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THE WEALTH ADVISOR

Give Yourself The Greatest Gift: Become Debt Free

If you are nearing retirement, the greatest gift you can give yourself is to become debt free. When you don't owe anything on your credit cards or a mortgage, there's no interest to pay and no monthly payments to drain away dollars that you'd much rather spend on things you really need or want. You'll be amazed at how much extra money this will put at your disposal.

But unless you win the lottery or get a big inheritance, becoming debt free requires careful financial planning, sound investment choices, determination, commitment—and, in most cases, several years to get the job done.

Where do you start? Begin by taking a look at the Big Three:

1. Credit card debt
2. Car payments
3. Home mortgage

Get rid of your plastic debt first. Credit cards tend to carry high interest rates, and using a card to pay for everything from groceries to online purchases can build up a large account balance almost before you know it. Paying down that debt probably will require a systematic plan—for example, budgeting for a particular monthly payment and making it religiously until your balance hits zero. But it also will help if you at least temporarily stop using your credit cards. You can start paying with plastic again once you've reached your goal, but even then, make sure you're able to pay all that you owe each month. Many accounts don't charge interest if you pay the full balance, and you'll avoid rebuilding the debt that you've worked so hard to eliminate.

Next, turn to your car loans. You may not be paying as high an interest rate on these as on your credit card accounts, but the monthly payments still can be substantial. If you adjusted your budget to free up extra money to retire credit card balances, you could now use that cash to accelerate paying off your vehicle loans. Keep your cars as long as the upkeep costs don't become prohibitive, and then consider using savings rather than another loan to buy replacements.

Once vehicle debt is eliminated, you're ready to tackle the big one: your monthly home mortgage payments. Expert opinions differ about whether it's wise to pay off a mortgage as quickly as possible. If inflation rises at a rapid pace, for example, it may be better to keep the mortgage, because you'll make future payments with dollars that have lost some of their value. Also, interest rates on home loans are extremely low now, and you could lock in a rock-bottom rate that will reduce your long-term interest expenses. But if you're planning to stay in your home indefinitely and you like the idea of a debt-free retirement, you could refinance for a shorter loan term or make extra principal payments to pay off the house more quickly.

If you don't plan to stay in your current home, the expense of refinancing may not be warranted, and

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The Federal Reserve's New Guidelines For Raising Interest Rates

The Federal Reserve (Fed) has now changed its position about when to alter its policy on interest rates. In the past, a traditional approach was expressed in targets related to dates in the future. Now the nation's central bank has targeted a 6.5% unemployment rate and a 2.5% inflation rate. Once these new economic marks are met, consideration will be given by the Fed to raise rates.

The Fed previously had said it would keep rates "exceptionally low" until 2015. It appears the Fed now has an economic calendar mandate. If inflation stays below 2.5% or unemployment is greater than 6.5%, the Fed has indicated it will not be compelled to raise rates.

What does this mean to you? Money market accounts and certificates of deposit (CDs), which provide FDIC insurance, have been generating little income in recent years. However, it was an acceptable parking place while the economy healed. With inflation in check and slow, steady growth holding up, the economy in the months ahead may well meet the Fed's benchmarks and interest could start to rise again for the first time in years.

The Fed's new approach to interest rates makes it wise to review investments that you look to for income before interest rates and bond prices change direction. Our advisors can discuss options with you for the fixed income portion of your portfolio.

Best Personal Regards,

Donald N. Hoffman, MS, CPA
President

Avoid These 7 Investment Mistakes

One thing that can be puzzling about stock market investors who have struggled in the past: They make some of the same mistakes over and over. Here are seven prime examples.

1. You try to "time" the stock market. Typically, timing strategies are based on selling stocks when you believe the market has topped out and buying when you think it has hit rock bottom. The problem is that nobody—and we mean NOBODY—has a crystal ball that's foolproof. It's far better to stick with a well-diversified, balanced portfolio based on your personal circumstances.

