Entrust Group

December 2007 Issue

IRA & 401(k) Insights

Message From the Editor

Welcome to the December edition of the IRA Insights Newsletter. Our newsletter program is just one of the educational resources available from Entrust to help you control your self directed retirement investments. Explore all of the educational opportunities by visiting our web site www.TheEntrustGroup.com.

In the last four years, *The Entrust Group* has expanded its national presence to over 30 offices. Entrust is the only self directed account plan administrator that serves customers through a nationwide network of locally owned and operated offices. These local offices and skilled professionals are the cornerstone of our commitment to provide clients with the finest service, educational opportunities, and most importantly handle your transactions quickly and efficiently.

This year, Entrust and our offices will build on our commitment to educating clients by launching a variety of exciting new educational programs. We love to hear from our readers. Our goal is to write articles that educate you about all the benefits of self-directed retirement plans. If you have a topic you would like to see in an upcoming issue, please let me know.

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How the Richer Family Grows Richer

By: H. Quincy Long

Ira N. Richer, a 56 year old self-employed consultant, his wife, Hope Tobe Richer, Ira's 51 year old stay at home wife, and their 17 year old son, Will B. Richer are interested in saving money in self-directed accounts at Entrust. How much money can they contribute based on Ira's $30,000 net income from his consulting practice?

Roth and Traditional IRAs

Roth IRA – Anytime from January 1, 2007 through April 15, 2008, Ira and Hope can both contribute to a Roth IRA for 2007. Even though Hope does not earn wages, she can still contribute to a Roth IRA based on Ira's income. Even if he doesn't claim net income of over $30,000 on his Schedule C, Ira can contribute $5,000 into each Roth for 2007 ($4,000 base contribution plus a $1,000 catch up contribution since they were both at least 50 years of age by December 31, 2007).

Additionally, Ira may contribute $6,000 into each Roth IRA for 2008 as early as January 1, 2008 (the base contribution increases to $5,000 in 2008). Assuming their son Will has compensation of at least the amount of his contribution, he may also contribute $4,000 to his own Roth IRA for 2007 and $5,000 for 2008.

About: *IRA & 401(k) Insights*

IRA & 401(k) Insights is a monthly publication. This publication is for anyone interested in self-directing their retirement funds and investing in nontraditional assets. Entrust does not give investment advice. Nothing in this publication is intended as tax, legal or investment advice. Entrust does not sell securities or other investments products.

Deadline for article consideration is the 15th of each month. To subscribe to *IRA & 401(k) Insights*, call 888-340-8977 or email:

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Traditional IRA – Ira and Hope could have contributed the amounts described under the Roth IRA into Traditional IRAs, but their total contributions to both their Traditional IRAs and their Roth IRAs cannot exceed the annual contribution limit of $5,000 per person over the age of 50. In this case they elected to put the entire contribution into their Roth IRAs. If neither Ira nor Hope were covered by a retirement plan at work, their contributions to a Traditional IRA would be fully deductible no matter how much income they earned.

Roth Conversion – If Ira or Hope has money in a Traditional IRA (including a SEP IRA), that money can be converted into a Roth IRA provided that their Modified Adjusted Gross Income (MAGI) is $100,000 or less in the year they do the conversion. Any amount they convert is added to their taxable income for the year, but no penalties are assessed for doing a Roth conversion. ***Important Note:*** In 2010, the amount of modified adjusted gross income made by Ira and Hope will not affect their ability to do a Roth conversion. Also, they may pay 50% of the taxes from the 2010 conversion in 2011 and 50% in 2012.

Work Plans

Ira can also have an employer plan based on his self-employment consulting income. With any of the work plans discussed below, Ira must also cover any other employees under the plan. This may affect which plan he chooses for his business. We will assume that Ira has no employees. Having any of the work plans discussed below does not affect Ira's or Hope's ability to contribute to a Traditional or Roth IRA, but above certain income levels it will affect the deductibility of a Traditional IRA contribution.

SEP IRA – Ira can choose to have a SEP IRA plan into which he can contribute up to a maximum of 20% of his net Schedule C income (or 25% of his wages if he is paid through a company). The plan can be set up and funded at any time prior to Ira's tax filing deadline, including extensions (i.e. October 15, 2008 if Ira files for an extension). Since Ira's net Schedule C income was $30,000 in our scenario, he can contribute $6,000 to his SEP IRA at Entrust (the contribution limit would be $7,500 if Ira were paid wages from a company instead of reporting his income on Schedule C as self-employment income). If he wants to, in January of 2008, Ira can begin making contributions for 2008 to his SEP IRA.

