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Estate Planning Considerations for Your Children

It takes special care to create an estate plan that efficiently distributes your assets and meets your goals for every person and cause that are important to you. But no part of the process means more to most people than that which involves their children. After all, for most of us, our children are our most important legacy, and how your estate documents treat them will have an impact long after you're gone.

To help organize this process, it is useful to think of children in three categories: minors, young adults, and grown adults.

Minor Children

Children from infancy through high school have a different set of needs than children of other ages. One is simply to be able to rely on an income for daily needs that approximates your income in case you're no longer there for them. The challenge is to provide an instant estate for which life insurance is typically the best answer.

There are a number of rules of thumb for how much life insurance to buy — from four to 10 times your annual income. The right amount should be the result of a thorough needs analysis of your entire family, which can be accomplished by asking several questions, including:

- ✔ How much do the two of you already have saved?
- ✔ Will your spouse be able to work full- or part-time? If so, what will child care cost?
- ✔ Will your children go to public or private elementary and secondary schools?
- ✔ How much will your children need in college funds by the time they're ready to attend?
- ✔ How much will your spouse need for retirement, and how much of that will he/she be able to accumulate on his/her own?

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Estate Planning

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After you determine how much life insurance to buy, you need to think about who will raise your children if you and your spouse both die before the children become adults. This calls for naming a guardian in both of your wills. If you don't have a will, a state court will appoint a guardian for you, and it may not be someone you or your spouse would have wanted for this role. In addition, parents might also wish to designate a person to manage the children's assets. It can be the same person as the guardian, but designating an unrelated third party, such as an attorney, banker, or trust company officer, appeals to some people.

Among the other major decisions you have to make is whether and how to split your assets between your surviving spouse and your children, and if you leave some assets directly to your children, how to determine the split among them.

Young Adults

Once children reach the age of majority — which in most states is 18 — a new set of considerations enters the picture. By this age, your children no longer require a guardian and are legally capable of spending their money in any way they want — and therein lies a potential problem. What if you leave $250,000 for college and instead your children decide to waste the money and skip college?

One way to control how the inheritance is spent is to establish a trust with a schedule for distributions. One option is to delay a full distribution until they reach a certain age, like 25 or 30. Another choice is to give them a series of partial distributions at ages that make sense to you given what you know about your child. Another strategy that is becoming increasingly popular is the incentive trust. This vehicle makes payouts contingent on your child's achievement of specific accomplishments — like maintaining a certain grade point average; graduating from college, graduate, or professional school; marrying; or buying a home.

Adult Children

Many of the same kinds of considerations that apply to minors and young adults can also influence your decisions on how much money to leave to your adult children. Do they, their spouses, or their children have special medical needs? Have your adult children fallen on hard times or are they irresponsible with money and would only waste it? How many children do they have and how much help will they need to finance their educations?

Another consideration has as much to with your own objectives for minimizing estate taxes. If your estate is much larger than you and your spouse's combined estate-tax exemptions, you might want to shrink it with an aggressive campaign of gifts to your children and grandchildren. On the other hand, any funds you leave to your children might encumber them with estates equally as large as yours or larger with the same tax challenges. In this case, you might want to transfer some of your assets to a generation-skipping trust, which bypasses your children and names your grandchildren as the beneficiaries.

Don't go it alone when mulling over these decisions. Please call your financial advisor to discuss this in more detail. ❍❍❍

Making Progress Toward Your Goals

Having trouble making much progress toward your financial goals? Consider these five basic tips:

✔ **Set exciting financial goals.** Putting money aside for a distant goal, rather than spending that money now, is a difficult habit for most people to acquire. To help, set exciting goals that will motivate you to achieve them. Then quantify your ultimate goal and interim goals so you'll have a way to track your progress.

✔ **Spend less than you earn.** The amount of money left over for saving is a direct result of your lifestyle. Since you will typically want a similar lifestyle after retirement, your lifestyle decisions will impact you now and in the future. To get a grip on your spending, take time to analyze your expenses and set a budget. Reduce nonessential expenses.

