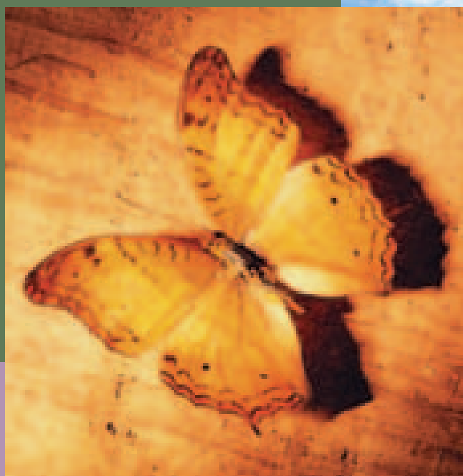


STRATEGIES FOR WEALTH MANAGEMENT

Financial Planning for High Net Worth Individuals

CPS INSURANCE SERVICES SINCE 1974

STRATEGIES FOR WEALTH MANAGEMENT

CONTENTS

ACHIEVING YOUR FINANCIAL GOALS

Congratulations! You have successfully handled the challenges of running a business or managing a career, choosing investments, and building your wealth. Your challenge now, however, is perhaps even greater: astutely managing the assets you have accumulated to fully achieve your financial goals.

This challenge has become more complicated under the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA) and the larger Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). The highlight of the former act is a major reduction in tax rates on dividends and long-term capital gains, while the highlight of the latter is a sweeping overhaul of estate tax law that went into effect in 2002. Other provisions affect your income tax and retirement planning. Whatever happens, to fully benefit, you need to take the right steps — at the right time.

This booklet provides insight into both the general concepts of personal wealth management as well as specific strategies to help you achieve your goals. We hope it encourages you to craft and implement a masterful wealth management plan. We also hope it helps you realize that successful wealth management calls for professional guidance.

Please review the ideas presented in this booklet, then give us a call to discuss your situation. Our professionals can lead you to strategies that best suit your needs.

BUILD A FRAMEWORK

You may feel financially strong but disorganized. What you need is a realistic framework so you can better seize financial opportunities as they arise. To develop this framework for your financial decisions, follow the four D's:

1. ***D***etermine where you are today,
2. ***D***ecide where you want to be in the future,
3. ***D***evelop a plan to move toward your goals, and
4. ***D***ive in to make it happen.

This process is ongoing; you must monitor the plan and adjust it as necessary to ensure that you are moving in the right direction. It is a simple concept — yet many who lay the groundwork for a plan fall short when it comes to implementing it. Don't be one of them.

MEASURE YOUR NET WORTH

Before you can create a wealth plan, you need to take a snapshot of where you are today financially. Net worth is measured as the excess of all your assets over all your liabilities. In other words:

What You Own – What You Owe* = *Net Worth

Traditionally, assets and liabilities are shown on a net worth statement in order of liquidity — that is, according to how soon they are available or due. For example, cash in your checking account is available on demand, while equity in your real estate requires you to sell the property to gain access to its worth. So cash is listed before the real estate. Liabilities are viewed in a similar way. The balance due on your credit cards should be paid before your home mortgage, so credit card debt is listed before the mortgage.

The worksheet in Chart 1 will help you determine your net worth.

Chart 1

Net worth worksheet

NET WORTH

A. Cash and cash equivalents (checking accounts, money market accounts, CDs, etc.)	$ ___________
B. Marketable investments (stocks, bonds, mutual funds, etc.)	$ ___________
C. Other investment and business assets (partnership interests, closely held businesses, cash value of life insurance, etc.)	$ ___________
D. Retirement assets (IRAs, 401(k)s, Keoghs, SEPs, etc.)	$ ___________
E. Personal assets (residences, autos, furnishings, jewelry, artwork, etc.)	$ ___________
Total assets (A+B+C+D+E)	$ ___________
F. Personal debt (credit cards, personal loans, 401(k) loans, alimony, taxes, etc.)	$ ___________
G. Investment debt (margin loans, real estate investment loans, etc.)	$ ___________
H. Personal mortgage debt (mortgages, home equity loans)	$ ___________
Total liabilities (F+G+H)	$ ___________
Net worth (total assets less total liabilities)	$ ___________

WORKING ASSETS

Total working assets* (A+B+C+D above)	$ ___________
Investment debt (G above)	$ ___________
Net working assets (working assets less investment debt)	$ ___________

** Working assets are those assets that have the potential to grow and/or generate income. They are assets, other than your residence, that will provide financial independence for you in the future. The closer you are to financial independence, the greater the percentage of your total assets should be your working assets.*

SET YOUR GOALS

Now that you know what you have, you must decide what you want from the wealth planning process. Would you like a comprehensive view of your financial future? This entails reviewing and analyzing all aspects of your finances (such as estate planning, insurance, investments and retirement) and creating a detailed, comprehensive plan for each area.

Or are you interested only in suggestions on specific financial issues? For example, if you have just sold a business, you may need direction on how to invest the proceeds. Or you may want to calculate the required minimum distributions from your retirement accounts. Even if your immediate focus is on only one issue, be sure to understand how it affects other aspects of your wealth picture.

Next you need to set desirable and realistic goals. This means balancing financially prudent strategies with emotionally acceptable thresholds. What looks good on paper may not always feel right in your heart. Try to meet these objectives by setting short- and long-term goals and prioritizing them within each category.

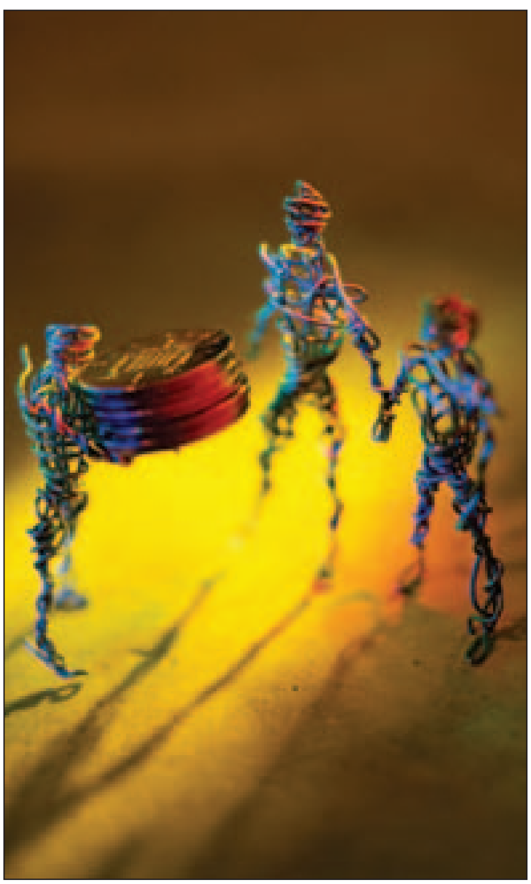
Common goals include the following:

- To accumulate a sizable estate to pass on to your heirs,
- To increase the assets going to your heirs by using various estate planning techniques,
- To tie in charitable desires with your own family goals,
- To accumulate enough assets to buy a business, a vacation home, etc.,
- To be able to retire comfortably,
- To have sufficient funds and insurance coverage in the event of serious illness or loss,
- To develop an investment program that may provide a hedge against market fluctuations and inflation, and
- To minimize income taxes.

When developing a plan, keep in mind the need for flexibility. Your personal and financial situation often changes with the major and minor life events you experience. Births, deaths, illnesses and marriages can affect your goals profoundly. Once you've set your goals, you can move toward the future. The rest of this booklet will discuss the key areas of any wealth plan and possible strategies for achieving your goals.

DEVELOPING YOUR ESTATE PLAN

You may be surprised to discover how large your estate tax obligation turns out to be. The estate tax relief under EGTRRA may not eliminate your estate tax liability. The act is subject to a sunset provision, which means the estate tax will be back in 2011 after its repeal in 2010 if no further legislation is passed. But in the meantime, the act has dramatically changed how you can reduce your gift and estate tax obligations. With careful gifting and planning, you can maximize the amount of wealth you can transfer to your heirs. Consider your options today to ensure your assets are managed and passed on the way you intend.



