

Advanced Markets Matters

Form 1040 Opportunities

A Financial Professional's Guide



Form 1040: A Valuable Planning Tool

Your client's income tax return is a valuable planning tool. It details personalized financial circumstances and risk exposures. Let's examine various Form 1040 line items for the unique planning opportunities they may offer.

1040 – Line-by-Line

Use this guide in combination with our client-facing Form 1040 Opportunities Key (CF-70-50001):

Step 1: Familiarize yourself with this guide and Form 1040 before using the Key with clients.

Step 2: Place the Key beside a tax return. Review the highlighted line items. Create a conversation around the issues and concerns that are revealed.

Step 3: Take notes. Refer back to them when preparing for future client meetings.

Step 4: Take advantage of our marketing materials and other resources that address client needs.



1040 Opportunities: Line 7 – 8B

Line 7 – Wages

Generally, this is your client's total taxable wages (shown in box 1 of their W-2s). This is the money they earned from an employer. If married and filing jointly, both spouses' income is added together.

OPPORTUNITY

Income replacement should be considered for both spouses.

Going one step further and reviewing their W-2s may reveal amounts excluded from taxable income. Many W-2s show a summary of elective deferrals to 401(k)s, 403(b)s, 457(b)s, SIMPLE 401(k)s and SIMPLE IRAs. Designated Roth contribution amounts may also be listed.

OPPORTUNITY

Ask about your client's retirement savings plan and what percent of their current income they need in retirement. Annuities can be a retirement income source.

Line 8a – Taxable Interest

Interest income from a savings account, checking account, money market or CD is on this line. Bond interest may also be here. It's important to understand a client's reasons for choosing such low-risk, low-return taxable investments.

OPPORTUNITY

Fixed or indexed annuities may offer sufficient protection against market volatility while offering higher, tax-deferred returns. Life insurance can provide death benefits and may leverage a smaller amount into a larger gift or inheritance.

Proof Point: Financial Strength

If a client invests conservatively, highlight the financial strength of the insurance company. Review its Comdex ranking and industry ratings, as these may be important considerations.

Line 8b – Tax-Exempt Interest

Tax-exempt interest (such as from municipal bonds) is shown here, even though it's not taxable at the federal level. It's used in calculating taxability of income items such as Social Security benefits and may help push retiree income levels above a taxable threshold.

OPPORTUNITY

Money left to accumulate in a deferred annuity is not taxed until withdrawn. This may help reduce the amount of Social Security benefits subject to tax.

1040 Opportunities: Line 9a – 13

Line 9a – Ordinary Dividends

Depending on the source of your client's dividend income and if they count on it to pay living expenses, it may help to reposition the income into a tax-deferred or possibly tax-free investment. If a client is collecting Social Security, consider how much the dividend income affects taxation of the Social Security benefit. Money left to accumulate in a deferred annuity is not taxed until withdrawn. This may help reduce the amount of Social Security benefits subject to tax. Investment or passive income also exposes higher-earning clients to the risk of possibly paying an additional 3.8% in Medicare surtax on net investment income (NII).

OPPORTUNITY

If the dividends are unneeded for current income, they may provide a ready source to fund an annuity.

Line 12 – Business Income

Line 17 – Partnership/S Corporation Income

Line 28 – Self-employed SEP, SIMPLE and Qualified Plans

If your client has pass-through business income from a sole proprietorship, partnership, limited liability company or S corporation, contributions to a SEP, SIMPLE, or qualified plan can reduce taxable income and ensure they take advantage of incentives that encourage retirement saving. Review risk exposure, growth opportunity, income certainty, tax efficiency, and beneficiary protection of existing plans.

OPPORTUNITY

Evaluate whether existing plans meet client needs. If no amount is reported, discuss the advantages of such plans in retirement.

Planning Point: Pass-Through Deduction

There may be an additional incentive to lower taxable income for business owners of pass-through entities in 2018. The Tax Cuts and Jobs Act provides a new 20% deduction for certain pass-through business income. For 2018, the deduction is available in full for single filers with taxable income at or below \$157,500 and married filers with taxable income at or below \$315,000.

OPPORTUNITY

Contributions to a qualified plan are excludable from income. Using funds in taxable investments to purchase nonqualified deferred annuities may also make sense. The income earned on tax-deferred annuities is generally not included in income until distributed.

1040 Opportunities: Line 13 – 15

Line 13 – Capital Gain or Loss

Capital assets may expose higher-earning clients to an additional 3.8% Medicare surtax. Mutual funds and ETFs may generate capital gains (short-and long-term) from intra-fund trading.

OPPORTUNITY

Discuss the impact of taxes on investment return and the benefits of tax-deferred compounding.

