Volume 33 • Number 5

Financial *Planning Strategies*

A Financial Planning Update

From the Desk of:
Tate Christopher
Investment Advisor Representative

FOOTHILL SECURITIES INCORPORATED
Investing in your Future Since 1962™

3751 Sunswept Drive
Studio City, CA 91604
(800) 318-6050
tchristopher@foothillsecurities.net
CA Insurance Lic. # 0B19335

Some Things to Consider When Making Regular Charitable Gifts

Sometimes, our desire to give can lead us into making commitments that are difficult to fulfill. Any endeavor worth undertaking, especially one that can benefit others, deserves our careful consideration *before* we take action. Therefore, when contemplating charitable giving, you may want to consider the following points:

- **Choose your causes.** Worthy causes abound and often demand our immediate attention. Choose a limited number of organizations that concentrate on areas that are important to *you*, and then research what kind of help is needed.
- **Budget your gifts.** Include charitable gifts when planning your annual budget. Distributing your donations throughout the year may lessen the impact on your finances and increase the total you may be able to give.
- **Plan your volunteer activities.** Volunteering can be a rewarding experience, especially when you're able to see the fruits of your labor. Carefully determine the time you have available to ensure your best efforts for the cause, and avoid taking on too much.
- **Review your plans.** Just as you review your annual financial budget, look at

(continued on page three)

Use a Mortgage When Lending Large Amounts to Your Children

Parents often find that once their children are grown and have left home, they may still require financial help. Although adult children may earn their own money, the cost of living and the acquisition of such things as a home may be beyond their means. As a result, many parents may want to provide a "lending" hand. While large loans from parents to offspring are quite common, it is important to pay attention to the tax rules that apply to such transactions.

Liening on Your Child

One beneficial way to establish a loan is to make sure that your child can receive a deduction for the interest he or she pays to you. To accomplish this you must prove to the Internal Revenue Service (IRS) that your loan is a mortgage. Unlike other types of interest, mortgage interest secured by a principal residence is still fully deductible. Have an attorney

(continued on page two)

Use a Mortgage When Lending Large Amounts to Your Children

(continued from page one)

draw up a mortgage agreement so you can take a lien on your child's house. This method is generally used for substantial loans over $10,000.

Setting Rates

With that completed, you can set the interest rate you want to charge. If you use a fair market rate, the tax rules are straightforward. You pay income tax on the amount of interest you receive and your child deducts that amount from his or her income. The IRS determines fair market interest rates monthly.

However, if you charge your child a below market rate or no interest at all, the tax accounting becomes more complex. In fact, you may pay tax on more interest than you actually receive—and a gift tax, as well. On the other hand, your child could deduct more than he or she actually pays you.

A Case in Point

Here's how it works: Suppose you lend your child $150,000 at 3% interest when the market rate is 4%. Your child pays you $4,500 a year in interest instead of a fair market amount of $6,000. Under the IRS rules, you still have to pay income tax on the full $6,000, and your child can deduct all $6,000 even though he or she didn't actually pay that amount. The IRS then considers the $1,500 difference as a *gift* from you to your child subject to gift tax rules. As long as that amount—combined with any other gifts to your child that year—remains below the $14,000 annual gift tax exclusion in 2013 ($28,000 for gifts made by a married couple), you won't have to pay gift taxes.

An offer of financial help from a parent can make a big difference in setting a child off on the road to homeownership. However, before making a loan to any of your children, be sure to establish the required payback interest rate and schedule, so the benefits you provide your child do not negatively affect your own personal financial situation. $

Insuring Your Car, Home, *and* Your Income

Just think about it for a moment. What would you do if you suddenly became ill or injured and lost your income-earning ability for an extended period of time?

For many of us, this is not an everyday concern, nor is it exactly dinner party conversation material. We rarely consider the possibility of becoming sick or sustaining an injury from an accident mainly because we never think it could happen to us. However, if a disability were to prevent you from working for an extended period of time, how would *you* maintain your family's standard of living?

If you're employed by a larger company, your employer may provide **disability income insurance**. But, what if you are self-employed, or your company does not provide disability benefits? In either scenario, it would be up to *you* to make sure you are covered.

One way of protecting yourself is by self-insuring, or keeping a *large* savings account. However, even one year of disability could wipe out years of accumulated assets. Depending on the circumstances, the ramifications of not working for a long period of time could eventually have an impact on your family's current lifestyle.

One way to help protect yourself and your family from the financial implications of a sudden disability is to own an **individual disability income insurance** policy. This type of insurance is designed to meet your specific needs for quality, value, and cost. Be sure to consult with a qualified insurance professional to help determine an appropriate amount of coverage to help protect your assets. $

Some Things to Consider When Making Regular Charitable Gifts

(continued from page one)

your annual time/value budget. Revise your volunteer commitments to include those where the rewards have been the greatest for both you and your cause.