UNDERSTAND TRANSFER TAX RATES AND EXEMPTIONS

Here's a simplified way to compute your estate tax exposure. Take the value of your estate, net of any debts. Remember that this includes everything you own individually, including the face value of any insurance on your life. It also includes a percentage of the assets held jointly with your spouse (generally 50%) and others (the percentage depending on various factors).

> ***Note that the gift tax exemption does not increase beyond $1 million, and even in 2010 the gift tax is not repealed.***

Subtract any assets that will pass to charity on your death — such transfers are deductions for your estate. Then if you are married and your spouse is a U.S. citizen, subtract any assets you will pass to him or her. Those assets qualify for the marital deduction and avoid estate taxes until the surviving spouse dies. The net number represents your taxable estate.

During your life or at death, you can pass up to the exemption amount free of gift and estate taxes. This amount will increase until the estate tax is eliminated in 2010. (See Chart 2 on page 6.) But note that the gift tax exemption does not increase beyond $1 million, and even in 2010 the gift tax is not repealed — so lifetime gifts of more than $1 million will be subject to tax.

Chart 2

Transfer tax exemption increases and rate reductions

Year	Estate[1] and GST tax exemption[2]	Highest estate, GST and gift tax rates
2003	$1 million[3]	49%
2004	**$1.5 million**	**48%**
2005	$1.5 million	47%
2006	$2 million	46%
2007	$2 million	45%
2008	$2 million	45%
2009	$3.5 million	45%
2010	(repealed)	35% (gift tax only)
2011	$1 million[4]	55%[5]

[1] *Less any gift tax exemption already used.*
[2] *The gift tax exemption is $1 million for all years.*
[3] *The GST tax exemption is $1.12 million.*
[4] *The GST tax exemption is adjusted for inflation.*
[5] *The benefits of the graduated estate and gift tax rates and exemptions are phased out for estates/gifts over $10 million.*

Source: U.S. Internal Revenue Code

If your taxable estate is equal to or less than the exemption and you haven't already used any of the exemption on lifetime gifts, no federal estate tax will be due when you die. But if your estate exceeds this amount, it will be subject to estate tax. (See Chart 3 for 2004 marginal rates.) The top rate will gradually decrease through 2007, but is restored to pre-EGTRRA levels in 2011, following the estate tax repeal in 2010. (See Chart 2.)

The estate tax will be back in 2011 after its repeal in 2010 if no further legislation is passed.

USE THE UNLIMITED MARITAL DEDUCTION

Your estate generally can deduct the value of all assets that pass in a qualified manner from you to your spouse during your lifetime or at your death, provided your spouse is a U.S. citizen. The assets may pass either outright or in trust. For transfers to noncitizen spouses, an annual exclusion applies to gifts of present interests.

Don't assume the easy way out is the best way out. You could pass all of your assets to your surviving spouse tax-free using your marital deduction, but if your combined estates are greater than the exemption amount, your heirs could suffer the consequences. That's because when your spouse dies, the assets will be included in his or her estate for tax purposes. And, to the extent your taxable estate exceeds the available exemption, your estate will be subject to tax. With a little planning (see credit shelter trust discussion on page 9), you could reduce your estate tax liability.

MAKE LIFETIME GIFTS TO REDUCE ESTATE TAXES

Gifts you make during your lifetime are subject to federal gift tax. But you can exclude gifts of up to $11,000 per recipient each year. This amount is indexed for inflation, and only in increments of $1,000, so likely will not increase again for a few more years. This exclusion is $22,000 per recipient if your spouse joins in the gift. Thus, if one spouse actually gifts $22,000 to someone, both spouses can elect to split the gift and treat it as if they each gave $11,000. You can make gifts to as many people as you like.

To take advantage of the annual exclusion, the law requires the donor to give a present interest in the property to the recipient. This usually means the recipient must have complete access to the funds. But a parent or grandparent might find the prospect of giving complete control of $11,000 a year to the average 15-year-old a little unsettling.

Fortunately, you can get around this by setting up certain kinds of trusts, such as a Crummey trust (see page 10) or a minor's trust, where the gift will qualify for the annual exclusion even though the recipient does not have complete access to the gifted assets. Please contact us for more details.

Chart 3

2004 gift and estate tax rates

Taxable estate (after deductions)	2004 tax	Marginal tax rate (tax on next dollar)
$1.5 million	$0	45%
$2 million	$240,000	48%

Source: U.S. Internal Revenue Code

SELECT THE BEST PROPERTY TO GIFT

Consider both estate and income tax consequences and the economic aspects of any gifts you'd like to make. To minimize estate taxes, make gifts of property with the greatest future appreciation potential. To minimize income taxes, gift property that hasn't appreciated significantly since you've owned it. Why? Because your basis in the property generally carries over to the recipient, who will owe taxes on any gain when he or she sells it.

This strategy may be less advantageous when, with the repeal of the estate tax in 2010, beneficiaries will no longer receive a step-up in basis to fair market value for inherited property. Currently, when heirs sell inherited property, they don't pay capital gains tax on appreciation that occurred before their loved one's death.

Wealth planning tip 1

CONTROL ASSETS WHILE YOU GIVE THEM AWAY WITH AN FLP

Family limited partnerships (FLPs) can allow you to gift assets while maintaining control of them. In establishing the partnership, you, as grantor, become the general partner. As such, you make all decisions regarding the assets held in the FLP. Thus, even if you hold only a 1% general partnership interest, you control how the FLP's assets are invested and distributed (subject to a fiduciary level of responsibility). The recipients, generally family members, are gifted limited partnership interests. Using discounts, you can make annual gifts that qualify under the annual exclusion. You can fund the partnership with cash, marketable securities, real estate, corporate stock (except S corporation stock) or other types of assets. (Recent court cases have made FLPs somewhat controversial, so take caution in setting one up.)

The basis of inherited property is typically considered the asset's value on the date of the loved one's death. So, it has made sense to wait to transfer highly appreciated assets until your death. Even in 2010, this may be a smart strategy for at least a portion of your assets because $1.3 million in assets plus another $3 million for assets going to a spouse will still receive the step-up.

For property that is expected to decline or has declined in value, your best bet is to sell the property to take advantage of the tax loss. You may then gift the sale proceeds.

BEWARE OF THE GST TAX

The generation-skipping transfer (GST) tax was designed to limit an individual's ability to transfer wealth to successive generations without incurring a gift or estate tax at each generation. It is equal to the top estate tax rate. (See Chart 2 on page 6.)

Fortunately, there is a GST tax exemption, which, beginning in 2004, will be equal to the estate tax exemption. (Also see Chart 2.) Gifts to skipped generations also qualify for the $11,000 annual gift tax exclusion under certain conditions.

When properly used, this GST tax exemption allows some degree of long-term wealth building even when the estate tax is in effect. But be careful: The GST rules are complex and call for careful planning.

Using trusts in a gift or estate plan can provide significant tax savings while preserving some control over what happens to the transferred assets.

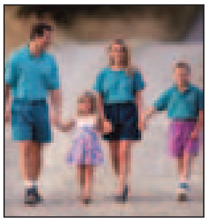
PLAN WITH TRUSTS

Trusts are effective estate planning tools. They may be revocable (the grantor reserves the right to change the terms or recover the assets at any time) or irrevocable (the grantor cannot alter the terms or recover the assets during the trust's existence). Using trusts in a gift or estate plan can provide significant tax savings while preserving some control over what happens to the transferred assets. Here's a look at some of the most common trusts:

Credit shelter trust. If you are married, you can use a credit shelter (or bypass) trust to take advantage of both your and your spouse's estate tax exemptions. When the first spouse dies, assets worth the available estate tax exemption pass to a trust, from which the surviving spouse gets the income for his or her life, plus principal distributions at the trustee's discretion.

When the surviving spouse dies, the remaining principal usually passes to the children and, because the surviving spouse did not control the trust, the trust assets bypass estate tax in the second estate. To use the trust, each spouse must own assets individually that he or she can pass into this trust on death.

QTIP trust. In some circumstances, you may hesitate to leave property outright to your spouse, who would then have complete control over it during life and the ability to distribute it as he or she wished at death. A qualified terminable interest property (QTIP) trust is a viable alternative.



