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FINANCIAL AND TAX PLANNING

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How The New Health Law Affects Business Owners

The massive new health care legislation passed last spring—the Patient Protection and Affordable Care Act of 2010—will have a long-lasting impact on businesses. Most companies will soon have to provide health insurance for employees, though some small businesses will be able to use tax credits to offset the cost of this benefit. And while some provisions take effect right away, others will be phased in over the next few years. Here are the likely new rules in several important areas.

Coverage requirements. After 2013, employers with 50 or more full-time employees will be subject to "play or pay" rules—if the companies don't provide "minimum essential coverage" to full-time employees, companies will have to pay a penalty. For this purpose, a full-time employee is anyone who works at least 30 hours a week. The monthly penalty will be based on an annual amount of $2,000 for every full-time employee, not just the ones without coverage, though the first 30 employees will be subtracted from the calculation.

Help for owners of small businesses. From 2010 through 2013, a business with 10 or fewer employees and average annual wages of less than $25,000 can claim a tax credit to offset the cost of mandated health coverage. A smaller credit applies to companies with as many as 25 employees and average annual wages of up to $50,000.

Health insurance exchanges. Beginning in 2014, state-based insurance exchanges and the Small Business Health Options Program (SHOP) will offer coverage to individuals and small businesses with up to 100 employees. States may allow companies with more than 100 employees to purchase coverage in the SHOP exchange after 2016.

Free-choice vouchers. Also starting in 2014, employers that provide minimal essential coverage must offer qualified employees a free-choice voucher to enroll in a state health insurance exchange. Qualified employees have household incomes that don't exceed 400% of the federal poverty level and a required contribution for health insurance premiums of between 8% and 9.5% of household income. The amount of the voucher, provided in lieu of a company's normal coverage, would equal what the employer would otherwise have to pay for an employee's insurance.

Automatic enrollment. Eventually—it's not clear when this provision will take effect—an employer with more than 200 employees will have to automatically enroll full-time employees in its health plan, though workers will be able to opt out of the coverage.

Minimum coverage. Effective in 2014, a health benefits package will have to provide a comprehensive set of services, cover a minimum of 60% of the

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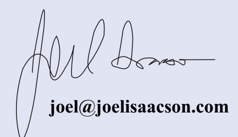
Road To Recovery Picking Up Steam

The third quarter was very strong for equities, with the S&P 500 up 11.3%. The Federal Reserve's $600B Treasury bond purchase program and November's landslide Republican victory may very well provide the environment necessary to propel the economy towards a more robust recovery.

The Fed hopes its latest round of quantitative easing will help push borrowing costs lower, encouraging homeowners to refinance and businesses to hire more people. As the dust settles from the elections, Congress will gather for the last 2010 "lame duck" session with a list of very important items to address. Among the most critical issues: what to do with the expiring Bush tax cuts, the seemingly annual AMT debate, and eliminating uncertainty around the current estate tax laws.

With the Congressional houses now split, progress will only be made if leaders on both sides of the aisle can meet in the middle on issues affecting Americans. A bright note in an otherwise unattractive political environment: more often than not, political "gridlock" is good for the markets, as is the third year of a presidential term.

Please contact us if you would like to discuss any of these issues and how they relate to your personal circumstances. As always, we thank you for your continued confidence and we extend our best wishes for the holiday season.



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Caveat Emptor: Long-Term Care Policies

Most long-term care (LTC) insurance policies today are much better than those offered in previous decades. Still, there remain potential drawbacks, and would-be buyers need to make sure they know what they're getting and that it suits their needs.

Many early LTC policies paid benefits only for "skilled nursing home care" for a limited period of time. Moreover, there were often stringent requirements to qualify for benefits, such as having to spend three days in a hospital before going into a nursing home.

Most states now require LTC policies to provide benefits for all levels of care, and competition among insurers has led to innovations that make LTC insurance a significantly better value. Yet these policies remain complex and expensive, and getting the right mix of benefits means understanding the LTC landscape. Consider these factors:

Range of coverage. Most policies offer benefits for care in a variety of settings, including at home, in an assisted living facility, and adult day care as well as in a nursing home. Payment may vary with the setting, so make sure the specified amounts cover the cost of care in your area. And beware of hospitalization requirements, because only about half of nursing home admissions follow a hospital stay.

Benefit triggers. Usually, LTC benefits are available once the insured needs assistance performing a specified minimum number of activities of daily living (ADLs) — commonly including eating, bathing, dressing, "toileting," continence, and mobility. Better policies kick in when someone requires help with just two or three ADLs. Some policies also begin coverage when there is "cognitive impairment."

Waiting period. Most policies specify a 90-day waiting period between the time need is demonstrated and the beginning of benefit payments. However, it is important to check the policy's definition of a "waiting period," as it could refer to either calendar days or service days.

Premiums. The younger you are when you begin coverage, the lower the premium, which will also be affected by the range of policy benefits you choose, including type of policy (reimbursement, indemnity, or cash); health status; waiting period; and inflation factor chosen (simple, compound, or none).