- **Consider a testamentary gift.** If you are fortunate enough to be in a position to increase the amount you donate, or if you are concerned about the future of the organizations you support, consider making a testamentary gift.

Testamentary Gifts

Generally, a testamentary gift is a promise of funds to be given from your estate upon your death. However, using your estate in this way may cause complications. Your intended gift could be reduced if any of the following apply:

- The fair-market value of your assets decreases before your death.
- Unforeseen estate expenses must be met from your assets.
- Your will is contested.

You may be able to protect your gift from estate problems through the establishment of a **trust**. However, the associated legal and administrative costs may have an adverse impact on your gift.

Protection for Your Charitable Gift

Your intentions—and your gift—can be protected from the complications above through the use of **life insurance**. The potential of life insurance may even result in a larger gift than you had originally intended.

The policy can be owned by the charity and removed from your estate, generally protecting your gift from taxation, creditors, and legal contest. It can be purchased and maintained with funds that you contribute to the charity, and as such, your contributions are tax deductible as a charitable gift. As owner of the policy, the charity can decide whether to use your gift to pay the premiums or let the policy lapse. As **beneficiary**, the charity will receive the proceeds of the policy at your death. Depending on the type of policy purchased and the charity's willingness to use your contributions to maintain the policy, these proceeds may be guaranteed and may increase over time. In addition, the proceeds may exceed the amount you would have otherwise given outright during your lifetime or upon your death, depending on the policy type and other factors.

The satisfaction that can come from preparing your charitable gifts ahead of time can be extremely rewarding. When protected with life insurance, your gift could result in the ability to yield more than you ever imagined possible. It may help provide essential funding for your chosen organization, enabling the continuation of its good work.

Be sure to consult a qualified insurance professional to determine the appropriate strategy for your unique circumstances. $

Note: All insurance guarantees are based on the financial strength and claims paying ability of the issuing insurance company.

Securing Future Care with a Special Needs Trust

Caring for a child or an adult with special needs can be emotionally challenging for parents, family members, and other caregivers. In addition, the economic issues that result from providing special care often strain current and future family finances. This is further complicated by the potential loss of government benefits if finances are improperly managed. Therefore, families must plan carefully, for both present and future care. Often, an important part of such a plan is a **special needs trust**.

A special needs trust can be invaluable in providing care for a child or other dependent with special needs, and can be used to help with finances, often without affecting eligibility for government benefits. However, in order to maintain the individual's eligibility for **Supplemental Security Income (SSI)** and **Medicaid**, trust assets can be used only for "extras," such as transportation, therapy, or day care—*not* for essentials such as housing, clothing, or food.

Funding a Special Needs Trust

There are no limitations on how much money or what type of assets can be put into a special needs trust. In this respect, a properly written and executed special needs trust can be used to receive inheritances and gifts. Usually, the parents of the trust beneficiary are **co-trustees** and actively manage trust assets. In general, income from trust assets is taxable to either the trust (if the income remains in trust) or to the trust beneficiary (if income is paid out).

Special needs trusts are typically funded with gifts made to the trust by parents or others. Under current tax law, a taxpayer can make a gift of up to $14,000 in 2013 to as many individuals as he or she so chooses ($28,000 for a married couple) without incurring any Federal gift taxes. This is known as the **annual gift tax exclusion**. Although the annual gift tax exclusion normally cannot be used for gifts made to trusts, there are exceptions that may warrant further exploration. In addition, the **applicable exclusion amount**, which is the amount that can be excluded from estate taxes, could be used by an individual to fund a special needs trust. However, using the applicable exclusion amount during one's lifetime eliminates its usage at the donor's death.*

Besides making gifts to a special needs trust, it is also common to have a **life insurance** policy (or policies) transferred to, or purchased by, the trust. When the insured (typically a parent) dies, the policy's death benefit proceeds become part of the trust and are used for the ongoing support of the trust's beneficiary (the dependent with special needs).

Another benefit of a special needs trust is that it avoids **probate** if the parent/trust donor dies. If the parents are the trustees, they can also name a **successor trustee(s)** to manage trust assets, including any inheritance.

Providing for the Future

A special needs trust can help ensure that a child or an adult with special needs will be provided for beyond the limitations of government benefits. Parents and caregivers may feel more confident in knowing that their child or other loved one will be cared for in the years ahead. Remember that the laws affecting the usage of special needs trusts vary from state to state. Be sure to consult a qualified professional before making any definitive arrangements. $

*Under current law, Federal estate taxes in 2013 have an applicable exclusion amount of $5.25 million and a top tax rate of 40%.