

Financially Speaking

With Trisha Arndt, CFP®

Financial Gifts that Really Pay Dividends

Several of our nieces and nephews are now officially teenagers and I found myself at a loss about what to give them this year for Christmas. They either want things that are way outside my planned budget (no, I'm not buying you a car) or they just want money – and how boring is that to wrap!

While this is a new dilemma for me, it is one that many of my clients face – and ask me for help with – every year. A lot of my clients would really like to give gifts to their children and grandchildren that will have a true long term financial benefit to them – not just fund a trip to the mall. Rather than giving a handful of cash I have a number of suggestions for them to consider.

If you would like to give some money, but want it to be put towards something significant down the road, consider setting up a Uniform Transfer to Minor Account (UTMA) – sometimes called a custodial account. A UTMA allows you to put money away on behalf of a child without having to set up a trust or hire an attorney. UTMA's can easily be set up with most banks or investment companies and, as the donor, you can appoint yourself or some other adult to look after the account. Just about any type of savings or investment account can be held in a UTMA – to make it interesting and start teaching the child about investing I often suggest buying a stock of something the child has an interest in (think McDonalds or Disney).

Make sure that you fully understand UTMA's before setting one up. A couple of important things to know include the fact that any assets remaining in the account when the child reaches the age of majority (21 in Wisconsin) become the child's to do with as they will and that substantial UTMA assets can affect the amount of financial aid a college-bound child will receive.

Speaking of college, one of the most valuable things in the world is an education, and you can contribute towards that education by setting up a section 529 college savings account for the child. For money that is specifically meant for college, a 529 plan offers a number of advantages. For starters, you won't owe taxes on investment earnings throughout the year and, if withdrawals are used to pay for qualified higher-education expenses, they can be tax-free. If you are a Wisconsin resident and use the Wisconsin 529 Plan (www.edvest.com) you may also qualify for a tax deduction for making the contribution. Please note that fees, expenses and features of 529 plans can vary from state to state, and by investing in a plan outside your state of residence, you may lose any state tax benefits.

Additionally, money in a section 529 account remains the property of the account owner, not the child who the money is supposed to benefit. You can elect to change the beneficiary of the account down the road and use it for education expenses for that new

individual – or you can keep the money and withdraw it for your own use (in which case taxes and penalties may apply). Earnings must be used to pay for qualified higher education expenses to be federally tax-free. The earnings portion of a nonqualified withdrawal will be subject to ordinary income tax at the recipient's marginal rate and subject to a 10% penalty. Because 529 plan assets are the property of the owner, not the child, they typically have a relatively limited impact on financial aid eligibility.

Please remember that 529 plans involve investment risk, including the possible loss of funds. There is no guarantee a college-funding goal will be met. 529 plans are subject to enrollment, maintenance and administration/management fees and expenses.

If the child is old enough to have earned income and you would really like to contribute towards their long term financial security, consider putting money in a Roth IRA. Roth IRAs are retirement accounts that have the potential to grow completely tax free if used for a qualified purpose. There is also some flexibility for taking withdrawals prior to retirement so it could potentially help with something like a down payment on a house.

Unless the child is under 18, a Roth IRA would be owned and controlled by person who you set the account up for, not you as the donor, so you want to be sure the individual is responsible enough for that.

There are a number of things to consider with each of the options outlined above, including gifting and tax implications, that you need to be sure you understand fully. Make sure that you consult with a qualified tax and/or financial professional before deciding to open an account.

And if you aren't in a position to give a financial gift, but would like to make sure your children and grandchildren develop some financial wisdom, consider talking to them about basic financial concepts. You'd be amazed at how many times clients tell me they remember talking with their grandparents about owning stock and looking at dividend checks they had received. It's never too early to talk about things like delaying gratification today for a greater payoff down the line.

Another idea is giving them a book that is appropriate for their age level. I picked up a copy of "The Everything Kids Money Book" at a conference a couple of years ago and my kids love it – especially the stories about the history of money. I've heard good things about "The Wall Street Journal Guide to Starting Your Financial Life" for those a bit older - and I'm sure there are many other good options available.

However you decide to do it, there are ways to give a gift to the younger loved ones in your life that can potentially benefit them for years to come.

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