COLORADO FINANCIAL MANAGEMENT®

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All Things Financial Planning

by Jason Foster, Attorney
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Greetings!

There has been much discussion this year about publishing a financial planning newsletter to complement the Economic and Market Review letter Brad authors and distributes. Considering the vast number of planning topics and the ever-changing financial planning landscape, it makes sense to share our knowledge and insights with you – so without further ado, here is the first edition.

My hope in putting together such a letter is to explore subjects that are relevant to your interests and needs. We have a wide range of experience here at CFM and I plan to tap the collective knowledge of CFM planners and advisors in putting this newsletter together. The goal is to publish one each quarter, and we will do our best to honor this commitment.

Within this newsletter we will explore a comparison between Wills and Living Trusts, how social security survivorship functions, and the basics concerning a Roth IRA. Separately from this publication, we plan to have quarterly financial planning discussions in person in each of the 3 office locations covering planning subjects we believe you will benefit from. Topics will include tax planning techniques, retirement planning, health insurance and estate planning strategies, and we plan to invite guest speakers to enrich the discussions, depending on the complexity of the subject matter. The projected start date for these financial planning “get togethers” will be the fourth quarter of 2019. Stay tuned for a more formal announcement of the first topic in the series.

Estate Planning with Wills or Living Trusts – What Makes Sense?

By Jason Foster, Attorney and Director of Financial Planning

I thought I would start by discussing the use of Wills and Living Trusts in your estate planning. Many clients might not be sure why their attorneys have advised them to do one or the other, and in my experience, much depends on the preference of the attorney. Regardless, both provide the blueprint for the administration of your estate when you pass away. But while there are many similarities, there are also some key differences which we will explore below.

Wills. The benefits of a will involve its simplicity in drafting and application. Once filed with the court it informs everyone who will inherit at least some of your property (keep in mind, retirement accounts, life insurance and jointly titled property will pass to beneficiaries and joint account holders and are not controlled by your will). A will must be probated, but in Colorado, this process is relatively inexpensive and reasonably efficient. And while no one necessarily wants to have the courts involved, there are some benefits to having an open probate matter – creditors can be closed out and probate court offers a forum for disagreements to be resolved. It provides clear deadlines for challenging the will and the final distribution of estate assets.

One clear disadvantage is the lack of privacy – the entire world has the opportunity to know what your heirs will receive through subsequently filed accountings of the estate assets and liabilities. For larger estates, you may not want everyone to know what your heirs are about to receive.

A will also is not an efficient estate planning vehicle for property situated outside of the state. If you own vacation property or land outside of Colorado, your personal representative might have to manage probates in multiple states. Lastly, disability and incapacity planning can be more effectively managed through the use of living trusts, as will be discussed below.

Living Trusts. A living trust manages your assets while you are alive and the distribution of assets at your death. You are named the trustee of your own assets and your spouse or an adult child is typically named the successor trustee, and in some instances your co-trustee. Living Trusts are revocable at anytime while you are alive – which means you can move assets in or out without tax consequence. You maintain complete control over the assets.

Upon your death, the living trust becomes irrevocable and the successor trustee will follow the living trust instructions regarding the distribution of assets. There is no court involvement for assets transferred into the trust prior to your death, which results in maximum privacy. Pour-over wills are used to "catch" non-transferred assets and put them into the trust to avoid a full probate administration of the estate.

The continuity of management of the living trust's assets upon your death is a major benefit. Stocks, securities, real estate, business interests, and any other assets of the trust can continue to be managed without interruption while debts, expenses of last illness, funeral bills, taxes, etc., can be paid. There is no delay in transferring assets of the living trust after death. This can be important when the family has immediate financial needs and requirements upon your passing.

When utilizing a living trust, a major advantage over a will is the ability to administer real property outside of Colorado without court involvement. If the living trust owns the real property, a burdensome and costly ancillary probate proceeding can be avoided altogether in the state where the property is located. A living trust drafted in Colorado will be recognized and honored by other states.