2. You have zero patience. If you're looking for instant gratification, the stock market will disappoint you more often than not. Just as for the tortoise and the hare, slow and steady usually wins the race, while those who act too swiftly finish behind. Be content to hold some stocks for a long time before you reap rewards.

3. You refuse to recognize reality. All too often, investors operate with blinders on, but the cold hard facts can't be ignored. If you have a favorite stock you were convinced would turn a profit and it simply hasn't worked out, don't throw good money after bad. Dump the losers and hold on to the winners without allowing emotion to rule the day.

4. You put all of your eggs into one basket. No matter what the projections are for any particular stock, sector or asset type, it's not smart to bet your entire wealth on its performance. Diversification is a key element of a sensible plan for virtually every investor. It's all about balancing the search for reward with the need to reduce risk. Although there's less chance you'll make a killing if you diversify, you reduce your exposure to a catastrophe.

5. You overemphasize past performance. It may be boilerplate language in investment prospectuses and related materials, but it's also true: "Past performance is not necessarily indicative of future results." Don't build your portfolio around particular stocks just because they've been profitable without evaluating their current and future prospects.

6. You ignore the impact of taxes. It only makes sense to consider the tax ramifications of your investment decisions—especially now, with investment and income tax rates set to rise in 2013 and the arrival of a new 3.8% Medicare surtax for high-income investors. But it also can be a mistake to let taxes drive your decisions. Weigh all of the relevant economic factors when you buy or sell stocks.

7. You don't have a plan. Many investors take a hit-or-miss approach to their portfolio. They buy and sell on whims without coordinating their activities. But you're more likely to be successful if you develop an overall plan that is suitable for your situation. Having a strategy and having the discipline to stick with it is the hallmark of successful investing. We would be glad to provide whatever assistance you need. ●

Be A College Savings Know-It-All

Now that the kids are back in school, you can take a deep breath and relax—or maybe not. There's little financial rest for the weary if you plan on footing the bill for a child's future higher education, including college and perhaps graduate school. And if you have more than one child, that only multiplies your savings problems.

Fortunately, there are several proven methods for setting aside funds to help pay for a child's college education. You also may be eligible for certain tax breaks when your child finally attends school, although some tax advantages are reduced or eliminated for high-income families. And finally, your child might qualify for other relief that can defray part of college costs.

How much do you know about the potential benefits and pitfalls of education saving? Use this brief quiz to test your knowledge:

1. To qualify for federal need-based college aid, a student:

a) Must have a high school diploma or General Education Development (GED) certificate.
b) Must be enrolled at an accredited university.
c) Cannot have any other outstanding loans.
d) Cannot be your dependent on your tax return.

2. When a custodial account is established under the Uniform Gifts (or Transfer) to Minors Act:

a) Income is taxed to the trust.
b) Income is taxed to the child.
c) Income is taxed to the parents.
d) Income is tax-free.

3. A "prepaid tuition plan" is a kind of:

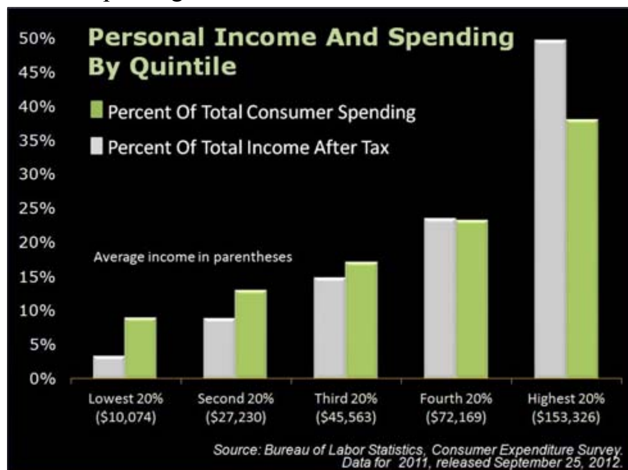
a) Minor's trust.
b) Section 529 account.
c) Custodial account.
d) Coverdell Education Savings Account (CESA).

