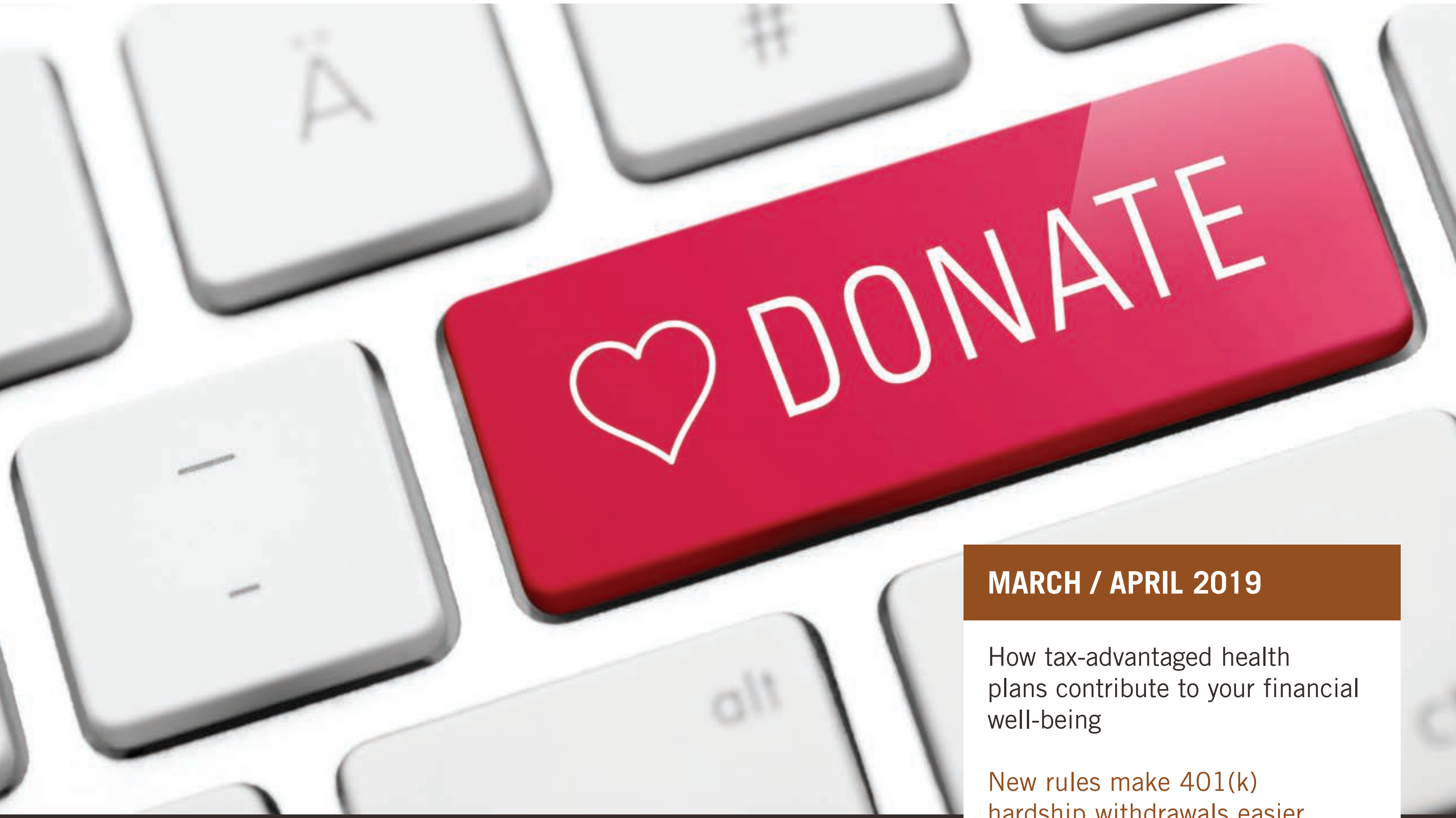
WEALTH MANAGEMENT ADVISOR



SUBSTANTIATING CHARITABLE GIFTS: DO YOU KNOW THE RULES?

Substantiating charitable gifts: Do you know the rules?