Living trusts allow you to assess how a co-trustee will handle the management and responsibility of your assets. In a sense, you can give your spouse or adult child co-trustee a "trial run" while you familiarize them with the assets and complexities of your estate assets. This can be especially important for larger estates when there are concerns whether a spouse or adult children have the capacity to manage the wealth and business affairs of the family.

But there are some disadvantages to a living trust arrangement. Drafting a living trust can come with a higher price tag. Attorneys charge more, not only because the trust can involve drafting complexities, but also due to the need to re-title assets in the name of the trust to maximize privacy and efficiency. This must be done correctly, and it makes sense to have your attorney oversee this process, especially if there are business and real estate assets involved.

There may also be an inconvenience in following the formalities of operation concerning the living trust – assets held by the trust are handled in a slightly different manner than you were accustomed to when you owned them outright. But these concerns are manageable with proper instruction and guidance.

Less of a disadvantage, but more of an observation – assets transferred into living trusts do not provide creditor or liability protection. Thus, if one of your goals is to shelter assets from such claims, this approach to asset protection is generally not successful. Also, neither a will or living trust, on its own, is a tax savings vehicle, and both require language to protect exemption amounts or to do other tax planning.

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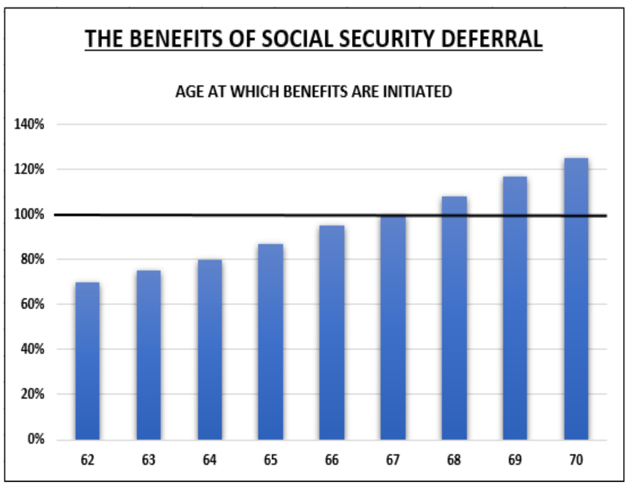
Whether a living trust or will is the best approach for you, depends on many of the factors discussed within this article. A careful review of the types of assets you have and a discussion concerning your goals and objectives will help in making an informed decision. If you have any questions about your estate plan, we are happy to review everything in context, providing observations and recommendations to you.

The Basics of Social Security Survivorship
by Tim Dutton, Associate Financial Planner

As you work, you pay into a government run system that is designed to provide some retirement benefits later in life. The more you pay in and the longer you work the more the available benefit will be later. **Beginning at age 62**, you become eligible to access this same system for these retirement benefits. As the below chart illustrates, if you delay taking these benefits, which may or may not be advantageous depending on your circumstances, you can receive a larger, fixed payout for the rest of your life. At age 70, you have maximized the eligible benefit available and should begin taking these benefits. These are the basic premises of the social security system.



But what happens to these benefits when you die? Will anything be left for your spouse and children? The loss of a primary wage earner's income and their corresponding social security benefits can be devastating to families. To alleviate this issue, the government will assist by providing income to survivors based on credits accumulated. Only certain members of the family are eligible based on select criteria, but these benefits can be more valuable than many individual life insurance plans. Let's explore how the system works for survivors:

Earning Survivor Benefits. Generally, social security eligibility begins after **10 years of work or 40 credits earned** (an average of 4 credits per year). The exact number of credits you need for family members to be eligible for survivor benefits depends on your age when you die. The younger you are, the fewer credits needed, but the maximum you will ever need is 40 credits. An exception to this general rule applies to a surviving spouse with dependent children – survivor's benefits are still available if 6 credits or more have been earned within 3 calendar years prior to a wage earner's death.

