

JOE LEE'S FINANCIAL NEWS DIGEST

A COMPILATION OF INFORMATION AND IDEAS FOR EFFECTIVE MONEY MANAGEMENT



Moneyline

The Other Rule On Diversification

By Joe Lee

How's your tax diversification? These days, many are taking a fresh look at their risk diversification, but tax diversification is another important aspect of an effective and efficient accumulation strategy.

Here are the basics:

There are just two broad categories of taxation when it comes to saving and investing: Pre-Tax and After-Tax. For many years the prevailing strategy was to focus most of our attention on maximizing pre-tax investments such as 401(k) plans, with the hope of deferring income that would be taxed at a high bracket until retirement, when in a presumably lower bracket.

The problem is fewer and fewer people believe they will actually be in a lower tax bracket later on, and with the way the federal deficit is increasing, higher taxes may indeed be in our future. But even if tax brackets remain at current levels, one way to maximize future net retirement income is to work at accumulating both pre-tax and after-tax assets.

Drawing just half of your retirement income from the pre-tax side could land you in a lower bracket, while drawing the other half from after-tax assets that may be able to provide tax-free or partially tax-free retirement income.

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Financial Front

NEWS BRIEFS AND HIGHLIGHTS FROM THE FINANCIAL WORLD

Lump-sum pension payouts may not be available to all holders of defined-benefit plans. A new law requires employers to tell their workers if a defined-benefit plan is fully funded; that is, if it has all the money needed to pay all its obligations. Fully funded plans may offer retirees either a series of payments or a lump-sum payout, but plans that do not have enough money to pay in full at least 80% of employees are allowed to pay only 50% of a retiree's pension in a lump sum. And plans that do not have enough money to pay at least 60% of employees do not have to make any lump-sum payments at all. Ask your defined-benefit plan's manager for details on the financial health of your company's plan.

State-run prepaid tuition plans may be a better deal than 529 plans, which have suffered severely in the market downturn. With a prepaid plan, you pay the cost of tuition today, in a lump sum or monthly installments, and you are guaranteed that your child's tuition will be covered at your state college or university. Prepaid plans protect against tuition increases—but they require that your child go to a state school.

Looking for a lost savings bond? Go to TreasuryDirect.gov and download Form 1048, *Claim for Lost, Stolen or Destroyed US Savings Bonds*. Fill in the following information: the bond owner's name, address and Social Security number; approximate issue date; and serial number, if available. Once the form is certified at a bank, mail to the Department of Treasury (the address can be found on the form). With the serial number, the

process will take three to four weeks; without it, you may be waiting months to get a duplicate bond.

Don't depend on 4% annual withdrawals to get you through retirement. This common approach says to withdraw up to 4% of your portfolio in the first year of retirement and then increase the amount for inflation annually. But if you do this, you could run out of money. *Example:* If you have only a 2% to 3% annual return for the first five years of retirement, this plan means that you have a 64% chance of running out of money in less than three decades.

Penalty rates on credit cards are heading sharply higher. The Discover Card recently raised its default rate, which can be triggered by missing a payment or going over your credit limit, to a 31% annual percentage rate (APR). Bank of America raised default rates for some customers to 30%. Credit card issuers are very skittish about risk and are quick to raise rates for consumers exhibiting any signs of financial distress. *Self-defense:* Make all of your payments on time.

Wit & Wisdom

"My riches consist not in the extent of my possessions, but in the fewness of my wants."

— J. Brotherton

Stimulus Scams Are Flourishing On The Web

By Kathy Kristof, Tribune Media Services

The ink didn't have time to dry on the American Recovery and Reinvestment Act before the con artists started crawling out on the Web.

"Learn exactly how I got this check for \$36,383!" proclaims one site that promises to help you "get your share" of payments from the stimulus law.

Another promises a helpful guide: "How to get your free stimulus grant before it's too late!"

There are copious government grants to be had, but these sites are scams, said Eileen Harrington, acting director of the Bureau of Consumer Protection at the Federal Trade Commission. Worse, once one site is squashed, another pops out like a cockroach.

Harrington held a recent news conference to expose two sites that the FTC had investigated in the weeks after the act's passage. Neither site could be found a week later. But search for the now-missing sites and you'll find dozens more.

In a brilliant example of misinformation, one outfit purports to be a scam-busting site, investigating the promises of government-grant Web sites and rating them with up to five stars. It warns users to "avoid government-grant information scams." However, the site's "top recommendations" lead you to sites that do exactly what Harrington warned about.

What's the game?

Each of the sites proclaims that you can get information on hundreds of

government grants, worth tens of thousands of dollars, for nominal shipping and handling fees. The disclosed fees range from \$1 to \$3. The sites have you pay that pittance with a credit card.

But in reality, they're planning to charge you much, much more -- and to be clear,

"Grants to help you pay off your credit cards? Get real."

most of these grants really aren't available to average consumers anyway. So in most cases, you're going to wind up paying a lot of money to these Web sites while probably not getting much of anything in return.

The catch is buried in the "terms and conditions," which coincidentally are hard to find.