Line 15 – IRA Distributions

Total IRA distributions are on line 15a, including distributions from traditional IRAs, Roth IRAs, SEPs and SIMPLE IRAs; the taxable portion of distributions is on line 15b. Many IRA distributions are fully taxable, with the same amount reported both places. If different, then either nondeductible contributions or Roth contributions/conversions were made. Clients can exclude nondeductible contributions only if they filed Form 8606 in years contributions were made or distributed. While Roth contributions are not on the 1040, the taxable amount of Roth conversions and distributions is on Line 15b.

OPPORTUNITY

Is this rate of distributions/withdrawals sustainable? Clients worried about running out of money can consider annuity products with lifetime income options. If the income is not needed, clients can explore using these funds to purchase life insurance, possibly with an accelerated death benefit rider to help cover future long-term care costs.

OPPORTUNITY

If RMDs must be taken but are unneeded, a qualified charitable distribution (QCD) may be an option. It allows annual direct transfers to a charity up to \$100,000 of tax-deferred IRA savings. Excluding such amounts can keep them from increasing adjusted gross income and triggering increased income taxes on Social Security benefits and increased Medicare insurance premiums.

Practice Point: IRA Documentation

Counsel clients to save certain forms:

- Form 5498s (IRA Contribution Information)
- Form 1099-Rs (Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.)
- Form 8606s (Nondeductible IRAs)

Roth IRA contributions are not reported on tax documents but clients should keep track of them. It's their responsibility to show that IRA distributions are not taxable (because either amounts were already taxed or are Roth IRA tax-free qualified distributions).



1040 Opportunities: Line 16 – 32

Line 16 – Pension and Annuity Distributions

Total pension and annuity distributions are on line 16a; the taxable portion is on line 16b. Most pension distributions are fully taxable, with the same amount in both places, unless the client contributed after-tax contributions to the employer plan or contributed to a Roth 401(k). Contributions to nonqualified annuities are recovered either on a pro rata basis (if annuitized) or on a last-in-first-out (LIFO) basis (if a withdrawal).

OPPORTUNITY

Don't be misled by the word "pension" in the title. All employer qualified plans are reported here. Employer plans and nonqualified annuities can be reviewed for fund appropriateness and lifetime income opportunities.

Line 20 – Social Security Benefits

If your client receives Social Security benefits, they may be retired and living on a fixed income. Do they know a portion of their Social Security benefits may be taxable?

OPPORTUNITY

This is an opportunity to discuss tax-efficient products.

Line 32 – IRA Deduction

Contributions to Traditional IRAs may be deductible if client income is within certain limits or clients/spouses are not participating in employer retirement plans.

OPPORTUNITY

If clients are not eligible to make deductible contributions, they may be able to make Roth IRA contributions. If they have too much income to contribute to a Roth, they can still contribute to a nondeductible IRA.

Note: To make any contribution to any IRA, clients must have compensation.

2018: Roth and Tax Reform

Planning Point: Roth IRA Opportunity

Roth IRAs may make more sense since tax reform. They are generally indicated if taxpayers believe taxes will be higher at distribution time than at contribution time. Under the new tax act, individual tax rates are reduced and income thresholds modified. These lower rates are scheduled to expire at the end of 2025 and revert to the higher 2017 rates in 2026. So with income taxes “on sale,” it may make sense to contribute to Roth accounts to the extent possible.

Taxpayers who make too much money to contribute directly to a Roth IRA may be eligible for an employee’s Roth 401(k). If not, they can make a nondeductible contribution to a traditional IRA (if under 70½). They can then convert the traditional IRA to a Roth IRA. Currently, there are no income limits on nondeductible contributions to traditional IRAs and none on converting a traditional IRA to a Roth IRA. If a taxpayer does not have money in any traditional IRAs, the after-tax IRA funds are converted tax free. If a taxpayer has pre-tax money in any traditional IRA, tax is due on the conversion.

It may even make sense for IRA owners to convert traditional IRAs each year if they can do so in lower income tax brackets. IRA owners who expect they and their beneficiaries will always be in a very high tax bracket may want to convert their entire IRA as quickly as they can. It’s important to consider the effect of conversion and increased AGI on the capital gains tax rate, the taxation of Social Security benefits and the increase in Medicare premiums.



1040 Opportunities: Line 56 – 62

Line 56 – Taxes

If the client owes taxes, there may be opportunities to reduce the amount of future taxable income.

OPPORTUNITY

Explore the opportunities in IRAs and qualified retirement plans as well as in nonqualified annuities and life insurance.

Line 59 – Additional Tax on IRAs, Other Qualified Retirement Plans, etc.