A QTIP trust can be used to provide your spouse with lifetime income while preserving the principal for beneficiaries you choose, such as children from a previous marriage. And if you write the trust provisions to permit it, the trustee may also make distributions from the principal for the surviving spouse's benefit during the trust term. You can arrange for a portion of your assets to be left outright to your spouse, with another portion left in the trust.

QDOT. A qualified domestic trust (QDOT) is used when the surviving spouse is not a U.S. citizen. Transfers to a noncitizen spouse generally do not qualify for the marital deduction unless property passes to the surviving spouse in a QDOT. The rules and requirements for a QDOT are beyond the scope of this overview. We can help guide you if your spouse is not a U.S. citizen.

Crummey trust. Normally gifts to trusts do not qualify for the annual exclusion because they are not considered to be of a present interest. But if the beneficiaries have the right to withdraw the gifted assets during the tax year, then the gift is considered a present interest. This is where a Crummey trust can help. It generally gives beneficiaries the right to withdraw the assets, on notice, for a period of time during the tax year, usually for a 30- to 60-day window. This provides you with a way to make gifts for the future that qualify for the annual exclusion.

GRAT and GRUT. Grantor-retained annuity trusts (GRATs) and grantor-retained unitrusts (GRUTs) are irrevocable trusts into which you place assets and then receive the income from those assets for a defined number of years. At the end of the trust term, the principal passes to the beneficiaries. In a GRAT, the income you receive is an annuity based on the value of the assets on the date the trust is formed. No additional gifts are allowed to a GRAT. In a GRUT, you retain a right to receive a percentage of the value of the property as determined each year.

Assets in these trusts avoid probate, and their value is frozen for gift and estate tax purposes. You also maintain some control because you select the trustee and set the trust terms. The present value of the income stream you receive reduces the ultimate principal that passes to the beneficiaries. This substantially reduces the value of the gift when compared with an outright gift of assets. If you outlive the trust term, all of the assets (plus appreciation) will be excluded from your estate, because you retained no interest in the trust assets at death.

QPRT. By using a qualified personal residence trust (QPRT), you can remove substantial value from your taxable estate. You gift your home to the QPRT, which then legally holds the title. You receive the right to live in the home for a set number of years. At the end of this period, the residence is typically distributed from the trust to your children.

At the time of the transfer, you are gifting the value of the home, less the value of your right to live in it for the designated period. A QPRT is especially effective when real estate values are depressed and you expect an upturn in the real estate market. The primary risk with a QPRT is that if you die during the trust term, the value of the home at the time of your death will still be included in your taxable estate. You can establish two QPRTs, but one must be for your principal residence.

TRANSFER BUSINESS OWNERSHIP

If you are a family business owner, you have additional estate tax saving tools at your disposal. Transferring business ownership can preserve your business and accumulated wealth — if planned properly. Consider the following:

Family business exclusion. If an active family business makes up 50% or more of your gross estate and you meet certain other requirements, your estate qualifies for a family-owned business exemption. The exemption, in combination with the estate tax exemption, equals $1.3 million. But the act increases the estate tax exemption to $1.5 million in 2004, and effectively eliminates the family-owned business exemption. (See Chart 2 on page 6.)

Estate tax deferral. Normally, estate taxes are due within nine months of death. But if closely held business interests exceed 35% of the adjusted gross estate, your estate may qualify for a tax payment deferral. If so, your estate needs to make interest payments on only the estate tax owed on the value of the business until five years after the normal due date. The tax is then paid on the closely held business interest over 10 equal annual installments. Thus, your estate can defer paying a portion of the tax for up to 14 years from the original due date. (See Case study I.)

Section 303 redemption. Your company can buy back stock from your estate without the risk of the distribution being treated as a dividend for income tax purposes. The distribution is treated as a sale or exchange of the stock. Because the basis is stepped up to fair market value, no income tax is due on the distribution. Generally such a distribution must not exceed the estate taxes and funeral and administration expenses of the estate.

Case study I

SAVING TODAY BY PAYING TOMORROW

Marjorie owned a small distribution company that accounted for 50% of her estate. When she died in October 2003, her total estate tax liability was $2 million. Half of the liability is due at the normal due date of her estate tax return in July 2004 (nine months after Marjorie's death). The other $1 million of liability could be paid in 10 installments, starting in July 2009 (five years and nine months after Marjorie's death), and ending in July 2018. Marjorie's estate would also have to pay interest on the unpaid liability each year.

One caveat: The value of your holdings in the business must exceed 35% of the value of your adjusted gross estate. If the redemption qualifies under Section 303, this is an excellent way to fund payment of estate taxes.

Buy-sell agreements. Buy-sell agreements protect owners and their heirs in the event of death or disability, or at retirement. For closely held business owners, buy-sell agreements can also be structured to minimize estate taxes. If done correctly, the valuation for the buy-sell agreement will set the value for estate taxes. Buy-sell agreements also typically restrict a shareholder's ability to transfer shares outside the current ownership group without the other owners' consent.

Valuation discounts. Your business may be your most valuable asset. But because it doesn't trade on the open market, arriving at an appropriate value for closely held business stock can be complex. Shares of closely held businesses often have a reduced value.

A minority discount is generally available if you gift less than a 50% business interest to a recipient. In addition, you may be able to claim a discount for lack of marketability, because the partial interest transferred generally won't have a ready market and would be difficult to sell at full value. But not all discounts are available to donors after death. Thus, to achieve the largest discount, consider making gifts during your lifetime.

GIVING TO CHARITY

Charitable giving helps you reduce your estate tax bill while aiding your favorite organizations. Direct bequests to charity are fully deductible for estate tax purposes, as are partial bequests. Lifetime gifts remove assets — as well as future appreciation — from your taxable estate and are deductible on your income tax return. In addition to tax advantages, contributing to charity is a good way to leave a legacy in your community or to instill in your heirs a sense of social responsibility.

CREATE CHARITABLE TRUSTS

You can leave assets, or income from the assets, to both charity and family members. A split-interest trust is often used in this instance:

CLT. A charitable lead trust (CLT) provides income to chosen qualified charities during the term. When the term expires, the principal goes to the trust's designated beneficiaries — often family members. The trust must pay the annuity at least annually. If you establish the trust during your lifetime, the amount subject to gift tax is reduced by the present value of the annuity going to charity. You also will be entitled to a charitable deduction on your income tax return.

> *You can use a CRT during your life to retain an income stream and then pass the principal to charity at your death.*

CRT. A charitable remainder trust (CRT) is basically the reverse of a CLT — the beneficiaries receive the annuity and the charities receive what is left when the trust term expires. You can use a CRT during your life to retain an income stream and then pass the principal to charity at your death. Another benefit: After you make the gift, the trust can sell the trust assets free of capital gains tax because the gain is treated as if realized by a tax-exempt organization. Full sale proceeds are then available to buy taxable income-producing securities. You can receive an income tax deduction when you create the CRT based on the present value of the assets ultimately passing to charity.

For both CLTs and CRTs, the annuity can be either fixed, based on the initial fair market value of the trust (an *annuity* trust — CL*A*T or CR*A*T), or variable, based on the fair market value of the trust at the beginning of each year (a *unitrust* — CL*U*T or CR*U*T). The annuity can be for either a set term or the life of the donor or donors.

Another option is a gift annuity, which works similarly to a CRT. You contribute an asset to a charity that agrees to make annual payments back to you (and/or another beneficiary) either for a specified number of years or — more typically — until death. You can take an income tax deduction on the value of the donated amount minus the present value of payments back to you or your family and limited to 30% of your adjusted gross income. If the charity sells the asset, neither you nor the charity must pay capital gains tax on the proceeds. But you will owe some tax when you receive payments.

Wealth planning tip 2

SAVE MORE CAPITAL GAINS TAX BY GIVING COLLECTIBLES TO CHARITY

When you are thinking of contributing to charity, consider giving from your gallery instead of your investment portfolio. Gains on collectibles are taxed at a top capital gains rate of 28% — not the 15% rate that applies to gains on most long-term property — so you save taxes at a higher rate. You get a deduction for your gift's full market value, subject to certain threshold limitations for adjusted gross income. The collectibles donated must be consistent with the charity's purpose.

