

THE PERSONAL PLANNER

Personal Financial Planning Tips for Today and the Rest of Your Life



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I'm writing this early (6/24), trying to get ahead of quarter-end activities falling in conjunction with the Independence Day holiday/vacation time, etc., so we still have a week to go in the markets and, well, anything could happen. We've seen extreme downside volatility in the last half of June brought on by a seemingly emotional over-reaction to a mildly positive news release by the Federal Reserve Open Market Committee. Go figure. As always, we will be making portfolio changes to try to keep this downturn from becoming a major portfolio decline for clients should it continue.

On a personal note, we lost Kate's father on June 2nd, suddenly and unexpectedly, and found much of the next few weeks consumed with family matters. Karl Schulz will be missed. Thank you for your kind wishes.

Bruce Heling, CFP CPA
June 24, 2013

July 2013

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Mid-Year Planning: Accounting for New Tax Rules



The American Taxpayer Relief Act of 2012 (ATRA), passed in early January, permanently extended a host of expiring tax provisions. It also largely set the rules for tax planning for 2013 and beyond. As you take stock of your tax situation this year, here are a few new wrinkles to keep in mind.

New top tax rate

The six tax brackets (10%, 15%, 25%, 28%, 33%, and 35%) that applied for the last several years have been made permanent for most individuals. That's really good news, since it removes a great deal of uncertainty going forward (it's always easier to plan when you know what the tax rates will be the following year).

But higher-income individuals and families will have to contend with a new top federal income tax bracket starting this year, paying tax on a portion of their income at a rate of 39.6%. The new 39.6% rate applies to individuals with taxable income exceeding \$400,000; married individuals filing joint federal income tax returns with taxable income exceeding \$450,000; married individuals filing separate returns with taxable income exceeding \$225,000; and individuals filing as head of household with taxable income exceeding \$425,000.

Higher rates on investment income for some

Most individuals won't see any change in the rate at which they're paying tax on long-term capital gains and qualifying dividends. If you're in the 10% or 15% marginal income tax bracket, a special 0% rate will generally apply. If you are in the 25%, 28%, 33%, or 35% tax brackets, a 15% maximum rate will generally apply.

If you're in the new top 39.6% tax bracket, though, it's going to be a little different starting this year--that's because in 2013 a new maximum rate of 20% will generally apply to some or all of your long-term capital gains and

qualifying dividends.

And keep in mind that a new Medicare contribution tax now applies to some or all of the net investment income of individuals with more than \$200,000 in modified adjusted gross income (\$250,000 for married couples filing a joint federal income tax return, and \$125,000 for married individuals filing separate returns). The Medicare contribution tax is 3.8%, and is in addition to other taxes that apply.

Other considerations

- This year, if your adjusted gross income (AGI) is greater than \$250,000 (\$300,000 if you're married and file a joint return, \$150,000 if married filing separately, and \$275,000 if you file as head of household), your personal and dependency exemptions will be phased out in part or in full. Similarly, your itemized deductions may be limited.
- If you itemize deductions, note that the AGI threshold for deducting qualified medical expenses on Schedule A increased this year from 7.5% to 10% for most individuals. If you or your spouse will be 65 or older by the end of the year, though, the 7.5% threshold will continue to apply for 2013.
- The rules allowing qualified charitable distributions from IRAs were extended through 2013. This popular provision allows individuals age 70½ or older to make qualified charitable distributions of up to \$100,000 from an IRA directly to a qualified charity; the charitable distributions are excluded from income and count toward satisfying any required minimum distributions for the year.

Make time to plan

It's never easy to set aside the time to analyze your current tax situation and project how you'll be affected by recent changes. But it's important to do so while you still have time to implement a plan and take action. This year, it's particularly important to consider all of your options if your income level brings you within range of one or more of the new provisions targeting higher-income individuals.

Choosing a Retirement Community



Homes available within retirement communities can be as diverse as the communities themselves, and range from small apartments in the city to luxury homes on the ocean. No matter which type of home you choose, make sure it will meet your needs both now and in the future.

Perhaps you've seen ads for a new "over 55" luxury condominium development in your town. Or another winter of shoveling has finally convinced you that it's time to move to a warmer climate. You're looking forward to life in a retirement community, but with so many options, how do you choose the right one?

Beginning the search

The first step is to think about where you want to live, how you want to spend your retirement years, and what type of home you can realistically afford. All retirement communities are designed with the needs of older adults in mind, but they provide different living arrangements, activities, and services.

One option that's become increasingly popular is the "active adult" community. Usually centered around a fitness facility, a clubhouse, or a golf course, this type of community offers many social and recreational opportunities, such as clubs, meals, and walking trails.

Other retirement complexes are geared toward individuals who want flexible living arrangements and services. These complexes may contain a variety of housing types, including independent-living, assisted-living, and long-term care facilities. They often offer extended assistance with daily tasks such as shopping and housekeeping, and emphasize easy access to health care.

