Planning for Generations
Family Wealth MANAGEMENT

Financial Perspectives

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Savings Bond Changes That Could Trap You

How many people have gotten U.S. Savings Bonds as gifts or as part of a workplace savings plan only to file them away in a drawer and never think of them again? Plenty. According to the U.S. Bureau of Public Debt, $12.5 billion in savings bonds remain outstanding that are past final maturity and no longer paying any interest whatsoever.

This is a problem for several reasons. First, the bonds are basically dead money—a free loan to the U.S. government until the owner decides to call it in by redeeming the bond. Instead of earning money in another investment, the money in the bond sits earning nothing.

Second, once a savings bond reaches final maturity, its owner is required by the IRS to report all the interest accrued on the bond as taxable income for that year.
Failure to do so may result in the payment of penalties, back taxes, and the restatement of prior year returns—not an inviting prospect.

The reason $12.5 billion in savings bonds remain unredeemed, though, is not due solely to owner forgetfulness. Some is due to the mistaken assumption by people that if they don't redeem the bonds, they don't have to report the interest. The root of the problem lies in the fact that for an instrument that is often the first investment given or received in life, U.S. Savings Bonds present some surprising traps that make them tough to manage properly.

First, how many other investments do people have where they never get a statement apprising them of the value of their investment or its recent performance? With savings bonds, you either have to call the Bureau of Public Debt or go to its website at www.treasurydirect.gov to find out what the bond is worth and what interest rate it's paying.

$12.5 billion in U.S. Savings Bonds are past final maturity and no longer pay any interest whatsoever and, apart from being "dead money," these bonds can pose nasty surprises

Second, how often do you find an investment where the issuer never notifies you the investment has reached maturity? In fact, on some U.S. Savings Bonds you can look all over the bond itself and find no indication whatsoever of when it matures. Again, to get that information, you must call the Bureau of Public Debt or go to its website.

The government recently created another potential problem spot with the Sept. 2004 elimination, of new HH bonds. These bonds allow owners of Series E, EE or matured H bonds to roll over a minimum $500 of bonds into HH bonds, which then do not

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Spring Update

I'd like to bring you up to date on what we've been doing (and what we plan to do) to improve our product and service offerings. First, to help us deliver an even better client experience, we are creating a Client Advisory Board. The objective will be to help us evaluate our products, services and project and planning ideas to ensure that we are fully connected to the needs of our clients. Our team is selecting several clients to meet twice a year for a two-hour meeting at a nice location, followed by cocktails and a relaxing dinner. You will be receiving a special client survey form in the near future. Please complete and return it within one week of your receipt.

By the way, check out our new website (**familywealth.info**). Weekly updates on this site will be our main communication channel in the future. In August, we will have the ability to aggregate all of your accounts onto one customized report that will show the performance of your entire portfolio. Finally, we have upgraded our computer security, not only to protect the integrity of your data from hackers but also to recover in the event of a disaster.

We truly value your opinion and look forward to creating the kind of experience that you want to tell your friends and family about. Here's wishing you a healthy and happy spring, and I'll have more to review in three months.

Martin V. Higgins

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How To Avoid Common IRA Mistakes

There's just too much to know about IRAs. But some things are too important not to know—such as how to avoid these common mistakes.

Have A Backup. Most IRA owners name a primary beneficiary when they open their account, but they may fail to name a contingent beneficiary. A beneficiary is the person who inherits your IRA when you die. A contingent beneficiary is the person who gets your IRA if your primary beneficiary dies before you. Not naming a contingent beneficiary can cause unnecessary tax liabilities.

Typically, IRA owners name their spouse as beneficiary. That works fine as long as your spouse outlives you. She can put the inherited IRA in her name and take minimum required distributions based on her own life expectancy. But a problem can arise if she dies before you do.

You could name a new beneficiary after your spouse's death—if you think of it. But it's not as though the institution that has custody of the IRA will ever prompt you to do that. And if you don't, and you die without a specified beneficiary for the account, the IRA is likely to go into your estate. If you are less than 70½ at the time of your death and your IRA goes into your estate, the IRA assets will have to be withdrawn within five years. If you are older, the distributions can be stretched out over what would have been your life expectancy, based on IRS actuarial tables. In either case, though, the money will come out more quickly than if you had named a child as contingent beneficiary. Then, the child could have taken withdrawals based on his or her own life expectancy—a much longer time period. That would let the IRA assets continue to grow tax-deferred—or tax-free in the case of a Roth IRA.

With an IRA, seemingly small mistakes made when you set up your account or inherit it can cost you dearly

A Matter Of Trust. Some common mistakes can occur when an IRA owner names a trust as beneficiary. A trust can be used to protect IRA assets from creditors and to make sure your wishes are carried out after you die. But you cannot name a garden variety trust as beneficiary. It requires a trust with special wording. Also, when an IRA owner dies, a custodian could mistakenly name a trust as the IRA owner—thus making the entire IRA immediately taxable. What's the right way to do it? If you want your IRA to have the benefits of a trust after you die, your IRA must name a special trust that qualifies as a "designated beneficiary." You can then name your loved ones as beneficiaries of the trust. This will preserve the IRA's tax deferral while seeing that the money is disbursed according to your wishes as outlined in the trust.