Eligibility for Survivor Benefits. A **surviving spouse** is eligible for the maximum benefit available at full retirement age (FRA). The FRA for survivors born between 1945-1956 is age 66, with the FRA gradually increasing to age 67 for those born in year 1962 or later. A widow or widower is eligible for reduced benefits as early as age 60. A disabled surviving spouse can begin receiving benefits as early as age 50, and a surviving spouse caring for the child of the deceased worker can receive benefits at any age.

Unmarried **children under age 18** (or up to age 19 if attending elementary or secondary school full time) are also eligible for benefits. Children can receive benefits at any age if disabled prior to turning age 22. In some cases, the government will pay social security to stepchildren, grandchildren, step grandchildren, or adopted children. **Dependent parents** are entitled to social security if they are 62 or older, qualify as dependents and the deceased provided for at least half of their support.

Divorcees can also be eligible to receive social security. If they were married for at least 10 years, they can begin receiving benefits at age 60 (or beginning at age 50, if disabled). The benefits received by the surviving former spouse will not affect the benefit amounts available to other eligible survivors. The 10-year length-of-marriage rule will not apply if the surviving former spouse is caring for their joint child who is under age 16 or disabled.

If surviving spouse remarries prior to age 60, they likely will be denied benefits. If they remarry after age 60 (or age 50 if disabled), surviving spouse can receive benefit payments based on either the work record of the deceased spouse or new spouse, whichever is higher. If the surviving spouse does remarry prior to age 60, then divorces or is widowed, the survivor benefit will be available again.

Calculation of the Benefit. The amount you and your family could receive in social security benefits is based on the **average of your highest 35 years of earnings**. The higher the monthly average, the higher the survivor's monthly benefit. Below is a table detailing the percentage of the deceased spouse's basic benefit available as a benefit to survivors:

Survivor Type	% of Worker's Basic Benefit Amount
Widow or widower at FRA or older	100%
Widow or widower under FRA	71-99%
Widow or widower, at any age, with a child under the age of 16	75%
A Child	75%

To review your eligible social security benefit, and potential survivor's benefit visit www.ssa.gov and select *my* Social Security account at the bottom of the page. You will need to create an account and then you can access your online statement with benefit information.

Lump Sum Death Benefit. At the death of the social security beneficiary, the government will pay a **one-time lump sum of $255** to the spouse or child if certain requirements are met. This payment was originally intended to cover burial costs. However, no adjustment has been made to the $255 amount and inflation has eaten away at its usefulness. Survivors still must apply to receive this payment within 2 years of the date of death.

Applying for Benefits after the Death of a Spouse. Although the death of a spouse or parent involves challenging circumstances, as a survivor eligible for social security, you should apply for the benefits as soon as possible. Benefits will be based on the date of application and not the date of death of the family member.

You can apply by phone or in person at a local Social Security Office. These offices will provide advice and guidance as you navigate your way through the system. Below is a list of original or certified copies of documents required by your local Social Security Office:

- Death certificate
- Your social security number and the social security number of the deceased
- Birth certificate
- Marriage certificate, if a widow or widower
- Birth certificates and social security numbers of dependent children, if available
- Most recent W-2s or a federal self-employment tax return of the deceased
- Bank and account number for deposit

What if My Spouse Dies While I Am Receiving Social Security? If you are receiving benefits on your own work record and your spouse dies, you may be eligible for a combined benefit equal to a higher calculated amount. If you are receiving spousal benefits already, the government will change these benefits to survivor's benefits when you report the death of your spouse.

Right to Appeal. The government can make errors in calculating eligible benefits. An earnings miscalculation for a particular year, or failing to utilize your highest earning years in calculating your social security payments would result in a correctable error. Once a mistake is recognized, do not delay in appealing the benefits decision. Your local Social Security Office can guide you through this appeals process. You can either represent yourself or obtain an attorney who specializes in social security law to assist in challenging the calculation.

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Social Security is a critical component to income and retirement planning here at CFM as we optimize the cash flow available to you and your family. Knowing how the system works while you are living, and how it will operate after you are gone for the benefit of your surviving spouse and family is vital to any financial plan. If you have questions about social security or how it fits into your overall financial plan, your financial advisor would be happy to have this conversation with you.

