, only $3,000. Like the Solo-k this *employee* contribution can't exceed 100% of compensation. Also like the Solo-k, you can make *employer* contributions but are limited to only 3% of your net earnings from self-employment.

Considerations
For most, the best plan is the one that allows the greatest contribution for your situation.

The major benefit of the Solo-k is that you may be able to contribute significantly more to your plan than you would most likely be able to contribute to a SEP or SIMPLE. The major drawback is that the Solo-k is not as simple to administer. Establishing the 401(k) requires more forms and documentation than opening a SEP or SIMPLE IRA. And, once the plan assets reach $250,000 you're required to file Form 5500 with the IRS every year, increasing administration expenses.

If you're not interested in maxing-out your contributions and can contribute as much as you're willing then you'll probably choose a SEP or SIMPLE IRA for its simplicity. However, if maximizing your contribution is of utmost importance then the Solo-k will probably be your best choice and can provide options such as Roth contributions and even loans, which are not available with the SEP.

I encourage you to consult with your tax professional or a third-party administrator and consider all your retirement plan options to find the most appropriate one for you and your business.

Kevin is an Investment Manager at Roffman Miller

The New Tax Law

By Susan Arnold

On January 1, 2018, most provisions of the new tax law will take effect. Here we compare some of the major provisions of the new law with the previous tax code and discuss how they may affect your personal taxes:

Individual Income Tax Rates

- The new law maintains seven individual **income tax brackets**, but changes the tax rates and thresholds. It seems that almost every taxpayer would see a lower effective tax rate *if all else was held equal*.
- **Capital Gains Tax Rate** – no changes
- "**Kiddie tax**" rules are simplified. The net unearned income of a child subject to the rules will be taxed at the capital gain and ordinary income rates that apply to trusts and estates. Thus, the child's tax is unaffected by the parent's tax situation.

Deductions

- The itemized deduction for **state and local income and property taxes** is now limited to a total of $10,000.
- For current mortgage holders, there is no change to **mortgage interest deduction**. But for new loans, interest is only deductible on $750,000 loans or less (down from $1million). Additionally, homeowners may not claim a deduction for interest on new or existing home equity loans beginning Jan. 1, 2018.
- There is no longer a deduction for **miscellaneous itemized deductions** which were formerly deductible to the extent they exceeded 2 percent of adjusted gross income. This category included items such as tax preparation costs, investment expenses, union dues, and unreimbursed employee expenses.
- **Charitable donations** – changes in other areas of the tax code affect the deductibility of charitable donations
- Taxpayers can continue to deduct **medical expenses** that exceed 7.5% of AGI , but that level steps to 10% on Jan. 1, 2019.

Personal Exemptions and Standard Deductions

- **Previous law:** $4,050 **personal exemption** per person, which means a married couple with two dependents would receive a personal exemption of $16,200. The **standard deduction** for married filing jointly was $12,700 for tax year 2017; $9,350 for heads of households, and$6,350 for single taxpayers
- **New law:** Starting in 2018, taxpayers can no longer claim personal or dependency exemptions. The new law increases the standard deduction to $24,000 for joint filers, $18,000 for heads of household, and $12,000 for singles and married taxpayers filing separately.

The Personal Exemption was the amount that you could deduct from your income for each taxpayer and most dependents on your return. The Standard Deduction is the amount that you can deduct from your income before calculating your tax liability if you do not itemize your deductions. The net effect of eliminating one and increasing the other is that the bigger your family is, the worse off you are under the new tax law – something that may be offset by a more generous Child Tax Credit (depending on your household income).

Miscellaneous

- New 529 plan rules allow for up to $10,000 per year to be used for elementary and secondary school costs
- The top estate tax rate stays at 40%, but the exclusion amount doubles to $11.2 million per individual

The overall impact will be different for everyone. Many taxpayers will no longer be itemizing deductions because their available deductions have been reduced or eliminated under the new tax code, or the new standard deduction is higher than their itemized deductions (or both). Those making charitable contributions may need to consider giving directly from an IRA if they can't overcome the new standard deduction. Hopefully we have illustrated the areas with the most impact on you, and we encourage you to speak to your tax advisor about these changes before making any tax related decisions.

Susan is an Investment Manager at Roffman Miller

Bitcoin: Fad or Future

By Bob Hofmann

Even the Beatles would be impressed by the hysteria surrounding Bitcoin. Hardly a day goes by without someone asking me about it. The questions come from long-term clients and from the friends of my young children. The most common question being: “What is Bitcoin?”

Bitcoin is the first decentralized cryptocurrency. This means that it’s not backed by a central bank like the dollar is backed by the United States Federal Reserve Bank (FRB). Bitcoin is not a physical asset, rather it’s an intangible asset that only exists on a computer hard drive in the form of zeroes and ones. Bitcoin proponents would argue that the world banking system is flawed. Since the US Dollar is no longer backed by gold, the fiat currency can be manipulated by the FRB by printing more money. Bitcoin on the other hand supposedly has a finite limit of 21 million bitcoin. Bitcoin is designed to be scarce, anonymous and a world-wide store of value. The anonymous creator goes by the name of Satoshi Nakoamoto.

Bitcoins are created through a process called “mining.” Since bitcoins are a digital asset they can only be mined through computers. The founder of Bitcoin created a series of math problems and if the problems are solved successfully new Bitcoins are created. As new Bitcoins are created the math problems become more difficult and solving the equations requires more and more computing power. The cost of electricity to mine Bitcoins is accelerating quickly and soon the cost of mining may exceed the value of Bitcoin.

I wouldn’t write the greenback’s obituary just yet. Bitcoin is just in its infancy and it certainly doesn’t have the ability to replace a major currency any time soon. The US Dollar is still backed by the future tax revenues of the United States and this income stream is the most predictable, powerful and diverse in all the world.

A big risk to Bitcoin is government intervention. To date there have been a number of countries who have outright banned Bitcoin. Two of the world’s largest countries, China and Russia, have imposed strict regulations around Bitcoin ownership. Also, there have been numerous reports of terrorist groups using cryptocurrencies to finance illicit activities. The world banking system is continuously trying to prevent money laundering, funding to terrorist organizations, tax evasion and other illicit activities. Governments are anti-anonymity.

Clients have also been asking why the price of Bitcoin is soaring. I heard an interview with Mark Cuban who summed it up fairly well. Mark thinks Bitcoin is a “collectable” and he compared it to fine art and baseball cards. In each case the value is entirely subjective. Value is what someone is willing to pay to own it. The same can be said for Bitcoin. There is no rational explanation for the meteoric rise in this cryptocurrency’s price. It’s simply a bubble. Bubbles can go on for a very long time and there’s no way to know when they will end. I won’t go as far as Jamie Dimon, the CEO of JP Morgan, who said that Bitcoin is a “fraud” that “won’t end well.” In my opinion Bitcoin is a highly speculative, intangible collectable. Investors who buy Bitcoin should only use money that they’re prepared to lose. It’s true that the party can continue for a lot longer than anyone anticipates but the risks are mounting. This bubble will one day end, as all bubbles do. If Amazon begins to utilize Bitcoin for payment processing then I’ll likely change my opinion. Until then, crypto-buyer beware.

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