

For Clients and Friends of Financial Connections

This was a busy summer for Jill and Brian.

- ◆ Jill took an adventure cruise to Iceland and Greenland
- ◆ Brian and Jill conducted a financial planning and cash management session for the Financial Planning Association's pro bono day for executive directors of non-profit organizations
- ◆ Both attended the National Association of Personal Financial Advisors' West Region conference in Portland
- ◆ We hired Kimberly Wohler as our assistant
- ◆ Brian bought a home in San Francisco

**Quarterly Newsletter,
3rd Quarter 2006,
10/16/2006**

Your third quarter reports are enclosed. Please give us a call if you'd like to get together to review your portfolios or let us know about any change in your financial life.

Stock Market and Indexes

The recent headlines state the Dow Jones Industrial Average (DJIA) reached new highs in early October. The previous high occurred *six years ago*. What do the headlines ignore?

The Dow tracks only 30 stocks—hardly “the market.” No one knows why this is the index always quoted, other than the fact that it was the first prominent stock index.

The S&P 500 covers the largest stocks and seems more representative. It is still 12.5% off its March 2000 high. The technology-slanted NASDAQ is still about 55% below its peak.

All the above numbers exclude the returns earned from dividends. If journalists ever quoted the numbers including dividends, the results would show:

DJIA—reached a high in November 2004; current dividend yield is 2.2%

S&P 500—down 2.2% off its March 2000 high; current dividend yield is 1.8%

NASDAQ—very few dividends to help; current dividend yield is 0.8%

Dividends

As you can see from the above information, dividends take an important role in enhancing returns. We expected an upswing in companies paying or increasing dividends after the tax rate declined to 15% for qualified dividends in 2003. The trend did start to increase but declined as of September 2006.

Example

To keep the numbers simple, assume a 10% return.

In 1926, dividends accounted for 41% of the total return of the S&P 500. Currently, 1.8% or 18% of the return for the S&P 500 is from dividends. That means the stock price has to increase 8.2%—considerably above historical returns.

Part of our investment strategy is to look for mutual funds that emphasize dividends. Our expectation is that these mutual funds will be less dependent on stock prices to provide a return and, we hope, lower volatility.

HELPING YOUR HEIRS

It is an unfortunate reality for us at Financial Connections that some of our clients are in failing health. We think the following “tips” from Deborah Levenson, a fee-only financial planner in Newton, MA, offer something we all need to consider.

- ✓ Make sure your trust and will are updated to reflect who you want as successor trustee/executor. If your children are under 18, make sure you still want the designated guardians. Also check your advance directive and durable power of attorneys.
- ✓ Create a file or notebook with information heirs might need. Samples of what you might include are:
 - ◆ Net worth statement (lists all assets and debt)
 - ◆ Contact list of appropriate people
 - ◆ Last wishes
 - ◆ List of valuables
 - ◆ Key to documents' location(s)
- ✓ Check beneficiary designations of insurance policies, retirement plans, etc. Once we set up an account, we tend to forget to update them—yet children grow up, and we may have grandchildren, and some may divorce.
- ✓ Do not keep original stocks and bonds in a home or safe deposit box. Deposit these documents into your account (we don't charge for “holding” these securities in your account). This change helps ensure that heirs won't overlook assets when settling the estate.
- ✓ Make sure there are sufficient liquid assets to settle the estate. Monthly bills still need to be paid while an estate is being settled. You can put aside money in a money market or have an account that is payable-on-death to the successor trustee/executor
- ✓ Write an ethical will or family letter. This document can discuss family history, share values, explain estate decisions, or talk about feelings to those who remain behind. Some helpful advice can be found at:
 - ◆ www.ethicalwill.com
 - ◆ www.personalhistorians.org

Communicate with your family. It is recommended that at least every 5 years or if you alter your estate plan, you meet with successor trustees/executors and primary heirs to bring them up-to-date. Thus you will eliminate the element of surprise later.

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NEW TREND FOR RELATIVES PROVIDING CAREGIVING

Not uncommonly, a daughter or daughter-in-law is the one who takes care of an older parent. A new trend is called a personal-service or personal-care agreement between the caregiver and the employer.

The *Wall Street Journal* on September 7 had the following example:

One woman recently signed a "binding employment contract." Her mother will pay her to provide the following services:

- ◆ Arranging and taking her to doctor appointments
- ◆ Paying her bills
- ◆ Keeping her house

According to the National Alliance for Caregiving and AARP, 21% of the U.S. adult population provides unpaid care to seniors or adults with disabilities. Nearly 60% of these caregivers also have a family and a paying job. Many find it necessary to quit their jobs.

