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BFAS Money Line

Uneven Recovery

As our economy ever so slowly grows, we fear getting “**Europe disease**”. Europe, at least parts of it, is in worse shape than we are. Unfortunately, they don’t have the federal institutions to quickly and decisively administer the “medicine” that we have.

While Europe has a parliament and a central bank, the 16 member countries have not given these entities the power needed to act unilaterally. Decisions are subject to approval by the 16 individual countries.

If Europe fails to bolster confidence in its ability to respond to financial adversity, the union may split apart. The poorer southern European countries may leave the union and default on their debt rather than face the “depression-like” economy required to meet their obligations within the union.

Although efforts have been made to help Greece, time will tell whether the efforts will be successful. This success or failure will likely impact economic growth in some way across the globe.

Optimists are talking about stock returns in the high single digits this year, pessimists are talking about a double-dip recession starting next year. As usual, one or the other will prove correct with 20/20 hindsight. Those of us without working crystal balls are maintaining fairly conservative portfolios.

Has anyone noticed that **China stopped buying treasury notes back in October?** China is now using its money to invest in oil and other commodities world-wide to support the future needs of its growing economy. And the many predictions of dire consequences such as much higher interest rates? It hasn’t happened yet. However, **observers predict a coming time when bondholders will demand a much higher return for holding treasury bonds in view of our country’s poor and worsening fiscal condition.**

During an election year, both parties will shy away from making the difficult decisions needed to get our country back into fiscal balance. Exhibit 1 is the commission the President initiated with a December (after the election) report date. It’s difficult to believe that the commission will recommend entitlement reform (fastest growing part of the budget) due to the many constituencies who will protest.

On the other hand, raising taxes won’t be popular, but **since 47% of the people**

don't pay taxes, it would be easier to support raising taxes than reducing entitlements. Note: Congress, two months after passing a requirement to "pay-as-you-go" for all future legislation, is expected to pass $200 billion in spending this month under an "emergency" exception to the just-passed bill. Does that sound like fiscal discipline to you?

A trillion dollars a year in excess spending will be difficult to rein in. Are you ready for higher premiums for Medicare? Higher deductibles? Government pay reductions? Reduced cost of living adjustments? It's going to hurt all of us to get back into fiscal balance. **Everyone's ox has got to be gored**.

One of the things I see frequently is **concentrated stock positions**. Either a person has inherited a big position, been awarded stock options or accumulated positions at work. Many times this stock is a solid company, but makes up in excess of **25% of the person's portfolio**.

Such a large position of even the most admired stock is inherently risky. No one knows when some unforeseen event will torpedo the stock's price (Toyota, BP, ENRON, Worldcom, etc.) I **recommend holding no more than 5% of your portfolio in any one stock, no matter how great it is**. Note: the latest Kiplinger magazine (pre-spill) sings the praises of the high dividends (6%) paid by BP. The stock is down 20% since the oil spill.

Small cap stocks continue to beat large cap stocks as is typical coming out of a recession. All categories are up double digits.

One category not listed that has performed surprisingly well is real estate. Housing prices have started showing a pulse, but one wonders what will happen now that the home purchase credit has ended.

Commercial real estate loans look like a looming train wreck. Between 2010 and 2014, about $1.4 trillion in commercial real estate loans will come due. In almost half of those loans, the property is worth less than the loan. Expect hundreds of billions in commercial foreclosures and a **continuation of the trend in bank failures (mostly smaller/regional**).

Asset Class	1 Yr Rtn (04/30/10)
S & P 500	**+ 38.85%**
NASDAQ	**+ 43.32%**
Lg Cap Gwth	**+ 36.48%**
Lg Cap Val	**+ 38.57%**
Mid Cap Gwth	**+ 43.19%**
Mid Cap Val	**+ 49.74%**
Sml Cap Gwth	**+ 45.79%**
Sml Cap Val	**+ 53.50%**
Foreign	**+ 34.43**
Interm Corp Bds	**+ 16.75%**
Foreign Bds	**+ 15.96%**
Commodities (DJ – AIG)	**+ 21.98%**

Odds and Ends

Health Care Insurance – The recently passed health care bill will have far reaching implications for us all. Here are **some highlights of the changes expected this year**:

Prohibits lifetime and annual benefit spending limits (9/23/10)

10% tax on indoor tanning (7/1/10)

Prohibits non-group plans from canceling coverage (9/23/10)

Allows dependents to stay on parent's policies through age 26 (9/23/10)

Require coverage of most preventative services without cost-sharing (9/23/10)

Provide $250 rebate to Medicare beneficiaries in the Part D donut hole

Almost 25% of Medicare users have Medicare Advantage plans. In 2011, the government will reduce what they will pay for these plans, so you will likely see premium increases. Those with individual or group policies will see premium increases as well since the law increases the insurance company's liability: no cap on benefits, no cost sharing for preventative treatments.

Military members with adult dependents under 26 may not be able to add them to their Tricare policies for another year or so due to the need for separate legislation and contract negotiation to take place.

The health care bill also requires large group health insurers to spend 85% of premium dollars on clinical services (80% for individual and small group plans). This only slightly higher than what is happening currently.

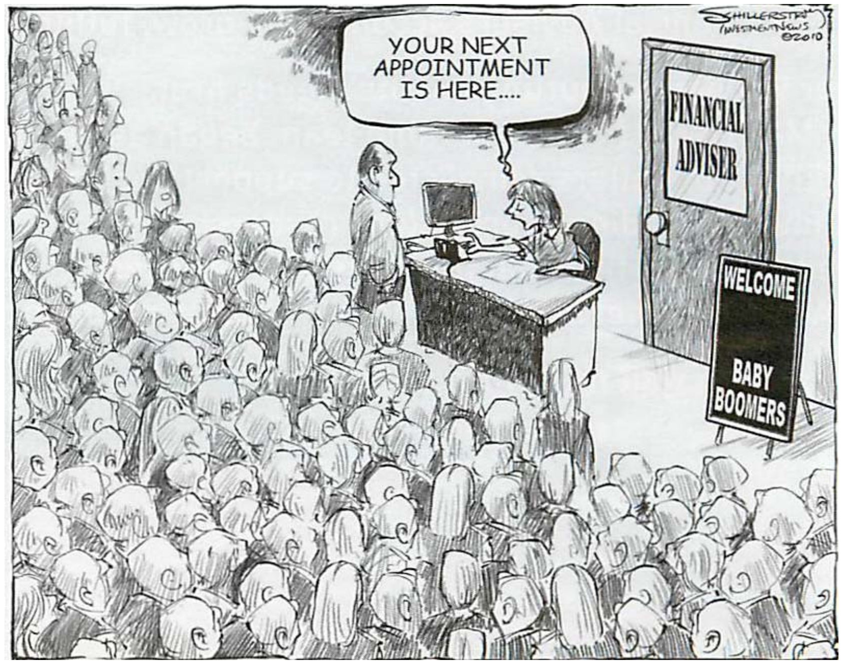
So, does all the other 15% - 20% of premium dollars go to profit? No, it pays for all administrative costs, premium taxes to the states, distribution costs (commissions) to insurance agents who market the insurance and explain the policies to you. **Health insurance company profits actually were slightly more than 2% of revenues last year, although they average about 6%.**

Yet, to hear it in the media, you'd think health insurance companies were the next "robber barons". If they wanted higher profit margins, they should change their business to farm and construction machinery, Tupperware, railroads, Hershey sweets, Yum brand foods, and Yahoo (all of whom had higher profit margins than health insurance).

Thus, the mandated changes will raise health insurance company costs which will inevitably be passed on to you. These higher premiums due to "government mandates" will be then touted as exhibit number 1 in the continuing drumbeat for the government to manage all health care.

Health Care and Taxes – One tax, the 10% tanning tax, has already been mentioned.

The elimination of the business deduction for companies who provide prescription drug coverage to their retirees will cost companies billions. AT&T reported a $1 billion hit alone to their earnings. This deduction was initially started to encourage companies to provide drug coverage for retirees. Now the opposite will happen and retirees will be dependent upon Medicare Part D (and subject to the donut hole).



New Medicare surtax of .9% for couples earning over $250k starting in 2013.

