WEALTH & LEGACY PLANNING

What This Looks Like — and How to Accomplish It

A whitepaper exploring how true wealth and legacy planning differ from traditional financial planning and the importance of building a well-rounded team of legacy planning experts.

TriFound

trifound.com

(800) 727-6577

Instead of just working with a financial advisor, most wealthy people work with a wealth manager, a CPA and an attorney.

There is a fundamental difference in the way that most average, middle-class people think about financial planning and investing and the way that wealthy people think. This difference in thinking makes it difficult for many people to achieve long-term financial success.

The average person views financial planning and investing through a narrow lens. However, wealthy people view them as just one component of a much bigger picture that also includes tax, estate and legal planning. Your financial plan should be designed with the impact of taxes and legal developments on your investment portfolio and estate in mind.

The problem is that most people choose to work with a financial advisor who isn't looking at this big picture. Typically, financial advisors are incented to grow their clients' financial assets. Their compensation is based on portfolio growth so this is where their focus lies. But there's so much more to your overall financial picture than just growing your assets.

Wealthy people realize this, along with the importance of broadening their team of experts to include more than just a financial advisor who wants to grow their assets. Instead of just working with a financial advisor, most wealthy people work with a wealth manager, a CPA and an attorney.

Successful financial and legacy planning requires the input and perspective of each one of these different professionals. Ideally, these experts will work together to ensure that all components of your legacy plan are coordinated with each other. This is the best way to accomplish your long-term financial and legacy goals.

When you have a wealth manager, CPA and attorney working together on your team, you can be assured that each component of your legacy plan is serving its intended purpose. These components may include a wide range of different financial, legal and estate planning, and accounting products and services.

FINANCIAL PRODUCTS

The financial products your wealth manager will use to help you accomplish your goals can be divided into three broad categories:

CASH EQUIVALENTS

A big part of wealth and legacy planning is managing cash correctly. The main use of cash equivalents in a wealth plan is to provide safety and liquidity so cash can be easily accessed when the right investing opportunities arise.

It's important to realize that regardless of the interest rate environment, cash always provides a zero percent return when inflation is factored in. So cash equivalent investments like savings and money-market accounts and certificates of deposit (CDs) should only be utilized as short-term parking places for cash until you're ready to invest the money.

One investment that can provide a greater return than a savings account or CD but still allow access to cash is a fixed annuity. Some fixed annuities can be purchased with riders that allow for penalty-free withdrawals. With this kind of liquidity, a fixed annuity can be a great tool for earning a relatively high rate of return on cash while you wait for the right market conditions to invest.

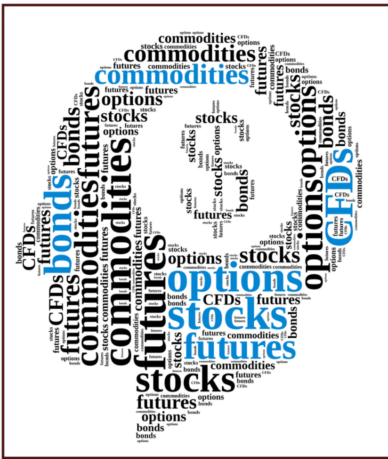
INCOME GENERATION

One common retirement income strategy espoused by many financial advisors is to live off of the income produced by your investments while leaving the principal intact. However, this can severely restrict your retirement lifestyle as well as result in unintended tax consequences later in life or for your heirs.

A better strategy is to not be overly concerned about spending your principal, but instead to increase your withdrawal rate in order to maximize your income. This will enable you to enjoy the money that you've worked so hard to accumulate during your lifetime. However, very few financial advisors will recommend this for the simple reason that their compensation is based on the amount of assets they're managing for you. If you spend your principle, this will result in less compensation for them.

For example, most financial advisors will tell you to withdraw no more than the required minimum distribution (RMD) from your retirement plan each year in order to keep your assets under management (and their compensation) as high as possible. In most situations, however, you will benefit more by exceeding your RMD than continuing to defer income and the payment of taxes until later — especially if your tax bracket now is lower than it will be when you're older. This is an example of "losing the battle but winning the war."

In order to implement strategies like these, you need to work with a wealth manager who is willing to think outside of the box. For example, your wealth manager should perform actuarial calculations on an annual basis to determine how much money you can comfortably withdraw from your principal.



Your wealth manager should have at his or her disposal a wide range of financial products designed to meet your income goals.

Your wealth manager should have at his or her disposal a wide range of financial products designed to meet your income goals. These typically include the following:

- **Real estate investment trusts (REITs)** — A REIT is a company that owns and operates income-producing real estate property or mortgages. REITs that trade on major U.S. stock exchanges are highly liquid, unlike individual real estate holdings. REITs typically offer high yields and also pay dividends, which makes them a good tool for generating income.
- **Bonds** — Bonds are debt securities issued by borrowers in order to raise money from investors. They are issued by governments — including the federal and state governments and local municipalities — and corporations. In return for lending money, you receive interest payments during the life of the bond and repayment of the bond's face value (or principal) at maturity.

