HIGHTOWER
RDM Financial Group

RDM Financial Group
RDM Financial Planning Team
10 Wright Street
Westport, CT 06880
203-255-0222
800-899-3219
rdm@rdmfinancial.com
www.rdmfinancialgroup.com

Wealth Due to Inheritance

At RDM, we understand that wealth is more than money - it's about freedom, security, philanthropy, legacy and balance...we help you coordinate multiple financial goals through a maze of tax, legal and investment options. It is critical to understand, develop and implement effective, long-term strategies that align with your objectives and prepare you for the future.

Wealth Due to Inheritance

What is it?

Introduction

If you're the beneficiary of a large inheritance, you may find yourself suddenly wealthy. Even if you expected the inheritance, you may be surprised by the size of the bequest or the diverse assets you've inherited. You'll need to evaluate your new financial position, learn to manage your sizable assets, and consider the tax consequences of your inheritance, among other issues.

Issues that arise in connection with an inheritance

If you've recently received a bequest, consider the possibility that the will may be contested if your inheritance was large in comparison with that received by other beneficiaries. Or, you may decide to contest the will if you feel slighted. If you're the spouse of the decedent, you may elect to take against the will. Taking against the will means that you're exercising your right under probate law (governed by the statutes of your state) to take a share of your spouse's estate, rather than what your spouse left you in the will, because this is more beneficial to you. Another possibility is that you may disclaim the bequest if you're in a high income or estate tax bracket, or don't need or want the bequest.

Caution: *Some states allow no-contest clauses to be included in wills. If a will has such a clause and someone contests the will and loses, he or she gets nothing.*

Evaluating your new financial position

Introduction

It's important to determine how wealthy you are once you receive your inheritance. Before you spend or give away any money or assets, decide to move, or leave your job, you should do a cash flow analysis and determine your net worth as a first step toward planning your financial strategy. Your strategy will partly depend on whether you have immediate access to, and total control over, the assets, or if they're being held in trust for you. In addition, you need to know what types of assets you've inherited (e.g., cash, property, or a portfolio of stocks).

Inheriting assets through a trust vs. inheriting assets outright

When you inherit money and assets through a trust, you'll receive distributions according to the terms of the trust. This means that you won't have total control over your inheritance as you would if you inherited the assets outright. With a trust, a trustee will be in charge of the trust. A trustee is the person who manages the trust for the benefit of the beneficiary or beneficiaries. The initial trustee was named by the individual who set up the trust. The trustee will likely be your parent or other family member, a close family friend or advisor, an attorney, or a bank representative. The trust document may spell out how the trust assets will be managed and how and when trust income and assets will be paid to you, and it will outline the duties of the trustee.

Know the terms of the trust

If you're the beneficiary of a trust, the following should be done to ensure that your interests are protected:

- Read the trust document carefully. You have the right to see the document, so if you can't get a copy, hire an attorney to get it. Go over the document yourself or with the help of a legal or financial professional, making sure you understand the language of the trust and how its income and principal will be distributed to you. You may be the beneficiary of an irrevocable trust (can't be changed), or you may be the beneficiary of a revocable trust (can be changed). In addition, determine whether certain practices are allowed or prohibited. For example, one common trust provision prohibits a beneficiary from borrowing against the trust. Another can prevent the beneficiary from paying creditors with assets of the trust. An additional provision usually prohibits creditors from attaching a beneficiary's share of the trust.
- Determine if the trust income is sufficient to meet your needs. Is the trust heavily invested in long-term growth stocks or nonrental real estate? Or, is the trust invested in things that provide income to you now, such as rental real estate or money market funds? From your agent (e.g., attorney, accountant) or trustee, get the income statements used to calculate how much income will be distributed to you.
- Get to know your trust officers (if any) and find out how much the trustee fees are. Then, compare the fee with the average in your state or county (you might ask your local bank for this information). You may be able to negotiate the fee if it is too high, especially if the estate is large.

Working with a trustee

In some trusts, the trustee must distribute all of the income to the beneficiary every year. This type of trust may be simple to administer and relatively conflict free. You may want to work with the trustee or other professionals to ensure that the annual trust distribution is adequate to meet your needs.

In other trusts, the trustee may decide when to distribute trust income and how much to distribute. If this is the case, open communication with the trustee is important. You'll need to set up a sound budget or financial plan and carefully prepare your request for a trust distribution if it is out of the ordinary. It's in your best interests to find a way to work with the trustee. In most states, trustees are difficult to replace, and although they're not supposed to lose money on investments, they're not usually penalized if the trust performs poorly. If you decide to sue the trustee for mismanaging the trust, his or her legal fees may be paid for from the trust.

