Schneider
WEALTH STRATEGIES

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WEALTH MANAGEMENT REPORT

Five Tax-Smart Ways To Transfer Your Wealth

If you're like most well-to-do people, one of your main financial objectives is to transfer wealth to your heirs with a minimum of tax erosion. Several estate planning techniques could help you move closer to that elusive goal. Consider these five opportunities:

1. Lifetime gifts. One of the simplest wealth transfer methods also can be one of the most effective. By giving away property to other family members during your lifetime, you remove those assets from your taxable estate. If you plan carefully, you can make direct gifts without incurring any gift tax liability. And you also may be able to leave assets to your heirs under favorable tax conditions.

The primary tax breaks are:

- An annual gift tax exclusion covering transfers of up to $14,000 per year per recipient ($28,000 for gifts by a married couple). You can make these gifts to as many people as you like.
- In addition, everyone is entitled to transfer a total of $5.49 million in 2017 (the amount is indexed to inflation) in lifetime gifts and bequests without tax consequences.
- Inherited property currently benefits from a "step-up" in basis—the value of the assets, for calculating taxable investment gains, is what they're worth at the death of the person who made the bequest, rather than when he or she acquired them. That can reduce future taxes. (But note that lifetime gifts don't get a step-up.)

2. Intra-family loans. Usually, you can lend up to $10,000 to a child or another relative with no strings attached—and no questions asked by the IRS. You don't even have to charge interest. However, if the borrowed amount exceeds $10,000 and you don't charge a reasonable interest rate, the IRS will consider the amount you didn't charge as interest income to you. One exception is that on loans of $100,000 or less, the amount of interest you're treated as receiving annually for tax purposes is limited to the child's net investment income for the year.

3. Dynasty trusts. This type of trust is designed to span several generations. You transfer selected assets—say, a combination of stocks, bonds, and real estate—to a trust managed by an independent trustee, usually a professional or financial entity. The trust may be created during your lifetime or through your will. Once the trust is established, it is irrevocable, so you give up control over the assets and the right to change beneficiaries. Depending on the terms, income may continue to accumulate within the trust or be paid out to beneficiaries. The trustee also may have discretion to use part of the principal for the health, education, support, and maintenance of the beneficiaries, or under other circumstances.

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The Best Places In The Country To Retire

"**Go west, young man, go west"** was an expression first used by John Babsone Lane Soule in the *Terre Haute (*Indiana*) Express* in 1851. It appealed to famed New York journalist Horace Greeley, who rephrased it in an editorial in the *New York Tribune* in 1865: "Go West, young man, and grow up with the country."

The country indeed has grown up in the past century and a half, and the new advice well could be, "Go south, old man [or woman], go south."

That's essentially what the website WalletHub reported recently when it compared information about 150 metro areas and listed what it calls the best places in the country to retire. Topping the list was Orlando, FL, with Tampa, FL, coming in second. Florida cities took three of the top four spots with Miami picked as No. 4 best place to retire. Cape Coral came in seventh, giving the Sunshine State four of the top 10 rankings.

Scottsdale, AZ, was ranked third best and Sioux Falls, SD, fifth. Rounding out the top 10 were Las Vegas, NV, sixth, Atlanta, GA, eighth, Minneapolis, MN, ninth, and Los Angeles, CA, tenth.

Sioux Falls fifth? How did a far-flung area in the Snow Belt get such a lofty rating?

WalletHub statisticians used four sets of criteria in arriving at their conclusions: cost of living, recreational activities, quality of life, and health care availability.

Sioux Falls ranked No. 1 in health care and No. 19 in affordability.

By comparison, San Francisco, CA. – No. 11 – ranked No. 1 in activities, but came in as the 146th most expensive place to live in the U.S.

Teach Employees About Computer Scams

Computer criminals seem to be stepping up their efforts to steal your personal and financial information—and your money.

The two most common approaches are the "tech support" scam, aimed primarily at individuals, and the "ransomware" scam, mostly used against businesses.

In a typical tech support scam, unsolicited phone callers say they are calling about "Windows," the popular operating system of computer software giant Microsoft. Don't believe it.

Microsoft says it never makes unsolicited phone calls about Windows computer problems.

Do not allow such a caller to take control of your computer. Hang up the phone immediately. This scam has been around since 2009.

Ransomware schemes have been around even longer, since 1989 when a disturbed biologist sent infected floppy discs to an AIDS conference sponsored by the World Health Organization.

This scam is aimed at businesses primarily because all it takes is for one employee to click on a link that then allows a scammer to take control of a business's computer system by shutting down the system or paralyzing it with encrypted, unintelligible jargon.

The scammer then demands a ransom, usually to be paid through an untraceable virtual currency such as bitcoin, to unlock the system and return it to normal.

