

Don't Wait Until Catastrophe Strikes to Discuss Money Issues with Older Relatives

Talking about a parent's finances needs to happen long before the elder is ill or incapacitated. In fact, the best situation is when the older relative raises the conversation first.

In Hurricane Katrina's aftermath, we should all be aware that planning makes serious emergencies more manageable. Nevertheless, many families don't discuss finances until a crisis occurs. An older relative may be unable to understand questions or express their wishes in detail. If there is no plan, family members grasp at responsibilities – or shirk them – without any idea of what the older relative would prefer.

What's critical to understand is that such talks go far beyond money. They are discussions about independence and basic preferences for the way an individual wants to live or die. And demographers believe that with the rising number of single Americans – those divorced or never married – these conversations will become increasingly complicated as they fall to nieces and nephews, younger friends or designated representatives.

If you are a younger relative wondering how to manage the conversation and get control of the situation, here are some suggestions:

Decide what's important to talk about first: Maybe this conversation isn't just about where the will or health care power of attorney is. Maybe this conversation is about you noticing that a parent or loved one is moving slower, is more forgetful, is clearly looking like their health has taken a turn for the worse – and maybe that's why you want to know where the will is. Jumping into money issues first is usually a mistake. Deal with immediate health and lifestyle issues first.

Explain why you want to talk about finances: In some families, having a successful financial discussion means several attempts and some frustration. Don't let yourself become angry or frustrated – just keep starting the conversation until it catches on. It might make sense to say something like, "You've always been so independent, Mom. I just want you to give us the right instructions so we do exactly what you want."

Write down questions: When a parent or relative is unconscious or unresponsive, the younger relative is immediately in the drivers' seat. That's why it's critical to make a list of questions for the elderly relative to answer in detail. The basics: where important papers are, how household expenses are paid, who doctors and specialists are, what medicines are being taken and whether there's a will, an advanced directive and a funeral plan (and money or insurance proceeds to pay for it).

There may be dozens more questions beyond these based on your family's personal circumstances. But in creating this list, ask yourself: "What do I need to know if this person suddenly becomes sick or dies?"

Offer to get some advice: If you don't fully understand your relative's financial affairs, it might make sense for you both to talk to an attorney, tax adviser or CERTIFIED FINANCIAL PLANNER™ professional. A qualified adviser can offer specific suggestions on critical legal documents that should be in place and ways to make sure accounts to pay medical and household bills are accessible to the older person and the designated friend or relative who will hold power of attorney.

Plan a caregiving strategy: You should discuss the relative's preferences and trigger points for various stages of health care. An individual always wants to stay in his or her home, but you should have an honest discussion about how much you can do at home as a caregiver and whether various services (home health aide, geriatric care manager, assisted living) should be introduced at various stages. Talking through what a parent will be able to live with at various health stages – and putting that information in writing – will save plenty of doubt and bitterness later.

Discuss liquidating the home: If an elderly relative becomes sick and irreversibly incapacitated, the equity in his or her home may come under consideration as a resource to pay uncovered medical or household maintenance. Since the home is both a major asset and an emotional focal point, it's best to get good advice and spell out specifically what the elderly relative wants done with his/her property and under what conditions.

Make sure everyone knows the plan: Once you settle on a strategy, make sure all family and friends understand the plan and their assignments.

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Gear Up for Last-Minute Tax Savings – Katrina and Otherwise

The biggest yearend tax news is tied to the worst natural disaster in U.S. history, but taxpayers outside the federally declared Hurricane Katrina disaster area might also consider these tax moves before yearend:

Max out your office retirement accounts: If you haven't contributed the maximum to your employer-sponsored 401(k) or 403(b), at least try. Under the age of 50, individuals can contribute a maximum of \$14,000 to both plan types in 2005. This year, savers over the age of 50 can make an additional "catch-up" contribution of \$4,000.

Max out your business retirement accounts: For a Simplified Employee Pension (SEP) or a Keogh plan, business owners can deduct up to 20 percent of self-employment income or 25 percent of salary if you're an employee of your own company up to a maximum of \$42,000. The newer Solo 401(k) plans created in 2001 allow contributors under age 50 to sock away a maximum of \$42,000 in 2005. If you're over age 50 at yearend, you can contribute \$46,000.

Give to charity: If you itemize, your contributions are tax deductible – just make sure you have receipts for donations of \$250 or more. And thanks to the Katrina Emergency Tax Relief Act of 2005, individuals who donate to qualified charities may deduct 100 percent of contributions made between Aug. 28 and Dec. 31.

Use up those flex-spending dollars: Use them or lose them. As long as you spend dollars in those accounts for qualified healthcare items by your company's deadline date, you'll be able to benefit from all the dollars in that account. An important note -- there was a federal tax law change that allows workers to have up to 2.5 months into the following year to incur qualified healthcare expenses. But unless your company's plan was amended to reflect that change, you'll have to order contact lenses, get that last little bit of dental work done or stock up on prescription meds before the clock strikes 12 on New Year's Eve. Check with your HR department now.

