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Financial Planning Strategies

A Financial Planning Update

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How Charitable Giving Can Benefit Donors

Kelly and Bob regularly set aside a small portion of their budget for charitable donations. In addition to feeling good about supporting a number of worthy causes, they've been able to deduct the value of their charitable gifts from their Federal income tax return. Now, the couple thinks it is time to make a larger charitable contribution. Their intention is to donate some stock they purchased years ago for $1,000 that has since increased in value to $50,000.

Before Kelly and Bob move ahead, they realize that there are a couple of issues that need to be resolved. For instance, Bob is reluctant to make the donation because, by doing so, he realizes their children will not reap the benefits of the stock. On the other hand, Kelly wants to make sure the donation is advantageous to both them *and* the charity. Upon careful review, the couple has come up with a plan that helps alleviate their concerns. Here's a closer look.

The first step for the couple is to address Bob's concerns. They can do this by purchasing a **life insurance policy** in an amount that is equal to the value of the stock—that is, $50,000. Through the life insurance, they can help ensure that their children ultimately receive a benefit that is generally commensurate with the value of the donated stock. They will increase their expenses because of the policy's premiums, but, as you'll soon see, donating the stock may actually help pay for the policy.

Next, the couple can address Kelly's concern by donating the *actual stock* to the charity, rather than selling the stock and then donating the proceeds. There are two reasons for this decision.

First, if they sold the stock, they'd realize a gain of $49,000 ($50,000 - $1,000), that would, in turn, result in a capital gains tax of $7,350 ($49,000 x 15%). Therefore, the couple's donation would be reduced from $50,000 to $42,650, if they choose to pay the tax from the proceeds. Or, they would need to cover the tax with other funds. By donating the stock directly to the charity, any appreciation in the stock's value is not taxed (either to the couple or to the charity).

Second, the income tax benefit generated by a deduction for a charitable gift is based on the **fair market value (FMV)** of the gift and the couple's Federal income tax bracket if the stock being donated is appreciated, qualified, publicly traded stock (if not, the amount eligible for the charitable deduction is limited to the cost basis of the property donated). So, assuming the couple is in the 28% Federal

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Disability Income Insurance: Protecting Your Most Valuable Asset

Have you ever wondered how you would manage financially if you were to sustain an injury or illness that left you unable to work? How long could you maintain your standard of living, pay your bills, and cover your daily expenses? The likelihood of such an event may be greater than you think. According to the Council for Disability Awareness (2014), Americans underestimate their chances of experiencing a long-term disability: 64% of working Americans believe they have a 2% or less chance of being disabled for 3 months or more during their working years; however, the reality is that the odds of experiencing a long-term disability are about 25%.

To be prepared for such a situation, it is important to *plan ahead*. To help protect yourself, you may wish to purchase an **individual disability income insurance** policy, which would replace a portion of your income in the event that you experience a qualifying disability. Consider the following when choosing among the coverage options:

- **Definition of Disability.** Carefully review the policy's definition of disability. Some policies may provide coverage if you are unable to work in the occupation in which you were employed or for which you were trained, or if you can no longer earn as much as you once did in that field. In contrast, other policies may offer coverage only if you are unable to work in *any* occupation. In other words, if you were to sustain a disability but were able to work in a lower skilled, lower paying job, you may not receive benefits.
- **Residual Benefits or Partial Disability Coverage.** Under specific circumstances, if you become disabled and are only able to earn a *portion* of your previous income, residual or partial disability coverage pays a percentage of your benefits.
- **Guaranteed Renewable.** With this feature, the insurer cannot refuse to renew your policy prior to the policy expiration date or change any terms, except for premium cost, as long as you continue to pay your premiums on time.
- **Guaranteed Insurability.** This provision allows you to increase your coverage amount, even if you experience health changes that would otherwise prevent you from obtaining additional disability coverage.
- **Cost-of-Living Adjustment (COLA).** This feature helps protect your benefits against the effects of inflation during a long-term disability.

It is important to note that the cost of a disability income insurance policy varies according to the scope of coverage you choose, and there may be an additional premium for adding any **riders**.

The Outlook without Protection

Without a disability income insurance policy in place, there are alternatives, but they come with shortcomings. For instance, you could self-insure. But, even if you save 10% of your salary each year, one year of disability could easily deplete many years of savings. Or, perhaps your employer provides group disability insurance. Unfortunately, **employer-sponsored plans** are often limited in scope and duration, and generally coverage is not portable upon termination of employment. **Workers compensation** may be an option if an injury occurs on the job. However, eligibility and benefits vary by state.

To qualify for **Social Security** disability benefits, specific criteria must be met, and you may have to wait several months for payments to begin. Social Security disability was not intended to be an individual's sole source of disability income. Benefits are often less than what is needed to cover living expenses.