FORM A PRIVATE FOUNDATION OR DONOR-ADVISED FUND

You or your family can form a private foundation to support your charitable activities or to make charitable grants according to your wishes. If the foundation qualifies for tax-exempt status, your charitable contributions to it are deductible, subject to certain limitations.

Deductions for donations of appreciated capital gain property to a private nonoperating foundation are limited to your basis in the property, unless the property contributed is qualified appreciated stock. In this case, you can claim a deduction for the appreciated value of the stock, not just your basis.

As an alternative to using a private foundation, consider a donor-advised fund. This fund is essentially a small-scale private foundation that requires much less administration. Generally a large public charity sponsors the fund, but you make a contribution that is used to create a pool of funds you control. Various factors will determine whether such an arrangement is appropriate for you.

Although you may have fewer incentives for creating a foundation or donor-advised fund in light of the increasing estate tax exemption (and potential ultimate repeal), both are still useful options. Please call us to discuss how a private foundation or donor-advised fund could fit into your plan.

MAKING THE MOST OF RETIREMENT ACCOUNTS

Retirement accounts provide a favorable way to accumulate significant wealth. The best known plans are probably IRAs and 401(k) plans, but others are also available. If you are self-employed or own your own business, you may have a Keogh, profit-sharing (see Case study II) or money-purchase plan. Small employers usually establish simplified employee pensions (SEPs) or savings incentive match plans for employees (SIMPLEs) to contribute toward both their employees' and their own retirement. Nonprofit organizations can offer their employees 403(b) plans.

MAXIMIZE YOUR CONTRIBUTIONS

Usually it is beneficial to contribute as much as possible to retirement accounts because of their tremendous tax advantages. First, you may be able to deduct IRA contributions, depending on the type of IRA and your adjusted gross income (AGI), and other plan contributions are usually made pre-tax. Second, and probably more important, earnings and appreciation on retirement account funds compound tax-deferred (and in some cases tax free — see Wealth planning tip 3 on page 16) until you withdraw them.

The power of tax-deferred compounding is extraordinary and over extended periods can increase your wealth substantially. And you can put away more money than ever — especially if you are age 50 or older. (See Chart 4.)

MINIMIZE THE TAX CONSEQUENCES OF DISTRIBUTIONS

What are the consequences of distributing money from your retirement plans? Age, health and, in some cases, life expectancy are all factors that can affect your retirement distributions.

Case study II

BUSINESS OWNERS CAN PARLAY RETIREMENT PLANS INTO EVEN BIGGER TAX SAVINGS

David wants to set up a retirement plan for his business that will both help him provide an appealing benefit to attract and keep quality employees and allow him to maximize his own plan contributions. His business advisor suggests he set up a profit-sharing plan. Even if David's company suffers a slow year and he can't afford to contribute cash until after year end, that's OK. He has until the due date of his return to make contributions to the plan, as long as he creates the plan before year end. If David receives a six-month extension, he could have as long as 8½ months after year end to contribute. David can contribute and deduct as much as 25% of eligible employees' total compensation — including his own — up to annual limits ($40,000 per participant in 2004).

Distributions from traditional IRAs and qualified plans are taxed as ordinary income. The key to minimizing income taxes is to take distributions in years you have lower taxable income and thus will fall into a lower marginal tax bracket, or years you

Chart 4

Retirement plan contribution limit increases

Year	401(k)s, 403(b)s, 457s and SEPs	401(k)s, 403(b)s, 457s and SEPs for taxpayers 50 and over	Traditional and Roth IRAs	Traditional and Roth IRAs for taxpayers 50 and over	SIMPLEs	SIMPLEs for taxpayers 50 and over
2003	$12,000	$14,000	$3,000	$3,500	$8,000	$9,000
2004	**$13,000**	**$16,000**	**$3,000**	**$3,500**	**$9,000**	**$10,500**
2005	$14,000	$18,000	$4,000	$4,500	$10,000	$12,000
2006	$15,000	$20,000	$4,000	$5,000	$10,000	$12,500
2007	$15,000	$20,000	$4,000	$5,000	$10,000	$12,500
2008	$15,000	$20,000	$5,000	$6,000	$10,000	$12,500

Source: U.S. Internal Revenue Code

have extremely high deductible expenses, such as medical costs or charitable contributions, to offset the distribution income.

AVOID EARLY WITHDRAWALS

Generally, until you reach the age of 59½, you can't withdraw funds from your retirement plans without paying a 10% penalty tax. The 10% tax is in addition to regular income tax. There are, however, exceptions. For example, the 10% penalty does not apply to distributions made after the owner's death or disability.

Distributions from nondeductible contributions or that are part of a series of substantially equal payments over your life expectancy (or the life expectancy of you and your beneficiary) also are not subject to the penalty.

Wealth planning tip 3

AVOID TAX ON GROWTH — FOREVER — WITH A ROTH IRA

If your adjusted gross income doesn't exceed the limits, you can make a nondeductible contribution (or roll over traditional IRA funds) to a Roth IRA up to the annual limit in Chart 4 (reduced by contributions to all your other IRAs for the year).

So with no deduction for the contribution, what's the benefit? You don't pay taxes or face the 10% early withdrawal penalty for qualified distributions. That means you (or your beneficiaries) pay no income tax — ever — on growth in the account. A distribution is qualified if the Roth IRA has been open for more than five years and the distribution is made:

- On or after you reach age 59½,
- To your estate or beneficiary after your death,
- As a result of you becoming disabled, or
- For first time homebuyer expenses of up to $10,000.

But perhaps the biggest benefit is that you can continue to make contributions after you reach age 70½ — and continue to reap the benefits of tax-free growth — which you can't do with a traditional IRA. In 2006, EGTRRA allows you to designate as a Roth contribution all or part of your contribution to your employer-sponsored retirement plan — if the plan includes this option. The contribution will be subject to the same rules as a Roth IRA.