Get advice now on the AMT: The Alternative Minimum Tax (AMT) is affecting significantly more middle-class and upper middle-class taxpayers. If you're planning to exercise stock options or have a lot of deductions, talk to a tax professional before the end of the year to see if any action can be taken relevant to your personal situation.

Give to the ones you love. Individuals can give up to \$11,000 per year per recipient without triggering gift tax and thereby reduce the value of their estate.

Offset capital gains: If you have a large net capital gain so far this year, you might want to consider selling some losing investments to generate a loss before yearend.

Generally, realized capital losses are first offset against realized capital gains. Any excess losses can be deducted against ordinary income up to \$3,000 (\$1,500 if married filing separately) on line 13 of Form 1040. Doing so could reduce the amount of tax you pay this year. However, remember that if you do sell stock to generate a loss, you are prohibited from purchasing substantially similar investments within 30 days before or after the sale that generated the loss.

Don't forget increased mileage deduction: Thanks to the high price of gas, the standard business mileage-rate deduction was raised to 48.5 cents per mile for business miles driven from Sept. 1 through Dec. 31. The 40.5-cent rate will remain in effect for the first eight months of 2005, though. Other taxpayers will benefit from an increased mileage deduction as well – those claiming the rate for moving expenses or driving related to medical needs will see the rate rise to 22 cents a mile for the final four months of the year, up from 15 cents for the first eight months.

Postpone income: If you're due a bonus or clients owe you money, see if you can afford to have them hold off writing a check until January. It will lower your taxable income. But remember – it's the date on the check that matters, not when you deposited it. Also, if you are retired and receiving systematic withdrawals from your retirement plan, it may make sense to stop remaining payments for the year if you don't need the income.

Consider a sales tax deduction: You're allowed to deduct *either* your sales tax or your state income tax, whichever is greater. If you're planning to buy any of the following big-ticket items that typically charge sales tax – vehicles, motor homes and RVs, homebuilding materials and prefabricated homes – you might opt for the sales tax deduction if that exceeds what you owe for state income tax.

Fund a 529: If you haven't started a 529 college savings plan for your child, do it. Your contributions to a 529 plan can grow tax-free, you can take tax-free withdrawals to pay for college expenses, and you may also enjoy a state-tax break. A good place to learn the basics of 529 plans is www.savingforcollege.com.

Your First Year of Retirement – Do You Know how Much You’ll be Able to Spend?

There are thousands of resources that tell you how to manage your retirement savings while you’re still working for that nest egg. So why are so many new retirees suddenly paralyzed with financial fear when they finally quit working?

Some of it is natural; retirement is a big lifestyle change and many people question whether they’re spending too much during that first crucial year. Surprisingly, freedom can be very expensive. But that nervousness may also be an indication that an individual hasn’t received as much instruction in how they will spend during retirement as they’ve received saving for it.

A huge nest egg – or a nest egg that seems huge – sounds great. But the death of traditional pensions and the rise of (often-underperforming) self-directed retirement plans have made it tough for individuals to easily predict what they’ll actually have to spend. And without a complete plan that takes into account personal circumstances, financial goals, inflation, the rising cost of health care, increased longevity and ultimately long-term care, retirement money probably won’t last as long as you do.

As the official Baby Boomer retirement wave begins, some financial advisers have begun to elevate the discussion to post-retirement spending and investing as a way to repair pre-retirement planning. Individuals who have worked with financial and tax advisers including CERTIFIED FINANCIAL PLANNER™ professionals, should have a much clearer picture of how they should manage their spending in the first five years of retirement.

If you haven’t, it’s time to get some help.

For potential retirees who want to eliminate those first-year jitters, here are planning ideas to implement as soon as possible:

Define a vision of retirement and revisit it every year: Anyone who has worked successfully with an investment manager or financial planner has addressed the kind of retirement they want and how old they’ll be when they start it. A retirement that includes world travel and a general increase in leisure-time spending may, believe it or not, cost significantly more than a pre-retirement lifestyle with a 60-hour workweek built in. A retirement with rewarding part-time work built into the picture might make the other goals more affordable. A person who manages his or her finances or works with an expert needs to revisit those goals annually to assess whether they will still be able to afford a particular style of retirement at the age they plan to start it.

Track working-life expenses for 3-6 months: This is where that vision of retirement starts getting real. Knowing for the first time what an individual spends on lattes and late-night carryout may cause a radical shift in behavior -- from spending to saving.