  Municipal bonds are an especially useful income generation tool in certain situations due to their tax benefits. Meanwhile, a special type of corporate bond known as high-yield bonds (or junk bonds) offers the potential for higher returns in exchange for assuming more default risk. These bonds carry a credit rating of BB or lower by Standard & Poor's or Ba or lower by Moody's Investors Service.
- **Jumbo CDs** — These certificates of deposit have higher denominations than regular CDs (discussed above under cash equivalents) so they pay higher rates of interest, which can make them a good income generation tool. The minimum investment for a jumbo CD is typically $100,000.
- **Long-term annuities** — In exchange for a single payment or series of payments to an insurance company, you will receive a series of regular payments at some time

in the future. The most common type of long-term annuity is a deferred annuity, which can provide you with a steady stream of income during retirement — either for a set number of years or for life.

- **Dividend-paying stocks** — Some stocks pay out cash to shareholders on a one-time or regular basis, such as quarterly. These cash payments can serve as a source of income, whether during or before retirement.
- **Unit investment trust (UIT)** — A UIT is a fixed portfolio of securities that features a low minimum investment and high liquidity. UITs can generate income by investing in securities that pay dividends.

LONG-TERM POSITIONS

Managing your long-term positions is the third component in your overall wealth management financial plan. All financial products that aren't geared toward managing liquid cash or generating income are considered long-term in nature.

You have two options for your long-term positions: Either liquidate and spend them eventually or pass them on to your heirs. For the former, many people ascribe to the belief in "buying low and selling high." While this is certainly preferable to the opposite — buying high and selling low — it's not always preferable to buying assets low and never selling them.

With your long-term positions, it's not just about growth — it's also about taxes and maximizing after-tax returns. For example, let's say you purchased stock in Apple Corp. in late 2004 for $4 a share. Today, the stock is worth about $112 a share. You could certainly make a case for selling it today and pocketing a nice gain, but you'd also be facing a hefty capital gains tax burden. If you instead left it alone and let it keep growing, it would pass tax-free to your heirs after you die.

Among the financial products at your wealth manager's disposal for managing your long-term positions are the following:

Managing your long-term positions is not just about growth — it's also about taxes and maximizing after-tax returns.

- **Common stocks and stock mutual funds and exchange traded funds (ETFs)** — Stocks, also called equities, are shares of ownership in publicly traded companies. They represent a claim on a company's assets and earnings. Stocks can be owned within mutual funds and ETFs. Mutual funds are collections of stocks operated by money managers, while EFTs are similar to mutual funds but trade like common stocks.
- **Commodities** — These are basic goods used in commerce — for example, oil, precious metals, agricultural products and natural gas. Commodities are bought and sold on exchanges like the Chicago Board of Trade and the New York Mercantile Exchange.
- **Options and futures** — These are sophisticated investing tools that take investing in common stocks and commodities a step further. An option is a contract that sets a price at which you can buy or sell a stock on a future date. Options to buy are "calls" while options to sell are "puts." Meanwhile, futures are contracts to buy or sell commodities on a future date.
- **Private equity** — This is a source of investment capital used mainly by affluent individuals and institutional investors to purchase the equity and debt of private companies, or to buyout public companies.

- **Closely held business interest** — If you own an interest in a closely held business, you and your wealth manager will strategize together about the role of your business in your long-term financial and estate plans.

LEGAL & ESTATE PLANNING PRODUCTS

In its simplest terms, estate planning is the process of planning ahead to make sure that your personal possessions and assets are distributed in the most efficient manner according to your wishes when you die. This includes planning for the reduction of estate taxes that must be paid by your heirs.

Trusts are the main legal tool used by wealth managers and attorneys to accomplish estate planning objectives.

Trusts are the main legal tool used by wealth managers and attorneys to accomplish estate planning objectives. There are two broad categories of trusts: living trusts and testamentary trusts. Living trusts are established during your lifetime to transfer property to a trustee while you're alive, while testamentary trusts take effect after you die.

Living trusts, meanwhile, can be revocable or irrevocable. With a revocable trust, you retain control of the trust's assets and can revoke or change its terms at any time. With an irrevocable trust, you no longer own the assets and can't make changes without the consent of the trust's beneficiary.

Among the most commonly used types of trusts are the following:

- **Charitable remainder trust (CRT)** — This trust enables you to leave assets to both a qualified charity and your heirs. Your heirs would receive exclusive rights to all trust distributions until their interests have terminated, at which time your charitable beneficiaries will receive the assets that remain in the trust. A CRT can also be structured to provide you with annual income for up to 20 years or until your death.
- **Irrevocable Life Insurance Trust (ILIT)** — This trust would assume ownership of the proceeds of a life insurance policy so these proceeds aren't included in your taxable estate. Death benefits are deposited into the trust where they're held on behalf of your beneficiaries. If life insurance proceeds are held in trust instead of transferred directly to your spouse, these proceeds cannot be taxed as part of your estate.
- **Grantor Retained Annuity Trust (GRAT)** — Here, you would transfer assets to the trust, which will make annuity payments back to you for a designated number of years. After this time, any assets remaining in the trust are distributed as a gift to your heirs or other named beneficiaries. Many different types of assets can be placed in a GRAT, including collectibles and shares in a closely held business.