✔ **Save the money before you see it.** If you have to find money to save every month, you'll probably find there isn't much left after paying all the bills. Typically, a better strategy is to set up an automatic savings program where money is automatically deducted from your bank account every month and deposited directly in an investment account. Another good alternative is to sign up for your company's 401(k) plan, having funds withdrawn every paycheck.

✔ **Don't let debt sabotage your goals.** If a significant portion of your income is going to pay interest on loans, that leaves less available for saving. Strive to eliminate all debt except your mortgage. Pay cash for all purchases so you don't incur additional debt. Pay down your existing debts by using additional funds to pay off the debt with the highest interest rate.

✔ **Invest, don't just save.** The ultimate value of your investment portfolio is a function of two factors — how much you save and how much you earn on those savings. Become comfortable with various investments, so you'll feel more comfortable investing in more aggressive ones that offer potentially higher return. ❍❍❍

When Is It Time to Sell a Stock?

As difficult as it can be for some people to decide to buy a stock, it can be just as difficult to decide when to sell it.

In truth, there's no single rule for determining when to sell a stock. But one thing can help: knowing why you came to own the stock in the first place. If you set a specific goal, it's far easier to let a stock go once it has reached that goal.

To provide a focus here, we're going to consider two kinds of scenarios. The first is when you've made money on the stock. The second is when you haven't, either because the stock price has been flat, or it's lower than when you bought the stock.

When You Have a Profit

Short of needing money, is there any reason to sell a stock that has made a profit? The very idea seems to fly in the face of the fact that failing to let their winners run is one of the most common mistakes individual investors make. Nonetheless, there are several reasons for selling some or all of a position in a profitable stock:

✔ **The company has fundamentally changed character and is unlikely to continue to grow in value.** This is often very difficult for casual investors to assess until it's too late, but it's not at all uncommon. Think of some leading examples from the last 20 years or so: AT&T, Enron, General Motors, and Lucent, just to name a few. For years, and in some cases for decades, these were gold-plated, blue-chip stocks. But then something changed, not always in a dramatic fashion.

There are at least two different ways to detect that kind of change. One is by tracking the company's fundamentals and changes in long-term trends. Were the company's highest levels of sales, profitability, and market share more than three to five years in the past? Has it been overtaken by competitors that once were far behind? Has it cut its dividends more than once, severely reduced its research and development spending, taken on unusually high levels of debt, or has its credit rating been reduced several times in the past few years? All of these could be signs that the company isn't what it used to be and your money is more likely to fare better in another stock.

Another way to detect change at a company is to study the chart of its price changes over time. Adjusted for splits, was the stock's highest price many years in the past? Has the long-term trend line shifted to a flatter or negative slope? Is the stock having trouble piercing through resistance points that are far below its highest levels? These, too, can be signals that there are better places for your money.

✔ **You need to rebalance your portfolio.** One of the tools professional money managers use for raising long-term portfolio returns and reducing risk is to rebalance. That means selling some shares of positions that have grown out of proportion to your asset allocation strategy and using the profits to buy more shares of issues that have gone down in price. This has the effect of locking in some of your gains while increasing your potential return by leveraging more shares of an investment that later recovers in price.

✔ **You've identified a better opportunity.** This is closely related to the first reason. The difference here is that the stock you own hasn't changed its intrinsic character, but another stock with similar or better risk characteristics offers better returns, either through growth or dividends.

When You Have Losses

This is the easier of the two scenarios because it can come down to answering one simple question: if you didn't already own it, would you buy it today? If not, sell. If so, keep it. If you would buy it, it's because the fundamentals haven't changed. But if you're not skilled at this assessment, you could be making a mistake.

The danger is that you may not recognize the need to sell. Sometimes stocks go down for reasons that have nothing to do with the underlying value of the company. It could be because of a bad economy or bad news to which the market overreacts. These could actually mark opportunities to buy more shares at a cheaper price.

