

# Breed's Hill Newsletter

## Planning Your Financial Future

### What to Do After the Death of a Loved One



Losing a loved one can be a difficult experience. Despite the emotional trauma involved, you may also be responsible for handling a variety of financial, legal, and administrative tasks. You may find yourself unsure

of where to begin and what to do.

However, do not be hasty when settling your loved one's estate. Important decisions need to be made regarding distributions, which must be made in compliance with the will and applicable laws. Seek an experienced estate planning professional for advice. The following suggestions may provide a roadmap to help you navigate through the process.

#### Initial tasks

**Note:** *Some of the following tasks may have to be completed by the estate's personal representative.*

- Upon the death of your loved one, call close family members, friends, and clergy first because you'll need their emotional support.
- Arrange the funeral, burial or cremation, and memorial service. Hopefully, your loved one will have made arrangements ahead of time. Then notify family and friends of the final arrangements and place an obituary in the local paper (often the funeral home will handle this for you).
- Obtain certified copies of the death certificate (again, the funeral home should be able to get copies for you).
- Find and review your family member's finances, and look for relevant documents such as a will and trusts, deeds and titles to motor vehicles.
- Report the death to Social Security. If your loved one was receiving benefits via direct deposit, request that the bank return funds received for the month of death and thereafter to Social Security. Do not cash any Social Security checks received by mail. Return all checks to Social Security as soon as possible.

- Make a list of assets and debts. Be on the lookout for pension plans, IRA, 401(k), and other retirement plans owned by the deceased, as well as life insurance policies, bank accounts, and investments. Notify those named as beneficiaries of assets such as life insurance and retirement plans.
- Make sure mortgage and insurance payments continue to be made while the estate is being settled.
- Contact all credit card companies and let them know of the death. Cancel all cards unless you're named on the account and wish to retain the card.

#### Within 1 to 3 months of death

- File the will with the appropriate probate court. If real estate was owned out of state, file ancillary probate in that state. If there is no will, contact the probate court for instructions or contact a probate attorney for assistance.
- Notify creditors by mail and by placing a notice in the newspaper. Claims must be made within the statute of limitations, which varies from state to state (30 days from actual notice is common). Insist on proof of all claims. Notify heirs named in the will. Often, the probate process will require formal notification to heirs and others named in the will.

#### Within 6 to 9 months of death

- Federal and/or state estate tax return(s) may need to be filed, usually within nine months of death, although state laws may vary.
- Also, federal and state income taxes are due for the year of death on the normal filing date, unless an extension is requested. If there are trusts, separate income tax returns may be necessary.
- Update your own estate plan if your loved one was a beneficiary or appointed as an agent, trustee, or guardian.

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Estate Planning: Consider the Tax Basis of Gifted or Inherited Property

For College Savings, 529 Plans Are Hard to Beat

How long could it take to double your money?

Do I need to pay estimated tax?



**An asset's tax basis can be important when deciding whether to make gifts now or transfer property at your death. When you make a gift of property during your lifetime, the recipient generally receives your basis in the property. When you transfer property at your death, the recipient generally receives a basis equal to the fair market value of the property as of the date of your death. The difference can substantially affect the amount of taxable gain when the recipient sells the property.**

## Estate Planning: Consider the Tax Basis of Gifted or Inherited Property

Tax basis can be important when deciding whether to make gifts now or transfer property at your death. This is because the tax basis of the person receiving the property depends on whether the transfer is by gift or at death. This, in turn, affects the amount of taxable gain subject to income tax when the person sells the property.

### What is tax basis?

The tax basis of an asset is used when determining whether you have recognized a capital gain or loss on the sale of property for income tax purposes. (Gain or loss on the sale of property equals the difference between your adjusted tax basis and the amount you realize upon the sale of the property.) When you purchase property, your basis is generally equal to the purchase price. However, there may be some adjustments made to basis.

### What is the tax basis for property you receive as a gift?

When you receive a gift, you generally take the donor's basis in the property. (This is often referred to as a "carryover" or "transferred" basis.) The carryover basis is increased — but not above fair market value (FMV) — by any gift tax paid that is attributable to appreciation in value of the gift. (Appreciation is equal to the excess of FMV over the donor's basis in the gift immediately before the gift.) However, for the purpose of determining loss on a subsequent sale, the carryover basis cannot exceed the FMV of the property at the time of the gift.

**Example:** Say your father gives you stock worth \$1,000 and the gift incurs no gift tax. He purchased the stock for \$500. Your basis in the stock, for the purpose of determining gain on the sale of the stock, is \$500. If you sold the stock for \$1,000, you would have gain of \$500 (\$1,000 received minus \$500 basis).

Now assume that the stock is only worth \$200 at the time of the gift and you sell it for \$200. Your basis in the stock, for the purpose of determining gain on the sale of the stock, is still \$500, but your basis for determining loss is \$200. You do not pay tax on the sale of the stock. You do not recognize a loss either. In this case, it would have been better if your father had sold the stock (and recognized the loss of \$300 — his basis of \$500 minus \$200 received) and then transferred the sales proceeds to you as a gift.

