

Become familiar with wealth-transfer strategies

To retire comfortably, you need to save and invest regularly.

For example, you need to contribute as much as you can afford to your 401(k) and IRA.

But once you retire, you'll need to switch gears somewhat and move from wealth-accumulation strategies to wealth-transfer strategies.

An effective wealth-transfer strategy can help you accomplish a variety of goals, such as distributing your assets the way you choose, avoiding probate and reducing estate taxes.

And you can explore a variety of wealth-transfer tools, including the following:

- **Gifting** — You can give up to \$12,000 per year to as many people as you'd like without incurring gift taxes.

And if you want to help a child or grandchild pay for college through a Section 529 college savings plan, you can bunch the \$12,000 limit over five years to make one \$60,000 gift, or one \$120,000 gift if it comes from you and your spouse.

(If you group the contributions together this way, you won't be able to make another \$12,000 gift to that same child or grandchild for the next five years.)

- **Will** — A will is simply a plan for distributing your assets to family members and other beneficiaries.

If you were to die intestate (without a will), state laws would determine how your assets should be distributed — and there's no guarantee that the end result would be what you would have chosen.

- **Beneficiary designations** — Many of your financial assets — including annuities, life insurance, IRAs and 401(k) plans — allow you to name a beneficiary.

Upon your death, your beneficiary will automatically receive these assets, avoiding the sometimes time-consuming, expensive (and public) process of probate.

Because beneficiary designations supersede any instructions you might put in a will or living trust, it's essential that you periodically review these designations to make sure they reflect your current wishes.

- **Trusts** — Different trusts can help you accomplish a variety of wealth-transfer and estate-planning goals.

For example, a revocable living trust can help you leave assets to your heirs without going through probate.

You can also structure the trust to stagger payments over a number of years, rather than all at once, or include other restrictions or incentives.

An irrevocable life insurance trust allows you to keep the death benefit of your life insurance policy outside your estate, so the insurance proceeds won't increase your estate tax liability.

And a charitable remainder trust allows you to transfer an appreciated asset — such as a stock or piece of real estate — to a charitable trust, thereby allowing you to defer or even avoid capital gains taxes on the sale of the asset.

Plus, the trust can provide you with a lifetime income stream while the remainder of the assets can be distributed to your favorite charities.

As you can see, trusts are versatile instruments — but they are also complex.

Consequently, you'll need to consult with your tax and legal advisers regarding your particular situation.

In fact, all the wealth-transfer techniques we've looked at will require some careful thought and preparation on your part — so don't wait too long before getting started.

Time has a way of sneaking up on all of us — but it's especially sneaky when we're unprepared.

What do new tax laws mean to you?

As you know, the U.S. Congress has adopted some measures to help avoid the much-feared "fiscal cliff." At this point, important spending decisions have been put off, but new tax laws are in place — and, as an investor, you'll want to know just how this legislation will affect you.

Let's look at the impact of the tax laws on three different income levels:

Up to \$200,000/\$250,000 — If you earn less than \$200,000 (if you're single) or \$250,000 (if you're married and file jointly), your income tax bracket will not change, nor will the tax rates assessed on dividends you receive from stocks or long-term capital gains you receive from selling investments that have appreciated in value. However, a 3.8% Medicare tax will apply to the lesser of your net investment income or your modified adjusted gross income in excess of the \$200,000 or \$250,000 levels, respectively.

\$250,000 — \$400,000 — If your adjusted gross income is at or more than \$250,000 (for single filers) or \$300,000 (for married couples), your itemized deductions will begin to phase out, as will your personal exemption deductions, possibly resulting in higher effective tax rates. And the 3.8% Medicare tax will apply to part, or all, of your investment

income. But your tax bracket stays the same, as do the tax rates on dividends and capital gains.

