John Fiege, CFP®

CERTIFIED FINANCIAL PLANNER™

Objective Advice to Help You Reach Your Goals & Find Peace of Mind

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Greetings,

We hope that you had a fantastic summer**.**

We recently received a fraudulent e-mail purporting to be from the Virginia Credit Union. While it appeared legitimate, we realized it was a phishing scam when it asked for an account number. Remember that the financial institutions you deal with will NOT ask you for social security numbers or account numbers by e-mail. As a rule of thumb, we recommend that you never use e-mail to communicate important numbers to anyone.

Housing Market and Credit Crunch – Delinquent loans and foreclosures of "bad" mortgages, mostly in the subprime market, are causing thousands of people to lose their homes. And there are too many vacant homes, causing existing homes in many areas of the country to lose value. The Eastern Shore has been hit fairly hard. This unhappy scenario may last through 2008 and possibly well into 2009. How will this affect other areas of the economy, such as retail sales? The problems with the housing market and sub prime loans are complicated enough that no one is really sure what the extent of the fallout will be. This may be an opportunity to buy real estate and hard-hit mutual funds at a "low" price, but stay within your asset allocation model.

Fed Rate Cut - The Federal Reserve cut a key rate by half a percentage point last week and the stock market cheered with a large rally. For those of you holding Adjustable Rate Mortgages (ARM's), home equity lines and credit card balances this is probably good news, as rates tied to the prime rate have mostly come down.

Long-term fixed rates may have been better choices for people who could only afford more loaned dollars by going to variable rate instruments which lower costs early on but can seriously impact payments down the road. Choosing the right loan for you depends on many factors; adjustable rates make good planning sense in a reasonable number of circumstances.

The key point to remember now is that rates are very low on a historical scale, and have much more room to go up than to go down. Don't delay locking in a good rate now to try to gain a fraction of a percent lower rate. Long-term loan rates may go up in the not-too-distant future, and very large (jumbo) loans may be much more difficult to obtain than they have in recent years, even for people with good credit scores.

Financial writer Suze Orman recommends putting down at least 10% on a mortgage loan, though 20% is best to avoid private mortgage insurance (PMI). If you need PMI, she recommends paying for it upfront to save money over the lifetime of the loan.

As always, keep money you will need in the next three to five years in liquid investments and not in the stock market. Stay diversified and rebalance periodically.

Higher oil prices are here again, even without major damage from hurricanes (so far). Good for most energy stockholders, bad for consumers. If you use oil to heat your home, plan on budgeting 10% – 20% more than you did last year given the same temperatures, usage and energy efficiency. Natural gas (propane) cost projections are mixed, but be prepared for increases there as well. If you are invested in energy stocks, there may be room for continued growth as demand increases internationally.

Online Banking – Most local banks encourage online banking now, and we recommend you investigate it for both convenience and cost savings if you're comfortable with computers. You can pay bills, transfer funds, and much more without waiting in line.

Online savings banks - ING Direct, HSBC Direct, Emigrant Direct, et al. – are still generally able to pay better interest rates than branch banks. However, local banks are now competing better, especially for loyal customers. Much of your savings may be able to earn 2.5-5% per year if you ask your bank for the best savings and checking accounts. The very best accounts pay interest comparable to that paid by short-term CDs.

If you don't keep all your savings locally, we strongly suggest keeping a comfortable level of emergency funds in local banks for quick access.

Have Children? - How much money are you saving for your children's education and future? How much are you spending on dining out? An article in the August 2007 *Investment Advisor* Magazine states: ". . . 58% of parents surveyed spent more on dining out in a given year than they saved for their kids' education, according to the Alliance Bernstein [Investments] research."

College Savings Vs. Retirement Savings - On this topic, the experts are unanimous! Retirement savings must take priority over college savings. Borrowing is not an option in retirement!

Health and Education Exclusion Trust (HEET) – Designed for the wealthy (suggested net worth $10 million), HEET's are a way to pay tuition for any level of education for one generation or more. To avoid a generation-skipping transfer tax, you must include two features in the HEET. First, payments from the trust must go directly to the educational institution (for tuition only) or health care provider. Second, a charity must be the beneficiary of the trust. Some HEET's are set up so that the charity receives the annual income of the trust. If you are thinking about a HEET, you need to contact a good tax attorney. And remember that you will still need to fund a 529 savings account or make some other arrangement for room and board.