### What is the tax basis for property you inherit?

When you inherit property, you generally receive an initial basis in property equal to the

property's FMV. The FMV is established on the date of death or on an alternate valuation date six months after death. This is often referred to as a "stepped-up" basis, since basis is typically stepped up to FMV. However, basis can also be "stepped down" to FMV.

**Example:** Say your mother leaves you stock worth \$1,000 at her death. She purchased the stock for \$500. Your basis in the stock is a stepped-up basis of \$1,000. If you sold the stock for \$1,000, you would have no gain (\$1,000 received minus \$1,000 basis).

Now assume that the stock is only worth \$200 at the time of your mother's death. Your basis in the stock is a stepped-down basis of \$200. If you sold the stock for more than \$200, you would have gain.

### Make gift now or transfer at death?

As the following example shows, tax basis can be important when deciding whether to make gifts now or transfer property at your death.

**Example:** You purchased land for \$25,000. It is now worth \$250,000. You give the property to your child (assume the gift incurs no gift tax), who then has a tax basis of \$25,000. If your child sells the land for \$250,000, your child would have taxable gain of \$225,000 (\$250,000 sales proceeds minus \$25,000 basis).

If instead you kept the land and transferred it to your child at your death when the land is worth \$250,000, your child would have a tax basis of \$250,000. If your child sells the land for \$250,000, your child would have no taxable gain (\$250,000 sales proceeds minus \$250,000 basis).

In addition to tax basis, you might consider the following questions:

- Will making gifts reduce your combined gift and estate taxes? For example, future appreciation on gifted property is removed from your gross estate for federal estate tax purposes.
- Does the recipient need a gift now or can it wait? How long would a recipient have to wait until your death?
- What are the marginal income tax rates of you and the recipient?
- Do you have other property or cash that you could give?
- Can you afford to make a gift now?

## For College Savings, 529 Plans Are Hard to Beat



### 529 plan assets reach \$353 billion

As of June 2019, assets in 529 plans reached \$353 billion — \$328 billion (93%) in college savings plans and \$25 billion (7%) in prepaid tuition plans.

Source: Strategic Insight, 529 Data Highlights, 2Q 2019

**Note:** Investors should consider the investment objectives, risks, charges, and expenses associated with 529 plans before investing. More information is available in each issuer's official statement and applicable prospectuses, which contain this and other information about the investment options, underlying investments, and investment company, and should be read carefully before investing. Also consider whether your state offers a 529 plan that provides residents with favorable state tax benefits and other benefits, such as financial aid, scholarship funds, and protection from creditors. As with other investments, there are generally fees and expenses associated with participation in a 529 plan. There is also the risk that the investments may lose money or not perform well enough to cover college costs as anticipated.

Raising kids is hard enough, so why not make things easier for yourself when it comes to saving for college? Ideally, you want a savings vehicle that doesn't impose arbitrary income limits on eligibility; lets you contribute a little or a lot, depending on what else happens to be going on financially in your life at the moment; lets you set up automatic, recurring contributions from your checking account so you can put your savings effort on autopilot; and offers the potential to stay ahead of college inflation, which has been averaging 3% to 4% per year.<sup>1</sup> Oh, and some tax benefits would be really nice, too, so all your available dollars can go to college and not Uncle Sam. Can you find all of these things in one college savings option? Yes, you can: in a 529 plan.

### Benefits

529 college savings plans offer a unique combination of features that are hard to beat when it comes to saving for college, so it's no surprise why assets in these plans have grown steadily since their creation over 20 years ago.

**Eligibility.** People of all income levels can contribute to a 529 plan — there are no restrictions based on income (unlike Coverdell accounts, U.S. savings bonds, and Roth IRAs).

**Ease of opening and managing account.** It's relatively easy to open a 529 account, set up automatic monthly contributions, and manage your account online. For example, you can increase or decrease the amount and frequency of your contributions (e.g., monthly, quarterly), change the beneficiary, change your investment options, and track your investment returns and overall progress online with the click of a mouse.

**Contributions.** 529 plans have high lifetime contribution limits, generally \$350,000 and up. (529 plans are offered by individual states, and the exact limit depends on the state.) Also, 529 plans offer a unique gifting feature that allows lump-sum gifts up to five times the annual gift tax exclusion — in 2020, this amount is up to \$75,000 for individual gifts and up to \$150,000 for joint gifts — with the potential to avoid gift tax if certain requirements are met. This can be a very useful estate planning tool for grandparents who want to help pay for their grandchildren's college education in a tax-efficient manner.

**Tax benefits.** The main benefit of 529 plans is the tax treatment of contributions. First, as you save money in a 529 college savings plan (hopefully every month!), any earnings are tax deferred, which means you don't pay taxes on the earnings each year as you would with a regular investment account. Then, at college

time, any funds used to pay the beneficiary's qualified education expenses — including tuition, fees, room, board, books, and a computer — are completely tax-free at the federal level. This means every dollar is available for college. States generally follow this tax treatment, and many states also offer an income tax deduction for 529 plan contributions.

