Current Financial Topics

December 2010

JAS Financial Services, LLC
Joseph A. Smith, CPA/ PFS, JD®, AEP
Member
3451 Harrison Street
Evanston, IL 60201
847-328-8011
joe@jasfinancialllc.com
www.jasfinancialllc.com

Our goal has always been to help our clients make wise decisions. Knowing what you need, want and wish is essential to achieving your goals. Successful planning requires an effective relationship with our clients. Understanding our clients' concerns and emotions has a significant impact on the alternatives that should be considered. My years of experience have provided the opportunity to understand where our clients are and what is ahead. Our objective is to bring order to a chaotic world. Progress should be measured periodically. Life events and/or changed goals may require changes to your plan. The choice of action should permit flexibility for the unanticipated. ********************* Wishing you the best for a healthy, happy and prosperous New Year. ******************** Referrals are always appreciated.

************ Joe

In this issue:

Five Hot Topics in 2011

Roth conversions, mortgages, and health-care reform were a few of the most talked about topics in 2010. Here's a look at five topics you're bound to hear about in 2011.

Social Security: saving the system

How to strengthen Social Security has been a political hot potato for many years, but calls for reform are growing louder as the time when program costs will permanently exceed tax revenues draws closer. The most recent annual report from the Social Security Board of Trustees projects that this will occur in 2015 (one year earlier than last year's report predicted) and notes that trust funds will be exhausted in 2037. Social Security is the most common source of income for retirees, and debate over how to save it will rage in 2011.

Microlending: small loans count

Microlending--the practice of extending small loans to individuals and businesses who otherwise could not borrow money--has traditionally targeted entrepreneurs in developing countries. But as the credit crunch prevents many Americans from borrowing money through traditional channels, more are turning to microlending sites and companies to obtain funds. And more investors are offering to make microloans in return for the potential to earn somewhat higher returns than a savings account can offer. Until the economy improves, look for this trend to continue.

Microlending recently got a boost from the Small Business Jobs Act, passed in September, that expanded the Small Business Administration's microlending program. Funding for the program was increased, and business owners may now be able to borrow up to $50,000 (previously, the limit was $35,000) to use for working capital or other needs.

Education: expanding opportunities

Education-related debates will certainly heat up in 2011. The current administration is committed to reforming primary and secondary education and has drawn up a blueprint for overhauling the Elementary and Secondary Education Act. This Act (currently known as No Child Left Behind) is long overdue for reauthorization, and Congress will likely be debating it in 2011.

In addition, much attention is being focused on ways to make college more accessible and affordable. One initiative funded by the Bill and Melinda Gates Foundation awards grants to nonprofit and governmental institutions to develop effective online education opportunities. Currently the focus is on developing online courses and tools that can help more Americans attend college and prepare for careers, while saving students and schools money.

Energy: greener days ahead

"Going green" is a catchphrase that's likely to get even more press in 2011. One important green initiative currently pending in the Senate is the Homestar Act. This Act provides substantial rebates to homeowners who purchase and install energy-saving equipment or goods or who complete whole home retrofits.

Even the lowly lightbulb finally gets a makeover in 2011. The Federal Trade Commission is requiring that lightbulb packages carry labels that estimate yearly energy costs, the bulb's life span and light appearance, and brightness measured in lumens so that consumers can better compare new energy-efficient bulbs.

Wellness: saving lives and money

Look for employers to roll out, or expand, employee wellness programs this year in an effort to promote healthier living and curtail health insurance costs. The Health-Care Reform Act passed last year included funding for new wellness programs established by small employers, and makes it easier for all employers to offer substantial incentives to employees for participating. Also, new health insurance plans and many existing plans (including Medicare) must now fully cover preventive care services such as immunizations and screenings for certain health conditions.

First Milestones Mark Need for Financial Advice

If you're just starting out, you might not give much thought to working with a financial professional. You may associate the process with retirement--a retirement that seems so far off that more immediate concerns take precedence. The fact is, though, a financial professional can prove to be a valuable resource to those just starting out. And, while there's never a bad time to seek professional advice, early life-changing events make it especially important to take stock of your financial situation.

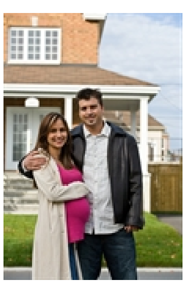
Starting a career

It may seem counterintuitive--when you're starting out, it's often more about future potential and possibilities than focusing on the present. But this is actually the perfect time to begin building a relationship with a financial professional. It's also the perfect time to establish good financial habits, like building an adequate cash reserve, starting to save on a consistent basis, and establishing a good credit history. You may need help implementing a spending plan (aka "budget") that will help you to meet current financial needs and still enable you to make progress toward your future goals.