The Federal Bureau of Investigation estimates that since 2015, U.S. companies have paid a total of $25 million to ransomware scammers.

The ransomware scam can start with a phone call much like the ones used by tech support scammers. In such a case, an employee is urged to allow the caller to obtain access to a business's computer system. Again, don't do it! Ever!

Today's version of the increasingly complicated scam also can start with a "phishing" email that asks a business computer user to click on a link to a website, article, or photograph that appears to be legitimate.

Scammers, in fact, are adept at creating legitimate-looking company names, fake caller IDs, and bogus company logos.

Business owners may be able to avoid these pitfalls by educating their employees about ransomware scams and how they work.

First, tell your employees never to take an unsolicited phone call from a stranger and then allow the caller access to your company's computer system.

Tell your employees not to rely on caller ID numbers to authenticate calls.

Also tell them about phishing emails that offer information or rewards if an enclosed link is clicked on.

Tell them never to click on a link from an unknown source, even if the email contains a legitimate-looking company name and logo.

If your employees don't know the source of an email, tell them not to click on a link or attachment – ever! ●

Sidestepping A Life Insurance Trap

Life insurance can be a lifesaver for a family whose main breadwinner unexpectedly passes away. But there may be steps you should consider that go beyond buying sufficient coverage to protect your family.

A primary goal is to keep life insurance proceeds from being included in your taxable estate, which could reduce their value. Normally, that will happen if the proceeds are payable to the estate or are received by someone else for the benefit of the estate. So the first step in avoiding this trap is to designate beneficiaries such as a spouse or a child who don't fall into those categories and to grant them full control over those assets. But that may not be the entire solution.

Even if proceeds aren't made payable to the estate, they count as assets of the insured person's taxable estate if he or she possessed "incidents of ownership" in the policy on the date of death. Furthermore, this rule applies to any incidents of ownership transferred during the final three years before death.

What is an "incident of ownership"? The definition goes beyond mere legal ownership and rights to the economic benefits of a policy. The list includes items such as the power to change beneficiaries; to revoke assignments of benefits; to obtain loans against the policy's cash value; to pledge the policy as collateral for a loan; and to surrender or cancel the policy. But the right to receive dividends and the right to veto the sale of an insurance policy by a trustee of an irrevocable life insurance trust aren't considered incidents of ownership.

If you buy life insurance and transfer all incidents of ownership in the policy more than three years before your death, all of the proceeds will be exempt from

Take Your Best Shot At College Financial Aid

Will your child enter college soon? However much you have managed to save, it may fall short of the very high cost of today's higher education. Financial aid—in the form of grants, loans, or work-study programs—could help make up the difference, but your child will have to apply for this needs-based aid, and that means completing the Free Application for Federal Student Aid, or FAFSA.

Even if you don't think you'll qualify for financial aid, there's no harm in trying, and you may be surprised by the results. Even students from the wealthiest families are eligible for work-study programs. And some colleges offer generous aid packages to families with relatively high incomes. So filling out the FAFSA almost always makes sense.

Nuts and Bolts of the FAFSA

The FAFSA form can be daunting. It has 130 questions about your family's assets and income. You'll have to enter information about the size of your household, your family income, the number of students in college, and most of your assets, though retirement savings are excluded. Your answers are used to determine your "expected family contribution," or EFC. That's the amount you'll be expected to contribute to your student's college education for one year. The lower the EFC, the more financial aid you may be entitled to receive.

The FAFSA is available online at www.fafsa.ed.gov. Due to a recent change, you now can file the FAFSA for the 2017-18 school year as early as October 1, 2016. (Previously, you would have been required to wait until January 1, 2017). File the form as early as possible because financial aid often is awarded on a first-come, first-served basis.

To fill out the form, you'll need detailed income and expense data from the "base year" for the student and the parents. Some common income items are:

- Wages, salaries, commissions, and tips
- Self-employment income
- Taxable interest
- Dividends and capital gains
- IRA distributions
- Pensions and annuities
- Rental income
- Income from alimony payments

Under another change, the base year for the 2017-2018 school year is the 2015 tax year. (It would have been 2016 before.) And it's the base year—not the year your child will be entering school—that really matters.

If you still have a few years before your child heads off to college, you may be able to take steps to minimize your income in the base year that's used for FAFSA calculations. Again, the base year is the tax year that ends more than a year and a half before your child starts school. So, if your son or daughter begins classes in the fall of 2018, 2016 is the base year to focus on. For 2019, it's 2017, and so on.

7 Ways to Reduce Base-Year Income

These seven strategies could help you reduce your adjusted gross income (AGI) for FAFSA purposes—and might have tax benefits as well:

1. Transfer income-producing assets to your child. This can help because your income counts against financial aid more than your child's does. And at least some of the future earnings on those assets will be taxed at your child's lower rate.