TAKE MINIMUM DISTRIBUTIONS

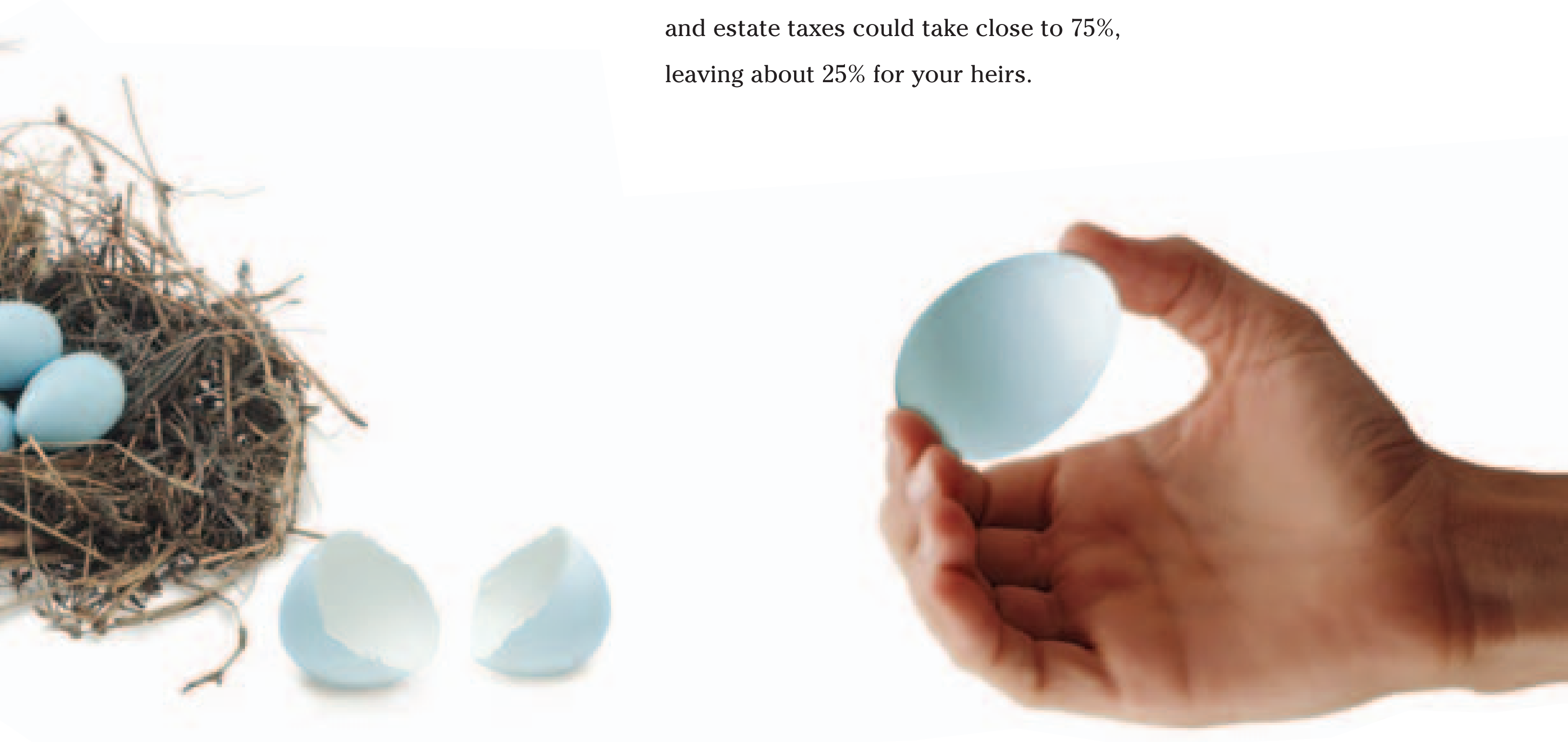
You must start taking minimum distributions by April 1 of the year following the year you turn age 70½. This is known as the required beginning date (RBD). The starting point for determining the required minimum distribution amount for a given year is the balance as of Dec. 31 of the prior year. For IRAs, all your accounts must be aggregated to calculate the minimum distribution, but you can choose the account(s) from which to take distributions. More and more people are withdrawing only the minimum required amounts to maximize continued tax-deferred growth.

Now the rules are simpler. In fact, everyone now uses the same tables to calculate the appropriate amount. The new tables reduce the required minimum distribution amount for almost everybody.

Qualified retirement plans, such as 401(k)s, must be amended to accept the new rules before you can use them. Review your situation to determine the best way to proceed.

STRETCH OUT DISTRIBUTIONS WITH FAMILY BENEFICIARIES

Retirement plan assets held at death are the most heavily taxed assets. With large accumulations of retirement assets, income and estate taxes could take close to 75%, leaving about 25% for your heirs.



Be careful when calculating the proper amount, because failure to withdraw the minimum amount in any year could result in a 50% excise tax on the shortfall. This is particularly important in light of new reporting rules that require IRA custodians to report your required minimum distribution amount to the IRS.

On your death, your surviving spouse beneficiary may still roll over an IRA into his or her own IRA. For surviving spouses who have not yet reached age 70½, this can further defer the distribution.

One way to help reduce the income tax bite on retirement plan assets is to have your children, as beneficiaries, elect to receive distributions over their life expectancies (rather than shortly after your or your spouse's death). Thus, income taxes are payable over time, only as distributions are made to the beneficiaries, and more is left to grow tax-deferred. More people are withdrawing only the minimum required amounts from inherited retirement accounts to maximize the period assets can grow tax-deferred.

DETERMINING YOUR INSURANCE NEEDS

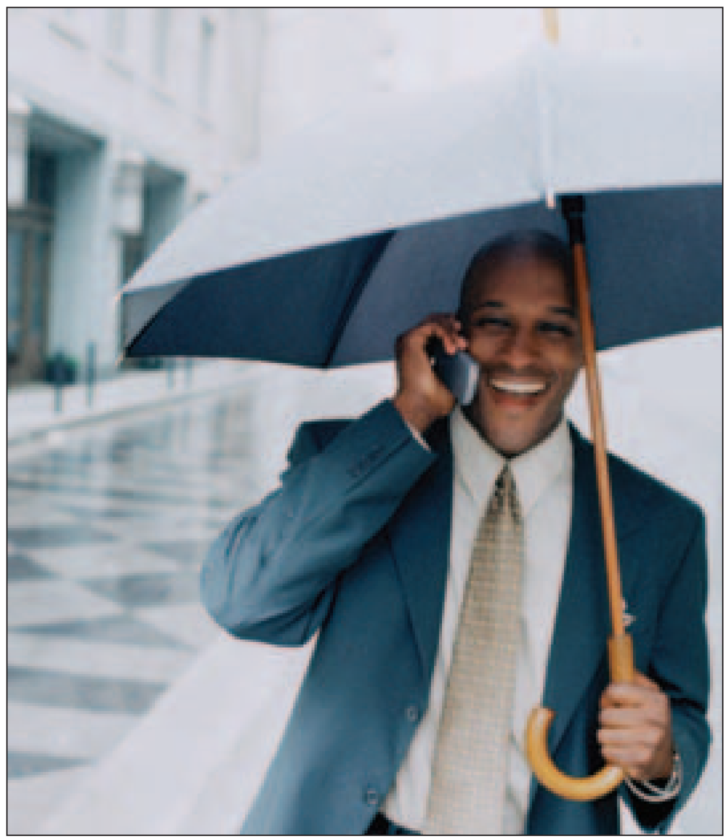
Insurance — whether it's life, disability, long-term care, or property and casualty — ultimately protects your family's future. But many people are underinsured. If you fall into this group, a premature death or disability, a large property loss, or a lawsuit could cost you a big chunk of your assets — or even leave you (or your family) financially devastated. To fully protect and provide for your family while minimizing your premiums and the tax consequences, you must carefully determine your insurance needs and then obtain the appropriate coverage from a financially strong insurance company.

LEVERAGE LIFE INSURANCE

Life insurance may be the most powerful type of insurance because it can replace income, provide liquidity to equalize assets among children active and inactive in a family business, or be a vehicle for passing on leveraged funds free of estate tax — all in a single package. And though the estate tax is decreasing and will be temporarily eliminated in 2010 (see Chart 2 on page 6), your estate may very well face at least some estate tax liability. Insurance can provide liquidity to pay these estate taxes.

Here are the three key steps you need to take when purchasing life insurance:

1. *Quantify your need.* To estimate the amount of life insurance you need, consider your current investments and the support your family will require. Ideally, life insurance should replace most or all of your wage contribution to the family for a readjustment period of several years after death. Life insurance should also cover the cost of funding children's education and paying off mortgages or other debts.



Then look at any liquidity problems your estate may have. Estates are often cash poor, and your estate may be composed primarily of illiquid assets such as closely held business interests, real estate or collectibles. If your heirs need cash to pay

Even if your estate is of substantial value, you may want to buy insurance simply to avoid the unnecessary sale of assets to pay expenses or taxes.

estate taxes or for their own support, these assets can be hard to sell. For that matter, you may not want these assets sold.

Even if your estate is of substantial value, you may want to buy insurance simply to avoid the unnecessary sale of assets to pay expenses or taxes. Sometimes second-to-die insurance makes the most sense. Of course, your situation is unique, so please get professional advice before buying life insurance.

2. *Choose the right form of ownership.* Choosing the proper form of ownership is just as important as selecting your beneficiaries. If you or your spouse owns the policy, the insurance proceeds could be subject to estate taxes on the surviving spouse's death. If your children own the policy, the proceeds will not be included in your estate, and you can use the annual $11,000 exclusion for making gifts to them to pay the annual premiums. But you must be confident that your children will actually pay the premiums. Other possible owners include an irrevocable life insurance trust (ILIT — see Case study III on page 20), a family limited partnership (FLP — see Wealth planning tip 1 on page 8) or limited liability company (LLC), or your business.

Generally, to reap maximum tax benefits you must sacrifice some control and flexibility as well as some ease and cost of administration. To choose the best owner, you must consider why you want the insurance, such as to replace income, to provide liquidity or to transfer wealth to your heirs. You must also determine the importance to you of tax implications, control, flexibility, and ease and cost of administration.

