CIA Report

Financial Intelligence

Capital Intelligence Associates
Arthur Kraus, ChFC, CLU, CAP
Mitchell Kraus, CFP®, CLU, ChFC, CAP
1250 6th Street, Ste. 300
Santa Monica, CA 90401
310-820-9797
akraus@capintelligence.com
www.capintelligence.com

Upcoming Webinars

Strategies for Charitable Giving Oct. 22, 2014, 1:30 PM
Do you want to give more or give smarter? This seminar covers the Elements of Charitable Giving, Tools and Techniques you can use and finally we give some Planning Tips.

Connecting with Grandchildren Nov. 20, 2014, 11:30 AM
Have grandchildren? Want to learn how to better help them in their lives. This seminar will give ideas on how to connect with them, teach them and support them

Social Security, Medicare and Your Retirement Dec. 16, 2014 1:00 PM
This seminar will explain how Social Security & Medicare work, what is being done to ensure their survival, and how you can plan for your retirement & medical care so that they do not have to rely heavily on either program

October 2014

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Christmas Already?

As we write this newsletter in late September, we have started to notice Christmas decorations being sold at some of our local stores. We remember when the holiday season didn't start until after Thanksgiving. More recently Christmas goods weren't sold until after Halloween. Now it seems the beginning of fall is when some start thinking about the holidays.

With that in mind, and knowing that this is our last newsletter until 2015, we thought we'd take this time when often families get together for the holidays to talk about passing on more than just your financial assets, but ways to share what is important to you when your family gets together in the months to come and ways to make a difference individually.

The American dynasty families such as the Rockefellers and Carnegies have family meetings each year where multiple generations come from far and wide to discuss family business and to make sure they're educated on items of importance to the family that aren't taught in school. While their wealth is out of reach or impractical for most American families, its easy to use the holidays as a time to reflect and share important values to future generations.

In the Kraus household, it is Thanksgiving that we almost always have all 3 generations of Kraus' in one place. (Art and Rini, 4 sons, 3 wives and 9 grandchildren). Art uses that time with everyone together to share stories and tell what he has learned to be important of over his lifetime. Grandchild #3, Cameron has had projects through school to have everyone in the family what they are thankful for and reads all the statements aloud to the group.

Another way to make a difference is through philanthropy. When they were kids, Mitchell and his brothers were taken by their parents to skid row during the holidays to feed the homeless. How times have changed as there are many groups that do it now in masse and its a great way to give back with others.

Besides donating time, overall giving to charities goes up during the holiday season. Think about taking it a step further in your family. Instead of just writing a check to your favorite cause, think about bringing your children (of any age) into the equation. Ask them what causes they care about and in addition to the normal gifts you give, think about donating to your kids (or grandkids) favorite causes.

If you want to go to another level, consider setting up a Family Foundation or Donor Advised Fund. While the mechanics are too complicated for this article, the idea is you can set aside a bunch of money now, get the tax deduction, and give it out whenever you choose. Many families make formal or informal boards with their kids and grandkids to decide where the money goes. It's a great way to make a difference and to teach future generations about the underlying investments and values at the same time.

We know that many of you think the original meaning has been lost in the holiday season. It has become about gifts and sporting events and not about tradition and family. If you are looking at ways to pass on more than your assets, let us know and we'll talk. Because It's Your Legacy.™

Webinar Series

We have found that many of our client have the same concerns and interests and want to learn more. With clients across the country (and with LA Traffic) we find it tough to get together to have learning experiences. So, we're starting a monthly webinar series. Details are to the left. We hope you can listen live. The link to RSVP is on our website under Resources/CIA Seminar Series.

The goal is to be interactive, but if you can't make it, replays will be available a few days after completion.

Leaving Assets to Your Heirs: Income Tax Considerations

An inheritance is generally worth only what your heirs get to keep after taxes are paid. Here we have focused primarily on federal income taxes. Depending on your circumstances, you may wish to also consider federal estate tax and state income, estate, and inheritance taxes.

