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Guide...Protect...Preserve

Five Financial Snags To Face In A Second Marriage

"Blended" families, once unusual, have become increasingly common. They're typically the result of a divorce, after which one or both ex-spouses remarries, frequently to a husband or wife who also has children from a previous marriage. There are about one million divorces in the United States each year, and it's estimated that almost half of all families today are of the blended variety.

Unfortunately, not every "Brady Bunch" lives in bliss and harmony, and discord is particularly likely after your death. Consider these five areas in which your blended family might face avoidable financial snags.

1. Beneficiary designations. Writing a former spouse out of your will may be at the top of your post-divorce to-do list, but it's also crucial to remember all of the other places you designated your once beloved as primary beneficiary. That may include life insurance policies, retirement accounts, trusts, and annuities. And you likely shouldn't just write in the name of your new spouse. Deciding how and whether your new spouse and your own children share in your estate may involve complicated planning and could mean establishing one or more trusts—and you'll need to coordinate all beneficiary designations with the provisions of your revised estate plan.

2. Tax-free gifts. A relatively simple way to look after the needs of children from a first marriage is through a series of tax-free gifts. You may currently give $13,000 annual gifts to as many recipients as you choose without incurring gift tax liability. So, if you're relatively young, you might use this provision to begin transferring assets to your children (and possibly your grandchildren), presuming you can afford to gift that much. Over a decade or two, you could help your offspring build substantial savings. But your early death would undercut this strategy, and it's important to consider who's getting the money. For example, making yearly gifts to both a child and the child's spouse would enable you to give more but might put money in the hands of a son- or daughter-in-law who later divorces your child.

3. Estate executors. In simple estate planning situations, it often makes sense to choose a spouse or other trusted family member as estate executor. Particularly if that person stands to inherit a substantial part of your assets, he or she is likely to be conscientious about following the provisions of wills and trusts and making sure your wishes are carried out. But that approach isn't likely to work in a blended family. A new spouse or one of your children will have different interests and may not be able to agree with other family members. Unless you want a judge to sort out the mess, it's generally better to appoint an independent third party. Moreover, a professional acting as executor may provide other valuable

(Continued on page 4)

Employers Find Ways To Mitigate Liability On 401(k)s

It's time to take more responsibility for your 401(k) plan.

In the current economic environment, employees are blaming their employers for losses in 401(k) accounts. Many businesses have been accused of failing to meet their fiduciary responsibilities. High plan fees, poor communication and education, and lack of investment options all have come under fire, and there have been a rash of lawsuits against plan providers.

A recent survey by management consultant Hewitt Associates shows that employers have acted to improve their plans and protect themselves against such litigation. Almost seven in 10 respondents said they were very or somewhat likely to increase efforts to explain their 401(k) plans' fees, and 60% were very or somewhat likely to review their plan's governance structure. And more than half said they were very or somewhat likely to benchmark their plans against industry "best practices" this year.

One way to demonstrate you have acted properly in your employees' interest is to document the processes for meeting your responsibilities. Giving participants greater control over their investment decisions can also limit a fiduciary's liability. That means letting workers choose from a broad range of investment alternatives.

Finally, communication remains crucial. Make sure your employees know all of their rights and responsibilities under the plan.

Mary Jane Callaghan & Mitch Glicksman

Planning For A Child With Special Needs

The daily demands of caring for a child with autism or another developmental disability are daunting enough without worrying about future care. That may be why, in a recent survey, 62% of parents with disabled children said they hadn't established a plan for what would happen when the parents were no longer around. Moreover, about half of the surveyed parents said they planned to leave assets directly to the child, and 58% expected to designate the child as a beneficiary. Those decisions could make the child ineligible to receive public assistance, which could be crucial for the child's long-term welfare.

A better approach may be to create a "special needs trust" that can be funded now or through your will. (The money often comes from life insurance death benefits.) Structured correctly, this irrevocable trust will enable a special needs child to receive public assistance benefits while the trust covers other expenses—including for travel, recreation, and rehabilitation—that aren't fully paid for by government funds.

If the trust assets are used as a primary means of support, the disabled child may be disqualified from public assistance, just as would happen if the child received a direct bequest. To avoid problems, a special needs trust will have an independent trustee who controls distribution of trust assets but uses the money only to supplement government aid. A provision in the trust will typically prevent the trustee from using assets for "support, maintenance, welfare, and education" of the child.

Keep in mind, however, that laws governing trust language and operation may vary from state to state. In some states, for example, assets that remain in the trust after the disabled child's death must be used to pay back the government for public assistance benefits. But that provision doesn't limit the trust's ability to help a living child.