Certain penalty taxes are on this line. If there is an amount here, they may have taken a distribution from an IRA or qualified plan too early or too late, or contributed (and not withdrawn) more than allowed in a tax year, or they may have taken a distribution too early from a modified endowment contract (MEC) or nonqualified annuity. If they took a distribution from an IRA, qualified plan or nonqualified annuity subject to the 10% early distribution penalty, discuss whether other funds are needed prior to age 59½ and evaluate trying to satisfy the series of substantially equal periodic payments exception to the early distribution penalty.

OPPORTUNITY

If missing RMDs is a concern, then a qualified single premium immediate annuity may make sense – allowing clients to “fix it and forget it.” A qualified SPIA generally meets RMD rules for the annuitized portion of an account as long as distributions are paid for no longer than the client’s expected lifetime (or the expected lifetimes of the client and beneficiaries) and certain other requirements are met.

Line 62 – Taxes from Form 8960 (Net Investment Income Tax)

If your client checked the box for Form 8960, they are subject to an additional penalty tax on net investment income (NII). For 2018, the NII penalty tax of 3.8% is applied to the lesser of a client’s total NII or the amount their modified AGI exceeds the following threshold limits: \$250,000 for married filing jointly; \$200,000 for single, head of household or qualifying widow(er); and \$125,000 for married filing separately.

OPPORTUNITY

Discuss strategies to reduce NII and/or modified AGI. Non-taxable and tax-advantaged investments, such as Roth accounts and life insurance, can be exempt from income tax and NII tax. Nonqualified annuities grow tax-deferred and are not subject to income tax or NII tax until distributed. Maximizing excludable contributions to 401(k) plans and other qualified plans can also reduce modified AGI.

1040 Opportunities: Line 62 – 75

Line 75 – Refund

If your client is getting a refund, they may already have plans for spending or saving the extra money. But you may be able to show the client options that change their mind and put the money to better use in reaching retirement or legacy planning goals.

OPPORTUNITY

If your client is interested in any of the concepts revealed by a review of the Form 1040 Opportunities Key, a refund may be a source to fund their plans.

*Make Tax Time a
Time of Opportunities*



1040 Opportunities Key: Questions to Ask

Consider these questions to see where retirement and protection strategies may address your client's financial needs.

A Line 7 – Wages: How will you or your family replace income if you retire or become disabled?

B Line 8a – Taxable Interest: How is this invested? Are you interested in tax-deferred or tax-free income, or legacy planning?

C Line 8b – Tax-Exempt Interest: Is this reinvested? What role does this play in your financial plan?

D Line 9a – Ordinary Dividends: Is your dividend income consistent? Are you reinvesting? What role does this play in your financial plan?

E Line 12 – Business Income/ Line 17 – Partnership & S Corporation Income/ Line 28 – Self-Employed SEP, SIMPLE & Qualified Plans: Are you saving enough for retirement? Are you maximizing contributions? Do you want to lower taxes or invest more tax-deferred or tax-free?

F Line 13 – Capital Gain or Loss: How do taxes affect your rate of return?

G Line 15 – IRA Distributions: Are you retired? Was this planned? Can you sustain this? Is it a required distribution? Do you need this in retirement?

H Line 16 – Pension and Annuity Distributions: Are you retired? Does this meet your income needs? What happens when you die?

The image shows a 2017 U.S. Individual Income Tax Return (Form 1040) with various lines highlighted and labeled with letters A through J. The labels correspond to the questions listed on the left side of the page. The form includes sections for Filing Status, Exemptions, Income, Adjusted Gross Income, and various deductions. The labels A through J are placed over specific lines on the form: A is over Line 7 (Wages), B is over Line 8a (Taxable interest), C is over Line 8b (Tax-exempt interest), D is over Line 9a (Ordinary dividends), E is over Line 12 (Business income), F is over Line 13 (Capital gain or loss), G is over Line 15 (IRA distributions), H is over Line 16 (Pension and annuity distributions), I is over Line 20 (Social Security benefits), and J is over Line 32 (IRA deduction).

I Line 20 – Social Security Benefits: Have you done Social Security planning? Do you depend on this to meet everyday expenses?

J Line 32 – IRA Deduction: Are you or your spouse maximizing any deduction? Have you considered Roth IRA contributions or traditional IRA nondeductible contributions?

K Line 56 – Taxes: How do you feel about this number? Do tax rate changes affect you? Does taxation impact your retirement income?

L Line 59 – Additional Tax on IRAs, Other Qualified Retirement Plans: Did you take a distribution from an IRA or qualified plan too early or too late or contribute more than allowed? Did you take an early distribution from a modified endowment contract or nonqualified annuity?

M Line 62 – Taxes from Form 8960: Would you like to reduce or eliminate this?