An illness or injury that reduces or eliminates your primary source of income can be a financially challenging experience. Therefore, you may want to consider disability income insurance as part of your overall financial strategy. Be sure to consult with a qualified professional.

Planning for a Social Security Shortfall

The Social Security program offers a retirement benefit to workers and their spouses. You can start receiving benefits as early as age 62, which would be considered early retirement, or wait until you reach the **full retirement age** of 65 to 67 (depending on your year of birth). The benefits you receive are based on the income you earned over the course of your working life, and are subject to a maximum amount.

What you may not realize, however, is that Social Security was not originally designed to be a retiree's sole source of support. For most people, Social Security provides only a base level of income. The maximum benefit for a person who retires in 2015 at full retirement age is $2,663 per month. Therefore, it is important to plan for retirement by preparing to supplement Social Security.

Here are some important savings strategies that may help you reach your retirement funding goals.

Participate in your employer's retirement plan. Regular contributions to an employer-sponsored retirement plan, such as a **401(k)**, can be an essential part of your retirement savings program. Contributions to such plans offer three key benefits: they are made with pretax dollars; they reduce your current taxable income; and they have the potential for tax-deferred accumulation. Generally, these plans allow you to set aside a percentage of income each year, up to a maximum amount.

Open a traditional Individual Retirement Account (IRA). Contributions to a traditional IRA may be tax deductible, depending on your participation in an employer-sponsored retirement plan, your adjusted gross income (AGI), and your tax filing status. Potential earnings accumulate on a tax-deferred basis. For tax year 2015, you can contribute up to $5,500 (or $6,500 for individuals age 50 or older). If funds are distributed prior to age 59½, a 10% Federal income tax penalty may apply, unless certain qualified exceptions apply.

Consider a Roth IRA. Contributions to a Roth IRA are not tax deductible; however, qualified distributions, including potential earnings, are tax free if you have held your account for at least five years and are over age 59½. Like a traditional IRA, you can contribute $5,500 ($6,500 for individuals age 50 or older) to a Roth IRA in 2015. Note that the limit applies to the total of all IRAs that a person may hold in a given tax year. Contributions phase out for single filers with AGIs between $116,000 and $131,000 and for married joint filers with AGIs between $183,000 and $193,000, in 2015. Withdrawals made prior to age 59½ may be subject to a 10% Federal income tax penalty, unless certain qualified exceptions apply. *Note:* A nonworking spouse can fund an IRA or Roth IRA based on the earned income of the working spouse.

Purchase a fixed annuity. Because an annuity is not subject to income limitations, it can be a valuable addition to your long-term savings program. With a fixed annuity, premium payments accumulate on a tax-deferred basis, and you receive a guarantee that your money will earn interest at a specified rate and that your return (the money paid back to you) will occur on a set schedule in fixed amounts. In general, annuity payments are guaranteed by the issuing company and are based on that company's continued ability to pay claims.

It is important to plan for retirement by preparing to supplement your Social Security benefits. With a disciplined approach to saving, you will be on track to enjoying the retirement you envision. $

Financial Considerations for Unmarried Couples

Unmarried couples may choose to handle their finances in various ways. Some couples maintain separate finances. Others share some costs, while keeping income and other expenses separate. Still others pool all income and expenses. Without the legal rights and benefits of marriage, the "safest" approach may be for unmarried couples to maintain

separate finances. However, this is not always convenient, and in some cases it may hinder trust in the relationship. An awareness of potential problems associated with combining finances without the legal protections of marriage can help unmarried couples create an appropriate arrangement that will work well for their situation. $

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income tax bracket, a gift of $50,000 would result in a decrease in their income taxes of $14,000 ($50,000 x 28%). On the other hand, a gift of $42,650 would only result in an $11,942 decrease in their taxes ($42,650 x 28%). In effect, donating the appreciated stock outright produces a greater current year tax deduction and results in a greater tax savings than selling the stock and donating the proceeds after taxes.

Ultimately, the money saved from the tax deduction can be used to help offset the costs associated with the life insurance policy. The end result truly is a "win-win-win" situation. The charity wins because it receives the full value of the stock, Bob and Kelly win because they get a maximized charitable income tax deduction, and their children win because they eventually receive a life insurance death benefit that replaces some, or all, of the value of the stock.

Making the Most of It

If you would like to maximize the tax benefits of charitable giving, be sure to consult a qualified tax professional. There are some limitations on charitable giving based on the type of gift, the type of organization receiving the gift, and your **adjusted gross income (AGI)** for Federal income tax purposes. In addition, a charitable deduction is only available to taxpayers who itemize their deductions as opposed to taking a standard deduction. Nevertheless, the ability to receive an income tax deduction and possibly replace some of the donated wealth with life insurance makes charitable giving pay off for you *and* for the organizations you wish to support. $