

AWM Financial Planning

The 3 Year Checklist



Steve Giacobbe, CFA, CFP®
Accredited Wealth Management
6010 Brownsboro Park Blvd. • Louisville • KY • 40207
502-290-1905
sgiacobbe@accreditedwm.com • www.accreditedwm.com



A good retirement is not guaranteed but planning ahead can increase the odds you'll have one! Last month we wrote about the 5-year pre-retirement checklist, this month we touched on a few things to do 3 years before to the big date.

- Start to imagine what retirement means and will look like for you- will you work part-time, where you will live, what is going to make you happy, etc.?
- Track your spending closely and consider living on your projected income for 1 to 2 years prior to retirement as a "trial run."
- Start organizing and considering financial needs - insurance, health coverage, how to protect your spouse, estimates for Social Security, tax projections, etc.

Next month we will highlight the 1-year checklist. If you're thinking about retiring in the next few years, give us a call to get started on your plan.

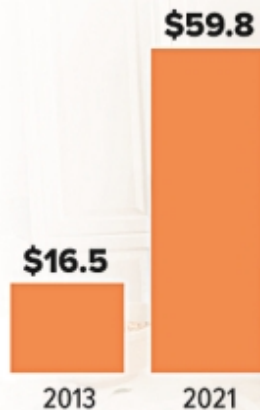
Investors Beware: This Surtax Is Creeping Up on You

High-income taxpayers are subject to a 3.8% net investment income tax (NIIT) from capital gains, dividends, interest, certain royalties, rents, and passive income if their modified adjusted gross income (MAGI) exceeds \$200,000 for single filers or \$250,000 for married joint filers. The number of taxpayers paying the NIIT has more than doubled since it took effect, mostly because these income thresholds were not indexed to inflation, and the revenue collected has more than tripled.

Number of taxpayers subject to NIIT (in millions)



NIIT revenue (in billions)



Source: Congressional Research Service, 2023 (uses IRS data)

Beware of These Life Insurance Beneficiary Mistakes

Life insurance has long been recognized as a useful way to provide for your heirs and loved ones when you die. While naming your policy's beneficiaries should be a relatively simple task, there are a number of situations that can easily lead to unintended and adverse consequences. Here are several life insurance beneficiary traps you may want to discuss with a professional.

Not naming a beneficiary

The most obvious mistake you can make is failing to name a beneficiary of your life insurance policy. But simply naming your spouse or child as beneficiary may not suffice. It is conceivable that you and your spouse could die together or that your named beneficiary may die before you and you haven't named successor beneficiaries. If the beneficiaries you designated are not living at your death, the insurance company may pay the death proceeds to your estate, which can lead to other potential problems.

Death benefit paid to your estate

If your life insurance is paid to your estate, several undesired issues may arise. First, the insurance proceeds likely become subject to probate, which may delay the payments to your heirs. Second, life insurance that is part of your probate estate is subject to claims of your probate creditors. Not only might your heirs have to wait to receive their share of the insurance, but your creditors may satisfy their claims out of those proceeds first.

Naming a minor child as beneficiary

Insurance companies will rarely pay life insurance proceeds directly to a minor. Typically, the court appoints a guardian — a potentially costly and time-consuming process — to handle the proceeds until the minor beneficiary reaches the age of majority according to state law. If you want the life insurance proceeds to be paid for the benefit of a minor, you may consider creating a trust that names the minor as beneficiary. Then the trust manages and pays the proceeds from the insurance according to the terms and conditions you set out in the trust document. Consult with an estate attorney to decide on the course that works best for your situation.




Disqualifying a beneficiary from government assistance

A beneficiary you name to receive your life insurance may be receiving or be eligible to receive government assistance due to a disability or other special circumstance. Eligibility for government benefits is often tied to the financial circumstances of the recipient. The payment of insurance proceeds may be a financial windfall that disqualifies your beneficiary from eligibility for government benefits, or the proceeds may have to be paid to a government entity

as reimbursement for benefits paid. Again, an estate attorney can help you address this issue.