2. Sell off stock losers. If you unload losing positions, you can use those losses to offset any capital gains plus up to $3,000 of ordinary income. That could limit your income in the base year.

3. Hold onto stock winners. Not selling assets at a profit, meanwhile, could also minimize your income. In both cases, though, you need to consider the investment prospects of the assets as well as the potential tax implications.

4. Contribute more to your 401(k). The money you have in your employer-sponsored retirement plans and IRAs doesn't count against you in the FAFSA calculations. Increasing your contribution can help reduce your AGI while at the same time you save more for retirement.

5. Postpone year-end bonuses. If you're in line for a large bonus at the end of the base year, see whether you can arrange to receive the payment in January rather than December.

6. Launch a new business venture. Most new companies show a loss in the first year of operation. That could help offset your income from other sources.

7. Borrow against your home. Loans don't count as income. If you need cash, you might tap into home equity rather than selling off securities and raising your AGI.

Be aware that some schools also require the CSS Profile for financial aid. This form requires more information than the FAFSA.

You'll need to file a FAFSA for every year that your child is in college. But the optimal approach is to maximize benefits in the first year and go from there. Your financial advisers can help. ●

federal estate tax. Although the transfer is subject to gift tax, in most cases you can shield the transfer from tax through the annual gift tax exclusion and generous unified estate and gift tax exemption. Or you might create an irrevocable life insurance trust, which also can help shield proceeds from estate tax.

Big changes in the estate and gift tax laws could be coming, but now is an opportunity to protect your interests under current law without risking future harm. ●

What's The Truth About Probate?

Have you heard horror stories from families that had to suffer through costly, protracted probate proceedings after a relative dies? The possibility is very real, especially if a will is contested. Yet while it might turn into a nightmare, sometimes probate works like a dream. Before you take drastic steps to avoid probate, it's important to know what it's likely to involve.

The first thing to know is that laws concerning probate vary from state to state. In some states, the process may be quick, while in others it's likely to be costly and take a while.

Probate is the court-supervised process of distributing the assets of someone who has died, according to that person's will. Even when there's no will, however, assets usually still have to go through probate. Among the exceptions are assets that pass via beneficiary designation, which normally can go to designated beneficiaries without passing through probate.

If there's a will and an executor, that person usually handles the probate process. When there's no will, the probate court will assign someone to assume those responsibilities. The person representing the person who has died will tally up and list the assets; pay outstanding debts, bills, taxes, and fees; and distribute the assets to beneficiaries according to prevailing laws. It is helpful to hire an attorney to assist a court-appointed representative.

Probate proceedings are open to the general public. And even if an estate is relatively simple, probate can eat up time and money, perhaps delaying the distribution of assets that family members are counting on. And the last thing grieving family members are likely to want is to be caught up in interminable meetings and legal wrangling.

One way to avoid the hassles of probate is to establish a living trust and transfer assets into it. The contents of a living trust don't have to go through probate, and the amounts and recipients of bequests remain private.

Yet in some states, probate can work to a family's benefit, especially if an estate is relatively small or someone has died without a will. State law can lay out a blueprint for ensuring that the right people receive the property. In addition, it may be better for the family to have the estate bear the cost of the probate process. The laws in some states include provisions for a relatively fast, inexpensive resolution to probate that may be preferable to using a living trust or other complex arrangements.

Your attorney can explain the laws in your state and help you decide how to proceed. ●

Ways To Transfer Your Wealth

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4. GRATs. With a grantor-retained annuity trust (GRAT), you transfer assets into the trust while retaining the right to receive annual annuity payments for a specified number of years. When the GRAT term ends, the remaining assets are distributed to the beneficiaries you named. The annuity payments you receive during the term of the GRAT and resulting gift tax value is calculated using a government rate for this purpose, which is currently relatively low. So while you continue to receive annuity payments based on that low rate during the GRAT term, if trust assets grow at a faster rate, the beneficiaries will benefit when they receive the balance remaining at the end of the trust term.

5. IDGTs. Often you might transfer assets to a trust and name loved ones as "income beneficiaries" who get the investment income the trust generates. That way, you'll avoid income tax on those future earnings. However, the trust will be taxed on that income, and the top 39.6% rate for trusts kicks in when income exceeds $12,400 in 2016. To avoid that result, the trust could be structured to be intentionally "defective," so that income is taxable to you instead of to the intentionally defective grantor trust (IDGT). The gift tax liability for transferring assets into the trust may be sheltered by the estate and gift tax exemption.

Other concepts, such as naming a trust as an IRA beneficiary, also can be helpful in certain situations. But the five listed here may help you achieve your goals.

Keep in mind, though, that trusts are complex, and you'll need professional assistance in structuring and implementing these estate planning ideas. ●

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