Inflation protection. The cost of all health care, including long-term care, is rising much faster than the overall cost of living. So it's essential that a policy increase benefits as costs rise—particularly if it could be years or even decades before care is needed.

Desirable policies are guaranteed renewable for life and cover pre-existing medical conditions. Additional riders and options may be worthwhile, but it's important to weigh the costs of extra benefits. We can help you find a broker to make sense of this complicated insurance market and help you find a suitable policy at a reasonable price. ●

Yield vs. Risk In Emerging Market Bonds

Stock markets around the world improved in 2009, but the spectacular growth came in emerging markets, which gained more than 75%, according to Barron's. Foreign stocks and bonds swept up a record $64 billion of American investor assets, with just more than half going into emerging market equities, $2.7 billion into emerging bonds, and the rest into developed market bonds. Meanwhile, U.S. equity mutual funds lost $40.3 billion in assets in 2009.

While the money flowing into emerging market bonds represented a small proportion of foreign investment, it was nevertheless a remarkable development. U.S. investors had paid little attention to those fixed-income securities until the global financial crisis reduced yields on U.S. government bonds to next to nothing. Because bonds of developing countries are considered riskier than U.S. Treasuries, they pay more—and recently, a lot more. Some emerging market debt now pays more than U.S. corporate high-yield bonds.

Emerging market bonds provide a good example of the trade-off between risk and return. U.S. Treasuries have historically been considered "risk-less" and pay little. Emerging bonds, which pay plenty, may bring considerable risks. The Dubai scare, when Dubai World announced in December 2009 that it had to renegotiate at least some of its $59 billion in debt, reminded investors of the 1998 crisis, when Russia defaulted on its bonds. Back then, some emerging market bond funds sported yields well into the double digits, as they did again in 2008, according to The Wall Street Journal.

Yet despite their volatility, emerging market bonds can serve as an effective tool for managing risk. They can squeeze a little extra yield out of the income portion of a portfolio while also decreasing risk, thanks to their

Roth IRA Conversion & Estate Planning

By now, you've probably been inundated with media stories and ads touting the benefits of Roth IRA conversions, which are now open to everyone, regardless of income. Roth IRAs are known for their ability to deliver tax-free income during retirement. But a Roth may realize some of its most significant advantages after your retirement has ended. When the future of the estate tax finally gets resolved, converting a traditional IRA to a Roth will likely reduce any estate taxes your heirs may owe. And it will definitely cut their income tax bill on distributions from inherited IRAs.

Qualified distributions from a Roth IRA that has been established for at least five years are completely exempt from income tax. You're eligible to receive this tax-free income once you reach age 59½, and qualified distributions are also possible in case of death or disability or to pay first-time homebuyer expenses (up to a lifetime limit of $10,000). Another plus is that with a Roth IRA, there's no rule requiring distributions that must begin for holders of traditional IRAs after age 70½. So if you don't need the money, investment gains in your account can continue to compound indefinitely without being eroded by taxes.

You will have to pay income tax on the portion of a Roth IRA conversion representing tax-deductible contributions and earnings, and it's best to cover that liability with funds from outside your IRAs. But converting to a Roth may be worth it for retirees looking to preserve a nest egg for their heirs.

Before 2010, you weren't allowed to convert a traditional IRA to a Roth in a year in which your adjusted gross income (AGI) exceeded $100,000. But the Tax Increase Prevention and Reconciliation Act of 2005 eliminated this dollar cap for conversions after 2009. Also, if you convert your retirement account in 2010, you can spread the income from the conversion over two years and pay your resulting tax liability in 2011 and 2012.

When you convert to a Roth IRA, you're effectively prepaying income tax for your heirs without using up the annual gift tax exclusion or your estate tax exemption. You can then use those valuable provisions to shelter other transfers from possible taxes. At the same time, you're able to reduce the size of your taxable estate—by paying the tax due on the conversion—and that could provide further tax savings, depending on what happens to the federal estate tax.

Nonspouse beneficiaries who inherit a traditional IRA normally must pay income tax on the distributions paid over their life expectancies.And though a Roth still requires heirs to make withdrawals spread out over their lifetimes, there will be no income tax for them to pay. That can result in substantial benefits even if a Roth account is established too late for its original owner to enjoy much of its bounty.

Consider the case of John, Jane, and their daughter, Mary. John converts his traditional IRA to a Roth in 2010 when he's 65. He names Jane as the sole beneficiary of the Roth, and when he dies at age 73, she is 70. Based on IRS tables, Jane's remaining life expectancy is 17 years. As a spouse, Jane can choose to treat the Roth IRA as her own and isn't required to take distributions. She designates Mary as sole beneficiary, and when Jane passes away at age 87, Mary inherits the Roth IRA. She's 55, and tax rules require her to take annual payments from the account that she could spread over her life expectancy of 30 years.