A special needs trust, like any other estate planning vehicle, needs to be part of an overall estate plan. One wrinkle here is that money you move into this kind of trust doesn't qualify for the annual gift tax exclusion ($13,000 in 2011) that otherwise limits tax liability on yearly gifts to individuals. Because of restrictions in the trust language of special needs trusts, transfers are classified as gifts of "future interest." That means parents who fund such a trust during their lifetimes will need to use all or part of their $5 million lifetime gift tax exclusion. As a result, asset transfers to other children may be more costly.

Good advice from experienced experts can make sure your special needs trust accomplishes its goals without shortchanging other family members. We can work with your attorney to help you establish a trust that protects everyone's interests. ●

Giving Up Control Over Your Finances

What are your estate planning goals? Chances are, you'd like to maintain control over your assets while you're alive, but you also want to devise a plan that will protect your loved ones if you become disabled. And you intend for your wealth to be distributed when, how, and to whom you want. Finally, you'd like to minimize erosion from federal and state estate and gift taxes.

In other words, you'd like to have your cake and eat it, too. It's possible, but only if you decide to relinquish some control over your financial affairs. And that is often easier said than done. What's difficult is that it's likely to be someone else, not you, who will notice you're beginning to slip a bit. But this is a sensitive issue, and even if your relatives realize that you need help with your finances, they may put off saying anything for years.

To avoid that situation, you may need to establish a system now that won't put any single person on the spot. One solution advocated by Rick Randall, president of the National Network of Estate Planning Attorneys, is to create a "disability panel" with one or more medical professionals along with family members and a financial advisor. The group would observe you and decide when it's time to transfer ownership of assets to a trust or other parties. In some cases, a relative you've given power of attorney might need to initiate legal proceedings to gain control over the assets.

It's crucial to have a doctor involved, Randall says, to provide an expert opinion not only about your current health and cognitive status but also to project that into the future. Family members also play an essential role. They are the ones closest to your situation, and they can help determine when your medical condition and mental health may be deteriorating. And you can choose people you trust to take a compassionate, measured

Recession Reshapes College Choices

At a time when getting into college has become more competitive than ever, the nation's economic crisis is making it harder for students and their parents to pay tuition and obtain financial aid. Those trends are affecting students' choices of where to apply and how many applications to send, and there are more hard choices to be made when admission letters arrive.

Families at all income levels, beset by job layoffs and mortgage woes, are trying to make college plans despite persistent economic uncertainties. At the same time, investment losses have forced many universities to cut back on scholarships and other aid. Rising numbers of private lenders, including such giants as Bank of America and Wachovia Bank, are pulling out of the student loan market, and lenders that remain have tightened requirements and raised interest rates and fees. And though government-backed loans carry lower interest rates, that pool of funds is limited.

Meanwhile, many households are cutting back on savings for college, and the value of education accounts has taken a hit. According to Morningstar Inc., all 79 of the tax-advantaged 529 college savings plans it tracks lost value in 2008, with most falling 10% or more. Another potential source of funds to pay for college—home equity loans or lines of credit—is also becoming more difficult to tap, according to Dennis Nostrand, vice president of enrollment management at the University of New Haven in Connecticut. "The value of homes has dropped, and banks are being extremely cautious in making home equity loans," says Nostrand.

David Hawkins, director of public policy for the National Association for College Admission Counseling, agrees that the economic slowdown is making it more difficult for families to plan for college. "They just don't know what to expect," Hawkins says. "We see students and parents attempting to hedge their bets by filling out more applications, a trend that has further fueled the increasing competition."

The average student today applies to five to seven schools, and some apply to 10 or more, Hawkins says. A generation ago, students typically applied to just two or three. "State colleges, which tend to cost much less than private institutions, are reporting higher-than-expected application numbers," says Hawkins. "Students and families are including state colleges in their application lists in larger numbers than in the past."

For example, Clemson University, a state school in South Carolina, has seen a 10% increase in in-state applications, and applications are up 18% this year at both the University of Idaho and the University of Central Florida. Binghamton University in New York, however, may take the prize, posting a 50% surge in applications for classes in fall 2009.

Another factor boosting the level of competition is steady growth during the past 15 years in annual numbers of high school graduates. That trend is expected to peak in 2009, when some 2.9 million teens will finish high school.

Students today have about a 70% chance of acceptance into a four-year college, according to Hawkins. Ivy League schools are among the most competitive, with some accepting fewer than one in 10 applicants, while a wide range of top-tier universities admits fewer than half of those who apply. Many very selective private colleges, despite their much higher costs, are also seeing application numbers rise. Private institutions often have more scholarship opportunities, some of which are not available through public schools.

In this intensely competitive environment, more parents are hiring educational consultants, sometimes when their children are only high school freshmen or sophomores, to help guide them through the application process. Yet while applications are surging at many colleges, pushing down the chance of being accepted, the economic crisis means universities often don't have the institutional dollars they once could use to convince admitted students to matriculate. "In the spring, when admission and financial aid letters go out, students and families are really going to have to take a close look at each school's combination of scholarships, grants, and loans," Hawkins says. "There is going to be some serious comparison shopping."