On the other hand, there can be very good reasons the stock has been going down and will continue to do so. If this is the case, the smart move is to cut your losses, no matter why you own the stock. You may want to prove to yourself that you didn't make a mistake in buying it, or you may be holding it because you inherited it from a dear relative who held it for decades. None of that will compensate you for more losses.

The bottom line is unless you have the skills of a highly trained and experienced professional, it's best if you don't make decisions to sell a stock on your own. Please call your financial advisor if you'd like to discuss this in more detail. ❍❍❍

Buying a Second Home?

For many Americans, owning a vacation home is a long-held dream. If it's one of your dreams, consider these five factors before you decide to purchase.

1. Where will the mortgage money come from? Your first financial priority, after meeting your living expenses, should be to build up rainy day savings of 3–6 months of living expenses and then fully fund your retirement accounts. If you've met those goals, weigh your desire for a second home against other priorities.

2. What is the total cost of second home ownership? The costs associated with owning a home go far beyond just the mortgage principal and interest payment. You'll also have to consider: mortgage closing costs, state and local property taxes, homeowners insurance, private mortgage insurance, homeowners association dues, maintenance, utilities, home security, and furnishings. At the same time, there can be substantial financial benefits to owning a second home, including tax deductions for mortgage interest, property taxes, and other homeownership-related expenses.

3. How does the cost of owning a vacation home compare to the cost of renting a vacation property? Many people who own a second home buy one in a place they visit frequently. It's important to consider how often you would actually use the vacation home. For many people, the total cost of owning a second home is much more than renting a home.

4. Will you use the second home as a source of income? Since 1987, the average annual home price increase was 2.8%, just a hair above inflation. So as a pure investment, a second home probably doesn't make sense. However, if you intend to stay in the home when you vacation or rent it out as a source of income, it can make sense to buy.

If you plan to use your second home as a source of income by renting it out, the tax implications may be different than if the home is just a vacation home. Explore those implications with your tax advisor.

5. What are prices like in the market(s) you're considering? By researching price trends in the market(s) you're considering, you can get a sense of whether homes are under or over price trends. If they're over, now might not be the best time to buy; if prices are below trend, you might be able to get a good deal. ❍❍❍

Everyone's Plan Is Different

Everyone's goals for retirement are different. Maybe your dream is to travel the world, or maybe it's to live closer to your grandchildren. Maybe your plan is to while away the days fishing or quilting, or perhaps you're planning to take up a second career. Maybe your goal is to save enough to leave a substantial sum to your beneficiaries. Whatever your dreams are, your retirement plan needs to reflect them — and because your dreams are uniquely yours, your retirement plan should be, too.

The biggest question most people have about retirement is: How much do I need? While that's not the only question, savings is not the only factor to consider, but it is an important one. And while using an online retirement calculator is fine to get a very rough idea of how much you might need for retirement, those calculators don't take your dreams or particular circumstances into account; as such, the amount you'll actually need for retirement can vary greatly from the number on the online calculator.

To properly plan for retirement, you have to consider all the options, all the aspects, and all the opportunities. ❍❍❍

Financial Thoughts

Approximately 47% of U.S. households have credit card debt, owing an average of $15,257 (Source: U.S. Commerce Department, 2013).

When asked what it takes to be considered wealthy, 50% of the respondents indicated no financial constraints on activities, 16% indicated surpassing a certain asset threshold, 10% indicated never having to work again, and 10% indicated ensuring a comfortable lifestyle for future generations (Source: *Wealth Management*, September 2013).

At public universities and colleges, 31.3% of students earn their bachelor's degrees in the traditional four years, while 52.5% of private university students do so. Only 57% of full-time college students graduate within six years. A third of students who borrowed money for college have never earned a degree (Source: *Wealth Management*, September 2013).

The average single man who turned 65 in 2010 contributed $61,000 to Medicare on an inflation-adjusted basis, but can expect to receive $180,000 in benefits (Source: Urban Institute, 2013).

Approximately 80% of Americans over age 55 are still working, the highest proportion in more than half a century (Source: Bureau of Labor Statistics, 2013). ❍❍❍

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