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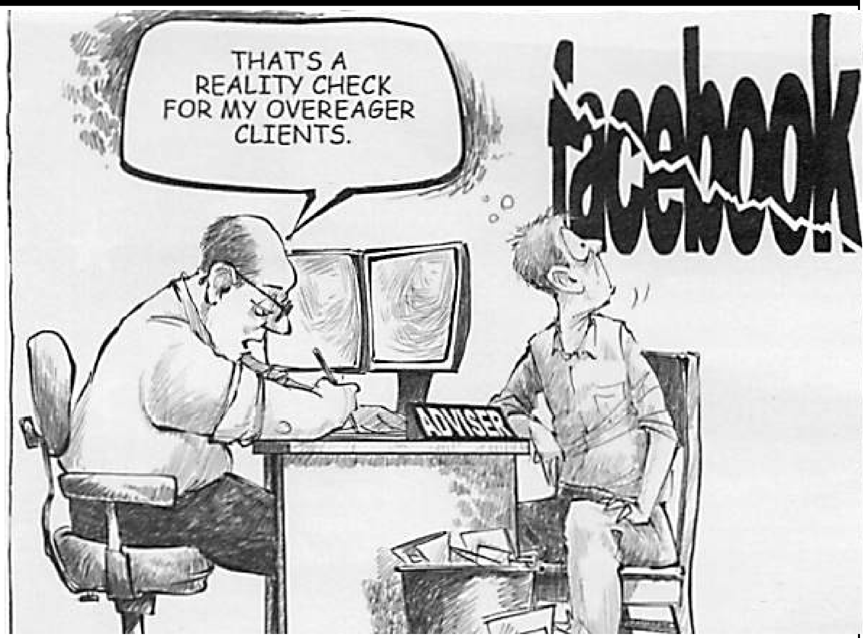
BFAS Money Line

Yo-Yo

When the economy rose in the first quarter and Europe seemed to be under control, the market rose 12.5%. The economy slowed in the second quarter, Spain had debt issues and the market dropped 3%. The economy continues to slow, although the market is rising again this quarter.

With economic growth so slow, debt and tax issues could cause a recession in 2013. Regulatory uncertainty, tax uncertainty, the looming potential US debt default, sequestration of $1 trillion and Taxamageddon in January 2013 would be the major causes. It would take a miracle for Congress to agree to compromises on such major issues during an election season (or during a lame duck session after the election).

In this political season, negative views on the economy could easily be blamed on one political persuasion or another. I read analysis saying the high corporate earnings (historically high) presage another 30% rise in the market. Other analysts point out that corporate earnings don't grow to the sky; they move in cycles and are near a peak. Thus, they say the market should be considered 30% overvalued.



This is not the first time we have faced challenges as a nation. Many times we have overcome challenges to move the economy forward. I am long term optimistic, short term pessimistic.

We continue to be in a Secular Bear Market which started in 2000. While the market has been up and down**, the S & P 500 is only up 18.5% since January 2000**. However, those invested in a **balanced** (mix of stocks and bonds) **portfolio have enjoyed a 60.7% increase (more than three times the market).** This is the third secular bear market in the last 100 years. The most recent was 1966 – 1982 and was followed by the 1982 – 2000 period bull market which averaged 17% annually.

However, we tend to react to what's going on right now and believe it's going to be the same forever. During the last bull market, people predicted it would last forever because "it's different this time" due to technology's giant leaps. Likewise, people predict our present secular bear market will last forever and will destroy retirement savings for millions.

I see **commentary that predicts doom for the dollar and our economy**. I can **trace most of that commentary to spokespersons of companies that sell gold and silver (big conflict of interest!).**

Some people are unable to see the cyclical nature of our economy. They see the present poor economy and are sure the end is coming. They may even leave the country to avoid the predicted doom. They will give up productive investments to purchase gold and silver (which have their own boom and bust cycles – gold has yet to return to its inflation adjusted peak reached in the 1970's).

A secular bear market is an insurance salesman's dream. They can promise 5% guaranteed returns (inside a variable annuity) to people scared by the market's gyrations. Of course, these returns come with much higher costs, limited investment options, restrictions on withdrawals and depend upon insurance companies staying out of bankruptcy in the predicted poor economy.

As noted earlier, balanced portfolios have returned 60% (5% per year) even in this secular bear market. This has been accomplished at much lower cost than variable annuities and better tax consequences (capital gains treatment of many gains, opportunistic tax lost harvesting reducing income taxes, full access to the money, etc.) The downside of the balanced portfolio is that it fluctuates somewhat and is not guaranteed. On the other hand, **when the bull market returns, balanced portfolios should achieve 8% returns, far higher than the insurance company's variable annuity 5% guarantee**.