N Lines 75 – Refund: Do you have plans for your refund? Talk to a financial professional first about how to make this refund work for you.

Form 1040 (2017) Page 2

Tax and Credits

38 Amount from line 37 (adjusted gross income) 38

39a Check ☐ You were born before January 2, 1953. ☐ Blind. Total boxes ☐ 39a

if: ☐ Spouse was born before January 2, 1953. ☐ Blind. checked ☐ 39a

b If your spouse itemizes on a separate return or you were a dual-status alien, check here ☐ 39b

40 Itemized deductions (from Schedule A) or your standard deduction (see left margin) 40

41 Subtract line 40 from line 38 41

42 Exemptions. If line 38 is \$155,000 or less, multiply \$4,050 by the number on line 55. Otherwise, see instructions 42

43 Taxable income. Subtract line 42 from line 41. If line 42 is more than line 41, enter -0- 43

44 Tax (see instructions). Check if any from: a ☐ Form(s) 8814 b ☐ Form 4972 c ☐ 44

45 Alternative minimum tax (see instructions). Attach Form 6251 45

46 Excess advance premium tax credit repayment. Attach Form 8962 46

47 Add lines 44, 45, and 46 47

48 Foreign tax credit. Attach Form 1116 if required 48

49 Credit for child and dependent care expenses. Attach Form 2441 49

50 Education credits from Form 8863, line 19 50

51 Retirement savings contributions credit. Attach Form 8880 51

52 Child tax credit. Attach Schedule 8812, if required 52

53 Residential energy credits. Attach Form 5695 53

54 Other credits from Form: a ☐ 3800 b ☐ 8801 c ☐ 54

55 Add lines 48 through 54. These are your total credits 55

56 Subtract line 55 from line 47. If line 55 is more than line 47, enter -0- 56

Other Taxes

57 Self-employment tax. Attach Schedule SE 57

58 Unreported social security and Medicare tax from Form: a ☐ 4137 b ☐ 8919 58

59 Additional tax on IRAs, other qualified retirement plans, etc. Attach Form 5329 if required 59

60a Household employment taxes from Schedule H 60a

b First-time homebuyer credit repayment. Attach Form 5405 if required 60b

61 Health care: individual responsibility (see instructions). Full-year coverage ☐ 61

62 Taxes from: a ☐ Form 8959 b ☐ Form 8960 c ☐ Instructions; enter code(s) 62

63 Add lines 56 through 62. This is your total tax 63

Payments

64 Federal income tax withheld from Forms W-2 and 1099 64

65 2017 estimated tax payments and amount applied from 2016 return 65

66a Earned income credit (EIC) 66a

b Nontaxable combat pay election 66b

67 Additional child tax credit. Attach Schedule 8812 67

68 American opportunity credit from Form 8863, line 8 68

69 Net premium tax credit. Attach Form 8962 69

70 Amount paid with request for extension to file 70

71 Excess social security and tier 1 RRTA tax withheld 71

72 Credit for federal tax on fuels. Attach Form 4136 72

73 Credits from Form: a ☐ 3408 b ☐ 8885 c ☐ 8885 d ☐ 73

74 Add lines 64, 65, 66a, and 67 through 73. These are your total payments 74

Refund

75 If line 74 is more than line 63, subtract line 63 from line 74. This is the amount you overpaid 75

76a Amount of line 75 you want refunded to you. If Form 8878 is attached, check here ☐ 76a

b Routing number 76b

c Type: ☐ Checking ☐ Savings 76c

d Account number 76d

77 Amount of line 75 you want applied to your 2018 estimated tax 77

78 Amount you owe. Subtract line 74 from line 63. For details on how to pay, see instructions 78

79 Estimated tax penalty (see instructions) 79

Third Party Designee

Do you want to allow another person to discuss this return with the IRS (see instructions)? ☐ Yes. Complete below. ☐ No

Designated person's name Phone no.

Personal identification number (PIN)

Sign Here

Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and accurately list all amounts and sources of income I received during the tax year. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Joint return? See instructions. Keep a copy for your records. ☐ Yes ☐ No

Your signature Date Your occupation Daytime phone number

Spouse's signature. If a joint return, both must sign. Date Spouse's occupation

If the IRS sent you an Identity Protection PIN, enter it here (see inst.):

Paid Preparer Use Only

Print/Type preparer's name Preparer's signature Date

Check ☐ if self-employed ☐ if not

Firm's name Firm's EIN

Firm's address Phone no.

Go to www.irs.gov/Form1040 for instructions and the latest information. Form 1040 (2017)

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No bank guarantee	Not a deposit	May lose value	Not FDIC/NCUA insured	Not insured by any federal government agency
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