Case study III

IT MAY BE CRUMMEY, BUT AN ILIT OFFERS AN ATTRACTIVE OWNERSHIP ALTERNATIVE

Jack decides to buy a life insurance policy to benefit his two college-aged children, Melissa and Ben. He wants to keep the proceeds out of his estate without giving the policy outright to his children, who are still learning to be financially responsible. His advisor suggests a widely used form of ownership — the irrevocable life insurance trust (ILIT). After Jack sets up the trust, he simply needs to make gifts to it that the trustee can use to pay the premiums. Melissa and Ben, as beneficiaries, will still receive the proceeds, but the trust will control how they are paid out.

Jack's advisor also suggests the trust include a Crummey provision. The resulting Crummey power allows Jack's gifts to be free of gift tax under the annual exclusion. Normally, gifts have to be of a present interest to qualify, and gifts to a trust are considered to be of a future interest. But by providing the beneficiaries with the right to withdraw the gifted money within a short, set period, the Crummey power makes the gifts present interests for gift tax purposes. After that right lapses, the trust then pays the insurance premiums. Jack does have to sit down with Melissa and Ben and explain to them that they will benefit more if they let the right lapse so the gifts can be used for premiums.

3. *Pick the insurer.* In addition to selecting a financially strong insurance company, you will need to critically evaluate a company's policy illustrations and computerized printouts showing how your money will grow. Dividend assumptions, future interest rates, mortality costs and overhead expenses all could significantly affect the amount of your future premiums.

LOOK AT DISABILITY INSURANCE

Long-term disability insurance is one of the most overlooked areas of wealth planning. It replaces your wage income, or a major share of it, if you suffer a disabling accident. Most people will become disabled for 30 days or more at some point during their lifetimes. Although Social Security covers most employees, its benefits are generally inadequate for individuals with a high standard of living.

The definition of disability is the most important feature of the policy. You will generally want a policy with the least restrictive definition possible. Other crucial matters include:

- The period you have to wait after becoming disabled before you are eligible for benefits,
- The length of time the benefits will be paid (to age 65 or for life), and
- The taxability of the benefits, which may be excludable if you bear the cost of insurance.

The potentially devastating effects of disability increase if you are a business owner. To further protect yourself — and your business — consider overhead insurance and key person insurance as well.

Overhead insurance covers expenses like rent, wages, benefits, loan payments and taxes. Key person insurance protects against losses, including decreased sales, productivity and profits, from the disability of a key employee. Some key person plans pay benefits to the business. Others pay directly to the employee, freeing up the employee's salary. Key person premiums are not tax deductible, but the benefits are tax-free.

EVALUATE LONG-TERM CARE INSURANCE

Although hard to face, there's a good chance you'll need some form of long-term care, and the resulting costs can be one of the biggest financial threats you face. Left unchecked, they can easily eat up a lifetime of built-up wealth.

Recently, long-term care insurance has become more popular as a way to keep assets for heirs, rather than use them to fund nursing home costs. It may provide daily benefits for home health care, institutional care or both.

Determining a precise combination of benefit amounts, elimination periods and inflation riders to meet your future needs can be challenging. One way to deal with this decision is to determine how much of the long-term care risk you can reasonably cover and then transfer the balance of the risk to an insurer.

Wealth planning tip 4

CONSIDER A SPLIT-DOLLAR PLAN

Split-dollar arrangements provide for a policy's costs and benefits to be split between two parties — often the insured (or a trust for his or her family) and his or her employer. The arrangement typically provides for a buyout of the employer's interest in the policy at retirement or some other date.

Recent legislation provides new guidelines for such arrangements, aimed at reducing or eliminating the income tax benefits. Review carefully how any new or existing plans may be affected by the notice.

DON'T FORGET ABOUT PROPERTY, CASUALTY AND LIABILITY INSURANCE

Property and casualty insurance provides coverage for your home and its contents, your automobiles, and your personal property. Excess liability coverage, commonly referred to as umbrella coverage, kicks in where your other coverage leaves off. Usually you cannot buy excess liability coverage unless both your homeowners and auto coverage meet certain criteria. If you serve on corporate or nonprofit organization boards of directors, you should also consider insurance to cover associated liability.

REFINING YOUR INVESTMENT STRATEGY

a volatile stock market makes a well-thought-out investment strategy more important than ever. However, your ideal strategy depends not on current market performance, but on your age, portfolio size, risk tolerance and desired rate of return, liquidity and cash flow needs, and income tax bracket. This means evaluating these elements and adjusting your asset allocation accordingly while considering the tax consequences. By sticking to your strategy and making refinements as necessary, you may better weather a stormy market.

RATE YOUR RISK TOLERANCE

All investments involve a trade-off between risk and return. A certain amount of risk is inevitable if you want your money to grow. Understanding your personal risk tolerance will help you make investment decisions you feel comfortable with.

Wealth planning tip 5

DOCUMENT YOUR STRATEGY IN AN IPS

Are you interested in steady growth or bigger opportunities for gains with more volatility? Do you have a current need for income? Once you evaluate these and other questions, you can develop your investment strategy and document it in an investment policy statement (IPS) based on your risk tolerance, desired asset allocation and other variables that can affect your portfolio structure. You can then use your IPS as a working model for monitoring your portfolio's structure and performance.

Although your personality influences your underlying risk tolerance, your stage of life and current wealth also affect it. As you move closer to retirement, you may be better off forgoing the highest potential returns and putting your money in more secure investments, such as bonds, because you would have less time to recover from a market downturn. But if you have a large amount of disposable income available for investing, you may be able to afford more risk — even under a shorter time frame.

ALLOCATE ASSETS AMONG THE 3 MAIN CLASSES

Asset allocation is one of the most important aspects of investment portfolio management. The objective of any asset allocation plan is to find the appropriate mix of expected risk and expected return to achieve your goals.

Diversifying your funds among the three broad investment classes — stocks, bonds and cash — is an important way to help minimize your investment risks. The first step is to decide how to distribute your resources among the three main classes. Then within each asset class, you face additional choices. Here are some of the options to consider for each class:

Stocks. You can choose among various categories of stocks, such as by size (large cap, mid cap and small cap), function (growth, value, income), geography (domestic, international) and market sector (technology, energy, financial services, basic materials) — each of which may respond differently to economic changes. Over the short term, stocks can be a risky investment. But over the long term, they have earned higher and more consistently positive returns than any other financial investment.

Bonds. As with stocks, you can choose among various categories of bonds, such as by taxability (taxable, tax free), issuer (private, federal government, state government, municipal government), or time frame (short, intermediate or long term). Bonds, though generally less volatile than stocks, also respond to economic changes. In particular, bonds are sensitive to market interest rate changes.

Cash and cash equivalents. These generally include short-term liquid instruments such as Treasury bills, commercial paper and money market funds.* This class is generally allocated the smallest percentage of resources, because, though you face minimal risk, you also reap lower rewards. You may want to maintain sufficient funds to cover cash needs in an emergency — perhaps three to six months' worth.

REMEMBER, TAXES TAKE A BITE OUT OF RETURNS

Individual investors in the stock and bond markets anxiously evaluate each investment with the goal of finding the best returns. Many factors influence investment choices, including personal goals, economic activity and market trends. And though tax consequences should not control investment decisions, you should recognize them as an important component of analyzing the true performance of your portfolio.

The tax rate you pay depends on the type of income (interest, dividend or capital gains) you receive. Reviewing after-tax returns enables you to better evaluate an investment's performance relative to its peers. In fact, many brokers, money managers and mutual funds* report their historical performance on an after-tax basis, which may soon become standard practice.

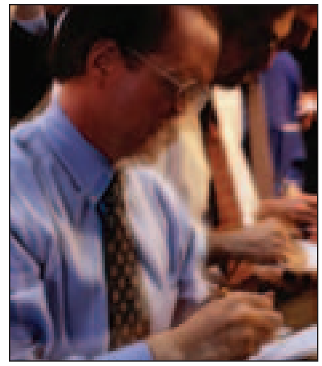
Because taxes are due as gains are realized, can a buy-and-hold strategy maximize after-tax returns? It's clear that active management creates turnover, which ultimately results in tax consequences. Taxes may increase when gains are realized or decrease when losses exceed gains.

