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Executive Compensation ■ Succession ■ Wealth Transfer Planning

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Rules of the Road for Taking an Early Retirement

Have you ever entertained thoughts of taking an early retirement? Suppose you're age 55 and could take home a pension income that amounted to 60% of your pay if you retire now. If your income is high, it may seem that you would be able to retire in reasonable comfort. However, before calling it quits, weigh all of the facts *carefully* to be sure an early retirement makes financial sense for you. Here are eight rules to consider if you're thinking about taking an early retirement:

Rule #1: Weigh the pros and cons of retiring now or in the future. Retiring at age 55 with, hypothetically, 60% of your income may seem like a good deal at first. But if you wait until full retirement age, you will have another 10 years of full earnings under your belt, along with any pay increases from promotions, merit raises, and inflation. This will provide you with more money to save for retirement, and ultimately, it may boost your Social Security and pension benefits. Also, if you consider the difference in the percentage you will receive now and in 10 years for example, 60% if you retire now versus 80% if you retire in 10 years retiring now may not seem as attractive.

Rule #2: Remember to factor inflation into your decision. If you think you could manage on 60% of your income, remember that inflation will erode your pension. If you retire today and let's say you receive a pension income of $1,600 per month for life, in 20 years at a 4% rate of inflation, you'll have the equivalent of $707 in today's dollars.

Rule #3: Prepare for longevity. The longer you live, the more money you'll need in retirement. Due to increased longevity, an early retirement plan must include a budget to meet the financial needs of several decades beyond the normal retirement age of 65.

Rule #4: Evaluate other retirement income resources. If you already have a sizable nest egg, or if you expect to collect a pension from a previous employer, the amount of your *current* employer-sponsored retirement plan may not be as robust. If so, perhaps you can exit the labor force earlier because you have other sources of retirement income.

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Ten Tips for Creating an Effective Estate Plan

Whether your estate plan is simple or complicated, many details can undermine the effectiveness of your plan. But, there are also ways to ensure the effectiveness of your plan. Here are 10 steps to help remedy or avoid some common estate planning mistakes:

Consider using a will to transfer property to children instead of owning property jointly. Unlike a will, a transfer of an interest in your property is irrevocable, which may prevent you from changing the disposition if circumstances change before your death. Holding the title to your personal residence jointly can result in partial loss of the capital gain exclusion if it is sold before your death. Therefore, it's often recommended that you use your will to make any property transfers that will occur upon your death.

Think before gifting property to your children. Parents often regret having made outright gifts to a child if the child subsequently divorces, and the ex-son- or daughter-in-law is awarded an interest in the gifted property by a court. Or, under other circumstances, the property may be taken pursuant to a legal judgment against the child. These problems can be avoided through proper use of trusts or a business entity, such as an LLC.

Ensure your assets pass according to your wishes upon your death. Many types of assets can pass to your heirs or others based upon beneficiary designations (e.g., life insurance, IRAs, brokerage accounts). The provisions of your will cannot change a beneficiary designation. Remember to account for items you've already designated when you create your will. Review your will, as well as all other beneficiary designations, when formulating your estate plan.

Know your estate's true value for Federal estate tax purposes. Many people are unaware of the fact that life insurance proceeds are included in their taxable estates if they own the policy. This could increase their total estate value to more than the amount sheltered from estate tax by the estate tax exemption which doubled in 2018 with the new tax law to $11.2 million.

Check changes in the law regarding state death taxes. Many states have "decoupled" their death tax from the Federal estate tax, which means your estate could be subject to death tax in a state, even if no Federal estate tax is due. However, with proper planning, this may be avoided. The laws of each state where you own property should be carefully reviewed to determine potential state death taxes and how to reduce them.

Review the portability provision of the estate tax exemption. Estate tax exemption may be transferred between spouses, so that if one spouse dies and does not use the full exemption amount, the remainder can be used by the surviving husband or wife, if he or she also dies. For estate planning purposes, this means that husbands and wives do not have to split assets between them, or be concerned about who holds the title on various assets. Yet, this does not eliminate the need for planning.

Maximize income tax basis "step-up" benefits at death. Consider holding low-basis/high-value assets to be given at your death, since the basis for capital gain computation purposes will be increased to fair market value at death. If the asset is given away, the basis remains at the property's original cost. However, the combination of stepped-up basis and a higher exemption in 2018 will reduce income and transfer taxes.

Specify your desired funeral arrangements. A pre-arranged funeral may relieve family members from additional stress upon your death. You can also prepare for the costs of a funeral.

Plan for a potential disability. Consider establishing advance directives, powers of attorney, and designated trustees, since costly and time-consuming court proceedings may be required in order to appoint a guardian or conservator to act on your behalf if you become incapacitated.

Review and update your estate plan regularly. Changes in the law and in your personal situation make it important to periodically review and update your estate plan so that it continues to reflect your wishes.