New 3.8% tax on unearned income for couples earning over $250k starting in 2013. This comes along with the expiration of the 15% capital gains tax rate this year, and the capital gains tax increasing to 20% in 2011. Thus, **capital gains taxes will increase 59% over the next three years for couples earning over $250k, 33% for everyone else**.

In 2013, the 7.5% floor on itemized medical deductions rises to 10%

These new taxes will make tax exempt income from municipal bonds and tax free income from Roth IRAs even more valuable.

Health Savings Accounts (HSAs) – one surprise in the new health care bill was that HSAs were allowed to remain. **An HSA is the cash flow vehicle that pairs with a High Deductible Health Plan**. HSAs can be a tax efficient way to pay for health care since you get **a tax deduction for contributions, tax free earnings through investment and tax free withdrawals for qualified medical expenses.**

You can **use the HSA to pay for current medical expenses, including expenses that your insurance may not cover, or save the money for future needs** such as:

Health Insurance or medical expenses if unemployed

Medical expenses after retirement (before Medicare)

Out-of-pocket expenses when covered by Medicare

Long-term care expenses and insurance

You can deduct up to $6,150 of contributions to your plan this year. Employee contributions to their HSAs are not subject to payroll taxes.

The health insurance requires you to pay for all

health care costs until you exhaust the high deductible, then the insurer typically pays 100% of any further costs that year. Some people worry that they will be paying the full cost of all procedures/services and will thus quickly exhaust their HSA each year. Not so! **You will be paying the insurer's negotiated rate for each item, not full rate.** Thus, locally, Optima has an HSA compatible High Deductible Health Plan and you would be paying the Optima negotiated rate.

The $6,150 you place into an account up front can be held at some other custodian than your insurance company. Thus, you can shop around for lower fees, interest rates, etc. You can even invest that money if you have the right custodian and you are not worried about having to sell low to pay medical bills.

I have heard of some people who will fund their account, then use their personal funds for expenses while leaving the health care dollars to grow. At age 65, they can use that money for their retirement tax free.

An HSA paired with High Deductible Health Insurance is a valuable tool. It's portable, has no "use it or lose it" rules and can be a tax free savings vehicle. Check it out!

Funding for Adaptive Equipment

I recently heard about a fund specifically designed to help people purchase adaptive equipment such as:

Wheelchairs/motorized scooters

Assistive technology training

Hearing Aids and Vision Aids

Augmentative Communication Devices

Modified Vehicles and Vehicle Modifications

Home Modifications and Ramps

Recreational Equipment (related directly to a disability)

Prosthetics and Orthotics

The source for all of this is the **NewWell Fund**, www.newwellfund.org, 866-835-5976. Funded by the General Assembly in 1995, the **NewWell Fund provides low interest loans with no down payment and long payment periods to lower payments**.

Who is eligible? Any Virginia resident with a disability or a caregiver of a person of any age with a disability can apply. How much can you borrow? You **can borrow up to $30,000 and beyond with exceptions**.

If you need help with the application, you can contact the Endependence Center, 461-8007.

SBP/SSI

You may recall my previous remarks about the negative effect of the military Survivor Benefit Plan (SBP) on military dependents with disabilities. In most cases, receipt of SBP by the child will eliminate critical government benefits like Supplemental Security Income (SSI) and Medicaid.

Thus, I have **long advised military parents of children with disabilities (1600 nationally) to NOT take SBP for children, and to use the Board for Correction of Military Records (DD Form 149) to cancel it if they have it now (before the military member dies).**

Last year, several Congressmen submitted bills or added amendments to the Defense Department bill to correct this problem by allowing the SBP annuity to be directed to a Special Needs Trust and not affect receipt of SSI/Medicaid. Unfortunately, none of the bills or amendments made it into last year's legislation.

Thanks to an update from Ron Grignol in Richmond, I'm told that **Senator Webb is once again submitting an amendment to the forthcoming Defense Department bill**. His committee is set to bring this up May 25th before a Senate vote on the Defense bill in July. Please contact him at http://webb.senate.gov/contact.cfm or 202-224-4024 to voice your support. If you are in another state, especially those with Senators on the Senate Armed Forces Committee, please contact them as well.

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