4. The maximum contribution to a

Top Income-Earners Driving U.S. Growth

Have you been surprised by the slow but steady growth in the U.S. economy over of the last three years and the accompanying doubling in U.S. stock prices in major indexes of the broad stock market? The explanation for these two very positive economic developments may lie in the distribution of income and spending in America, specifically, in their skew toward wealthier individuals. To be clear, it's not the top 1% of wealthiest Americans driving the recovery but the top two income quintiles, the middle class — the top 40%.

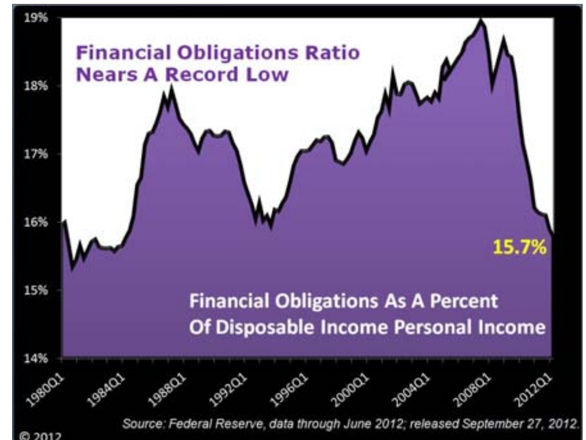
The top two income quintiles account for 61% of total spending in the U.S. economy, according to statistics released in September 2012 by the U.S. Bureau of Economic Analysis. The bottom two quintiles account for just 22% of total spending.



The top 40% of income earners in the U.S are in good enough financial condition to spend at a level sufficient to fuel slow growth, and recent economic reports indicate that this is likely to continue. Consider the following:

Auto Sales are recovering from the dismal period in 2008 and 2009. Because car sales collapsed during the recession, rising demand for new cars is likely to continue. "Cars have a limited useful life," says Fritz Meyer, an independent economist, "and the age of the fleet should propel new sales in the months ahead."

Housing Starts have rebounded strongly since the recession. The U.S. population increases by about three million a year, according to the U.S. Census Bureau. As a result, the nation needs about 1.5 million housing starts annually, Meyer says. In the years leading up to the recession — the housing bubble of 2005 and 2006 — housing starts soared to nearly two million. After the bubble burst and the recession took hold, housing starts plunged in 2009 to a low of about 400,000 annually. Since then, however, a recovery has pushed the rate to about 700,000 housing starts. Mortgage Bankers Association forecasts, along with the long-term population growth trend, support the case for a continued recovery in housing.



Household Balance Sheets are about as strong as ever. The Federal Reserve's financial obligation ratio, which measures consumers' fixed expenses compared to disposable income, has fully recovered since the recession. At 16%, households have 84% of after-tax income with which to make purchases.

"Consumers' ability to cover their monthly 'nut' has seldom been better," according to Meyer. "As incomes have recovered, household debt has been reduced and interest rates remain low."

The financial obligations ratio consists of estimated required payments on outstanding mortgage and consumer debt plus automobile lease payments, rental payments on tenant-occupied property, homeowners' insurance and property tax payments divided by disposable personal income.

The data on the top two income quintiles does not address whether wealth in America is more concentrated. But it does debunk the myth that the top 1% controls the American economy. It also shows, unfortunately, that individuals in the lowest income quintile are finding it difficult to meet expenses. Still, it is comforting to know that the nation's economy and the rise in corporate earnings behind the stock market's three-year rebound are driven by a broad demographic group, and their ability to continue to fuel a slow-growth recovery appears fundamentally sound. ●

Section 529 account:

a) Is limited by state law.
b) Is determined by the cost of each school.
c) Is determined by family size.
d) Is limited by your "modified adjusted gross income" (MAGI).

5. Distributions from a Section 529 plan are:

a) Allowed only after a child reaches age 18.
b) Terminated once a child reaches age 24.
c) Taxable if made directly to the school.
d) Tax-free if used to pay for qualified expenses.

6. A Section 2503(c) trust often is used to:

a) Avoid state limits on financial aid.
b) Avoid extra tax on a child's investment income.
c) Make tax-free distributions of earnings.
d) Establish a remainder for charity.