As you see below, the rise in the dollar has hurt foreign stocks and commodities. Large companies have performed better than mid and small companies:

Asset Class	1 Yr Rtn (07/31/12)
S & P 500	+ 9.13%
NASDAQ	+ 6.64%
Lg Cap Gwth	+ 2.56%
Lg Cap Val	+ 4.96%
Mid Cap Gwth	- 1.79%
Mid Cap Val	+ 0.58%
Sml Cap Gwth	- 2.25%
Sml Cap Val	- 0.53%
Foreign	- 11.45%
Interm Corp Bds	+ 6.08%
Foreign Bds	+ 2.66%
Commodities	- 11.40%

Odds and Ends

Cost of Waiting to Save for College – There is an online calculator now available that easily shows the impact of waiting to save for college. **Kansas' 529 plan website** has the following calculator: https://www.archimedes.com/amcentury/costwait.phtml , which allows you to see the impact.

For example, a parent seeking to fund a full four-year private education for a current eighth grader would have to save $3,426 a month for the next five years, assuming a 5% average return rate. By waiting an additional year to start saving, however, that parent would need to put away $4,395 a month to pay for the same education.

We all know that college is expensive, and getting more so. **This calculator shows you procrastinators out there that overcoming the inertia and starting to save now can have a huge impact**. You only need to input five pieces of information to get charts showing the savings amounts per month or annual lump sum payments.

So, check out the website and see if it motivates you to do something now, rather than later!

Student Loans – To the old saying that the only sure things are death and taxes, you can now add student loans. **Bankruptcy laws were recently changed so that student loans cannot be forgiven during bankruptcy**.

Now the **government is also withholding student loan payments from retirees receiving Social Security checks**! Not only can defaulting on student loans hurt your chances of buying a home and finding work, the government is deducting up to 15% of Social Security payments. About 115,000 people are feeling the bite thus far.

In many cases, it's not even debt for their own education! In the majority of cases borrowers went into debt (PLUS loans) later in life to help pay education costs for their children or other dependents (see article below for more on this).

Bankrolling Adult Children – In today's economy, this is epidemic (**93% of affluent baby boomers**). Many don't keep track of how much they are spending on their adult children. It's the little things that add up each month, not just the help buying a home or car. **Children are often our largest expense, well after they leave home.**

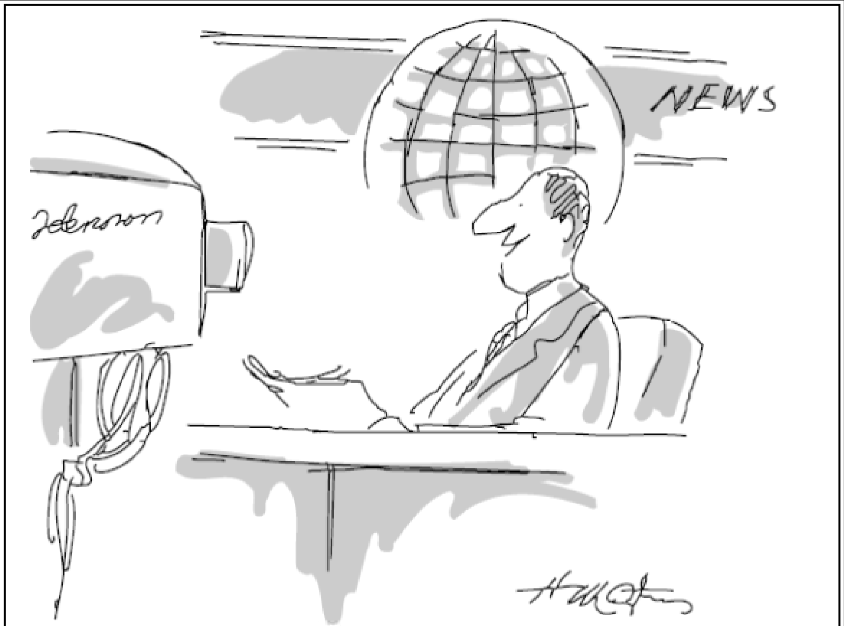
The concern is **how much damage this behavior is causing to future retirement savings**. Does that child realize that you might have to move in with them during retirement? Most of the time the money is coming out of discretionary spending, not retirement accounts, so we don't see the harm that is occuring.

About **71% of baby boomers are helping pay their kid's student loans and 55% have allowed children to move back into their homes and live rent-free. Some 53% have helped them buy a car and nearly half help with car insurance.** At the same time, just 24% are putting money away money for the future down from 44% five years ago.

Consider that Americans spend an average of $235,000 to raise a child to age 18 and then many help with college. Parents aren't just helping children during their 20's and 30's as they establish their careers. Many are having children in their 40's move home after a divorce and needing help getting back on their feet.