With each life milestone, a financial professional can help you develop a clear picture of your current financial situation, work with you to articulate and prioritize your financial goals and timelines, and recommend strategies and products that are appropriate for your objectives.

It's not all about the future, though. A financial professional can help you get the most out of your paycheck by working with you to maximize the value of tax-advantaged benefits offered by your employer, including employer-provided health coverage or a qualified retirement plan. In addition, you may need help with issues as common as paying back student loans, or as complicated as understanding employer stock options.

Getting married



You know you need financial help when key words used to solemnize the occasion include "…for richer or poorer…" There's the immediate financial aspects of a wedding (paying for everything), but--more importantly--there's the long-term financial challenges that come when two individuals combine their finances. Like the ghosts of boyfriends and girlfriends past, you each bring your own financial history, attitudes, and habits (both good and bad) to the union.

A financial professional can help you define your goals as a couple. You'll want to come up with a joint spending plan to help you achieve these goals, and decide on the mechanics of day-to-day money management. For example, will you combine your bank accounts or keep them separate? In cases where you and your spouse aren't on the same page, a third party can listen to all concerns, identify underlying issues, and help you find common ground. A professional can also work with you to make sure that you're making the most efficient use of employer benefits, including health insurance and qualified retirement plans, that you have adequate life insurance coverage, and that the investments you choose are appropriate for your goals, time frames, and risk tolerance.

Beginning a family

The period of time following the birth of a child is both exciting and stressful. It's time to completely reevaluate your financial situation, starting with your goals. For example, in addition to saving for your own retirement, it's time to start thinking about saving for your child's college education. Your existing spending plan is likely to be the victim of suddenly decreased income (if there's to be a stay-at-home spouse) or a significant new expenditure (child care). If nothing else, you need to account for the additional ongoing expenses that come with parenthood (e.g., baby formula, food, diapers, clothing).

With children in the equation, having adequate health insurance, life insurance, and disability income insurance takes on new significance, and you may want to work with someone to evaluate your needs, obtain appropriate coverage, and make sure your beneficiary designations reflect your wishes. It's also time to establish an appropriate estate plan--including a will, health-care proxy, and durable power of attorney--or to update an existing estate plan. A financial professional can help walk you through some of the issues involved, and can help you find an attorney if you don't have one already.

Need for advice grows over time

If you're like most people, your financial needs will grow more complex over time. As that happens, your need for financial advice will increase as well. By starting early, you're able to build on a solid financial foundation. With each life milestone, a financial professional can help you develop a clear picture of your current financial situation, work with you to articulate and prioritize your financial goals and timelines, and recommend strategies and products that are appropriate for your objectives.

Don't Want Your Annuity? You May Be Able to Sell It

Are you receiving annuity payments but you'd prefer a single lump-sum payment instead? As appealing as receiving a lump-sum payment might sound, you may be under the impression that you're stuck with those annuity payments and a lump sum is out of the question. Not necessarily. You may be able to exchange your annuity for a lump sum through a secondary market for annuities.

Why own an annuity?

Sometimes, receiving annuity payments is not your choice. For example, you may be getting annuity payments because you were named as a beneficiary of an annuity owned by someone who's deceased. Or, as in most cases, you probably purchased your annuity based on specific financial circumstances and goals. Some of the more common reasons for owning an annuity include:

- The need for a steady income stream for a specified period of time or for the rest of your life
- The appeal of a relatively low-risk investment such as a fixed annuity that may provide a guaranteed rate of return (subject to the claims-paying ability of the annuity issuer)
- The desire for tax advantages associated with deferred annuities, although interest earnings will be subject to income tax when withdrawn

Why a lump sum?

It is not uncommon for circumstances to change during your life, and some of your reasons for having an annuity may no longer apply. If you have a deferred annuity, one from which you have not begun receiving periodic payments, you might be able to cash in the annuity. However, there are some issues to consider. Interest earnings within the annuity will be taxable as income to you in the year you receive them. And, if you're under age 59½, you may face a 10% tax penalty on earnings unless an exception applies. Also, if your deferred annuity hasn't reached maturity, surrender or withdrawal charges may reduce the amount you'll receive.

On the other hand, if you've already started getting periodic payments, your insurance company might allow you to receive a lump sum equal to the present value of the future payments you'd otherwise receive. This is commonly referred to as the commuted cash value. But many companies don't allow this option, meaning once you begin receiving annuity payments, you can't accelerate them or receive a lump sum.

Another option: sell your annuity

A growing market known as the secondary annuity market has emerged which offers annuity owners the opportunity to sell the future annuity payments in exchange for a lump sum. Most annuities are eligible except "life only immediate annuities," where the payout isn't guaranteed to last a fixed period of time, as well as annuities in 401(k) accounts, 403(b) accounts, or IRAs. The amount you may receive from the sale of your annuity is primarily based on the total amount of payments expected to be made, the period of time over which the payments are to be made, the prevailing interest rates at the time of sale, the financial strength of the insurance company, and whether your annuity has a death benefit.