What has this accomplished? John lived for eight years after converting his traditional IRA to a Roth. Jane then had access to the account's tax-free income for 17 years, and Mary had the account for another 30 years. That's a total of 55 years for a Roth IRA established by 65-year-old John. Converting to a Roth creates a tax-free annuity for your heirs that should last well beyond your life expectancy.

To get these benefits, Roth IRA accounts must be properly titled and have the appropriate beneficiary designations. And after an account holder's death, nonspouse beneficiaries must begin required (but tax-free) distributions from the account by December 31 of the following year. Miss that deadline and the account will have to be liquidated within five years.

Tax laws are never written in stone, and future changes could reduce the effectiveness of this technique for maximizing tax benefits for your heirs. But for now, at least, a Roth conversion provides substantial estate planning benefits. If you'd like to explore whether it would make sense to convert your traditional IRA, please call to set up an appointment. ●

diversification value, and may provide a hedge against the fluctuating value of the U.S. dollar, as long as the currency of the country issuing the bonds isn't pegged to the dollar.

The governments of many developing countries have received high marks for their handling of the global financial crisis, and if they can follow up with sensible policies as economic growth returns, investors may be more willing to hold their bonds. At the end of 2009, the "risk premium"—the additional return investors receive for putting money into less stable holdings—on developing world bonds, as measured by JPMorgan's Emerging Markets Bond Index Global, had fallen to just under 3 percentage points above Treasuries.

Many investment experts believe U.S. holdings should account for a smaller proportion of investors' assets than they have in the past, and increasing exposure to international markets could include buying debt in developing countries. We can talk to you about the risks and rewards of such investments and help you review your portfolio mix. ●

Critics Overlook Advantages Of A 401(k)

The U.S. economy has served up plenty of negatives in the past couple of years, including a stock market that hit 12-year lows and 140 bank failures in 2009 alone. So it's not surprising that financial institutions and products have come under fire.

But in some cases, critics seem determined to throw out the baby with the bath water. That has certainly been true of the 401(k) retirement plan. Introduced during the great bull market of the 1980s and '90s, the 401(k) seemed a perfect alternative for companies that didn't want the expense and hassle of a traditional pension plan. The 401(k) let employees put away pre-tax dollars, and employers could offer workers matching contributions. Any company without a 401(k) was at a competitive disadvantage in recruiting top employees.

When the stock market plummeted in 2008, however, many 401(k) participants suffered big losses—just as almost every other investor did—and that led to claims that the 401(k) itself should be put to rest. A Time magazine cover story opined that "the ugly truth is that the 401(k) plan is a lousy idea, a financial flop, a rotten repository for our retirement reserves."

Wait a minute! Sure, these retirement plans have flaws—for example, some carry unreasonably high expenses and insufficient investment options. But they're still the best option for many employers looking to help employees save for a secure retirement. Here's why:

1. The 401(k) remains an important recruitment tool, particularly for small companies. It's a perk that helps employees feel they're being given something special. Workers know they can contribute to their own savings success and that their employer will help them.

2. The 2006 Pension Protection Act provides a "safe harbor" that lets your plan avoid the non-discrimination testing that's normally required to ensure that highly paid executives don't reap disproportionate benefits. If you automatically enroll all new employees (letting them opt out if they choose) and deduct 3% of their salary to contribute to the plan the first year, then 4%, 5%, and finally 6% in subsequent years, you need not test for discrimination—and may be able to offer more generous benefits to top management.

3. Some plan sponsors elect to match a percentage of employees' salary, contributing, say, 3% to workers' accounts. That's another way to avoid non-discrimination testing.

4. The 2006 act also encourages employers to retain financial advisors to provide one-on-one investment advice for employees—an option that could increase the value of your plan to its participants.

The 401(k) will not go away and remains the dominant way for employees to save for retirement, though some reforms may be on the horizon. ●

The New Health Law

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actuarial value of benefits and limit employees' annual cost-sharing.

Provisions for "grandfathered" plans. Company-provided health coverage in effect on March 23, 2010, when health reform became law, is exempt from many requirements of the legislation. But these "grandfathered" plans must now extend dependent coverage to age 26, prohibit cancellation of insurance, eliminate waiting periods of more than 90 days, and stop excluding children with pre-existing conditions. The plans have until 2014 to get rid of annual and lifetime limits on coverage.

Retiree health insurance. Through 2013, an employer may offer a temporary health reinsurance program to retirees over age 55 that are not eligible for Medicare.

Flexible spending accounts. Beginning in 2013, companies will have to limit annual contributions to flexible spending accounts (FSAs) for health care to a maximum of $2,500. (Future increases to that cap will be indexed for inflation.)

Information reporting. Beginning in 2012, a business that provides minimum essential coverage to individuals will have to verify the terms of that insurance in annual information returns to the IRS. The information returns will identify who has insurance, the amount of coverage, and any premiums paid by the covered individual.

These are just some of the many business-related provisions of the new law, and further details about how and when particular parts of the law will be phased in are still to come. But it's clear that most companies will now have to provide health insurance coverage to their employees, and you'll need to factor that major expense into your business plan. ●

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