For example, increasingly popular options for those 62 or older, who meet financial and health thresholds, are continuing care retirement communities (CCRCs) and fee-for-service continuing care retirement communities (FFSCCRCs). These adult communities offer, under one contract (and usually all in one location), an independent living unit (typically an apartment or cottage), residential amenities, and access to a continuum of long-term care services as residents' health and social needs change over time. These are just some of the options--many others are available.

The cost of convenience

Homes available within retirement communities can be as diverse as the communities themselves, and range from small apartments in the city to luxury homes on the ocean. No matter which type of home you choose, make sure it will meet your needs both now and in the future. More and more homes in retirement communities are incorporating universal design features, a trend that's likely to continue. These features include one-level living, extra lighting, easy-to-open doors and cabinets, and security systems that make day-to-day living simpler

and safer for people of all ages.

But the convenience of retirement living usually comes at a price. That price includes not only rental or mortgage payments, utilities, and insurance, but also any up-front or ongoing fees you'll owe. For example, a retirement community may charge a hefty fee for "buying in" to the community. One ongoing fee you may need to factor in is a homeowners or community association fee that may add hundreds, or even thousands, of dollars to your monthly housing costs. In general, the higher this fee, the more services or amenities are included, but make sure you understand what you're getting for your money. And don't forget about taxes. Even states with no state income tax may have high property taxes, sales and restaurant taxes, or "hidden" taxes on luxury goods or investments. A financial professional or tax advisor can help you determine the impact taxes will have on your finances.

And so that there are no unpleasant surprises, you should also consider the potential for costs to rise. Living in a community where costs for housing and services are constantly on the upswing is at best annoying, and at worst, financially devastating.

Try before you buy

Popular communities often have waiting lists, so it's a good idea to do your homework in advance. Start with a visit. If you're traveling out of town, find out if the community you're visiting offers a special travel package for potential residents--many do. If you're searching locally, visit each prospective community at least two or three times.

A checklist of questions to ask can come in handy when researching retirement communities. Here are a few items to include:

- Is the property well maintained?
- Is the atmosphere casual or formal?
- What social, recreational, and educational activities are available?
- Is public transportation nearby, or is van service available?
- Are pets allowed?
- Are guests restricted?
- Is medical care provided?
- Which services are included, and which are available at additional cost?
- Has the facility been accredited?

Most importantly, talk to residents and staff about their experiences--you'll get a much more realistic picture of life in a retirement community than you can glean from a brochure.



Portability allows a surviving spouse to use the unused applicable exclusion amount of the spouse who dies first to shelter property from federal gift and estate taxes. Portability of the exclusion between spouses would seem to make estate planning easier for many estates, but that may not always be the case.

Now that portability and the increased exclusion, which had been scheduled to expire in 2013, have been made permanent, it is probably a good time to review your estate plan and documents.

Portability of Applicable Exclusion Amount between Spouses

Transfers of property during life or at death are generally subject to federal gift or estate taxes. However, each taxpayer has an amount of property that can be sheltered from federal gift and estate taxes by the unified credit, called the "applicable exclusion amount."

Prior to 2011, each spouse was entitled to his or her own applicable exclusion amount, and any amount that a spouse did not use would be lost; so special planning was often used to insure neither spouse's exclusion was wasted.

In 2011 and later, the estate of the first spouse to die can elect to transfer any applicable exclusion amount that is not used to the surviving spouse. This is known as "portability." The applicable exclusion amount is redefined as equal to the sum of the basic exclusion amount of the surviving spouse and the unused applicable exclusion amount of the predeceased spouse, and the basic exclusion amount is equal to \$5 million as indexed for inflation each year (\$5,250,000 in 2013).

Now that portability and the increased exclusion, which had been scheduled to expire in 2013, have been made permanent, it is probably a good time to review your estate plan and documents. Portability of the exclusion between spouses and an increase in the basic exclusion amount should make estate planning easier for many estates.

Simple planning with portability

If you're planning today, you could transfer everything to your spouse at your death, and your estate can elect to transfer your unused applicable exclusion amount to your surviving spouse. Your spouse will then have an applicable exclusion amount equal to the sum of his or her own basic exclusion amount and your unused applicable exclusion amount, which your spouse can use for gift or estate tax purposes. For example, if you transfer your \$5,250,000 unused applicable exclusion to your surviving spouse, who also has a \$5,250,000 basic exclusion amount, your spouse then has a \$10,500,000 applicable exclusion amount in 2013 to shelter property from gift and estate tax. Such simple planning might be very practical for some married couples, especially where the spouses' combined estates are expected to be less than their combined applicable exclusion amounts.

