

What Should You Do with an Inheritance?

Will you ever receive a sizable inheritance? You can't plan on it. But if you do get one, you can plan on using it to help achieve some of your key financial goals.

Once you get word of an inheritance, what steps should you take? Above all, don't rush to act. If you are in the midst of the grieving process, it's hard to make good decisions about money. Consequently, you may want to consider "parking" your inheritance temporarily in a liquid vehicle, such as a cash or cash alternative investment. Don't fret if your inheritance isn't really growing much for a few months — you'll have time to put it to work later.

After you've parked your money and some time has passed, you can think about what to do with your inheritance. Here are a few ideas:

- *Get rid of debts.* Use your inheritance to pay off as many debts as you can, especially those consumer loans that are not tax-deductible and that carry high interest rates.

- *Establish an emergency fund.* This fund should contain six to 12 months' worth of living expenses. Without it, you may be forced to dip into your investments to pay for unexpected costs, such as an expensive car repair or a hefty medical bill.

- *Review and adjust your financial strategies.* If your inheritance is large enough, it may be a "game changer" in terms of how you pursue your financial strategies. For example, you may now be able to speed up your timetable toward retirement, if that's what you want. Or you may be able to pay more of your children's college education, thus freeing up more funds for your own retirement savings. In fact, by

investing your inheritance in certain ways, you can influence many desired outcomes that you've identified in your overall financial strategy. Your financial advisor can help you make those moves that are most appropriate for your individual needs.

- *Plan for taxes.* Unless you are "inheriting" your spouse's assets, you may be subject to some type of taxes when you receive an inheritance. Some types of inheritance, such as the proceeds from a life insurance policy, are tax-free. On the other hand, if you inherit a non-spousal 401(k) plan and are forced to take the money as a lump sum, which is likely because most 401(k) providers would prefer to remove the account from their books, your inheritance will be subject to federal, state and local income taxes. However, thanks to recent tax law changes, as a non-spouse beneficiary you can now transfer an inherited 401(k) to an IRA, which allows you to avoid immediately paying taxes on your inheritance. You'll still be required to take annual withdrawals, which are taxable, but the amount will be based on your life expectancy, so you can spread out your tax burden. To make sure you're making the right moves with an inherited 401(k), consult with your tax advisor.

You may get only one inheritance in your life — so do whatever you can to make the most of it.

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