End Game. Once you turn age 70½, the IRS requires you to take minimum annual withdrawals from your IRA based on your life expectancy. What IRA beneficiaries may not realize is that this requirement continues when the owner dies—even in the year of his death. The beneficiary must figure out what would have been the required minimum distribution and withdraw that amount. ●

If The Proverbial Bus Hits You, A Medical Power Of Attorney

Chances are, when you think of planning for unforeseen events, money is your first line of defense. But what if your financial health is fine and it's your physical health that fails you? An accident, a heart attack or stroke, Alzheimer's, cancer—any of these could quickly rob you of the ability to look after yourself and make crucial decisions about your care. Two documents—a living will and a medical power of attorney—could help ensure you are cared for according to wishes you set forth in healthier times.

A living will or health care declaration is a signed statement to medical personnel providing information on what you do and don't want with respect to your medical care. This document, which your state of residence may require to be notarized, lets you decide in advance whether or not you want to receive a transfusion, surgery, painkillers, cardiopulmonary resuscitation, and other life support in the event you become incapacitated.

But simply having a living will may not be sufficient to ensure your wishes are carried out. What if it isn't brought to the attention of medical personnel, or doesn't cover the specifics of a particular medical condition? You could still end up having decisions about your care made by an estranged family member or even a complete stranger. A medical power of attorney can help make sure that doesn't happen.

A medical power of attorney empowers another person—your health-care agent—to make health-care decisions on your behalf. Yet while this document takes effect as soon as you sign it, the agent will be able to act for you only if your physician certifies in writing that you're not competent to make your

Is Your Property Adequately Insured?

Getting the right property and casualty insurance coverage may not rank high on your list of financial priorities. Compared with investment decisions and estate planning issues, questions about the language in your homeowner's policy, say, may seem hardly worth considering. Yet the more successful you become, the more complicated your asset-protection needs are likely to be—and the more you have to lose. Suppose, for example, that in addition to your primary residence—a historic home—you also own a house at the beach and a condo in the city. The properties are in three different states. The value of your collection of Abstract Expressionist paintings has grown rapidly. And you just volunteered to serve on the board of directors of a charitable organization.

Almost every aspect of this situation could cost you dearly. Insurance laws may vary widely from state to state, different kinds of property require specialized coverage, and collections of art, antique cars, and other unique items may be difficult to protect fully. Meanwhile, serving on a nonprofit's board could subject you to additional personal liability.

Safeguarding yourself and your family may mean buying additional coverage, but more insurance isn't necessarily the solution. Rather, it's important to review all of your needs, consider specialized policies or policy options, and coordinate your coverage with other aspects of your financial situation. Here are several shortcomings that could prove costly.

• Leaving gaps in homeowner's coverage. Any homeowner needs to review coverage regularly to keep up with rising replacement costs. But insuring different kinds of homes in different locales poses extra challenges. If you buy insurance from more than one carrier, you may face contrasting rules, limitations, and policy renewal dates. For example, the liability limit on the policy for a second home might fall below the minimum on an excess liability policy designed to complement the insurance on your primary home. You could wind up responsible for the difference.

• Ignoring properties' unique characteristics. One perk of affluence is the means to own exceptional homes; one drawback is that they may be difficult to insure adequately. Standard homeowner's coverage won't pay for the materials and craftsmanship needed to rebuild that 19th century showplace you've painstakingly restored. Coastal homes may face hurricane damage, while a place in the California mountains could be subject to earthquakes or wildfires. Meanwhile, city co-ops or condos may need policies tailored to their building's or association's coverage.

• Underinsuring art and collectibles. Standard homeowner's policies limit coverage for the losses of antiques, furs, and other valuables. And while you could schedule additional coverage, insuring the real value of a collection of contemporary art or vintage muscle cars likely will require a specialized policy addressing several critical issues. How is the value of the collection determined? (You'll need a professional appraisal when the policy is designed, with frequent updates as items appreciate.) Will a damaged or destroyed item be paid for with cash, or will you be required to have it replaced or restored? Will additions to your collection automatically be covered?

• Forgetting to insure household employees. When someone works for you or your family, as a nanny, landscaper, personal assistant, or in another role, you could be liable for medical expenses and lost wages if the worker is hurt on the job. Several states require household employers to pay into a workers' compensation fund, while in other states it's optional, but providing such insurance may be mandatory for ensuring your financial well being. If an employee drives your car, also make sure he or she is included on your policy.

• Neglecting your liability as a board member. Excess liability coverage could help protect you if you're sued as a director of a nonprofit's board. Or for more comprehensive protection, you may want to consider special directors' and officers' liability insurance.