The following Web sites offer more information on caregiving contracts.

- ◆ www.naela.com National Academy of Elder Law Attorneys
- ◆ www.abanet.org/aging American Bar Association Commission on Law and Aging
- ◆ www.thefamilycaregiver.org National Family Caregivers Association
- ◆ www.caregiver.org Family Caregiver Alliance
- ◆ www.caregiving.org National Alliance for Caregiving

CHANGES FOR TRACKING CHARITABLE DEDUCTIONS

Monetary donations: Keep documentation (e.g., cancelled checks, bank statements, receipts, thank-you letters) for any donation you wish to deduct, *regardless of dollar value*.

Donations of items: From now on, you can deduct donated items only if the items are in "good" condition. "Good condition" has not yet been strictly defined. But when you donate the item, you might consider snapping a photo in case the donation's condition is questioned.

Little Known Facts of Interest

ODD AND AMUSING FACTS:

The first buttons were decorative ornaments fixed on clothing. The oldest ones date back to the Indus Valley civilization—before 3,000 B.C.

Buttonholes began to appear in the 13th and 14th centuries. It was a sign of wealth and luxury to have clothes with long rows of buttons with buttonholes.

In the 17th century Puritans condemned the button as sinful: they favored simpler hook-and-eye fasteners.

The most recent innovation, the Velcro button, was designed for people with arthritis.

FINANCIAL FACTS:

Statistics on mutual fund managers from Lipper Inc.:

- ◆ 8% of them have managed their fund since 1995
- ◆ 20% have managed only since 2005 or 2006
- ◆ 50+% of solo fund managers have been on the job only since 2003

**We offer gift certificates for financial planning. If you are interested in giving this unique gift to someone, please give us a call.*

MEDICARE PART B PREMIUMS FOR 2007 ANNOUNCED

In our last newsletter, we provided information on the percentage increase in Medicare Part B premiums based on your adjusted gross income (AGI) from 2005. At the time, the actual dollar increase was not established.

According to the Medicare Web site, the new monthly premium will be \$93.50. The table below reflects the actual dollars based on your AGI.

| You Pay | Single | Married Couple |
|----------|-----------------------|-----------------------|
| \$ 93.50 | Under \$80,000 | Under \$160,000 |
| 106.00 | \$80,000 - \$100,000 | \$160,000 - \$200,000 |
| 124.70 | \$100,000 - \$150,000 | \$200,000 - \$300,000 |
| 143.40 | \$150,000 - 200,000 | \$300,000 - \$400,000 |
| 162.10 | Above \$200,000 | Above \$400,000 |

GOOD NEWS FOR DOMESTIC PARTNERS AND NON-SPOUSAL HEIRS ON RETIREMENT PLANS

Your company or school has a retirement plan; usually a 401(k) or 403(b). If you are married, your heir is usually your spouse. If you are not married, it could be your child, sibling or domestic partner.

Up until now, only a spouse could take this inheritance and roll it over to an IRA. The advantages of rolling the money into an IRA are:

- ◆ Distributions that stretch over the life expectancy of the spouse. While a small amount might have to be withdrawn annually, the remainder can continue to grow tax deferred
- ◆ Because the minimum withdrawal amount is usually small, the income tax paid on the withdrawal is smaller

Non-spouses must withdraw the entire amount as a lump sum over 5 years or fewer—thus it is subject to a large income tax bill and has no opportunity to grow tax-deferred over the lifetime of the heir.

Effective 2007, the rules will treat spouses and non-spouses the same. For instance, a domestic partner will be able to rollover the company retirement plan to an IRA and have the same stretch-out provisions as a spouse.

For clients who opened SEP-IRAs instead of Keogh's or individual 401(k) plans because their domestic partners would not receive the stretch-out provisions, we can now change your plan in 2007 to maximize your contribution opportunity without penalizing the partner.

Hardship Distribution

Under current rules, a spouse or dependent could withdraw from an employee's 401(k)/403(b) plan for medical or financial emergencies. Non-spousal beneficiaries could not.

Effective 2007, this provision changes as well. It will allow domestic partners or other non-spouse beneficiaries to withdraw these funds for certain medical or financial emergencies.

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