* *An investment in a money market or mutual fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency, and that although they seek to preserve the value of an investment at $1 per share, it is possible to lose money by investing in these funds.*

Statistics show that the higher the turnover, the lower the after-tax returns, especially if turnover occurs within one year and gains are being taxed at ordinary income rates. The effect in any particular year may not be that significant. But over a number of years, the compounding can have a tremendous impact on a portfolio's growth. For example, the difference between a $100,000 portfolio growing after tax at 8% a year vs. a less tax efficient $100,000 portfolio of equally risky investments growing after tax at 6% a year* amounts to almost $150,000 over 20 years.

TIME THE RECOGNITION OF CAPITAL GAINS AND LOSSES

When selling securities and generating capital gains or losses, you have an opportunity to greatly impact your tax bill. If for the year you have net capital gains, you can take unrealized losses to offset them. If you have net losses, you can lock in gains on appreciated securities by selling them and absorbing the losses. (Only $3,000 of losses can offset ordinary income, but you can carry forward excess losses indefinitely.)



Also consider that the top tax rate applicable to long-term capital gains is 15% for most property held more than 12 months (see Chart 5), while the top rate for regular income tax is 35% for 2004.

That's a significant difference. If you can generate net long-term capital gains instead of ordinary income, you will save considerably on your taxes. As a result, investment strategies that emphasize capital appreciation over

Chart 5

Capital gain regular tax rates

Asset type and holding period	Sales through May 5, 2003	Sales after May 5, 2003
Held 12 months or less	35%	35%
Held more than 12 months	20%	15%
Exceptions to the 20% or 15% rates:		
Collectibles, such as artwork	28%	28%
Gain attributable to depreciation on real property	25%	25%
Assets purchased after Dec. 31, 2000, and held more than 5 years	18%	15%
Qualified small business stock held more than 5 years	14%	14%
Gain that would be taxed at 10% or 15% based on your regular income tax rate	10%	5%
Assets purchased after Dec. 31, 2000, and held more than 5 years that otherwise would be taxed in the 10% or 15% bracket	8%	5%

Source: U.S. Internal Revenue Code

* *These amounts are hypothetical and are used for example only.*

current income can significantly enhance after-tax portfolio returns. Of course, tax considerations are just a factor — if your investment strategy dictates selling a short-term security at a gain, don't let the taxes stop you. After all, you'll still net a significant percentage of your gain.

You can control the amount and timing of gains or losses recognized and whether the holding period is short-term or long-term on a securities sale by identifying which lots to sell. If you don't specify, your lots are considered sold according to first-in, first-out (FIFO). This could produce the highest taxable gains if those early lots were purchased at a price lower than later lots. For mutual fund shares, you have a choice of using FIFO, average cost (either single or double category) or specific identification.

Identifying shares with greater-than-12-month holding periods will qualify gains for the lower rates, but may also force you to swallow larger capital gains if the stock appreciated steadily while you held it. To take advantage of specific identification rules, you must give your broker written instructions before the sale.

If you have redeemed mutual fund shares and have had dividends reinvested over the years, the dividends increase your cost basis for calculating your gain or loss on sale or redemption. If you sell certain business or investment assets that qualify, consider selling them in installments to defer capital gains.

CONSIDER YOUR STOCK OPTIONS

Today, more than ever, companies are taking advantage of the motivational power of granting stock options as a form of compensation. These options may become a greater percentage of your income and net worth. If you hold these options, you should be aware of the tax implications of receiving and exercising them and, finally, of selling the underlying stock. There are two distinct types of stock options:

Nonqualified options. When nonqualified options, which are more common, are granted, they are not included in income unless the value is readily ascertainable. For the value to be readily ascertainable, the option usually needs to be actively traded on an open market. When you exercise the option, you recognize ordinary income for the difference between the stock's fair market value and exercise price. (See Case study IV.)

Incentive stock options (ISOs). The use of ISOs is limited because employers receive no compensation deduction for issuing them and the stock's value with respect to the option is capped in any year. The employee may exercise an ISO without recognizing any taxable income, but there still may be tax consequences due to alternative minimum tax calculations. If an ISO meets certain holding period tests, the sale of the underlying stock will qualify for long-term capital gains treatment.

Because the option price must be at least equal to the fair market value at the date of the grant, stock option holders often discover that they are not liquid enough to exercise the options. So, their options expire, and they receive nothing. Proper timing when exercising options is vital.

Case study IV

EXERCISING STOCK OPTIONS IS TAXING

Shannon exercises her nonqualified option to buy 1,000 shares of XYZ for $10 per share when the stock is trading at $30 per share. She recognizes ordinary income of $20,000 [($30 – $10) x 1,000 shares]. Shannon's employer gets a tax deduction for the same amount. Two years later, if Shannon sells the stock for $35 per share, she will recognize capital gains income of only $5 per share, or $5,000, because she already paid tax on the difference between $30 and $10 per share.

DON'T FORGET TO DEDUCT INTEREST EXPENSE

Interest on money borrowed to purchase or carry portfolio investments (investments other than passive activity or capital assets used in an active trade or business) is deductible only against investment income. Excess investment interest expense can be carried forward indefinitely and deducted against future years' investment income.

You may elect to treat net capital gains as investment income and trade off the taxability of such gains at the lower rate. This makes sense if you have excess investment interest expense that will not be used if you carry it over due to the lack of investment income in the next several years. Interest on funds borrowed to purchase or carry tax-exempt obligations is not deductible. For commingled accounts, allocating the interest expense against taxable and tax-exempt securities usually applies.

PROTECTING YOUR ASSETS

Asset protection planning is the process of organizing assets to shield yourself from future adverse financial circumstances, such as litigation. An asset protection plan may be as simple as diversifying your stock portfolio or as complex as setting up foreign trusts. It is generally impractical to protect all assets from creditors, but, by using asset protection planning, your entire net worth will not be fair game to future creditors. In addition to the techniques suggested below, insurance and retirement plans also can serve as asset protection tools.

TRANSFER ASSETS TO YOUR SPOUSE

With proper planning, a gift to your spouse can shield the gifted assets from your future creditors. But if your marriage should end in divorce, your then ex-spouse would still own those assets, so you will want to be confident in the stability of your marriage before making such a gift.

The main advantage of an offshore trust is that a provision in the trust instrument shields the trust assets from creditors.

SET UP AN FLP

Family limited partnerships (FLPs) can also be used in an asset protection plan. Most state laws protect the FLP's assets from creditors of the limited partners. Generally, FLPs can be formed without adverse tax consequences, and limited liability is provided to the limited partners. (We discuss FLPs in more detail in Wealth planning tip 1 on page 8.)

ESTABLISH AN OFFSHORE TRUST

The main advantage of an offshore trust is that a provision in the trust instrument shields the trust assets from creditors. Although this provision can also be put into domestic trusts, it can be "pierced" when the beneficiary is also the grantor. This is due to state laws prohibiting grantors from establishing trusts for their benefit that block existing and future creditors' access to the trust assets. The provision, therefore, generally is more effective in foreign trusts. But this is beginning to change — see Wealth planning tip 6.

Another advantage of the offshore trust is that the foreign jurisdiction's trust law generally applies. These laws typically provide for a short statute of limitations, and offshore trust sites typically don't recognize foreign judgments. Additionally, foreign jurisdiction laws generally define benefits that a grantor may retain without subjecting the trust assets to seizure by creditors. Due to their beneficial laws and treatment of trusts, some popular trust sites are the Cook Islands, the Cayman Islands and the Bahamas.

REDUCING INCOME TAXES

As with other aspects of your personal finances, income taxes can play a significant role in your ability to retain and increase your personal wealth. Therefore, reducing your income taxes is a logical way to preserve your personal wealth. It's important to consider how changes such as marriage, divorce, the birth of a child, a promotion, relocation, retirement, illness or sale of major assets can easily alter your taxable income from year to year. And thanks to JGTRRA and EGTRRA, over the next several years there will be even more changes for you to consider in your income tax planning.