Note: It is generally recommended that you designate IRA and other retirement plan beneficiaries, their shares, and any backup beneficiaries on the plan beneficiary form. This will help assure that retirement plan benefits pass as you wish at your death and that a beneficiary will be able to stretch distributions over his or her remaining life expectancy.

An inheritance is generally worth only what your heirs get to keep after taxes are paid. So when it comes to leaving a legacy, not all property is created equal--at least as far as federal income tax is concerned. When evaluating whom to leave property to and how much to leave to each person, you might want to consider how property will be taxed and the tax rates of your heirs.

Favorable tax treatment for heirs

Roth IRAs

Assets in a Roth IRA will accumulate income tax free and qualified distributions from a Roth IRA to your heirs after your death will be received income tax free. An heir will generally be required to take distributions from the Roth IRA over his or her remaining life expectancy. (Of course, your beneficiaries can always withdraw more than the required minimum amounts.) If your spouse is your beneficiary, your spouse can treat the Roth IRA as his or her own and delay distributions until after his or her death. So your heirs will be able to continue to grow the assets in the Roth IRA income tax free until after the assets are distributed; any growth occurring after funds are distributed may be taxed in the future.

Note: *The Supreme Court has ruled that inherited IRAs are not retirement funds and do not qualify for a federal exemption under bankruptcy. Some states may provide some protection for inherited IRAs under bankruptcy. You may be able to provide some bankruptcy protection to an inherited IRA by placing the IRA in a trust for your heirs. If this is a concern of yours, you may wish to consult a legal professional.*

Appreciated capital assets

When you leave property to your heirs, they generally receive an initial income tax basis in the property equal to the property's fair market value (FMV) on the date of your death. This is often referred to as a "stepped-up basis," because basis is typically stepped up to FMV. However, basis can also be "stepped down" to FMV.

If your heirs sell the property with a stepped-up (or a stepped-down) basis immediately after your death for FMV, there should be no capital gain (or loss) to recognize since the sales price will equal the income tax basis. If they sell the property later for more than FMV, any appreciation after your death will generally be taxed at favorable long-term capital gain tax rates. If the appreciated assets are stocks, qualified dividends received by your heirs will also be taxed at favorable long-term capital gain tax rates.

Note: *If your heirs receive property from you that has depreciated in value, they will receive a basis stepped down to FMV and will not be able to claim any loss with respect to the depreciation before your death. You may want to consider selling depreciated property while you are alive so that you can claim the loss.*

Not as favorable tax treatment for heirs

Tax-deferred retirement accounts

Assets in a tax-deferred retirement account (including a traditional IRA or 401(k) plan) will accumulate income tax deferred within the account. However, distributions from the account will be subject to income tax at ordinary income tax rates when distributed to your heirs (if there were nondeductible contributions made to the account, the nondeductible contributions can be received income tax free). An heir will generally be required to take distributions from the tax-deferred retirement account over his or her remaining life expectancy. (Of course, your beneficiaries can always withdraw more than the required minimum amounts.) If your spouse is the beneficiary of the account, the rules may be more favorable. So your heirs will be able to defer taxation of the retirement account until distribution, but distributions will generally be fully subject to income tax at ordinary income tax rates.

Note: *Your heirs do not receive a stepped-up (or stepped-down) basis in your retirement accounts at your death.*

Even though distributions are taxable, your heirs will nevertheless generally appreciate receiving tax-deferred retirement accounts from you. After all, they do get to keep the amounts remaining after taxes are paid.

Toxic or underwater assets

Your heirs might not appreciate receiving property that is subject to a mortgage, lien, or other liability that exceeds the value of the property. In fact, an heir receiving such property may want to consider disclaiming the property.

Always nice to receive

Life insurance and cash

Life insurance proceeds received by your heirs will generally be received income tax free. Your heirs can generally invest life insurance proceeds and cash they receive in any way that they wish. When doing so, yours heirs can factor in how the property will be taxed to them in the future.

