2 Money Moves to Help You Leave a Legacy

They'll let you save on taxes and you don't have to be a Rockefeller to use them

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Legacy is one of those hundred-dollar words. You might think you can't leave a legacy as part of your estate planning unless you're a Rockefeller or a celebrity. But there are many ways to leave a legacy that don't involve a gaggle of lawyers or complicated trusts.

Legacy planning is an important component to creating a successful financial plan. It's about establishing a strong financial foundation, ensuring a future for the next generations and making certain that your wishes will be carried out after you're gone — whether the assets will be left to family, organizations or charities.

So when you're doing your financial planning, it's key to structure a plan that lets you live the life you want, while guaranteeing that your beneficiaries will ultimately benefit the way you intend.

(**MORE**: 4 Smart Ways to Leave a Legacy)

Employing a particular IRA strategy and funding a 529 college savings plan for your grandchild are two ways to do it. Below are two financial planning questions worth contemplating that are related to these ideas and how they could let your legacy live on:

1. Do you have assets in a traditional IRA that you likely won't deplete in your lifetime?

If so, consider converting your traditional IRA to a Roth IRA. While high income often prevents investors from contributing to a Roth, anyone — regardless of income — can convert a traditional IRA to a Roth IRA. Then, once you've held that converted Roth IRA account for five years and have reached age 59 ½, all distributions are tax-free.

Significantly, there are no required minimum distributions (RMDs) at age 70 ½ with your new Roth the way there are with traditional IRAs. Therefore, you can let the Roth IRA grow tax-deferred throughout your lifetime, instead of having RMDs chip away at what you'll leave to your heirs.

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Although taxes are due on the IRA when you convert to a Roth, there's often a window of opportunity where it makes particular sense to do the conversion.
Let's say you retire at 65 and no longer earn a salary. In the years before you reach age 70 ½ and would need to begin to take RMDs from a traditional IRA, you'll likely be in a lower tax bracket than you were when you were working. That can be the ideal time to convert to a Roth not just because your tax bracket is lower but because it's not as high as it might be once RMDs would begin.

If you worry that you might wind up paying too much in taxes by converting should the new account decline in value, you need to know about what are known as the IRA re-characterization rules.

For example, if you convert a $300,000 traditional IRA to a Roth IRA and the new account's value then falls to $250,000, you'd still owe taxes on the full $300,000 converted. However, the IRS gives you until October 15 of the year following your Roth conversion to re-characterize the new Roth account to a traditional IRA in order to avoid taxes.

(**MORE**: How to Talk With Adult Kids About Inheritances)

Additionally, this re-characterized account can be converted again into a Roth IRA in the next tax year after the initial conversion or 30 days after the re-characterization, whichever is later.

You might want to hedge the market risk of a Roth conversion by converting your traditional IRA into several Roth accounts invested in very different asset classes (some in stocks, some in bonds, for example). Then, you'd re-characterize just the account or accounts with losses.

2. Would you like to help fund your grandchildren's college education?

If so, you can create an education legacy with a 529 college-savings plan.

As you may know, earnings in 529s compound tax-deferred and distributions are tax-free if they're used for qualified educational expenses. What you may not know is that 529s also offer a win/win scenario, letting grandparents help fund their grandkids' college costs while reducing their own estates' size through the plan's special accelerated gifting provision. (This is particularly valuable if the grandparent's estate is already larger than the current $5.43 estate exclusion limit.)

Although the annual limit to avoid owing gift taxes is $14,000 a year per beneficiary ($28,000 if you're married), the 529 college savings plan's special gift tax exemption allows up to five years of contributions in a lump sum of up to $70,000 in one calendar year ($140,000 if you're married). Accordingly, grandparents who gift $140,000 to each of five grandchildren can reduce their estate by $700,000 overnight, with no tax implications.

These sizable contributions can be repeated every five years and 529 accounts can be used for undergraduate or graduate school. If there are leftover dollars after the grandchild has completed his or her education, you can transfer the 529's balance to the grandchild's sibling or even the beneficiary's parent. The account could even eventually flow to the grandchild's own children.

Notably, tax-deferral and tax-free distributions make 529s a great alternative to traditional irrevocable trusts. That's because retained income (the money the trust creator is entitled to receive for a fixed number of years) is taxed to the trust and distributed income is taxed to the beneficiary. In 2015, trusts reach the highest tax bracket (39.6 percent) at just $12,300 of retained investment income.

In addition, 529s have low administrative fees compared to the costs of establishing and administering a trust.

Finally, 529s provide a surprising amount of control for donors. You control how the money is invested and who'll receive the distributions. As the account owner, you can also change beneficiaries and even cash out the 529 (subject to a 10 percent penalty and income tax on the earnings) if you change your mind about assisting your grandchild or need the money for another reason.

A Simpler Way to Leave a Legacy

Of course, keep in mind that creating a legacy can also be as simple as volunteering together as a family for a specific cause. The important thing is to lead with your heart and to plan ahead, so your wishes aren't left to chance later on.