When it comes to substantiating charitable contributions, form generally matters. A contribution may be perfectly legitimate, but if you fail to document it properly, you could lose a valuable tax deduction.

Recently, the IRS issued final substantiation regulations that originally were proposed 10 years ago. To avoid costly mistakes, it's important to familiarize yourself with the final rules.

Cash gifts

Any cash gift you make, regardless of amount, must be substantiated with *either* 1) a bank record or 2) a written communication from the charity (an email will suffice) showing its name and the date and amount of the contribution.

Eligible bank records include:

- Bank statements,
- Electronic fund transfer receipts,
- Canceled checks (including scanned images of both sides from a bank website), and
- Credit card statements.

Contributions made by payroll deduction must be substantiated with two documents: 1) a pay stub, W-2 or similar employer-furnished document showing the amount withheld during the year for payment to a charity, *and* 2) a pledge card or other document prepared by or at the direction of the charity showing the charity's name. Cash gifts of $250 or more require, in addition to a bank record or written communication, a contemporaneous written acknowledgment (CWA) from the charity. The CWA must include both the amount of the contribution and a description and good-faith estimate of the value of any goods or services provided in consideration of the contribution.

In a change from the proposed regulations, the final rules permit donors to obtain a single document from the charity that satisfies both written communication and CWA requirements. You need to obtain this substantiation by the *earlier* of your tax return's extended due date or the date you file your return.

WHAT TO DO WHEN YOU CAN'T GET A RECEIPT

Sometimes it's impracticable to obtain a receipt — for example, when you leave clothing or other items at an unattended drop site. In those cases, noncash gifts under $250 may be substantiated by maintaining "reliable written records" that contain:

- The information that would be required in a receipt (your name and address, contribution date and property description),
- The property's fair market value on the donation date, and the method you used to determine its value, and
- For contributions of clothing or household items, their condition.

The reliability of written records depends on the facts and circumstances, including their proximity in time to your contribution.

Noncash gifts

According to the IRS, noncash contributions less than $250 must be substantiated with a receipt from the charity showing the charity's name and address, date of the contribution, and a description detailed enough that even someone who isn't familiar with the property type will recognize it as the property being contributed. The level of detail required depends on the value of the gift and other circumstances. For example, if you donate securities to a charity, the receipt must include the name of the issuer, the type and amount of securities and whether they're publicly traded.

Noncash contributions of at least $250 and up to $500 require a CWA. And for donations between $500 and $5,000, you must obtain a CWA *and* file Section A of IRS Form 8283, "Noncash Charitable Contributions," with your return. The tax form provides a description of the property and certain other details, including the property's fair market value and the method of determining value.

For noncash contributions over $5,000, you must obtain a CWA, file Section B of IRS Form 8283 and obtain a qualified appraisal of the property (although no appraisal is required for certain property, including publicly traded securities). Form 8283 must be signed by you, your appraiser and a representative of the charity. For donations over $500,000, you must also attach a copy of the appraisal to your return.

Appraisal rules

Be particularly careful if you're required to get an appraisal. A qualified appraisal is prepared by a qualified appraiser in accordance with generally accepted appraisal standards. It must be signed and dated no earlier than 60 days before the contribution and no later than the extended due date of your return or, if you first claim the deduction on an amended return, the date you file the amended return.

Qualified appraisers must meet certain educational and experience requirements related to valuing the type of property involved. These requirements are satisfied by:

1. Successfully completing certain professional or college-level coursework and gaining two or more years of relevant experience, or

2. Earning a recognized appraiser designation from a professional appraiser organization.

The final regulations list certain individuals who *aren't* qualified, including the donor and donation recipient, appraisers who receive fees tied to the property's appraised value, and certain related parties. However, donors are permitted to obtain multiple appraisals and select the one to use for substantiation purposes.

Substantiate or lose it

Failure to follow the substantiation rules — including the selection of an appraiser — to the letter can mean the loss of valuable tax deductions. If you're uncertain about the requirements, talk to your tax advisor. ■

How tax-advantaged health plans contribute to your financial well-being

You've likely heard of these common tax-advantaged health care plans: Flexible Spending Arrangements (FSAs), Health Reimbursement Arrangements (HRAs) and Health Savings Accounts (HSAs). But do you know what they offer and, given your specific health and financial concerns, which one might be the best fit for you?