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The Potential Pitfalls of DIY Estate Planning

The one-size-fits-all, fill-in-the-blank forms that do-it-yourself estate planning sources provide may be attractive to some individuals because they cost a fraction of what attorneys typically charge. But is saving a few dollars worth the risk of doing things incorrectly?

Americans, by and large, are do-it-yourselfers. Books, websites, software programs, and even giant box stores exist solely to help ambitious Americans tackle all kinds of everyday challenges, from fixing leaky faucets to building backyard sheds. The same holds true for estate planning--there's certainly no dearth of information for those wanting to prepare their own wills and other important documents. However, do-it-yourselfers may want to exercise a bit of caution here.

Although do-it-yourself (DIY) estate planning can cost a fraction of what attorneys charge, depending on your personal situation, this may be a case of being penny-wise and pound-foolish.

Cheap, easy, and better than nothing

Proponents of DIY estate planning typically have two arguments:

1. **It's cheap and easy:** Creating a will and other estate planning documents on your own can cost far less than doing so with an attorney's assistance. You can find resources online and in the library that could help.
2. **It's better than nothing:** What happens if you die or become very ill without important estate planning documents? In that case, the state will make important decisions for you, such as how your property will be distributed, who will care for your minor children, and what medical care you'll receive if you are unable to make your wishes known.

These points are valid: For those who cannot afford to pay an attorney, DIY may be an economical alternative. For others, a poorly drafted will may be better than no will at all, especially when naming a guardian for minor children is involved. But there are several risks to DIY estate planning, including the risk that your wishes will not be carried out exactly as you intend.

Basic is not always ideal

Although DIY sources can typically handle the needs of simple estates, they generally are not appropriate for even the most common complexities such as children from a prior marriage, children with special needs, property that has appreciated in value resulting in capital gains, and estates that are large enough to be subject to estate taxes (typically those worth more than $5,340,000 in 2014). Also, DIY sources generally fail to take advantage of sophisticated estate planning strategies because they usually can't account for an individual's unique circumstances.

Further, you may make an error by failing to understand the instructions or by following the instructions incorrectly.

The result is that the documents you create could be invalid, ineffective, or contain legal language having consequences you never intended. You might not know if that is the case during your lifetime, but at your death your loved ones will find out and may suffer the lasting consequences of your mistakes.

You may benefit from legal advice

DIY sources provide forms but not legal advice. In fact, these sources clearly state that they are not a substitute for an attorney, and that they are prohibited from providing any kind of legal advice.

Estate planning involves a lot more than producing documents. It's impossible to know, without a legal education and years of experience, what the appropriate legal solution is to your particular situation and what planning opportunities are available. The actual documents produced are simply tools to put into effect a plan that is specifically tailored to your circumstances and goals.

Estate planning laws change

Laws are not static. They constantly change because of new case law and legislation, especially when it comes to estate taxes. Attorneys keep up with these changes. DIY websites, makers of software, and other sources may not do as good a job at keeping current and up-to-date.

Fixing mistakes can be costly and time-consuming

As previously stated, working with an attorney to create your estate planning documents can be very expensive, costing anywhere from several hundred to several thousands of dollars, depending on the complexity of your estate. But these costs are minor compared to the costs and frustrations that your loved ones may experience if there are serious errors in your DIY estate plan. Many more thousands of dollars and many hours with attorneys may have to be spent to undo what was done wrong. Before embarking on a DIY estate plan, consider these risks very carefully.

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Arthur Kraus, ChFC, CLU, CAP
1250 6th Street, Ste. 300
Santa Monica, CA 90401

Arthur D. Kraus and Mitchell S. Kraus are registered representatives with and securities offered through LPL Financial, Member FINRA/SIPC

This information is not intended to be a substitute for specific individualized tax advice. We suggest that you discuss your specific tax issues with a qualified tax advisor.

I'M AFRAID THERE'S NOTHING I CAN PRESCRIBE FOR PERSONAL FINANCIAL DISORDER.