Not only does this type of support potentially hurt future retirement, it can have negative consequences (resentment) in families with more than one child. On the other hand, the perceived inequality of support can lead to "matching" contributions to the "non supported" children, further depleting resources.

It's tough to say no, and hard to talk to your kids about being independent. Food for thought.



"... And on Wall Street, the markets generated another exciting day's worth of meaningless white noise."

Long Term Care – There was a recent case in Pennsylvania where **mom needed nursing home care**. She had very limited means; thus the **children applied for Medicaid** support for her. For whatever reason, the Medicaid approval/funding was delayed. The **nursing home sued one of the three children for the cost of caring for mom, and won!**

The son who was sued said he should not be held liable for mom's expenses; however **Pennsylvania law does allow holding children accountable for parental support**. Then, the son appealed saying the nursing home should have sued all three children rather than singling him out. The **judge declared that the nursing home had no obligation to sue all three**. Hence, the son was liable for tens of thousands of dollars in expenses (not including attorney fees).

Could that happen to you? Actually, **similar laws are on the books in many states (including Virginia).** They seem to have been rarely enforced. However, with state budgets reeling from the poor economy, you might see more states acting in a similar manner.

If you look down the road and can see a similar situation arising, you **might consider getting your siblings together to purchase a long term care policy for mom and dad.** It might save you money in the long term!

Taxes – On page one, I used the term, **taxamageddon**. That's a relatively new term referring to the year-end expiration of the Bush tax cuts, $1.2 trillion in automatic spending cuts because of the sequester and expiring payroll tax breaks. The total increase in taxes in 2013 could be $310 billion.

Ben Bernanke, chairman of the Federal Reserve, says "**U.S. fiscal policies are on an**

unsustainable path." Further he says, "**Recovery could be endangered by the confluence of tax increases and spending reductions that will take effect early next year if no legislative action is taken.**"

From a financial planner's perspective, planning in the face of this uncertainty is difficult at best. **If taxes are sure to rise, converting IRA accounts to Roth IRAs would make sense** in many cases. But, not everyone's tax rate will be the same or higher in retirement.

And what if we do the conversion, then Congress miraculously compromises and keeps the current tax rates? In 2010, President Obama agreed to a last minute extension of the tax breaks in late December. Could it happen again; with a lame-duck Congress?

Another major change upcoming is the estate tax. The **current law allows $5.12 million to pass to heirs** without federal estate tax and the **tax rate is 35%** for amounts over that. As of **January 1st, the exemption amount drops to $1 million and the tax rate climbs to 55%.** That would mean many estates now exempt would incur significant taxes!

Should those estates potentially at risk aggressively gift assets to heirs now and take advantage of the higher gift tax exemption? Giving up ownership of assets permanently can save on taxes, but can be hard to do emotionally.

No one wants to be dependent upon their heirs to maintain their standard of living. Can they make the gifts without compromising their standard of living?

Will Congress make a last minute compromise? Will estate taxes be part of a grand compromise? It looks like this may all go down to the last minute. I will be closely following the action and will review each person's individual situation to determine whether Roth Conversions or Estate Gifting is in their best interests.

How Things Work

There are some new rules for trustees of **Special Needs Trusts (SNTs**):

- **the trust may no longer compensate certain family members who provide care to the beneficiary with a disability**
- **the trust may no longer pay for travel costs of relatives to visit the beneficiary**
- **if the trust purchases a house or a car, they must be owned by the beneficiary or the trust.**

Social Security is re-emphasizing that SNTs are for the sole benefit of the person with a disability. In the past, the SNT has been able to pay for a family member to escort the beneficiary on a vacation. This is no longer the case.

If a family member is reimbursed for care of the beneficiary, that family member must now be medically certified, medically trained or approved to provide care.

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There is a new service available for children with disabilities in Hampton Roads. **Mike and Denise Murden have formed Janus Solutions to provide leadership development programs and resources to help teens and young adults with disabilities achieve independence.**

They will be providing **personal coaching** and **workshops** that will feature **guest speakers** and **community service and social opportunities**. They can provide seminars and other resources for parents and guardians of young people with disabilities.

They will be conducting **a pilot 10-week workshop starting in September.** This workshop, with space for 16 individuals, starts with a 45-minute intake session with each participant and their family members or guardians to ensure they accommodate all learning needs and understand each participant's goals for the program.

You can request their free "**Parent's Guide to Independence for Teens and Young Adults with Disabilities**" and receive their free newsletter with both local and national tips and resources.

Contact Mike or Denise at 757-788-1513, info@JanusSolutions.biz, www.JanusSolutions.biz

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