### Drawbacks

But 529 plans have some potential drawbacks.

**Tax implications for funds not used for qualified expenses.** If you use 529 plan funds for any reason other than the beneficiary's qualified education expenses, earnings are subject to income tax (at your rate) and a 10% federal penalty tax.

**Restricted ability to change investment options on existing contributions.** When you open a 529 college savings plan account, you're limited to the investment options offered by the plan. Most plans offer a range of static and age-based portfolios (where the underlying investments automatically become more conservative as the beneficiary gets closer to college) with different levels of risk, fees, and management objectives. If you're unhappy with the market performance of the option(s) you've chosen, you can generally change the investment options for your *future* contributions at any time. But under federal law, you can change the options for your *existing* contributions only twice per year. This rule may restrict your ability to respond to changing market conditions, so you'll need to consider any investment changes carefully.

### Getting started

529 college savings plans are offered by individual states (but managed by financial institutions selected by the state), and you can join any state's plan. To open an account, select a plan and complete an application, where you will name an account owner (typically a parent or grandparent) and beneficiary (there can be only one); choose your investment options; and set up automatic contributions if you choose. You are then ready to go. It's common to open an account with your own state's 529 plan, but there may be reasons to consider another state's plan; for example, the reputation of the financial institution managing the plan, the plan's investment options, historical investment performance, fees, customer service, website usability, and so on. You can research state plans at the [College Savings Plans Network](#).

<sup>1</sup> College Board, Trends in College Pricing, 2014-2018

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## How long could it take to double your money?

If you're saving for college, retirement, or a large purchase, it can be useful to quickly calculate how an anticipated annual rate of return will affect your money over time. To find out, you can use a mathematical concept known as the Rule of 72. This rule can give you a close approximation of how long it would take for your money to double at any given rate of return, assuming annual compounding.

To use this rule, you simply divide 72 by your anticipated annual rate of return. The result is the approximate number of years it will take for your money to double.

For example, if your anticipated annual rate of return is 6%, you would divide 72 by 6. Your money can be expected to double in about 12 years. But if your anticipated annual rate of return is 8%, then your money can be expected to double in about 9 years.

The Rule of 72 can also be used to determine what rate of return you would need to double your money in a certain number of years. For

example, if you have 12 years to double your money, then dividing 72 by 12 would tell you that you would need a rate of return of 6%.

Another way to use the Rule of 72 is to determine when something will be halved instead of doubled. For example, if you would like to estimate how long it would take for annual inflation to eat into your savings, you could divide 72 by the rate of inflation. For example, if inflation is 3%, then it would take 24 years for your money to be worth half its current value. If inflation jumped to 4%, then it would take only 18 years for your purchasing power to be halved.

Although using a calculator will give you more precise results, the Rule of 72 is a useful shortcut that can help you understand how long it might take to reach a financial goal, and what annual rate of return you might need to get there.



## Do I need to pay estimated tax?

Taxpayers are required to pay most of their tax obligation during the year by having tax withheld from their paychecks or pension payments, or by making estimated tax payments. Estimated tax is the primary method used to pay tax on income that isn't subject to withholding. This typically includes income from self-employment, interest, dividends, and gain from the sale of assets. Estimated tax is used to pay both income tax and self-employment tax, as well as other taxes reported on your income tax return.

Generally, you must pay federal estimated tax for the current year if: (1) you expect to owe at least \$1,000 in tax for the current year, and (2) you expect your tax withholding and refundable tax credits to be less than the smaller of (a) 90% of the tax on your tax return for the current year, or (b) 100% of the tax on your tax return for the previous year (your tax return for the previous year must cover 12 months).

There are special rules for farmers, fishermen, and certain high-income taxpayers. If at least two-thirds of your gross income is from farming or fishing, you can substitute 66-2/3% for 90% in general rule (2)(a) above. If your adjusted

gross income for the previous year was more than \$150,000 (\$75,000 if you were married and filed a separate return for that year), you must substitute 110% for 100% in general rule (2)(b) above.

If all of your income is subject to withholding, you probably don't need to pay estimated tax. If you have taxes withheld by an employer, you may be able to avoid having to make estimated tax payments, even on your nonwage income, by increasing the amount withheld from your paycheck.

You can use Form 1040-ES and its worksheets to figure your estimated tax. They can help you determine the amount you should pay for the year through withholding and estimated tax payments to avoid paying a penalty. The year is divided into four payment periods. After you have determined your total estimated tax for the year, you then determine how much you should pay by the due date of each payment period to avoid a penalty for that period. If you don't pay enough during any payment period, you may owe a penalty even if you are due a refund when you file your tax return.

Withholding and estimated tax payments may also be required for state and local taxes.