SIMPLE IRA - Another alternative is for Ira to have a SIMPLE IRA for his consulting business. This type of plan is appropriate for those with lower income levels or for those who have employees and who don't want to contribute an equal percent into their employees' retirement plans as they do for themselves. Assuming he had the plan set up by October 1, 2007, he can contribute $10,500 for 2007, plus $2,500 catch up because he is over age 50 by December 31, 2007. The $13,000 is considered salary deferral and must be contributed by January 30, 2008. Ira can also contribute an additional $831.15 as an employer contribution by his tax filing deadline, including extensions (i.e. October 15, 2008). This figure is calculated based on 3% of 92.35% of Ira's net Schedule C income (if Ira is paid wages, the calculation is simply the wage amount times 3%). Ira is considered both the employer and the employee since he is self-employed. The total 2007 SIMPLE contribution is $13,000 in salary deferral and $831.15 in employer contribution for a total of $13,831.15. This is an improvement over what he can contribute to a SEP IRA at his income level, but at income levels above approximately $60,000 (or around $48,000 if under age 50), the SEP is more advantageous, absent other factors.

Profit Sharing/401(k) Plan – The plan which Ira can put the most money into is an Individual 401(k) plan. A Profit Sharing/401(k) plan must be set up by December 31, 2007 if Ira wants to contribute or defer salary for 2007. In this plan Ira can defer $15,500 plus $5,000 catch up for 2007 out of his $30,000 net Schedule C income. In addition, Ira can contribute up to 20% of Ira's net Schedule C income (or 25% of his wages if he is paid by a company) into the plan, or $6,000. These contributions must be made by Ira's tax filing deadline, including extensions. This means that for 2007, Ira can get $26,500 into his Individual 401(k) plan with only $30,000 in earned income!

Even better, starting in 2006, Ira's salary deferral can be a Roth 401(k), which means that he will pay taxes on his salary deferral when he contributes, but will pay NO TAXES when the funds are distributed to him, provided they are qualified distributions. What an opportunity! Although Ira qualifies for a Roth IRA because of his income level, even if he makes too much money to qualify for a Roth IRA he can defer salary into a Roth 401(k). The employer contribution ($6,000 in Ira's case) is pre-tax, so part of Ira's withdrawals from the plan will be taxable and the portion relating to the Roth 401(k) will be tax free.

Additional Choices

Besides Traditional or Roth IRAs, an Individual 401(k) plan, SEP IRA or SIMPLE IRA for Ira's consulting business, the Richer family can also have two other types of accounts. These are the Health Savings Account (HSA) and the Coverdell Education Savings Account (ESA). Like the other accounts they have at Entrust, the HSA and the ESA can be self-directed.

Neither of these types of accounts is directly related to how much money Ira earns although, above certain income levels, Ira and Hope could not contribute to Will's Coverdell Education Savings Account.

Health Savings Accounts – Ira and Hope can save on taxes for 2007 by opening a Health Savings Account, or HSA. In order to do this, they have to have a special type of insurance plan, called a High Deductible Health Plan, or HDHP. Just having a plan with a high deductible does not necessarily qualify you for an HSA. Assuming Ira and Hope have a family plan, they can contribute up to $5,650 for 2007 up until April 15, 2008. Because Ira is over 55 years old, he can add an $800 catch up contribution for 2007 in addition to the regular contribution. Ira and Hope can split the contribution into 2 separate accounts or put all of it into one account. Starting in 2007, contributions are no longer limited by the deductible amount as they were in years past. Even if Ira and Hope have the minimum deductible of $2,200 for a family plan, they can contribute the maximum of $5,650 for the year. Contributions to HSA accounts are tax deductible, and there is no tax on the distributions if the money is used for qualified medical expenses. This truly is the best of both worlds!

Coverdell Education Savings Accounts (formerly **Education IRA**) – Since Will is under age 18, Ira can put up to $2,000 into a Coverdell ESA for 2007. Ira will receive no deduction for the contribution, but any earnings which are withdrawn for qualified education expenses are tax free. Qualified education expenses include certain expenses for grade school and high school as well as for college.