And you can sell the entire annuity or a portion of each annuity payment in exchange for a lump sum while continuing to receive the balance of the payments. For example, let's say you're receiving a monthly annuity payment of $4,000, which is to continue for 20 years. You only want half of each payment, so you sell your right to half of each payment (or $2,000) for a lump sum, while retaining the right to receive the balance of each payment ($2,000). The annuity buyer will receive a total of $480,000 ($2,000 x 240 months) at the end of 20 years. But you won't get the full $480,000 as a lump sum. Since the buyer has to wait to receive payments, the annuity buyer applies a discount rate to the lump sum paid to you (the discount rate varies by annuity buyer, the type of annuity you're selling, the length of time payments will be made, as well as other factors). It basically works the same way whether you sell a part of your annuity or the entire account.

What about taxes?

The gain (or loss) from the sale of your annuity is determined by comparing your cost basis (your investment in the annuity) to the lump sum you received. Any gain is taxed as ordinary income and not as capital gain.

Recently, the Interstate Insurance Product Regulation Commission, consisting of insurance regulators from 35 states, voted to allow insurance companies the discretion to terminate certain benefits, including death benefits, in the event of a change in ownership of an annuity contract. The value of annuities in the secondary market may be diminished if the annuity's death benefit is removed after its sale.

JAS Financial Services, LLC
Joseph A. Smith, CPA/PFS, JD®, AEP
Member
3451 Harrison Street
Evanston, IL 60201
847-328-8011
joe@jasfinancialllc.com
www.jasfinancialllc.com

Ask the Experts

Is buying a condo for my college student a good idea?

When parents estimate the amount of money they'll be spending on dorm rooms and off-campus apartments for the next several years, it's easy to see why many parents like the idea of buying a condo for their college student. But, assuming your child is responsible enough to take care of such a property, whether it makes financial sense to do so depends on several factors.

Recouping costs: The costs of owning the condo, minus any rent paid by roommates, should be less than what you would pay for a dorm or apartment over the same time period. Costs may include a mortgage (including points and fees), property taxes, homeowners insurance, condo dues, and maintenance costs. And if your child plans on having roommates, you may want to add an umbrella liability policy to your homeowners insurance to protect you now that you're a landlord.

Will you come out ahead in the end? The rate of housing appreciation varies by geographic area, so research the location you're targeting. And don't forget to factor in a broker's commission when you sell the property.

The right mortgage: For long-term real estate ownership, it often makes sense to choose the certainty of a fixed-rate mortgage. But for short-term real estate ownership, a three- or five-year adjustable-rate mortgage may make more financial sense because the lower initial interest rate translates into a lower monthly payment. But be aware that if housing prices drop before you can sell the property, you may end up owing more than the house is worth--a situation you want to avoid.

Tax benefits: You may be able to deduct mortgage interest and property taxes on a second property; however, the IRS limits the amount of itemized deductions high-income taxpayers can take. In addition, if rent is collected, rental property rules will apply: rent you receive will be considered income, and you'll be entitled to claim some expenses as business deductions. But second homes and rental property aren't eligible for the $250,000 per person exclusion that you get when you sell your primary residence. To learn more, consult a tax professional.

I plan to buy my child a condo for off-campus college housing. Is this purchase considered a qualified 529 plan expense?

Money withdrawn from a 529 plan to pay the beneficiary's qualified higher education expenses is tax free at the federal level (and typically at the state level too). Unfortunately, the purchase price of your child's condo is not a qualified higher education expense for 529 plans under IRS rules. But a room-and-board allowance may be.

IRS Publication 970, *Tax Benefits for Education,* spells out the rules for counting your child's room-and-board costs as qualified higher education expenses under your 529 plan. (Publication 970 refers to a 529 plan as a "qualified tuition program" or QTP.)

First, the student needs to be enrolled at college at least half-time.

Next, for students who live on campus, the room-and-board allowance figure is equal to the actual amount charged by the college.

For students who live off campus, the amount of room-and-board expenses that you can safely withdraw tax free from your 529 plan is equal to the "allowance" figure that the college determines for off-campus housing.

This room-and-board allowance figure is the one included in the official cost of attendance for your child's school and used for purposes of awarding federal financial aid. If you can't find this figure in the college's literature or website, call the bursar's office to determine the current qualified room-and-board costs for off-campus housing. The allowance for off-campus housing will not be greater than the amount for on-campus housing.

Before you buy your child a condo for college housing, make sure you understand the potential risks involved in such a transaction. Be careful not to overestimate your possible savings or the potential appreciation of the property, especially considering today's real estate market. And don't forget to objectively evaluate your child's ability to responsibly care for the property and act as landlord if roommates will be in the picture.