Roth IRAs – What Are the Benefits of These Accounts and How Do They Function
by Jason Foster, Attorney and Director of Financial Planning

The Tax Benefit. A Roth is a type of individual retirement account that allows you to contribute *after tax* money. Unlike a traditional IRA, your contributions to a Roth IRA are not tax-deductible. Account contributions will grow tax-free, however, and are not subject to tax when you withdrawal money, assuming certain requirements are met (detailed below). You also are not required by law to take any distributions like you are with a traditional IRA once you reach age 70 1/2. This allows you lots of flexibility in your retirement years as you manage your budget, cash flow, and the tax bill. You only have to take non-taxable distributions from a Roth when necessary, or not at all. If money remains in the Roth upon your death, your beneficiaries will receive these accounts tax free, and although the inherited Roths are subject to required minimum distributions, the payments amount to a tax free annuity benefit, paid out for the duration of their lives – a truly fantastic inherited gift to receive and utilize.

Contribution Rules Based on Income Levels. A person of any age can contribute to a Roth, as long as your contribution doesn't exceed your income earned (or your combined income for married couples), and your income earned doesn't exceed the earnings limitations imposed by law. To qualify to contribute the full amount allowed, you must have regular income of less than $122,000 for individuals. The ability to contribute is phased out completely once your adjusted gross income exceeds $137,000. For married couples, the full contribution amount starts at $193,000 and phases out at $203,000. The maximum contribution limit is $6000 for individuals under age 50, and $7000 for individuals age 50 or older. These income guidelines should be kept in mind as opportunities to contribute to a Roth present themselves, which could come in the form of a fluctuation in your income levels from year to year to finding yourself in a lower tax bracket in your retirement years.

Roth Conversion Option. So what if you make more then the above limitations? Can you still utilize a Roth? Enter the Roth Conversion opportunity. This process allows high earners to move money from a traditional IRA to a Roth IRA without being subject to the above income and contribution limitations. You'll have to pay taxes on the conversion at your current income tax rate – but the benefits of having assets grow tax free without the government forcing you to take distributions during your lifetime might make this a prudent move. There are a number of factors and variables, however, to consider in deciding whether to convert tax deferred money, and ultimately, how much to convert. We will discuss many of these considerations in detail in Part 2 of this discussion on Roth IRAs in our next newsletter.

Other Statutory Considerations. Once a Roth IRA is established, there is a 5-year vesting period from the initial contribution that must be satisfied prior to withdrawal to avoid both penalties and taxes on any gains. Distributions from a Roth account become tax and penalty free after the 5-year aging requirement, provided you have reached aged 59 1/2. The below chart is provided to illustrate these basic guidelines.

Taxation of Roth IRA Distributions

	Distribution within 5 years	Distribution beyond 5 years
Age < 59½	Income Tax: Yes (earnings only) 10% Penalty : Yes (earnings & taxable portion of prior conversion amounts)	Income Tax: Yes (earnings only) 10% Penalty: Yes (earnings only)
Age ≥ 59½	Income Tax: Yes (earnings only) 10% Penalty: No	Income Tax: No 10% Penalty: No

There are notable exceptions to the 59 1/2 age requirement. If you pass away and your beneficiary owns the account, if you access the account as a first time home buyer, or if you become disabled, then account distributions will not be subject to taxes or penalties. In addition, even if the 5-year rule has not been satisfied, you can always withdrawal the money you contributed without tax or penalty at any time because these withdrawals are considered a return of already taxed capital contributions, which will not be taxed by the government a second time.

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If you are in a position to contribute to a Roth or convert IRA money to Roth money, a full analysis should take place to determine whether or not this is the most prudent financial decision based on your specific circumstances. As previously stated, we will explore a Roth Conversion, and the complexities and variables when considering a conversion in Part 2 of this topic in next quarter's publication. But if you have questions about how a Roth functions and whether it makes sense to explore the option of opening a Roth account, let your financial advisor or our financial planning team know and we can assist you with this discussion and analysis.