Paid with pretax dollars

The primary advantage of an FSA is that it allows you to pay for qualified medical expenses with pretax income, thus cutting your tax bill. You can fund an FSA through a voluntary salary reduction, and your employer can also make contributions. Neither federal income taxes nor Social Security or Medicare taxes are deducted from contributions. For 2019, you can contribute up to $2,700 to an FSA.

At the beginning of each plan year, you decide how much to contribute to your FSA. It pays to give this some thought, because you may forfeit any balance in the account at year end. But your employer can provide a grace period of up to two and one-half months — or allow you to carry up to $500 into the following plan year.

For your FSA, you'll need to provide a written statement that documents the medical expenses incurred. Common qualified medical expenses include contact lenses, dental services, and eye exams and glasses.

Contributions excluded from income

Employers are the sole funders of HRAs, and they can contribute to them as much as they'd like. HRA contributions aren't included in your taxable income and, as with FSAs, HRA distributions used to reimburse for qualified medical expenses aren't taxed. Unused amounts in an HRA can be carried forward.

However, there's one downside to HRAs: If you're self-employed — or a partner or S corporation shareholder — you're not eligible to use them.

Tax-exempt and more

An HSA is a tax-exempt account used for qualified medical expenses. You can establish one with a qualified HSA trustee, such as a bank or insurance company.

You, your employer, family members and others can contribute to your HSA. For 2019, contributions are limited to $3,500 if you're an individual with self-only health care coverage. If you have family coverage, you can contribute up to $7,000. And if you're 55 or older by the end of the tax year, you can add an additional $1,000 to your HSA.

HSAs offer several benefits. For example:

- You can make contributions with pretax dollars.
- You're allowed to invest HSA money in mutual funds, stocks and some other securities, where it can grow tax-free.
- Distributions that cover qualified medical expenses incurred after you establish the HSA generally aren't taxed.
- Contributions can remain in your account until you need to use the money.
- HSAs are portable, so you can take yours with you if you change employers or quit your job.

Another advantage? You can contribute to your HSA until the tax return deadline, even if the contribution is for the prior year.

Beware of restrictions

If you're interested in opening an HSA, there are several restrictions you should know about. You must be covered under a high deductible health plan (HDHP). For 2019, the HDHP deductible must not be less than $1,350 for self-only coverage, or $2,700 for family coverage. Annual out-of-pocket expenses can't exceed $6,750 for self-only coverage, and $13,500 for family coverage. HSA distributions that aren't used for qualified medical expenses are subject to income tax.

In addition, you can't be claimed as a dependent on another person's tax return. In most cases, you (and your spouse, if you have family coverage) can't be covered under another health plan — including Medicare. If you'd like to continue contributing to an HSA after you're eligible for Medicare, you'd need to delay enrollment. This could expose you to penalties.

Nonhealth factors

Although FSAs, HRAs and HSAs are health savings plans, be sure to consider nonhealth factors, such as your tax exposure and other potential uses for your money, when deciding whether to participate in one. Consult your employee benefits manager and consider seeking outside financial advice. ■

New rules make 401(k) hardship withdrawals easier

If you experience financial difficulties, it may be tempting to tap into the savings you've accumulated in a 401(k) or similar retirement plan. Many plans permit hardship withdrawals, and the Bipartisan Budget Act of 2018 relaxed some of the rules surrounding these withdrawals. But even if it's easier for you to access your retirement savings in a pinch, doing so comes at a steep price.

How do you qualify?

Retirement plans may, but aren't required to, provide for hardship withdrawals. Typically, these withdrawals are allowed for:

- Unexpected medical expenses,
- Tuition and related fees and expenses,
- Costs related to purchasing a principal residence,

- Payments necessary to avoid eviction from, or foreclosure on, a principal residence,
- Certain expenses for repairing damage to a principal residence, and
- Burial or funeral expenses.