Summary

For the tax year of 2007, here is the maximum amount of money that the Richer family can put into self-directed accounts at Entrust:

	Maximum Contribution For Richer Family
Ira's Roth IRA	$ 5,000
Hope's Roth IRA	$ 5,000
Will's Roth IRA	$ 4,000
Ira's Individual (k)	$26,500
Ira's HSA	$ 6,450
Will's ESA	$ 2,000
Total	$48,950

Assuming all distributions are qualified distributions, the earnings from the Roth IRAs, the Roth 401(k), the HSA and the ESA are tax free forever! This means that the Richers can get richer by investing as much as $42,950 tax free and the balance on a tax deferred basis. All of these accounts can invest in real estate, real estate options, promissory notes, both secured and unsecured, LLCs, limited partnerships, private stock and much more. They can invest individually or in combination with each other. To find out more about these accounts, contact your local Entrust office today!

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QUESTION OF THE MONTH

Question

Can I make a contribution to a Roth IRA if I have earned income and am 72 years old? Can I use my Traditional IRA Required Minimum Distribution to fund the Roth IRA if I am eligible?

Answer

Yes, you can contribute to a Roth IRA if your over 70 1/2 and have earned income from providing personal services. Your RMD from your Traditional IRA is NOT earned income, but it is a source of cash that you could use to fund your IRA.

Is Your Reverse Exchange Not Working Out?

By: Dave Owens

Under the current law, a reverse 1031 exchange can be accomplished by following Revenue Procedure 2000-37. Under this technique, the Exchanger or Client typically purchases their replacement property before they have secured a buyer for their existing property and parks title to the replacement property with an Exchange Accommodation Titleholder (EAT). Most Qualified Intermediaries also act as Exchange Accommodation Titleholders.

This technique is very common and used by a number of real estate investors. The three common questions to consider are:

- How will the client pay for the replacement property?
- Can the client close on the sale of their relinquished property 180 days from the date the new replacement property is purchased?
- Has the client priced the relinquished property to sell?

There is no recourse if the client does not sell their relinquished property in 180 days. At that point the EAT would have to return the replacement property to the client. Does this sound confusing? Well, it is, but a qualified exchange company should be able to handle the transaction with very little problem.

One issue that a slow real estate market can cause in a reverse exchange is the relinquished property might not sell within the 180 days. Recently, the IRS released a private letter ruling regarding a technique that could help a failing reverse exchange where the relinquished property has not sold by the 180th day.

In a nutshell, this is how you could complete a reverse exchange if you have not found a buyer.

Let's assume Joe has started a reverse exchange. He has already found the replacement property and hired a 1031 company to purchase the replacement property. Let's assume he goes 150 days, and his relinquished property has not yet sold.

The private letter ruling allowed the client to sell this relinquished property "A" to a related party. For example, Joe's children form an LLC to purchase the relinquished property. Because Joe was a good client, his bank financed the purchase of relinquished property "A" to this new LLC. The sale was at fair market value, with all applicable closing costs paid. Joe has now completed his sale within the 180 days and upon final paperwork, his reverse exchange will be completed on time and qualify for 1031 treatment.

The caveat with this private letter ruling was that normally, when you sell to a related party, the related party must hold the property for 2 years. The IRS ruled that the related party 1031 rules do not apply.

Now let's say the kids have decided to sell relinquished property "A" after twelve months because the market has gotten better. The LLC the kids own lists the property for sale, and sells it for a 10% gain. The LLC would have to report the gain that would pass through to the kids' tax return. The important note is that if a gain or loss is recognized by the LLC, it would pass through to the members of the LLC. Joe is out of the transaction and cannot take any of the tax benefits – gain or loss.

While this is not a perfect solution to complete a reverse exchange, it does give the Exchanger some options. Many taxpayers do feel more comfortable about transferring a property to a related party. Keep in mind that a related party could also be a company that you, the Exchanger, own more than 50% of the shares.

Reverse exchanges have become commonplace. Please feel free to call 1031 Tax Free Strategies, LLC at 239-333-1031 for more information regarding your reverse exchange options.

Dave Owens, CPA, Certified Exchange Specialist is the managing member of 1031 Tax Free Strategies LLC, a company that specializes in 1031 Exchanges, Self-Directed Retirement Accounts, and Health Savings Accounts. If you have any questions, please call him at (239) 333-1031 or email at info2007@1031company.com.

TIP OF THE MONTH

Maximize your retirement savings by paying tax now (Roth 401k) so you do not have to later.