Potential need for more complex planning

There are a number of reasons why such simple planning with portability may not always produce the desired or best results. These might include (among others):

- You have family members or individuals other than your spouse who you would like to benefit prior to the death of your spouse.
- You have grandchildren or later generations who you would like to benefit. The \$5,250,000 (in 2013) generation-skipping transfer (GST) tax exemption is not portable between spouses.
- State exclusion amounts may be different than the federal applicable exclusion amount and may not be portable between spouses.
- The unused exclusion is not adjusted for inflation after the first spouse's death, and may not fully protect appreciating property from estate tax in the surviving spouse's estate.

Use of A/B trust arrangement

Prior to 2011, many married couples with estates that were greater than the applicable exclusion amount would set up an A/B (or A/B/C) trust arrangement. In general, the first spouse to die would transfer an amount equal to the applicable exclusion amount to the "B" or credit shelter bypass trust. The B trust could benefit the surviving spouse and their children, but the B trust would be designed to bypass the surviving spouse's estate. The balance of the estate would be transferred to the surviving spouse, either outright or using an "A" marital trust, and qualify for the marital deduction. In some cases, a "C", "Q", or QTIP marital trust was also used if the first spouse to die wanted to control who received the marital trust property at the second spouse's death. The A/B trust arrangement typically assured that there would be no estate tax at the first spouse's death and that neither spouse's applicable exclusion amount was wasted.

An A/B trust arrangement may still be useful, even with the availability of portability. For example, the B trust can be used to provide for family members or individuals other than your spouse (and even your spouse) prior to the death of your spouse. You could also allocate your GST tax exemption or state exclusion to the B trust. Also, appreciation of property after the transfer to the B trust should not be subject to estate tax at your spouse's death. The A trust could use your spouse's applicable exclusion amount, GST tax exemption, and state exclusion.

The use of trusts can also provide other benefits, such as control over who receives your property and when, investment management of trust property for trust beneficiaries, avoidance of probate, and asset protection.

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I just bought a vacation home. Do I need to purchase a specific type of insurance?

Insuring a vacation home is different from insuring a primary residence. As a result, you'll want to purchase insurance that is specifically geared to provide coverage for this type of property.

When insuring a vacation home, the type and cost of coverage will vary, depending upon the insurance company and the state in which your vacation home is located.

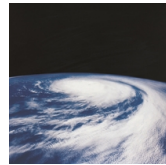
Most insurers offer at least some type of insurance that is specifically designed for second/vacation homes. Coverage under these types of policies can range from standard coverage that protects against certain named perils, to more comprehensive coverage that protects against all perils unless specifically excluded in a policy.

Keep in mind that, depending on what is covered under the policy, you may need to obtain additional protection (e.g., property or liability coverage) through either an endorsement or separate policy. In addition, if your vacation home is located in an area that is susceptible to flood damage--which is not covered under a standard vacation home

policy--you'll want to look into obtaining separate coverage for that peril as well.

Due to some of the unique circumstances surrounding vacation homes (e.g., high-risk location, not being occupied for long periods of time), vacation home insurance premiums are usually much higher than those for a primary residence. However, you may be able to save money by insuring your vacation home with the same company that provides coverage for your primary residence (some insurers may require this). In addition, you may be eligible for other discounts, such as those offered for newly built homes, nonsmokers, and homes that have a security system installed. Policy discounts will vary by state and insurer.

Because of the vast array of vacation home insurance products on the market, you'll want to be sure to shop around for the best coverage and rates. You may also want to contact the state department of insurance where your vacation home is located for additional information on the coverage and rate options that may be available.



Will my homeowners insurance policy cover hurricane damage?

It depends. While the types of coverage offered by standard homeowners insurance policies vary, windstorms are one of the basic perils that most standard homeowners insurance policies will cover. This means your policy should compensate you for loss/damage to your home that results from a hurricane or other windstorm (e.g., broken windows, torn roof, damage from fallen trees).

Keep in mind that if you live in an area of the country that is prone to hurricanes (e.g., the coastal region of Florida), an insurance company may exclude coverage for hurricane damage from a standard homeowners insurance policy. And even if an insurance company does provide coverage, homeowners insurance policies in states that are at a high risk for hurricanes often contain a separate, higher deductible for hurricane damage.

If you find that your current policy doesn't provide coverage for hurricane damage, you have a few options. First, check with your insurance company and ask if you can add windstorm coverage to your existing policy by purchasing an endorsement (an optional

coverage that gets attached to your policy). Another option is to shop around and see if another company will sell you a homeowners policy that includes windstorm damage as a standard covered peril. You may also want to check to see whether your state administers windstorm insurance plans that pick up where regular homeowners policies leave off. If you live in one of these states, you may be able to purchase a separate windstorm policy to provide you with coverage for hurricane damage.

Finally, keep in mind that hurricanes are often accompanied by flooding. In many cases, flooding can cause far more damage to a home and other property than high winds. Unfortunately, though, neither standard homeowners insurance nor a separate windstorm policy will cover flood damage. If you want this type of protection, you'll need to purchase a separate flood insurance policy. The National Flood Insurance Program offers flood insurance through the federal government and some private insurers.