\$400,000/\$450,000 — If you earn at least \$400,000 (if you're single) or \$450,000 (if you're married), you will be subject to the phase-out of deductions described above. More importantly, however, your marginal tax rate will rise from 35% to 39.6%. Plus, taxes on qualified dividends and long-term capital gains will rise from 15% to 20% — or, actually, 23.8%, when the 3.8% Medicare tax is added in. Consequently, you may have some decisions to make; at a minimum, you'll need to know how the new rates might — or might not — affect your investment choices. For example, if you rely on bonds to provide a source of income, be aware that your interest payments — taxed at your marginal tax rate — will now be taxed more heavily. As for capital gains, the slightly higher rates now give you even more incentive to be a "buy-and-hold" investor, which is usually a good strategy for most people. And the increase in dividend taxes doesn't detract from the key benefit of dividends — namely the ability to provide a potential source of rising income that can help keep you ahead of inflation. Keep in mind that dividends can be increased, decreased or eliminated at anytime without notice.

Overall, the changes in investment-related taxes are probably less substantial than many people had anticipated. And in any case, taxes are but a single component of investment decisions — and usually not the most important one. Rather than let taxes drive your investment choices, focus instead on whether a particular investment is appropriate for your individual situation, and if it fits your risk tolerance, and if it helps you diversify your portfolio. Diversification can help you reduce the effects of market volatility, though it can't guarantee profits or protect against loss.

Still, the new tax legislation is significant, so you should consult with your financial advisor and tax professional to determine what moves, if any, you may want to make. It's always wise to be up-to-date on what's happening in Washington — especially when lawmakers' decisions can affect your ability to achieve your important financial goals.

Are municipal bonds right for you?

Tax season will officially end April 15. Yet you can explore tax-smart investment opportunities all year round. And when you're looking at the fixed income side of your portfolio, you may want to consider two possibilities: municipal bonds and Build America Bonds.

You've probably heard of municipal bonds, but you may not be familiar with how they work. You can find two key types of municipal bonds: General obligation bonds finance the daily operations of a municipality or school district, while revenue bonds finance hospitals, utilities, airports, affordable housing and other public works. So when you purchase a "muni," you are helping support a community.

Of course, your investment will bring you some tangible benefits, too.

First, you'll receive regular interest payments. Furthermore, these payments typically are exempt from federal income taxes — and possibly state and local income taxes, too. If you're in an upper income bracket, you may find munis to be especially valuable. (Keep in mind, though, that some "private activity bonds," which are typically used to finance airports, housing or stadiums that can benefit private entities, may be subject to the alternative minimum tax, or AMT.)

Build America Bonds (BABs) share some similarities with tax-free municipal bonds, although BABs are taxable investments. BABs provide capital to municipalities so that they can build or improve infrastructure, including schools, roads, public buildings and so on. The U.S. Treasury pays state or local government issuers a subsidy equal to 35% of the interest they pay investors for buying the bonds.

BABs have proved quite popular among institutional investors, such as pension funds, that typically don't benefit from tax-free municipal bonds. But are they right for you?

It all depends on your individual situation. If you owned a BAB, your interest payments would be federally taxable, but you might get some state tax breaks if you live in the state where the bond is issued. Many BABs have long-term maturities, which may not be a problem if you're buying the bond for its steady interest payments and plan to hold it for its entire life. But if you think you might want to sell your bond before it matures, be aware that longer-term bonds, by their very nature, are subject to greater interest rate risk than shorter term bonds — that is, longer-term bond prices will be more affected by interest rate movements.

Furthermore, you'll have to consider credit risk — the possibility that the issuer of your bond will default or be unable to make payments. Remember, the municipality issuing the bond, not the federal government, backs a BAB. Although past performance is not a guarantee of future results, municipal bonds' historical default rates have been low.

Ultimately, you'll need to consult with your tax advisor before purchasing either a municipal bond or a BAB. Like all investments, they can provide you with benefits, but you need to be absolutely sure of what you're getting.

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