7. The current interest rate on student loans for college is:

a) 0%.
b) 1.7%.
c) 3.4%.
d) 6.8%.

8. The current maximum American Opportunity Tax Credit (AOTC) is:

a) $1,000.
b) $1,800.
c) $2,000.
d) $2,500.

Answers: 1-a; 2-b; 3-b; 4-a; 5-d; 6-b; 7-c; 8-d

Will Your Retirement Assets Last?

If you've been scrimping and saving for retirement, you may be hoping to relax when that red letter day finally arrives. But recent developments—such as rock-bottom interest rates on fixed investments, the threat of higher taxes, and economic uncertainty—might give you pause. Could you outlive your assets in retirement?

Perhaps. According to a study by the Employee Benefit Research Institute, about 44% of those born between 1948 and 1978—encompassing most Baby Boomers and those in Generation X—haven't adequately prepared for retirement. Here are six steps to protect you:

1. Set aside funds for fixed expenses. Consider how much of your retirement money will go for necessities such as food and housing, transportation, health care, and utility bills. Then try to squirrel away enough in safe but liquid assets to pay those costs for three to five years. If you have that kind of cushion, you won't have to cash out of your other investments during a downturn.

2. Live long and prosper. Medical advances and other trends are helping people live longer than they did just a generation ago, and you'll need to plan accordingly. One possible hedge is to acquire long-term care insurance to cover at least part of the cost of an extended stay in a nursing home. But these policies vary, so proceed with caution. Another idea is to purchase an annuity that can provide steady income through retirement.

3. Don't be overly conservative. Naturally, retirement isn't the time to speculate wildly in the stock market, but relying too much on more conservative investments such as bonds can be detrimental, too. Retirees looking for increased yield may opt for long-term bond funds, but be careful about locking into an investment that could backfire if interest rates start to rise. Consider intermediate bond funds to complement your portfolio.

4. Remember the "i" word. Although inflation hasn't reared its ugly head in recent years, most financial analysts say it's only a question of when, not if, it will return in a big way. Take inflation projections into account when figuring out how much you'll need to sustain you through retirement.

5. Diversify your portfolio. Stock market volatility can be a nightmare for retirees living on fixed incomes. To keep your portfolio on a steadier course, follow the basic investment principle of diversification. And because overcompensating with ultraconservative investments may do more harm than good, seek alternatives that match up well with fixed-income investments and equities.

6. Reduce the tax bite. Although tax planning is especially difficult now, learn to adapt to changing rules and conditions. For instance, it may be sensible to convert savings from a traditional IRA to a Roth to secure future tax-free payouts. ●

Give Yourself Greatest Gift

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depending on how much equity you've built up, you may be able to eliminate your mortgage by downsizing to a less expensive home. Moving away from an area with high housing costs could make a big difference, and you might realize enough on the sale of your current home to retire the mortgage and pay cash for your next property. And though depressed values in many areas mean you may not get top dollar for your current home, you'll likely pay less for the new one than you would during boom times for real estate.

If you take this approach, and if you've lived in your home for quite a while, it could make sense to make targeted renovations to prepare for a sale. You'll almost certainly want to do some exterior and interior painting and make other cosmetic improvements that will show off the house to its best advantage. Undertaking larger improvements—putting in a new kitchen or bathrooms, for example—may be less likely to pay off immediately, though that can depend on your local market.

In any case, you'll need to choose your contractors and designers with great care. That's especially true in retirement-heavy states such as Florida, Texas, Arizona, Nevada, and California, where homeowners sometimes have had to contend with fly-by-night outfits that do substandard work or leave projects undone.

To avoid problems, get multiple estimates for the work you're doing and interview each candidate carefully. Talk with other homeowners who've used the contractors' services and take a look at the finished projects if you can. All of this takes time, but it will be well worth it if you find someone who does good work at a competitive price.

Eliminating all of your debt could take several years, so the sooner you get started, the more likely you'll achieve your goal before you retire. Good luck! ●

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