Buying a Business with Your Individual(k) Plan

By: Keith Stunek

Use YOUR 401(k) or IRA Rollover Assets to
Finance YOUR Franchise or Business Start-up or Expand your business

If you have assets currently in a retirement plan, you may have the option of using these funds to purchase your own business or expand your current business with these assets.

An Individual(k) Plan is actually a Qualified Retirement Plan governed by the Internal Revenue Code of 401(a). What this means is that the investments allowed by these plans are more expansive than the investments allowed with an IRA. This allows you, as an individual, to actually use the assets held by these plans to purchase or invest in your business entity, such as a franchise.

The unique thing about an Individual(k) plan is you are allowed to MAXIMIZE your retirement plan funding, while MAXIMIZING your tax deduction and maintaining flexibility with the assets held by the plan.

Maximizing your retirement plan finding AND deduction with a Individual(k) plan allows you to contribute on an annual basis up to $50,000 for 2007. These contributions will be accounted for as follows:

- Employer contribution of up to 25% or your compensation
- Your salary deferral of $15,500 AND
- If you are over age 50, an additional $5,000

Example: Larry has an earned income of 200,000 per year. He is 54 years old and operates his business within a Corporation—*Larry Landscapes, Inc.*

For 2007, Larry will contribute as follows:

- $15,500 deferred
- $29,500 - 25% Employer Contribution
- $5,000 Catch up contribution

$50,000 – Total contribution

Individual(k) ROTH Provision:

With an Individual(k) plan, Larry has the choice of claiming the “deferral” amount (or any portion thereof) either as a tax deduction or as an after tax contribution as a Roth contribution. This would allow all the earnings on the deferral portion to potentially grow TAX FREE!

INTERESTING INSIGHTS

Have you determined your retirement income? Did you determine the tax consequences on the income? For information on a tax FREE retirement contact The Entrust Group.

Is your business your retirement? 40% of Americans consider that however, 60% of these individuals sell the business long before retirement. Will YOU have retirement savings for the years you operated your business for retirement?

Rollover contributions from existing retirement plans and/ or IRAs are also allowable which will increase the investment power of your Individual(k) plan.

The investment options with a Individual(k) plan are the same as any other retirement plan:

- Traditional Investments
- Self-Directed Investments
- Real Estate
- Limited Liability Company (LLC)
- ***Own your own business through your plan***
- ***Own a building with your plan and pay rent to your plan***

Individual(k) Qualifications:
To qualify for an Individual(k) plan, you must own or are in process of creating a business entity. The business should have no common law employees that work more than 1000 hours a year AND are over age 21, and your business must be profitable.

Once you have determined that you are eligible to establish an Individual(k) plan, you will need to establish the plan no later than 12/31/2007 for 2007.

Remember Larry the landscaper? Larry establishes an Individual(k) for 2007. Larry rolls over a $100,000 IRA Rollover from a previous employer that Larry worked for. Larry then makes a 2007 contribution of $50,000. Larry now holds $150,500 in his Individual(k) plan.

Larry incorporates his business and issues shares. Larry's Individual(k) plan "invests" $125,000 into the business and the shares are held by the Individual(k) plan. Larry then has an influx of $125,000 into the business with ability to purchase new mowers, trimmers, trailers, a new truck and a building to store the equipment.

The building that Larry buys contains four separate offices with a garage for each office. Larry the Landscaper rents from the Individual(k) plan of the four office/garage units. The remaining 3 units Larry rents to others that pay rent to the Individual(k) plan. This rent is "earnings" for the Individual(k) plan. The earnings is TAX DEFERRED.

In four years, Larry is approached to sell his business to a competitor. Larry sells the equipment, building and existing clients for $185,000. The gain of $60,000 PLUS the rent from the buildings for the 4 years is all TAX DEFERRED!

If you are looking to become a business owner or expand your business, and you're looking for ways to fund your endeavor, contact The Entrust Group office near you and learn how to use an Individual(k) plan to fund your business AND your retirement.

Keith Stunek is the Director of Training and Development for The Entrust Group.

What You Need to Know About Foreclosures – Crisis and Opportunity

By: Ben Brazda

After their honeymoon in the Florida Keys, Dennis and Sheryl Walker moved to Greeley, Colorado and soon purchased their first home with the help of a mortgage. Dennis sold used cars and Sheryl was on-call as a substitute teacher for the school district while she waited for a full-time opening. In spring of 2006, when they bought their home, the Walkers had a small down payment and they didn't have a very good credit score but were excited to hear that they could qualify for a loan. Sure, the loan was an adjustable rate mortgage (ARM) but this gave them the opportunity to become homeowners for the first time.