Caution: *No matter how trust funds are distributed, pay close attention to how the trustee handles the trust investments. Have your lawyer, accountant, or financial advisor look over the trustee's investment strategy. If your advisor determines that the trustee's investment strategy doesn't meet your needs or, worse, is unsound, discuss this strategy with the trustee or possibly ask the trustee to change his or her strategy.*

Inheriting a lump sum of cash

When you inherit a large lump sum of cash, you'll be responsible for managing the money yourself (or hiring professionals to do so). Even if you're used to handling your own finances, becoming suddenly wealthy can turn even the most cautious individual into a spendthrift, at least in the short run. Carefully watch your spending. Although you may want to quit your job, move, gift assets to family members or to charity, or buy a car, a house, or luxury items, this may not be in your best interest. You must consider your future needs, as well, if you want your wealth to last. It's a good idea to wait a few months or a year after inheriting money to formulate a financial plan. You'll want to consider your current lifestyle, consider your future goals, formulate a financial strategy to meet those goals, and determine how taxes may reduce your estate.

Inheriting stock

You may inherit stock either through a trust or outright. The major question to consider is whether you should sell the stock. This depends on your overall investment strategy and what type of stock you've acquired. If you acquire stock in a company, for example, and you now own a controlling interest, you'll need to look at how actively you want to be involved in the company or how much you know about the company. If you inherit stock and find that it doesn't fit your portfolio, you may consider selling it, depending on the market conditions.

Inheriting real estate

If you inherit real estate, such as a house or land, you'll probably have to decide whether to keep it or sell it. If you keep it, will you live there or rent it out? Do you hope that the house will appreciate in value, or are you keeping it for sentimental reasons? If you decide to sell or rent the house, you'll need to consider the tax consequences, as well.

Tip: *It's possible that you may inherit real estate or other assets together with others, and sales may require the other owners' assent or court action to sever the property.*

Short-term and long-term needs and goals

Once you've done a cash flow analysis and determined what type of assets you've inherited, you need to evaluate your short-term and long-term needs and goals. For example, in the short term, you may want to pay off consumer debt such as high-interest loans or credit cards. Your long-term planning needs and goals may be more complex. You may want to fund your child's college education, put more money into a retirement account, invest, plan to minimize taxes, or travel.

Use the following questions to begin evaluating your financial needs and goals, then seek advice on implementing your own financial strategy:

- Do you have outstanding consumer debt that you would like to pay off?
- Do you have children you need to put through college?
- Do you need to bolster your retirement savings?
- Do you want to buy a home?
- Are there charities that are important to you and whom you wish to benefit?
- Would you like to give money to your friends and family?
- Do you need more income currently?
- Do you need to find ways to minimize income and estate taxes?

Tax consequences of an inheritance

Income tax considerations

In general, you won't directly owe income tax on assets you inherit. However, a large inheritance may mean that your income tax liability will eventually increase. Any income that is generated by those assets may be subject to income tax, and if the inherited assets produce a substantial amount of income, your tax bracket may increase. Once you increase your wealth, you should look at ways to minimize your overall tax liability, such as shifting income, giving money to individuals or charity, utilizing other income tax reduction strategies, and investing for growth rather than income. You may also need to re-evaluate your income tax withholding or begin paying estimated tax.

Transfer tax considerations

If you're wealthy, you'll need to consider not only your current income tax obligations but also the amount of potential transfer taxes that may be owed. You may need to consider ways to minimize these potential taxes. Four common ways to do so are to (1) set up a marital trust, (2) set up an irrevocable life insurance trust, (3) set up a charitable trust, or (4) make gifts to individuals and/or to charities.

Impact on investing

Inheriting an estate can completely change your investment strategy. You will need to figure out what to do with your new assets. In doing so, you'll need to ask yourself several questions:

- Is your cash flow OK? Do you have enough money to pay your bills and your taxes? If not, consider investments that can increase your cash flow.
- Have you considered how the assets you've inherited may increase or decrease your taxes?
- Do you have enough liquidity? If you need money in a hurry, do you have assets you could quickly sell? If not, you may want to consider having at least some short-term, rather than long-term, investments.
- Are your investments growing enough to keep up with or beat inflation? Will you have enough money to meet your retirement needs and other long-term goals?
- What is your tolerance for risk? All investments carry some risk, including the potential loss of principal, but some carry more than others. How well can you handle market ups and downs? Are you willing to accept a higher degree of risk in exchange for the opportunity to earn a higher rate of return?
- How diversified are your investments? Because asset classes often perform differently from one another in a given market situation, spreading your assets across a variety of investments such as stocks, bonds, and cash alternatives, has the potential to help reduce your overall risk. Ideally, a decline in one type of asset will be at least partially offset by a gain in another, though diversification can't guarantee a profit or eliminate the possibility of market loss.

Once you've considered these questions, you can formulate a new investment strategy. However, if you've just inherited money, remember that there's no rush. If you want to let your head clear, put your funds in an accessible interest-bearing account such as a savings account, money market account, or a short-term certificate of deposit until you can make a wise decision with the help of advisors.

Impact on insurance

When you inherit wealth, you'll need to re-evaluate your insurance coverage. Now, you may be able to self-insure against risk and potentially reduce your property/casualty, disability, and medical insurance coverage. (However, you might actually consider increasing your coverages to protect all that you've inherited.) You may want to keep your insurance policies in force, however, to protect yourself by sharing risk with the insurance company. In addition, your additional wealth results in your having more at risk in the event of a lawsuit, and you may want to purchase an umbrella liability policy that will protect you against actual loss, large judgments, and the cost of legal representation. If you purchase expensive items such as jewelry or artwork, you may need more property/casualty insurance to protect yourself in the event these items are stolen. You may also need to recalculate the amount of life insurance you need. You may need more life insurance to cover your estate tax liability, so your beneficiaries receive more of your estate after taxes.