Life Insurance Payout Options

Most life insurance policies offer several options to the policy beneficiary, including:

 Lump sum payment	The most common choice. A one-time payment is made of the death benefit proceeds to the beneficiary.
 Lifetime annuity	The death benefit proceeds are converted to an income annuity, which makes a fixed, periodic payment to the beneficiary for the rest of his/her life.
 Fixed period annuity	Like the lifetime annuity, except the payments will be made over a specified period of time, such as 10 years, after which, payments cease.

Creating a taxable situation

Generally, life insurance death proceeds are not taxed when they're paid. However, there are exceptions to this rule, and the most common situation involves having three different people as policy owner, insured, and beneficiary. Typically, the policy owner and the insured are one and the same person. But sometimes the owner is not the insured or the beneficiary. For example, mom may be the policy owner on the life of dad for the benefit of their children. In this situation, mom is effectively creating a gift of the insurance proceeds for her children/beneficiaries. As the donor, mom may be subject to gift tax. Consult a financial or tax professional to figure out the best way to structure the policy.

As with most financial decisions, there are expenses associated with the purchase of life insurance. Policies commonly have mortality and expense charges. In addition, if a policy is surrendered prematurely, there may be surrender charges and income tax implications. The cost and availability of life insurance depend on factors such as age, health, and the type and amount of insurance purchased.

While trusts offer numerous advantages, they incur up-front costs and often have ongoing administrative fees. The use of trusts involves a complex web of tax rules and regulations. You should consider the counsel of an experienced estate planning professional and your legal and tax advisors before implementing such strategies.

Individual Bonds vs. Bond Funds: What's the Difference?

Individual bonds and bond funds can both provide an income stream, but there are important differences. An individual bond can offer more certainty and stability than a fund, while a fund can offer diversification that might be difficult to obtain with individual bonds.

Coupon, maturity, and yield

An individual bond has a coupon rate — the annual interest rate paid on the face value of the bond — and a maturity date, which is the date the principal is returned to the borrower. If you hold a bond to maturity, you will receive any interest payments due during the time you own it (typically paid quarterly or semi-annually) and the full principal at maturity, unless the bond issuer defaults. If you sell the bond on the secondary market before maturity, you will receive the market price, which may be higher or lower than the face value or the amount you paid, depending on market conditions.

By contrast, a bond fund does not have a coupon rate or a maturity date (with the exception of certain defined-maturity funds). A fund typically pays monthly distributions based on the bonds in the fund. The rate can change as bonds are replaced (due to maturity or sales), and as market conditions change. A fund also has fees and expenses, which reduce the interest paid, and fund managers can adjust to market conditions in various ways, depending on the fund's objective. Because there is no maturity date, you can hold the fund as long as the fund company remains in business. However, there is never a guarantee that you will receive your principal no matter how long you hold the shares. Fund shares, when sold, may be worth more or less than your original investment.

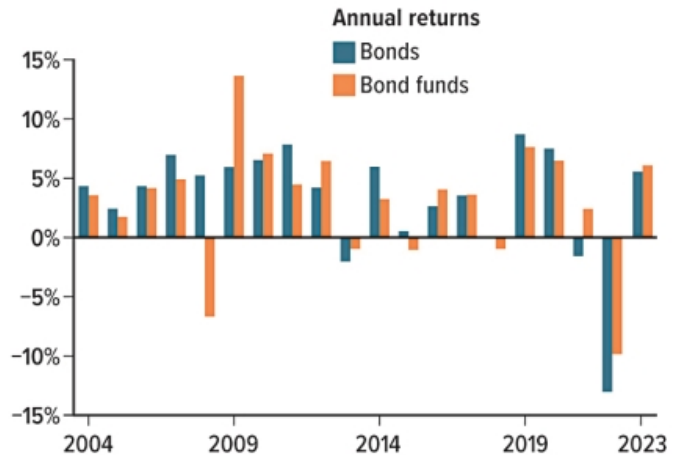
Yield is the expected return from a bond or bond fund, based on the interest rate and purchase price. If you buy a \$1,000 bond at face value with a coupon rate of 4%, the yield is 4%. But if you buy the same bond on the secondary market for \$800, the yield is 5%, because you receive interest based on the face value: $4\% \times \$1,000 \text{ face value} = \$40 \text{ interest} / \$800 \text{ purchase price} = 5\% \text{ yield}$. Bond fund yields are more complex, but the 30-day SEC yield (or standardized yield) offers a helpful comparison. This is typically calculated using the maximum share price on the last day of the month and projects annual net investment income assuming it remains the same as the previous 30 days.