Wealth planning tip 6

ALASKA AND DELAWARE TRUSTS MAY PROVIDE DOMESTIC ASSET PROTECTION

Recently, domestic trusts in some states have been designed to provide the same benefits that traditionally have been the exclusive province of offshore trusts. The idea behind these domestic "offshore" trusts is that you are able to get the same benefits domestically that used to require you to go offshore. Presumably, the trusts will provide the same asset protection benefit as offshore trusts, but the reality is that they haven't been tested to the same degree. Whether a state — or offshore — trust is appropriate for you depends on several factors. Please contact us to determine whether your situation warrants such a trust.

TAKE ADVANTAGE OF THE TAX CUTS UNDER TAX ACTS

The recent tax acts offer a variety of income tax relief you may benefit from. Here are two of the most significant changes that we haven't yet discussed in this booklet:

Tax rate cuts. Since 2001, a new 10% tax rate has applied to a portion of income that was previously taxed at 15%. In addition, other regular income tax rates begin decreasing in 2004. (See Chart 6.)

Chart 6
Regular income tax rate reductions

Year	27% rate reduced to	30% rate reduced to	35% rate reduced to	38.6% rate reduced to
2004 and after	25%	28%	33%	35%

Source: U.S. Internal Revenue Code

Expanded education tax breaks. Since 2002, there has been a new deduction for qualified higher education expenses, though adjusted gross income (AGI) limits apply. Also, the maximum Coverdell Education Savings Account (ESA — formerly Education IRA) contribution has increased from $500 to $2,000, and funds can also be used for elementary and secondary school expenses.

The biggest new education tax break may be the expansion of Section 529 plans. This includes expansion of the definition to include certain prepaid tuition programs established and maintained by private education institutions, and the exclusion from gross income of distributions used to pay qualified higher education expenses.

SHIFT INCOME TO CHILDREN

When you are in a high tax bracket, you may have opportunities to shift income to family members who are in lower tax brackets. By doing this, the family overall will keep more money after taxes. Among the strategies to shift income is making annual exclusion gifts to your children. (For more on the annual exclusion, turn to page 7.) For children age 14 and older, investment income will be taxed at their own marginal rate. But for children under age 14, only a minimal amount of unearned income will be taxed at the child's rate. The excess will be taxed at your marginal rate.

If you own a business, consider employing your children. Their salaries will be taxed at their marginal rates (even if they are younger than 14, because it's earned income), and they can usually make a Roth or a deductible IRA contribution to defer taxes and begin a savings program. Remember, you must pay your children what you would pay unrelated employees to do the same work and adhere to child labor laws.

By bunching certain deductible expenses into one year, you may be able to exceed the applicable floors.

ACCELERATE OR DEFER INCOME AND DEDUCTIONS

If you expect to be in a higher tax bracket next year, accelerating income into the current year and deferring deductions until next year could save you taxes overall. If you expect to be in a lower bracket, the opposite approach — deferring income and accelerating deductions — could be effective. Even if your marginal bracket remains the same, deferring income to a later year generally will be advantageous. And by bunching certain deductible expenses into one year, you may be able to exceed the applicable floors.

Also be sure to take all the above-the-line deductions — the income adjustments that determine AGI — you are entitled to. Because AGI determines your eligibility for various deductions, exemptions and credits, this strategy can reduce your taxes even further.

Wealth planning tip 7

AVOID PENALTIES AND DEFER LIABILITY WITH ESTIMATED TAX PAYMENTS

You may be penalized if your withholding and estimated tax payments don't meet the minimum required amounts. To avoid such penalties, during the current year pay 90% of your current year's tax liability or 100% of your prior year's liability. (If your adjusted gross income exceeds certain levels, you have to pay a higher percentage — 110% in 2004.) The second option can be beneficial if you expect your tax to increase, because you can defer any tax due in excess of last year's liability (or 110% of it) until April 15 of the next year.

BENEFIT FROM HOME OWNERSHIP

Owning a home offers many tax-saving opportunities. Don't miss out on any — be sure to take advantage of all that apply to you:

Maximize home-related deductions. You may deduct interest on debt on a first and second home, though limits do apply. Although you must include your main residence as one of the homes, you may choose any of your other homes as a second qualified residence, and you may change it each tax year.

If you refinance, you must use any excess principal taken out to substantially improve the home; otherwise interest on only $100,000 of such excess debt may be deductible. Thus, paying down your mortgage and tapping into that equity at a later date could severely restrict your ability to deduct the interest as mortgage interest.

Exclude gain from the sale of your home. The Taxpayer Relief Act of 1997 allows you to exclude up to $250,000 ($500,000 if married filing jointly) of the gain realized on the sale or exchange of your principal residence. You generally may not use this exclusion more than once every two years.

If you still incur a taxable gain on your home sale, examine your records from the last several years to determine whether you've overlooked any capital improvement expenses, such as from building additions. These costs reduce your taxable gain when added to your basis in the home.

Consider rental rules. If you rent a portion of any of your homes for less than 15 days, you need not report the income. If you or a relative use the home for personal use for more than 14 days or for more than 10% of the number of days the property is rented at fair market value during the year, your claim for deductions is generally limited to the gross income from the property.

Converting your residence from personal to rental use may benefit you if you can sell it only at a loss. The loss on such a sale is not deductible. If, however, you sell it after converting it for rental use, the loss is deductible because it is now a business and not a personal asset. Certain additional rules also apply.

PLAN FOR THE AMT

For 2004, the AMT exemption increases to $58,000 for joint filers (from $49,000), to $40,250 for single or head-of-household filers (from $35,750) and $29,000 for married persons who file separately (from $24,500). These amounts expire after 2004, returning the exemptions to pre-2001 levels of $45,000, $33,750 and $22,500, respectively.

PERSONAL WEALTH MANAGEMENT WORKSHEET

You can use many different strategies to manage your wealth. The ones that will work best for you will depend on your unique situation. To learn how to incorporate these strategies into your personal wealth plan, fill out the worksheet below. After you complete the checklist, fax or mail it to our office — or simply call to discuss your needs. We would be glad to help you create a wealth management plan that achieves your financial goals.

Please check all boxes that apply to your situation.

Do you have a wealth management plan in place?

- ❑ Yes (date last reviewed: ______________________)
- ❑ No, but I would like to develop one

My primary financial goals are:

- ❑ Building and protecting my estate
- ❑ Charitable giving
- ❑ Protection against loss/illness
- ❑ Protecting my investments
- ❑ Ensuring an adequate retirement income
- ❑ Minimizing taxes
- ❑ Transferring my business to my heirs
- ❑ Other ______________________________________

I would like to learn more about the following:

- ❑ How the new tax law affects my wealth management strategies
- ❑ Using gifting as part of my estate plan
- ❑ Setting up a trust for my heirs
- ❑ Transferring ownership of my business
- ❑ Using trusts to achieve my charitable goals
- ❑ Setting up a private foundation
- ❑ Long-term care insurance
- ❑ Maximizing my retirement income
- ❑ Planning my retirement plan distributions
- ❑ Using insurance as part of my estate plan
- ❑ Choosing the right type of insurance
- ❑ Split-dollar insurance plans
- ❑ Creating an asset allocation plan for my investments
- ❑ Creating a capital gains strategy
- ❑ Asset protection planning
- ❑ Shifting or deferring income
- ❑ Other ______________________________________

❑ My greatest wealth management concern/need is:

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Fax or mail this form to our office for more information, or call us to discuss your wealth management needs.

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NAME

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TITLE

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ORGANIZATION

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ADDRESS

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CITY STATE ZIP

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PHONE FAX

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E-MAIL

INSURANCE SERVICES SINCE 1974

CPS Insurance Services is celebrating 30 years of service to brokers. Our commitment to you is to continue to mix the latest technologies, with years of knowledge and service expertise. CPS is a major player in the advanced case market — with an in-house advanced planning and tax attorney providing expert guidance in advanced estate planning, investment strategies, corporate and personal tax planning, charitable trusts, benefits design, deferred compensation planning, corporate financial planning, as well as strategies for retirement and wealth management.

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