Impact on estate planning

Re-evaluating your estate plan

When you increase your wealth, it's probably time to re-evaluate your estate plan. Estate planning involves conserving your money and putting it to work so that it best fulfills your goals. It also means minimizing your exposure to potential taxes and creating financial security for your family and other intended beneficiaries.

Passing along your assets

If you have a will, it is the document that determines how your assets will be distributed after your death. You'll want to make sure that your current will reflects your wishes. If your inheritance makes it necessary to significantly change your will, you should meet with your attorney. You may want to make a new will and destroy the old one instead of adding codicils. Some things you should consider are whom your estate will be distributed to, whether the beneficiary(ies) of your estate are capable of managing the inheritance on their own, and how you can best shield your estate from estate taxes. If you have minor children, you may want to protect them from asset mismanagement by nominating an appropriate guardian or setting up a trust for them.

Using trusts to ensure proper management of your estate and minimize taxes

If you feel that your beneficiaries will be unable to manage their inheritance, you may want to set up trusts for them. You can also use trusts for tax planning purposes. For example, setting up an irrevocable life insurance trust may minimize federal and state transfer taxes on the proceeds.

Impact on education planning

You may want to use part of your inheritance to pay off your student loans or to pay for the education of someone else (e.g., a child or grandchild). Before you do so, consider the following points:

- Pay off outstanding consumer debt first if the interest rate on your consumer debt is higher than it is on your student loans (interest rates on student loans are often relatively low)
- Paying part of the cost of someone else's education may impact his or her ability to get financial aid
- You can make gifts to pay for tuition expenses without having to pay federal transfer taxes if you pay the school directly

Giving all or part of your inheritance away

Giving money or property to individuals

Once you claim your inheritance, you may want to give gifts of cash or property to your children, friends, or other family members. Or, they may come to you asking for a loan or a cash gift. It's a good idea to wait until you've come up with a financial plan before giving or lending money to anyone, even family members. If you decide to loan money, make sure that the loan agreement is in writing to protect your legal rights to seek repayment and to avoid hurt feelings down the road, even if this is uncomfortable. If you end up forgiving the debt, you may owe gift taxes on the transaction. Gift taxes may also affect you if you give someone a gift of money or property or a loan with a below-market interest rate. The general rule for federal gift tax purposes is that you can give a certain amount ($15,000 in 2019) each calendar year to an unlimited number of individuals without incurring any tax liability. If you're married, you and your spouse can make a split gift, doubling the annual gift tax exclusion amount (to $30,000) per recipient per year without incurring tax liability, as long as all requirements are met. Giving gifts to individuals can also be a useful estate planning strategy.

Tip: *The annual gift tax exclusion is indexed for inflation, so the amount may change in future years.*

Caution: *This is just a brief discussion of making gifts and gift taxes. There are many other things you will need to know, so be sure to consult an experienced estate planning attorney.*

Giving money or property to charity

If you make a gift to charity during your lifetime, you may be able to deduct the amount of the charitable gift on your income tax return. Income and other limits apply. Consult a tax professional for help. For estate planning purposes, you may want to make a charitable gift that can minimize the amount of transfer taxes your estate may owe. There are many arrangements you can make to reach that goal. Be sure to consult an experienced estate planning attorney.

DISCLOSURES

RDM Financial Group does not give tax or legal advice. Consult your tax advisor and attorney on all tax and legal matters.

This is not an offer to buy or sell securities. No investment process if free of risk and there is no guarantee that the investment process described herein will be profitable. Investors may lose all of their investments. Past performance is not indicative of current or future performance and is not a guarantee.

RDM Financial Group is a team of investment professionals registered with HighTower Securities, LLC, member FINRA/ SIPC & HighTower Advisors, LLC a registered investment advisor with the SEC. All securities are offered through HighTower Securities, LLC and advisory services are offered through HighTower Advisors, LLC.

This document was created for informational purposes only; the options expressed are solely those of the author, and do not represent those of HighTower Advisors, LLC or any of its affiliates.

Reprinted with permission from Broadridge Investor Communication Solutions, Inc. Broadridge Investor Communication Solutions, Inc.does not provide investment, tax, legal, or retirement advice or recommendations. The information presented here is not specific to any individual's personal circumstances. To the extent that this material concerns tax matters, it is not intended or written to be used, and cannot be used, by a taxpayer for the purpose of avoiding penalties that may be imposed by law. Each taxpayer should seek independent advice from a tax professional based on his or her individual circumstances. These materials are provided for general information and educational purposes based upon publicly available information from sources believed to be reliable — we cannot assure the accuracy or completeness of these materials. The information in these materials may change at any time and without notice.

RDM Financial Group
RDM Financial Planning Team
10 Wright Street
Westport, CT 06880
203-255-0222
800-899-3219
rdm@rdmfinancial.com
www.rdmfinancialgroup.com