The Walkers enjoyed their first summer and fall as homeowners and then were dumped on with snow from one of the longest and coldest winters Colorado had seen in years. Lacking an established clientele, Dennis' sales fell and the teachers remained surprisingly healthy so Sheryl's pay wasn't enough to make up the difference. They soon had to dip into their savings to cover the mortgage payments, and they were quickly running out of savings. Once all that snow had melted in late spring, the Walkers were behind on payments and after their third "When can we expect your payment?" letter, they received a notice that their rate was adjusting upwards as was their payment. A month later they got a letter notifying them of their **default** (violation of the loan agreement) and that foreclosure proceedings had begun.

Unfortunately, the Walkers' story is not as rare as one would hope. Up until the recent sub-prime mortgage crash, many people like the Walkers were approved for loans for which they may not have been financially prepared. These loose and perhaps questionable lending practices played a large role in creating the current record-setting foreclosure market. This is bad news for homeowners like the Walkers, but to a savvy investor, this is opportunity knocking. The key to answering the knock is understanding how foreclosure works.

When a borrower defaults on a loan, the bank will **foreclose** on the property. In a foreclosure, the bank has the right to

have the property sold to pay off the loan. This is not a good option for the borrowers and is not something that the bank wants either. Because of this, the borrowers typically have the following options to cure the debt prior to foreclosure:

1. If Sheryl managed to find a full time position and Dennis' sales picked up again, they could ask to resume the loan (and have their missed payments added to the end of the loan.)

2. The Walkers could ask to have the loan re-cast with more favorable terms that they could handle.

3. The bank may allow the Walkers to sell the property to cover the debt. In some cases, the bank may accept this option even if the sale price is less than the loan balance (short-sale or short payoff).

4. If the bank doesn't want the Walkers to sell the property, it's possible that they may accept the Deed in Lieu of Foreclosure. In this scenario, the deed to the property is signed over to the bank in exchange for removing the debt.

5. A brand new option is the FHA Secure Initiative (Federal Housing Administration), which provides re-financing options to borrowers like the Walkers who are in trouble due to a rate increase.

An added benefit to using one of these options is that they avoid the legal process of a foreclosure. If a solution cannot be negotiated, the bank will take the required legal action against the borrowers and the property will be sold at auction.

The most common method of foreclosure is called a **judicial sale**. In this scenario the county clerk or other officer puts the property up for public auction and the bank places the first bid. At the auction, the property is sold to the highest bidder which, in some cases, ends up being the bank. The bank does not want to have to sell the property so they will frequently place a low initial bid to encourage other buyers to outbid them.

The proceeds from the sale go first to pay off the debt, then to other creditors and finally to the borrowers if anything is left. In cases where the proceeds are not enough to cover the debt, the bank can request a deficiency judgment against the borrowers which would give them access to their other assets.

To the ever-observant investor, there are quite a few investment opportunities here. The most obvious, of course, is attending the foreclosure auction. Other options may include negotiating with junior lien holders, negotiating a short-sale with the lender or working directly with the borrower. Because the foreclosure process is different in each state, the key to a successful foreclosure investment is intricate knowledge of the process and the players and knowing what each player wants and can realistically expect to get from the situation.

Lady Luck smiled down on Greeley, Colorado. After asking a few of their friends, the Walkers discovered that Mark, a friend for 25 years, had a dormant 401(k) account. Mark knew the Walkers well enough to know that they always land on their feet, so Mark saw this as a great investment. After working with Entrust and a title company, a Note and Deed of trust was drafted under terms the three of them had negotiated and before long the Walkers had re-financed with a loan from Mark's IRA.

In any case, having cash ready to go in an IRA or 401(k) is the key to jumping on an opportunity such as a foreclosure. The first step is contacting your IRA administrator for details on getting an account established and funded. Step two is doing your homework and finding a real estate agent with foreclosure experience. Then, it's up to you to find the investment and work with your IRA administrator to get the deal done.

**The foreclosure process varies significantly from state to state, yet some of the same elements can be found across the board. A helpful resource for learning about foreclosures in your area is http://www.foreclosurelaw.org/*

* For the full version of this article please email bbrazda@ndira.com

* Special thanks goes to Gene Hayden for his help on this article.

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