• Failing to get frequent policy reviews and updates. Your financial life isn't static, and neither are your insurance needs. The value of a collection may increase; extensive home renovations could mean a sharp rise in the value of your property; and the retitling of assets as part of your estate plan—or because of divorce, a death in the family, or the birth of a child—could necessitate policy changes. Even lacking major events, you probably need a comprehensive review of all your insurance coverage at least every two years. ●

Ensures You Are Cared For Properly

own decisions. If that happens, the agent will be obligated to fulfill the directives spelled out in your living will and to make other decisions that may be needed.

Because your health-care agent could play such a crucial role in your care—potentially making life-or-death decisions—it's essential to choose someone you can count on to be loyal and assertive in carrying out your wishes. You'll probably also want an agent who lives nearby and can be on the spot quickly if the need arises.

Should your health-care agent also have financial control of your estate? That could help avoid conflicts of interest that may arise if different agents oversee the two areas of responsibility. For example, suppose you were a candidate for an expensive, experimental treatment that had a 50% chance of restoring you to health. While your health-care agent might consider those reasonable odds and recommend the treatment, paying for it could put your estate agent at odds with his or her responsibility—to preserve and grow your assets. By designating a single agent, you limit the possibility that your estate's interests could supersede your own. ●

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What Do You Want Loved Ones To Know?

Imagine it's dozens of years in the future, and your great-granddaughter is thinking about you, and how lucky she is to come from a good family and have what she wants in life. But she wonders how you felt when you started the family business, what obstacles you had to overcome, and what you dreamed of for future generations of your family. If you had the foresight to prepare an "ethical will," she would know all of that.

Often written as a letter to family and friends, an ethical will could supplement your legal will by sharing your values, wisdom, and family history. Some ethical wills offer advice on education, marriage, and money management.

Though the idea of leaving guidance to your heirs may have originated 3,000 years ago, it became popular only recently—and, like many other aspects of estate planning, the concept took off after the September 11, 2001 terrorist attacks. Today, estate planners, personal coaches, hospice care programs, and religious organizations use ethical wills to help people preserve personal legacies.

Susan Turnbull, whose firm, Your Ethical Will (yourethicalwill.com), writes ethical wills, describes them as the "soul" of your estate plan. "All the documents you complete in the traditional financial planning process answer the question, 'What do I want my loved ones to have?' Your ethical will is where you answer, 'What do I want my loved ones to know?' What people really care about leaving is their spirit and ideas. We have a legacy of wealth and property, but we also have a legacy of values and beliefs."

> *"Ethical wills are the 'soul' of your estate plan"*
> —Susan Turnbull

Turnbull says she encounters many different reasons for drafting an ethical will. People who lost their parents at a young age may want to make sure their values and stories are on record for their children. The parents of a disabled child might want to thank their other children for their emotional support. A business owner could explain to his family his reasons for leaving the bulk of his estate to charity.

While an ethical will may be cherished by your family and community, you are the first beneficiary, Turnbull says. "Reflecting on your life is always healthy," she says. "If you choose to share the document during your lifetime, as many do, it can invite meaningful dialogue. It could even help you reach out to estranged friends and family members."

And once you create this touchstone, you may not want to stop there. You may just want to go ahead and use it as a framework for drafting your estate plan for your financial assets.

You can download free software from Ethical Will (ethicalwill.com) that will guide you through the process of writing your own ethical will. Or if you fear the blank page, you could create an ethical will on audiotape or videotape. To learn more, read So That Your Values Live on: Ethical Wills and How to Prepare Them, by Jack Riemer and Nathaniel Stampfer (editors); and Ethical Wills: Putting Your Values on Paper, by Barry K. Baines. ●

Savings Bond Changes

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reach final maturity for another 20 years. Many people invested in savings bonds figuring they could defer reporting interest income by rolling over their bonds into HHs down the road.

"The government has pulled the rug out from under bond owners by taking away their ability to roll over their bonds," said Jack Quinn, CEO of SBPlanner.com, a website that provides savings bond analysis to financial advisors. "People face potentially serious tax consequences if they cannot defer the accumulated interest," he said, noting that Social Security and other benefits that are based on adjusted gross income may be affected.

If these drawbacks were not enough, two states—New Jersey and North Carolina—recently sued the federal government to gain control over their residents' matured, unredeemed savings bonds. The states say the feds are not trying hard enough to find the rightful owners of these unredeemed bonds and that they can better take over that responsibility through their "unclaimed property" programs.

That may be so, but while they undertake the laborious task of looking for people who bought investments more than 30 years ago, the states will be able to earn interest on the unclaimed bonds.

Meanwhile, bond owners who decide to redeem their bonds will have to go through the unclaimed property process. Given the process often takes six to eight weeks, many people will decide not to bother.

The federal government says it will not turn over its savings bonds to N.J. or N.C., but if the states were to win in court, many other states would surely follow.

The best way to handle the potential pitfalls of savings bonds is to pull them out of the drawer or safe deposit box now, said Quinn. It's important to know when your bonds reach final maturity, how much and when they pay interest, and how they fit into your financial plan.

Savings bonds may not be the plain vanilla, simple investments many people think. To avoid problems, they require research and monitoring. ●

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