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Imagine you could wave a magic wand and turn your baby granddaughter, Emily, into a millionaire. Believe it or not, you don't need to become a fairy godparent to give Emily a head start in life. Even a relatively modest amount tucked away using a so-called "stretch" IRA strategy could, under the right conditions, evolve into a rather substantial nest egg that Emily, or another beneficiary, can enjoy in years to come.

A Long-Term Strategy

The stretch IRA strategy is simply an Individual Retirement Account (IRA) in which earnings are allowed to grow tax deferred over a beneficiary's lifetime. If you have an IRA that you don't need to tap into to support yourself during retirement, you can opt to restrict your withdrawals to the minimum annual distribution required by the Internal Revenue Service (IRS) starting at age 70½. Required minimum distributions are based on your life expectancy and the amount of money in your account.

If you decide you want to stretch your IRA, you can add language to establish a trust that allows for the distribution of IRA assets to primary, and possibly secondary, beneficiaries. After you die, your beneficiary will be permitted to take distributions over time, based on his or her own age and life expectancy. This not only gives the investments in the account a chance to grow and compound, but it also means that income taxes owed on the IRA can be paid over an extended period of time.

If you choose a very young beneficiary, like Emily, the funds in the IRA may experience substantial compounding over the course of her lifetime. Provided Emily takes no more than the required minimum distributions during her younger years, she may amass a considerable sum by the time she reaches retirement.



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Is It Time to Incorporate?

In the minds of many people, a corporation is a big company whose shares are traded on Wall Street. But a business does not have to be large or public to become a “C” corporation. While you may have started your business as a sole proprietorship or partnership, your firm could benefit from adopting a more complex business structure as it seeks to expand or take on more employees. The most regulated of the business forms, the corporation nonetheless offers certain tax and legal advantages that could make it a suitable structure for many growing businesses.

The C corporation is a for-profit, state incorporated business, which is considered by law to be a unique entity separate from the individuals who own and run it. A corporation is created when shareholders file articles of incorporation with a secretary of state’s office. If a corporation conducts business outside the state in which it was organized, the company may be required by other states to register as a “foreign” corporation.

The organizational structure of a corporation involves three main groups: shareholders, directors, and officers. A corporation is owned by the shareholders, who are usually not directly involved in running the company unless they also serve as officers or directors. Instead, most shareholders influence corporate decisions by electing and removing directors, voting on amendments to the articles of incorporation, and approving or disapproving other major changes. The corporation’s officers, who manage the company’s day-to-day operations, are appointed by the board of directors. In most corporations, the board

has a supervisory role, intervening only in major business decisions.

Corporations, like individuals, are entitled by law to enter into contracts, loan and borrow money, own assets, sue and be sued, hire employees, and pay taxes—all without having to directly involve the shareholders. Corporations offer shareholders liability protection: While shareholders participate in profits in the form of stock appreciation and dividends, their personal assets are shielded from debt liability and lawsuits against the company.



C corporations pay corporate taxes, and the shareholders pay tax on the income they receive as dividends. This double taxation can be a disadvantage, particularly for owners who are not in a position to reinvest a significant portion of profits back into their business. On the other hand, corporate federal income tax rates, which start at 15%, may be lower than the shareholders’ personal income tax rates. Owners who can afford to do so may leave a portion of earnings in the company for future investment or to reduce their own income tax liability. The amount of corporate tax owed may, in any case, be relatively low after the cost of paying salaries and benefits is deducted.

Of all the business forms, C corporations have the greatest flexibility in raising money through equity financing. There are no restrictions on C corporation shareholder numbers, and owners are not required to be U.S. residents. C corporations may even be owned by other business entities.

Unlike sole proprietorships and partnerships, which often end upon the death or retirement of the owners, C corporations can last in perpetuity. Ownership in a corporation is easily transferable: When shareholders die or sell their interests, the corporation can continue to exist and do business.

The C corporation is not the appropriate structure for every business. While the independent status of the corporation offers many advantages, there are also some potential drawbacks to choosing this structure.

C corporation shareholders cannot, for tax purposes, offset the company’s losses against their personal income. As profits grow, the company will be faced with corporate tax rates as high as 39%. Because of the organizational complexity and regulatory burdens associated with this structure, the corporation is more expensive to establish and maintain than other business forms.

Each business structure has its advantages and disadvantages. Your choice will affect the taxes you pay and your personal liability risk, so it is important to choose the right entity for your business. For specific guidance, consult your tax professional. ■

Taxes and Your Estate: Reconcile Your Domicile

Increased mobility in today's society has changed the ways in which we live, work, and play. Compared to previous generations, it is now quite common for work and recreation arrangements to cross state lines, resulting in ownership of property and formal social relationships in more than one state. However, the expanded opportunities created by mobility may come at a price: the increased likelihood that several states may be able to tax your estate when you die. If you were to die today, do you know if more than one state would try to levy death taxes on your estate?