The Budget Act has eased certain requirements for plan participants seeking hardship withdrawals. Notably, it has eliminated the requirement that participants take all available plan loans before receiving a hardship distribution.

In addition, the Budget Act has eliminated the six-month period that previously prohibited participants from making new contributions following a hardship withdrawal. And it has expanded the types of funds available for hardship withdrawals. Now, participants can withdraw not only elective deferral contributions, but also qualified nonelective contributions, qualified matching contributions and earnings on these contributions.

Plans have some discretion in designing hardship withdrawal provisions. For example, a plan may allow withdrawals only from elective deferrals and earnings, even though it's permitted to allow withdrawals from other sources.

What are the consequences?

Most hardship withdrawals are subject to taxes and, if you're under age 59½, a 10% penalty. Suppose, for instance, that a 50-year-old taxpayer takes a $10,000 hardship withdrawal from a 401(k) plan. Assuming the taxpayer is in the 32% tax bracket, the amount left after federal taxes and penalties is only $5,800 ($10,000 - $3,200 tax - $1,000 penalty).

You may be able to avoid a 10% penalty if:

1. You're disabled,
2. Your unreimbursed medical expenses exceed 10% (for tax years 2019 through 2025) of your adjusted gross income, or
3. A court order requires you to give the money to your former spouse, a child or another dependent in connection with a divorce.

In addition to the impact of taxes and penalties, consider how permanently removing funds from your account will affect your retirement savings. Also keep in mind that, unlike most assets, the money in a 401(k) or similar tax-advantaged plan is protected from creditors. Think twice before relinquishing a rare opportunity to shield assets.

Are there other options?

Given the costs of hardship withdrawals, they should be viewed as a last resort. If you can obtain a traditional bank loan, that's probably a better option. If a bank loan isn't possible, find out if your plan allows loans. Not only will you avoid taxes and penalties, but these loans offer competitive interest rates and the interest payments go back into your account.

The downside of a plan loan is that you'll lose the benefits of tax-deferred growth on the amount you borrow. Plus, you'll have to repay the loan within five years. If you don't, or if you leave your job before the loan is repaid, the balance may be treated as a distribution that's subject to taxes and penalties. ■

Cash is king

The role this often-derided asset plays in your portfolio

Many investors shy away from cash investments, such as Treasury bills, money market funds, and savings accounts. Given their modest returns in recent years, that's not surprising. But cash plays an integral role in a well-diversified portfolio — particularly as interest rates tick up.

Relative stability

For starters, the low volatility and liquidity of cash investments provides stability in the event of a significant or prolonged market downturn. This is especially important if the length of time before you need to tap your portfolio is relatively short — for example, because you're nearing retirement or need college tuition funds.

Some investors view cash as a drag on their portfolio's overall returns, but the opposite can also be true. When you have a cash cushion, you can allocate funds to riskier investments that possibly offer significant growth potential over the long term. Psychologically, cash makes it easier to stay the course rather than sell these assets in a panic during turbulent times.

Additional benefits

Cash offers other advantages, including:

Lower downside risk. Because cash investments have little downside risk, they help to mitigate a portfolio's overall volatility. In the event of a market downturn, a portfolio with significant cash investments generally declines less than one without such investments.

Diversification. Cash offers diversity, which can be critical to a healthy investment portfolio. Different asset classes (for example, stocks, bonds and real estate) tend not to move in tandem with each other. Cash investments are good diversifiers because they typically have relatively low correlations with other types of assets.

Inflation protection. Keeping cash under your mattress is usually a bad idea because its value erodes over time as inflation drains its purchasing power. Cash investments, however, earn interest and, because of their very short durations, their interest rates tend to change quickly as market rates and inflation shift.

Insurance. Certain cash investments, such as deposit accounts and CDs, enjoy the added protection of FDIC insurance on balances up to $250,000.

Magic number

How much of your portfolio should be invested in cash? There isn't one correct answer to this question because an appropriate cash position is dictated by such factors as your financial situation, time horizon and risk tolerance. But 5% is generally considered the minimum for most diversified portfolios, and 10% to 20% is optimal for some investors. Work with your financial advisor to determine what's right for you. ■