Protecting Your Health and Wealth

A MONTHLY RESOURCE FOR PROTECTING YOUR ASSETS
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JERRY HILL
PUBLISHER
BENEFLEX FINANCIAL GROUP
WWW.BENEFLEXFINANCIAL.COM

Will Your Loved Ones Inherit Your Tax Liability?

Over the years, you may have made the most of tax-deferred investments. In many cases, this let you use the government's money to help compound the return that you had received. What if you don't plan to spend those dollars during your lifetime and prefer to let them grow for your beneficiaries? Without proper planning, you could end up leaving a big tax bill instead of financial security.

You might already know that when you die, your beneficiaries will owe income tax on distributions from your IRA, 401(k), and other retirement plans. However, did you realize that they will also have to pay tax on additional income that you were entitled to receive? This could include accrued interest on U.S. Savings Bonds, savings accounts and CDs; declared dividends; installment loan sales; and annuity and rental property income. When you combine your heirs' potential income tax bracket and the possible estate tax rate, up to 82 cents out of every dollar you had hopped they would receive from your deferred accounts could disappear.1 And this does not include any state taxes that might apply. There is, however, a way to reduce this double-whammy tax bite, but it only works if your beneficiaries or their tax preparers know about it.

Income in Respect of a Decedent (IRD) is the term that the IRS uses for income that you earned but did not receive while living. And the government gives it a special tax break by allowing your heirs to deduct estate taxes paid on IRD when they calculate their income tax due on this income.2 As a result, the double taxation could possibly be eliminated.

For example, suppose you have a taxable estate and left your daughter an IRA that you had funded with deductible contributions. First, the amount that you had put in, and all deferred income and appreciation would be subject to estate taxes. Then your daughter will have to pay income tax on each dollar she removes from the account. But if she takes advantage of the IRD deduction, each distribution from the IRA would be entitled to a tax deduction for the amount of estate taxes paid on that deferred income.

Besides telling your beneficiaries about the IRD deduction, there are other things that you can do to pass assets more tax-efficiently. Life insurance to pay estate and income taxes is one idea. Also you might want to consider giving property to your loved ones while you are alive. Another thought is to use up your tax bracket by taking maximum distributions from your IRA. I always recommend investors consult their own qualified tax, and financial advisor prior to making any investment decision.

For a free estimate on the tax liability that your heirs might face along with possible ways to reduce or eliminate this tax, please complete and return the enclosed coupon.

1.http://www.irs.gov/irb/2004-50_IRB/ar14.html#d0e1061 , http://www.irs.gov/formspubs/article/0,,id=112782,00.html#estate_max_rate_2003
2 http://www.irs.gov/pub/irs-pdf/p17.pdf, page 40, http://www.irs.gov/pub/irs-pdf/p559.pdf, page 11

Give Your Grandchild a Gift That Will Last a Lifetime

Birthday parties, holiday gifts and vacations: For many people, being a grandparent is an opportunity to share accumulated wealth with a grandchild. But have you considered giving your grandchild a gift that can last a lifetime?

Each state has adopted a Uniform Gift to Minors (UGMA) Act or a Uniform Transfer to Minors (UTMA) Act. These acts allow individuals — parents, grandparents, other relatives and even friends — to set up a custodial account for the benefit of a minor.

UGMA/UTMA accounts are not difficult to set up, because they don't require complex paperwork or trust documentation. There's no limit on the amount of money you may contribute (although, keep in mind that if you give more than $12,000 as an individual or $24,000 as a couple to a child in a year, your gift may be subject to federal gift taxes). And in most states, securities, insurance policies and annuity contracts, real estate, and other types of property can be contributed to an UTMA account (although real estate and other types of property cannot be contributed to UGMA accounts).

While the funds in these accounts are the property of the minor, the custodian (who can be a contributing relative) is responsible for managing the assets until the child reaches the designated age of majority, typically either age 18 or age 21. At this time the assets pass directly into minor's control.