The term **domicile** generally refers to the place intended to be your *permanent* home, as distinguished from the term "residence." Although you could have simultaneous residences in several states, in theory, you can have only *one* state of domicile at a time.

A problem may arise when theory and reality part company: when sepa-

rate states reach different conclusions by applying different definitions of "domicile" to the same set of facts. This may result in the apparent inconsistency of more than one state claiming the deceased was a "domiciliary," and each taxing that person's estate accordingly.

Under the Uniform Interstate Compromise of Death Taxes Act, the states involved may be able to reach a compromise in a specific situation. However, if the states involved have not adopted the Act or cannot agree on a solution, the estate in question could be fully taxed in *multiple* jurisdictions.

Establishing Your Domicile

Fortunately, there are steps that can be taken to establish your state of domicile. If you have moved, your "true" domicile may hinge on the *number* and *significance* of the con-

tacts you have with your former and present state. Among the significant factors used to make the case are the following:

- **Retention of "historical" home.** If you moved but did not sell a long-time residence in a former state, your intention to change your domicile may be questioned.
- **Business relationships.** In which state are your significant business contacts located?
- **Location of property.** Where is most of your significant real and tangible personal property located?
- **Social connections.** Where do you maintain political, civic, religious, and family connections?
- **Time spent.** Where do you spend the majority of your time?

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stretching an IRA into future generations

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Be Cautious

But before you integrate the stretch IRA strategy into your estate planning, you should be aware that this approach does come with some risks. If IRA assets decline in value, or if high inflation erodes the value of your savings, the hefty returns your heirs may have been counting on will not materialize.

It is also possible that the funds in your IRA may not grow, if you survive to be very old. If, for example, you live to age 95, the amount you will be able to leave Emily will be considerably less than if you had passed on a decade earlier.

Bear in mind, too, that a stretch IRA strategy works best when only the required minimum distributions are taken. If Emily withdraws additional funds to buy a car or pay the rent, the account may be quickly depleted.

Finally, it is important to consider the tax implications of including a stretch IRA strategy in your inheritable estate. While there is some talk in Washington of abolishing the federal estate tax and generation skipping transfer (GST) taxes, permanent repeal is by no means certain beyond the one-year reprieve scheduled for

2010. It is, therefore, advisable to take into account what impact the IRA could have on the tax liability of your heirs.

Despite these potential drawbacks, a stretch IRA strategy can be a tax-efficient means for passing on savings to future generations. While there is no guarantee that inheriting a stretch IRA from her grandparents will turn little Emily into a millionaire, it could help to make her own retirement a lot more comfortable. ■

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While you may feel your *intent* is clear, it is most likely that your *actions* will be viewed as the evidence of your intentions. Consequently, simple acts such as changing your voter registration to the new locale, changing your automobile registrations and driver's license, formally resigning from organizations in your former state, and formally joining organizations in a new state may be

viewed as evidence of your intent to change your domicile.

However, it is easy to imagine that under some circumstances, the lines may not be clear-cut. For example, if you moved to another state but maintained significant business and social relationships in your former state, where is your domicile?

In such situations where conflicting evidence exists, a good strategy

might be to first determine which state appears most advantageous in terms of death taxes and to determine how domicile is defined in that state. You can then focus on the factors most likely to make the various states involved look favorably upon your domicile.

For specific guidance, please consult your tax and/or legal professionals. ■

The Four Forms of Co-Ownership

Owning property with another individual or partner may be a complex relationship. Consulting with your legal professional can help you establish the ownership form in a way that will benefit you and your heirs. The four forms of co-ownership are as follows:

Tenancy in common is a form of co-ownership often used between unrelated persons. Tenants in common may own unequal shares of property; however, shares between partners are said to be "undivided," which means each owns a proportionate interest in the entire property. For example, if two individuals are equal tenants in common to a parcel of land, it is incorrect to characterize one co-owner as owning the west half and the other as owning the east

half. Rather, both own a one-half interest in the entire parcel.

Joint ownership is a specific type of co-ownership where each owner's legal interest is equal to the interest of every other joint owner. For example, if there are three joint owners, each joint owner owns an equal, undivided, one-third interest in the entire property. In addition, joint ownership carries the **right of survivorship**: When a joint owner dies, the surviving joint owners automatically succeed in ownership of the deceased joint owner's interest. Survivorship rights of a joint owner are given precedence over the claims of the deceased's creditors.

Tenancy by the entirety is a special form of joint tenancy solely

for married couples with one significant difference: The creditor protection of joint ownership extends to the lifetime creditors of the tenants by the entirety.

Community property applies to married couples who own property in any of the following nine states: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin. Regardless of whose name is on any ownership papers, any property accumulated during the marriage is "owned" by both parties.

Splitting property, for any reason, is generally a difficult task. Therefore, the decision to purchase property with another party is one that may require careful consideration. ■

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