As you and your children formulate their college admissions strategies, we can help you explore ways to pay tuition and costs that won't undercut your own retirement planning. Please give us a call. ●

approach. Knowing you've selected these team members may help you accept their judgment even when it goes against your own feelings.

How control will be transferred also needs to be settled well ahead of time, as part of your overall estate planning. And with estate laws currently up in the air, plans and documents may have to be revisited periodically to make sure they conform to the latest laws and strategies. Various kinds of tax-favored trusts are likely to be part of the equation, and you'll probably need to grant a durable power of attorney to someone you trust to act on your behalf.

Though looking ahead to the day when you'll pass the torch is never easy, the benefits can be enormous, and it's important to broach the subject with family members well before your health and competence become issues. We can work with you to establish a plan that meets your needs. ●

Retiree Relocation: Tax-Friendly States

Are you thinking about pulling up stakes when you retire? You may want to move to a state with warm temperatures and lots of sunshine, but there's also another kind of climate to consider—the tax climate. State taxes as well as federal levies can take a big bite out of retirement income, and some states devour decidedly more than others do. Here are several factors to take into account.

State income taxes. Seven states—Alaska, Florida, Nevada, South Dakota, Texas, Washington, and Wyoming—have no state income tax, and New Hampshire and Tennessee tax only investment dividend income that exceeds specified limits. However, many other states and the District of Columbia provide tax breaks for retirees, so you shouldn't automatically assume a no-tax state will be the best choice.

Retirement income. Most states that normally tax income provide partial exemptions for pensions. Even better, 10 states fully exempt income received from federal, state, or military pensions. And in Pennsylvania and Mississippi, all retirement income, including distributions from 401(k)s and IRAs, is state tax-free. Some other states impose high income tax rates on retirement income, however, with California leading the way at 9.55% on income of less than $1 million.

Social Security benefits. Up to 85% of the Social Security benefits you receive may be subject to federal income tax. However, the seven no-tax states, 27 others, and Washington, D.C. don't tax Social Security, though other special rules may apply. For instance, in Colorado, New Mexico, and Utah, you must add back a portion of Social Security benefits not taxed on a federal level when determining your eligibility for certain state income tax breaks.

Sales tax. These levies are often overlooked when retirees contemplate a move. On the plus side, five states—Alaska, Delaware, Montana, New Hampshire, and Oregon—currently have no sales tax, and other states may exempt food, medicine, and other necessities. But California has an 8.25% rate, and many cities and counties pile on additional sales tax charges. In Chicago and Los Angeles, you'll pay a combined rate of 9.75%—the nation's highest. And things could get worse. In 2009, 649 U.S. cities imposed new sales taxes or increased existing rates, while only 192 reduced sales tax rates (Source: Vertex Inc.).

Property taxes. The property tax burden varies widely throughout the country and even within states. The five states with the lowest median property taxes are Louisiana, Alabama, West Virginia, Mississippi, and Arkansas, while New Jersey, New Hampshire, Connecticut, New York, and Rhode Island have the highest.

Of course, tax rates aren't likely to be your only reason for choosing a particular retirement location. But it can't hurt to factor in these very real costs when planning your move. ●

Five Financial Snags

(Continued from page 1)

benefits to the estate.

4. Power of attorney. A power of attorney is a valuable estate planning tool, but your intentions may be thwarted if the wrong person gets this responsibility or it isn't handled properly. This legal document establishes the right for another person to act on your behalf, and that person could use it to transfer assets to a trust, for example, or to make annual tax-free gifts—basically, to take over any tasks you may be unwilling or unable to handle yourself. This authority can be either broad or specific—for example, it could be limited to selling securities or other possessions. Here, too, it often makes sense to give this power to a family member, but in a blended family that could lead to conflicts. Appointing someone from outside the family may be preferable, and it generally makes sense to have a durable rather than a general power of attorney.

5. Trusts. Various trusts can help sort out assets and interests for blended families. But even some trusts frequently used in such situations could cause problems. For example, a "qualified terminable interest property" (Q-TIP) trust can divide your assets between a surviving second spouse and the children from your first marriage. Typically, the spouse gets to use the trust income, while the children, as trust beneficiaries, receive the trust assets after the spouse dies. But this arrangement may spark disputes between the spouse and the children regarding management of trust assets, with the spouse possibly emphasizing current income while the children preferring asset appreciation. One solution is to give an independent trustee the ability to make adjustments so that everyone is treated fairly.

The bottom line is that the special dynamics of blended families make careful estate planning imperative. We can work with you and your attorney to create planning strategies and vehicles that serve the needs of you and your family. ●

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