One of the greatest benefits of an UGMA/UTMA account is the tax savings they can potentially offer. For example, if you save for a child's future by depositing money in a taxable account in your own name, any income generated by that account will be taxed at your highest marginal tax rate — in some cases up to 35%. But if you save for a child by depositing money in an UGMA/UTMA account, some or all of the income generated can be taxed at a lower federal income tax rate. For the 2006 tax year, if a child is under age 14, the first $850 in investment income is not subject to tax; the next $850 in investment income is taxable at the child's tax rate (in many cases 10%); and any investment income in excess of $1,700 is taxed at the parents' highest tax rate. After a child reaches age 14, all of the investment income is taxed at the child's rate.

This can sometimes result in a significant income tax savings. Consider an investment of $10,000 that generates $1,000 in taxable investment income over the course of the year. If you hold these assets in your name, and your top marginal tax rate is 25%, you'll pay up to $250 in federal income taxes on that income. If those assets are in an UGMA/UTMA account for a child who is younger than 14, however, the federal income tax bill will likely be only $20 (no taxes on the first $850 and 10% on the remaining $150). Please note, however, that state income taxes can still apply depending upon your state of residence. I always advise people to consult with their own qualified legal, tax, and financial advisor prior to making any financial decisions.

We can help you set up an UGMA/UTMA account and transfer the appropriate cash and/or securities into it; we can also give you other options for gifting. Just call the office or send in the enclosed coupon.

Many Seniors Have Inadequate Coverage for Long-Term Care [3]

You might think your HMO or other health insurance is great, and it may be. However, it might not cover the long-term financial ramifications of these illnesses:

- Limitations of Parkinson Disease
- Extra Care Needed to Deal With Chronic Arthritis
- Incapacity of Multiple Sclerosis
- Disability Caused by Stroke
- Care Needed by Alzheimer Patients

Many insurance plans are designed to address acute shorter-term illnesses – illnesses that the doctors can fix by admittance into a hospital, providing medical care, and then releasing you. But many illnesses do not behave this way. Many illnesses have a long term debilitating nature, and your insurance may not cover the long term care costs that are often associated with them.

According to a recent survey, 17% of people over 65 in the US have purchased long term care insurance to cover these costs.[4] Others who have not purchased this coverage could be under the impression that they are either covered by their regular health insurance, a government program, or that they won't ever have one of these illnesses. However, regular health coverage is only partial, as it typically does not cover the types of care often provided by nursing homes or community care providers. This type of care is commonly referred to as custodial or long-term care.

At $5,000+ per month for long term care, a person can accumulate a fairly significant long term health care bill. While many people would never consider being uninsured for routine health care, they seem to have ignored the risk that their health insurance might not cover the entire list of possible afflictions. I urge you not ignore this risk. Regardless of the wealth a person might accumulate during their lifetime, it could be compromised if they should get caught off-guard by a long-term nursing home stay. I always advise people to consult with their own qualified legal, tax, and financial advisor prior to making any financial decisions.

If you don't have this protection, I would also encourage you to consider it when your health is good. Remember—insurance companies often sell insurance to people when they don't need it.

If you do not even know the questions to ask, you can order our booklet "Mistakes in Buying Long Term Care Insurance" and then make an appointment with us to explore your options.◆

3 Derived from American Health Insurance Plans, association of 1300 insurance companies, study June 2004 http://www.ahipresearch.org/pdfs/18_LTC2002.pdf. Of 9 million cumulatively policies sold 70%, or 6.3 million remain in force and assuming all were sold to people age 65+ totaling 36 million people (US Census 2005 www.census.gov) then at most, 17.5% of people age 65+ have long term care insurance. Estimate corroborated by MetLife Mature Market Institute November 2004 "When it comes to long-term care insurance, 16% of men and 14% of women age 50 and older say they own it."

4 MetLife Survey Sept. 2004 nursing home costs, national average for private room is $70,080 per year.

Get this Valuable Free Information

Mail back to:
Jerry Hill
Beneflex Financial Group
11811 East Freeway Ste 545
Houston, TX 77029
800-926-9107 or 713-455-7087
Wealth@beneflexfinancial.com

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