Create a worst-case health scenario: For many, the biggest spending issue post-retirement is end-of-life care. That may mean paying for expensive experimental treatments to fight disease or long-term assisted or nursing home care. Some projections put annual nursing home costs at more than \$100,000 a year in the next two decades compared to their current annual range of \$45,000-\$60,000. While public aid picks up medical expenses for those who exhaust their assets in most states, most of us want more than minimal standards of care.

Build several annual budgets: There are many rules of thumb that govern retirement spending. A popular one is that no one should spend more than 4 percent annually of the present amount in their nest egg. Another is that retirees only need 70-80 percent of their last working year's income to be comfortable. There really is no one-size-fits-all solution because spending decisions are different at all stages of retirement. Since computers make this possible, every investor might consider doing one or more annual budgets that build various risk scenarios into their plan.

Shift into a retirement investment strategy in stages: With a clear majority of investors having inadequate retirement funds in place near or at retirement age, it may seem silly to talk about investing post-retirement. But the younger an investor is, the more valuable the conversation. With so many portfolios yet to recover from the 2000-2002 stock market slide, many investors have shifted their portfolios into real estate or other fast-growing investments that may leave them undiversified and subject to bubbles. Good advisers can help build more balanced portfolios that fit the exact needs of the investor as retirement nears.

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Katrina's Tax Effect - the Latest Changes

In the weeks after the devastation caused by Hurricane Katrina, the federal government has acted twice to provide tax relief to victims. It's probably not finished. Here is a summary of the latest tax relief provisions available to taxpayers in the four-state federal disaster area - Louisiana, Mississippi, Alabama and Florida. Implementing any of these items might work best with the advice of a trained tax professional.

Property and theft loss: The entire amount of a personal casualty or theft loss is deductible as long as the taxpayer can prove the loss occurred in the federally designated area after Aug. 24, 2005, was attributable to Katrina and it was not otherwise covered by insurance or other reimbursement. In most cases, casualty losses (fire, flood, etc.) are deductible only if they exceed 10 percent of an individual's adjusted gross income (AGI) with a \$100 floor. With a Hurricane Katrina disaster loss, taxpayers have the option of deducting it on an amended return for 2004 using form 1040X.

Extension for quarterlies: Taxpayers suffering damage and loss from Hurricane Katrina now have until Feb. 28, 2006 to file tax returns and pay any taxes due - this extension refers to any tax payments that were due after Sept. 15, 2005. Taxpayers who need to identify themselves as hurricane victims should write "Hurricane Katrina" in red ink at the top of their tax forms or any other documents filed with the IRS. Taxpayers who need to alert the IRS or have other hurricane-related questions can also call the special IRS disaster hotline at 866.562.5227.

Retirement plan withdrawals: Katrina victims who elect to withdraw funds from company retirement plans or IRA accounts to make repairs or pay bills will not be hit with the normal 10 percent early distribution penalty, even if they are under age 59 ½ as long as the withdrawals total less than \$100,000. They'll also be able to spread the tax burden of any income distributed from a retirement account over three years.

Hardship loan limits: If an employer or its pension or retirement plan offers "hardship loans," the maximum amount of those loans is temporarily raised from \$50,000 to \$100,000.

No loss in filing status: People who have moved to other states who can prove the effect of Katrina won't lose their tax breaks or filing status. They will also be allowed to use their 2004 income to compute their 2005 eligibility for things such as the child tax credit and the earned income tax credit. If someone filed as "head of household" for 2004, they can still do so for 2005, even if they are now living in someone else's home.

Sanctuary deduction: If a taxpayer is providing rent-free housing to Katrina victims for at least 60 days, they may receive a once-per-lifetime tax deduction of \$500 per person that they're housing up to a maximum deduction of \$2,000.

A one-time break on debt forgiveness: If a creditor forgives all or some of a hurricane victim's non-business debt, that person will not be treated as receiving taxable income.

Extension on insurance proceeds investment: For individuals who receive insurance proceeds in the case of a loss, the time they have to reinvest those proceeds to avoid recognizing a gain on the underlying insured property has been extended from four years (for individuals) to five.

Break for relief workers: According to the IRS, all workers assisting in relief activities in the covered disaster areas are eligible for relief whether or not they are affiliated with a recognized government or philanthropic organization. These individuals should also mark their appropriate forms with "Hurricane Katrina" written in red ink.

For more information: The IRS has several resources for disaster victims and those aiding them. Publication 2194, Disaster Losses Kit for Individuals, is being updated with new provisions of the Katrina Emergency Tax Relief Act of 2005. Publication 2194B, Disaster Losses Kit for Businesses, contains various IRS publications and forms related to claiming disaster losses. Victims of Hurricane Katrina can call the IRS toll-free disaster hotline at 866.562.5227 for assistance. Other financial tips for surviving disaster can be found on the Financial Planning Association's® Web site at www.fpanet.org/public.

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