Interest rate sensitivity

Bonds and bond funds are sensitive to changes in interest rates. Generally, when rates rise, the market value of existing bonds and bond funds falls, because newly issued bonds pay higher interest rates. Conversely, when rates fall, the market value of existing bonds and bond funds rises. This only applies to market values and would not affect an individual bond held to maturity.

Varied Performance

Individual bonds and bond funds have performed differently over the past 20 years. In part, this is because fund managers may respond to the market in different ways; for example, they might try to preserve yield over share price or vice versa. Note that the performance of individual bonds only applies to values on the secondary market, not to bonds held to maturity.



Source: London Stock Exchange Group, 2024, for the period 12/31/2003 to 12/31/2023. Bonds are represented by the Bloomberg U.S. Aggregate Bond TR Index, and bond funds are represented by the Thomson US: All Gen Bond - MF Index. Expenses, fees, charges, and taxes are not considered. The performance of an unmanaged index is not indicative of the performance of any particular investment. Individuals cannot invest directly in an index. Rates of return will vary over time, particularly for long-term investments. Investments seeking higher rates of return involve a higher degree of risk. Past performance is no guarantee of future results. Actual results will vary.

If you owned bond funds during the period that the Federal Reserve was aggressively raising interest rates, you may have been frustrated as you watched the value of your shares drop. Now that interest rates seem to have stabilized, share values are likely to stabilize as well, and they may increase if rates begin to decrease. Bond funds typically replace underlying bonds as they mature, and new bonds added to funds over the last two years will generally pay higher interest rates, increasing the interest paid by the fund. Although it is impossible to predict future market direction, bond funds may be poised to offer solid returns if rates remain stable or begin to fall.

Diversification does not guarantee a profit or protect against investment loss. Funds are sold by prospectus. Please consider the investment objectives, risks, charges, and expenses carefully before investing. The prospectus, which contains this and other information about the investment company, can be obtained from your financial professional. Be sure to read the prospectus carefully before deciding whether to invest.

Why Family Businesses Should Have Succession Plans

In recent years, the family drama surrounding an aging media mogul — and his unresolved succession plans — have been at the center of a hit television show. For family businesses, succession plans are designed to ensure the orderly transfer of ownership and leadership to the next generation. But relationships among family members are sometimes just as complicated in real life as they are on TV and monetizing a closely held business to help fund retirement often takes longer than expected.

In fact, only 34% of family businesses have a robust, documented, and communicated succession plan in place.¹ Much like the fictional billionaire in "Succession," some leaders avoid the issue because they love running their businesses and don't want to stop any time soon.

But one never knows what the future has in store. Even if you are happy, healthy, and determined to stay involved in your business for years to come, you might be glad you took the time to develop a thoughtful succession plan.

Set a target

It might be wise to have a realistic retirement date in mind. Any effort to identify and groom a successor might take longer than you expect. And if you plan to sell your company, it could take several years to find a qualified buyer, begin the ownership transition, and finalize the transaction. To get the best possible price

and terms, you may need to focus on improving the company's balance sheet before you put it on the market.

Stage your exit

Keeping your business in the family may be an easy decision if an adult child or another relative is capable, willing, and prepared to take over. If so, finding ways to reduce the value of the business on paper could help you gift ownership shares with fewer tax consequences.

Otherwise, it may be possible to sell your business to co-owners, outsiders, or even your own employees. Closing and liquidating the assets could be the only viable option for some businesses.

Invest for retirement

Making annual retirement plan contributions with some of your profits can build wealth outside of your business and help insulate your personal financial picture from risks associated with your business's distinct market. Building a separate investment portfolio might also provide greater flexibility during and after a transfer of ownership.

All investing involves risk, including the possible loss of principal, and there is no guarantee that any investment strategy will be successful.

1) US Family Business Survey, PwC, 2023

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