Portfolio Building/Reallocating - How many mutual funds or exchange traded funds do you have in your portfolio? Have you been adding money to existing funds for years and/or adding new funds? If so, you may have too many funds that serve similar objectives and still not be diversified sufficiently to get the best risk-to-return profile. You need to do an analysis of your portfolio to see how your objectives are being met and what steps you might need to take. We specialize in this area.

If you are just beginning to build a portfolio, consider a balanced fund or a target retirement fund which invests in both stocks and bonds, and try to put them in a tax beneficial account such as an IRA or an employer plan. The stocks should have large size companies mixed with some middle and small size companies in both the United States and the rest of the world. Later, you can add funds that are more or less aggressive as your risk tolerance allows. We use several low-cost mutual funds that provide an extremely well-diversified, asset-allocated portfolio targeted to your risk tolerance.

Generally speaking, individual stocks are best left to large portfolios. Stocks in small portfolios do not provide diversification and take unnecessarily high risks.

Municipal Bond Market - Virginia is one of 43 states that taxes the interest on the municipal bonds of other states but does not tax interest on its own municipal bonds. Is this practice constitutional? The issue revolves around possible unfair restriction of interstate commerce. In the next few months, the Supreme Court will hear arguments in Commonwealth of Kentucky vs. Davis and come to a decision. If the case goes against Kentucky, the Virginia assemblies will have to decide whether to begin taxing the interest on Virginia bonds or whether to discontinue taxing the interest on bonds of other states.

Survivor Guide - A widow or widower will need at least 10 -15 copies of a death certificate to go to the Social Security Administration, insurance companies, and financial institutions. Retirement accounts need to be handled very carefully to ensure you receive the best tax consequences for all beneficiaries. Other accounts need to be put in the name of the beneficiary. Make sure to notify a spouse's employer (and/or former employer(s)) as soon as possible to secure all benefits to which he or she is entitled. These might include health insurance. Also, there could be a time limit on notification. The Virginia Retirement System, for example, requires notification within 30 days if a spouse wishes to retain health coverage under his/her spouse's policy.

Estate Planning – Common mistakes in estate planning include:

1. Not having an attorney draw up estate documents – dying without a will
2. Not having a living will/health care power of attorney (p.o.a.) and a durable p.o.a.
3. Not having existing estate documents reviewed periodically
4. Putting off naming a guardian or trustee
5. Failing to establish a revocable living trust to avoid probate and provide various controls after death
6. Failing to re-title financial accounts to fund a trust
7. Failing to set up a credit equivalent trust if your estate will exceed $2 million
8. Not sharing your plans with your family – Important!
9. Leaving a hodgepodge of unorganized records or no records at all
10. Failing to change beneficiaries on life insurance policies, annuities, and qualified retirement savings accounts – A will cannot change the beneficiary named on these documents
11. Having too much property in one spouse's name only
12. Forgetting to make plans for pets
13. Not using an Irrevocable Life Insurance Trust (ILIT) to shelter large amounts of life insurance (over $500,000)

We can help you organize, understand and coordinate these efforts. You will need a good estate planning attorney to assist you in working through your wishes and needs and in producing the legal documents necessary to implement them.

Emotional Vs Rational Gift Planning – Current rules allow gifts of $12,000 per individual per year without tax consequences. Mistakes in gifting include:

1. Distributing money when children are too young or not ready
2. Holding on to money too long – until you are disabled, for example
3. Giving too much money and giving up tax savings
4. Not moving money from taxable accounts to qualified accounts
5. Giving unequal amounts to offspring
6. Avoiding good communications with family members

At the office - William Drinnon has left Financial Solutions to work full time with Bay Sys. This is a wonderful opportunity for William, and we wish him well. He and John still work together on a few projects. Due to his departure, Financial Solutions has discontinued providing Quick Books Pro Advisor services. We continue to focus on comprehensive financial planning, investments, and coordination of your plan with other financial professionals to make your life simpler.

If you have any questions, please do not hesitate to call John at 757-787-4693.