Early and thorough estate planning can help you reach your financial goals and help ensure that your wishes will ultimately be implemented. Be sure to consult with your tax, legal, and financial professionals. ■

Taking Charitable Giving to Another Level

Did you know that you can gift a new or existing life insurance policy to your favorite charity? When properly designed, a **charitable life insurance** program may improve your overall financial situation and offer tax benefits, all while supporting a charitable cause.

Generally, there are three methods used to gift a life insurance policy to a qualifying charity: a **charitable bequest**, a **charitable gift**, and a **charity-owned policy**. Regardless of the strategy, policy ownership and **beneficiary** arrangements play an important role in the planning process. A consultation with a qualified legal professional can clarify your goals and expectations, provide information on the limitations on charitable deductions, and help you achieve the desired results, while avoiding unnecessary complications.

A Comparison of Gifting Strategies

A **charitable bequest** is ideal if you would like a charity to benefit from the proceeds of an existing life insurance policy but do not wish to surrender control during your lifetime. By changing the designated beneficiary to a desired charity, you retain the benefits of owning a policy because **incidents of ownership** still exist in the policy. There is no immediate income tax benefit for this type of charitable gift. Upon your death, however, even though the proceeds will be included in your gross estate, a charitable deduction for the full value of the policy proceeds is allowed.

If you wish to receive an *immediate* income tax deduction for a gift of an existing policy, consider a **charitable gift**. By changing the beneficiary *and* ownership designations to a favorite charity, you can obtain an immediate gift tax charitable deduction for the policy. This deduction is based on the lesser of your cost basis or the value of the policy. You may also qualify for an income tax deduction.

If you make regular cash contributions to a charity, you may be able to leverage smaller gifts into a larger endowment. With a **charity-owned policy,** a life insurance policy—where permitted by state law—is purchased by and made payable to a charity of your choice. Policy premiums are technically paid by the charity. To offset this cost, you make annual cash gifts to the charity, and as a result, you may be eligible to deduct a portion of your charitable donations from your income taxes. A gift tax charitable deduction for the full value of the annual cash gift is allowed. This strategy creates a "win-win" situation for you and the recipient charity.

Know the Insurable Interest Laws

Regardless of your gifting strategy, be aware of the insurable interest laws in the state where the policy was originally purchased. Although the donor makes contributions to the charity in cash, which is then used by the charity to pay premiums on the life insurance policy, the life insurance policy insures the donor's life. Insurable interest is typically considered to be an interest based on family, marriage, or financial obligation; consequently, the charity's insurable interest in the policy

may be called into question, thereby jeopardizing the tax benefit and placing the policy proceeds in the donor's estate. However, a case for insurable interest can be anticipated and incorporated into the trust documents.

The Best of Both Worlds

If you are charitably inclined and are seeking tax advantages, the gifting of life insurance can offer unique planning opportunities. The potential for charitable income tax deductions or an estate tax reduction, combined with supporting a worthy cause, may make this type of gift appropriate for you. Usually, such charitable life insurance gifting strategies can be accomplished with few legal challenges and little publicity. Careful planning, with the guidance of a qualified legal professional, can help ensure that your charitable life insurance program is structured according to your wishes. ■

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However, don't expect Social Security to provide most of your retirement income. The Social Security Administration (SSA) projects that benefits will replace about 40% of the average worker's preretirement income and retirees may need 70% or more of preretirement earnings to live comfortably (SSA, 2017). Also, since the future of Social Security and **Medicare** is uncertain, you may have to provide more funds for future health care expenses.

Rule #5: Evaluate the economics of part-time work. If you decide to leave your present job, will you be securing employment elsewhere until you permanently retire and start collecting your pension? Keep in mind that it may be difficult to find another equally high-paying position. Although the prospect of part-time work may make it possible to consider an early retirement option, be sure you can depend on a reduced part-time income until full retirement.

Rule #6: Be aware of the early retirement impact on Social Security benefits. If you are under full retirement age and continue working after you begin collecting Social Security benefits, you may have to "give back" a portion of your benefits. In addition, if you continue working after you begin collecting Social Security, a portion of your Social Security benefits might be taxed. You can determine how much of your benefits will be included in your gross taxable income with a calculator found online at the Social Security Administration's website, www.ssa.gov.

Rule #7: Take an early retirement before downsizing or layoffs occur. Is there a chance your company will lay you off if you do not elect to leave on your own? Many companies now lay off high earners as part of their cost-cutting measures. If your company is experiencing financial difficulties and downsizing appears imminent, you may get a better deal through early retirement than through the company's severance package.

Rule #8: Understand the potential tax consequences of early retirement. If you opt for early retirement, in some cases you may incur a 10% Federal income tax penalty for early withdrawals from a qualified retirement plan. Keep in mind that withdrawals taken from an **Individual Retirement Account (IRA)** before age 59½ may also be subject to a penalty.

Early retirement may be a long-held dream and a financial possibility. But, before calling it quits, assess your situation carefully. You will have to live with the effects of your choice for the rest of your life. Take the time now to make sure it will be a smart decision in the long run. ■

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