Here are a few other types of legal tools used by wealth managers and attorneys to accomplish estate planning objectives:

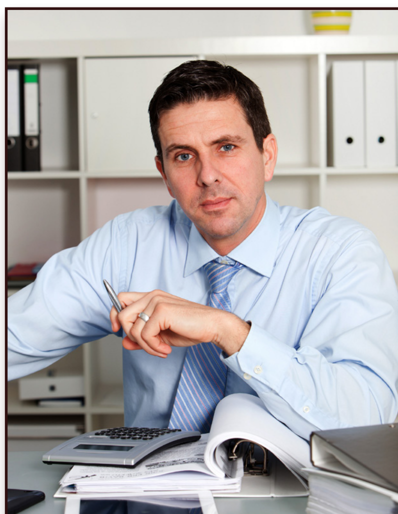
- **Endowments and private foundations** — An endowment is a donation of financial assets (such as investments or property) made to a nonprofit organization. There are several different kinds of endowments, including term, unrestricted and restricted endowments. A private foundation, meanwhile, is a nonprofit entity set up by a family primarily to make grants for scientific, educational or other charitable purposes.

- **Life settlements** — This is the sale of a life insurance policy to a third party for more than the policy's cash surrender value but less than its death benefit. A viatical settlement is similar but is used by someone who is terminally or chronically ill.
- **Premium financing** — With this tool, you would borrow the money needed to pay life insurance premiums instead of paying the premiums out of pocket. Utilizing premium financing would enable you to use leverage in order to put your cash to work for more productive purposes.

ACCOUNTING SERVICES

When most people think of accounting products, they mainly think of tax returns. Preparing tax returns is certainly a big part of a CPA's job, but CPAs can provide so much more from a strategic standpoint when it comes to wealth and legacy planning.

This is why it's so beneficial to have a CPA on your team of wealth and legacy planning experts. Your CPA should work closely together with your wealth manager and attorney in the implementation of the strategies and use of the products discussed in the previous two sections. The goal should be to use these strategies and products to maximize the use of tax brackets in order to minimize overall tax payments throughout your lifetime and by your heirs after you die.



Choosing the right form of entity ownership for your business is one of the most important decisions you must make — and your CPA will play a key role in this decision.

Your CPA can play an especially valuable role in wealth and legacy planning if you own a closely held business. Choosing the right form of entity ownership for your business is one of the most important decisions you must make — and your CPA will play a key role in this decision. The primary forms of entity ownership are as follows:

- **Sole proprietorship and partnership** — A sole prop is the simplest form of ownership and is often chosen by self-employed individuals and professional service providers. No new business entity is created — instead, business income and expenses are reported on Schedule C. This is filed with your personal tax return and the company's profit or loss is combined with other personal income. A partnership is similar to a sole prop but is used when there is more than one owner.
- **C corporation** — This is one of two types of incorporation in which a separate legal entity is formed for the business. Generally, incorporating shields you as the owner from any personal liability for business debts and obligations. C corporations can have an unlimited number of owners and issue both common and preferred stock. One drawback, though, is that they may be subject to double taxation.
- **S corporation** — Electing Subchapter S status avoids the potential double taxation of a C corp since income and losses pass through directly to the owner-shareholders. Potential drawbacks of S corps include limitations on the number of owners and classes of stock that may be issued, the deductibility of certain items and the potential tax impact of converting from C to S status.
- **Limited Liability Company (LLC) and Limited Liability Partnership (LLP)** — These are a hybrid between a sole prop or partnership and a C or S corporation, potentially offering the benefits of both. Typically, the owner is protected from personal liability for business debts and obligations while profits and losses pass through to shareholders, which avoids double taxation. These are not

tax entities themselves; instead, they enable you to choose a sole prop, partnership or C or S corp while benefitting from liability protection and pass-through income.

Another important service a CPA can provide as a member of your wealth and legacy planning team is assistance with business exit and succession planning. It takes years of careful advance planning to realize your long-term goals with regard to monetizing your business interests and passing the business on to successor owners.

For example, will proceeds from the sale of your business constitute the bulk of your retirement income? Or will you use these proceeds to start another business? And do you want to pass the business on to family members, transfer it to your employees and managers via an Employee Stock Ownership Plan (ESOP), or sell it to an outside buyer? Your CPA can help you answer important questions like these as you devise your business succession plan.

BROADEN YOUR PERSPECTIVE

If you still view financial planning and investing through a narrow lens, it's time to broaden your perspective to encompass true wealth and legacy planning. This incorporates the areas of financial, tax, estate and legal planning into an overall legacy plan that's designed with input from your wealth manager, attorney and CPA.

Please contact TriFound to discuss how we can help you create a true wealth and legacy plan.

TRIFOUND
trifound.com
(800) 727-6577