The fact that you're accepting these terms -- but not the terms themselves -- will pop up when you feed in your credit card number.

You have to hunt to find actual terms (that you've just accepted by being gullible enough to give your credit information). They're usually way at the bottom of the page in small type.

How much will you be charged? That depends on how quickly you discover the hidden fees and address them. Most offer a few days' "free trial," after which charges start to accrue.

One of the sites the FTC uncovered billed users a one-time fee of \$99, plus almost \$50 a month for an "online resource center." It also automatically signed up users for a second membership that cost \$30 a month, Harrington said. If you failed to follow complex cancellation procedures, you would pay more than \$1,000 over the course of a year.

Among the sites still operating, the charges ranged from \$70 to more than \$100 a month.

One site, for example, said in its terms and conditions that users are charged

\$74.95 a month for access to a "help center" after a seven-day free trial. "No refunds will be given for failure to use the requested and/or provided services," it said. The company's terms revealed that after 14 days a second "membership" kicks in, to a "mentoring center," which costs \$29.95 more a month.

Another top recommendation of the supposed scam-busting site charges \$39.95 a month (after seven days "free") and signs up users for two other services that total \$19 a month. The site also warns that the charges are nonrefundable.

You'd also read in the terms -- if you managed to find them -- that both of the sites guarantee nothing and users are cautioned to use the sites "at their own risk."

Aside from the hidden charges, Harrington said the biggest problem with the sites is that they mislead people into thinking that they're going to get grants to pay off their credit cards, mortgages or buy Christmas presents. Nothing could be further from the truth.

You can find real government grants at www.grants.gov. And you can see how government stimulus funds are being spent at www.recovery.gov.

But the average consumer wouldn't qualify for most of the government grants available. For example, the stimulus act created grants for those willing and able to recruit, train and manage AmeriCorps volunteers. It also set aside \$20 million for rural business development. But to get one of these grants, you'd need to be an existing government contractor, state or municipal agency or a nonprofit.

There are also grants for scientific research, clean-fuel technology and for those with ideas on how to make the criminal justice system more efficient.

Grants to help you pay off your credit cards? Get real.

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Long-Term Returns Not Always Consistent Year To Year

By Humberto Cruz, Tribune Media Services

You've heard it many times: Stocks are the best-performing investments over the long term.

But just how long is long term?

Financial advisers typically recommend investing in stocks the money we won't need for at least 10 years. But 10 years - or even 20 - sometimes is not long enough.

By my calculations, if you put \$10,000 in stocks on Jan. 1, 1999, and matched the return of the Standard and Poor's 500 Index, you ended up with just \$8,705 on Dec. 31, 2008, even after counting reinvested dividends.

That's the equivalent of an average compounded loss of almost 1.4 percent a year - the worst 10-calendar-year stretch ever for stocks as measured by the S&P 500 and predecessor indexes of large-cap U.S. stocks. The previous worst was a nearly 0.9 percent average annual loss in 1929-1938, during the Great Depression.

And yet, as late as the end of 2006, \$10,000 invested in the S&P 500 Index 10 years earlier would have grown to \$23,011 - an average annual compounded gain of about 8.7 percent.

Conclusion: Ten-year market returns, as reassuring as they seem when they are good, range all over the map and depend heavily on which period we are measuring.

"The returns from any particular period are an unreliable anchor for long-term return expectations," said chartered financial analysts Francis Kinniry Jr. and Christopher Philips in an article published by Vanguard's Institutional Investor Group. (In its best 10-year period, the S&P 500 chalked up average annual compounded gains of about 20 percent. Over 20 years, returns have ranged from average gains of about 18 percent to just 3.1 percent).

Yet, many investors mistakenly believe that "average" stock market

returns are the returns they can expect consistently. When they don't, many abandon stocks and miss out on strong gains that often follow down periods.

The average historical long-term

"The returns from any particular period are an unreliable anchor for long-term return expectations."

return for the S&P 500 Index is about 10 percent a year. But the index rarely comes close to returning 10 percent any particular year.

In the past 40 years, returns have ranged from a gain of 37.5 percent in 1995 to last year's 37 percent loss. Only twice - gains of 10 percent in 1993 and 11 percent in 2004 - did gains range between 8 and 14 percent.

I've run into many investors, however, who believed they would be averaging 10 percent a year or close to it all the time, or at least every few years.

My fear is that many may now shun stocks forever. The percentage of American households investing in stocks already had fallen from a peak of 57 percent in 2001 to 47 percent early last year, according to a study in February and March 2008 by the Investment Company Institute and the Securities Industry and Financial Markets Association, both industry groups. The bear market that lasted until 2002 likely contributed to Americans' lower appetite for risk, the study said.

I expect last year's market drop will lower this appetite further as future 10-year returns will look lousy for years. Even if stocks gain 10 percent a year for the next nine years, the average annual compounded return for the 10-year period ending Dec. 31, 2017, would be



only about 4 percent.

And yet - again historically, but with no guarantees - strong market gains tend to follow periods of declines. Provided their total allocation to stocks does not exceed their risk tolerance, investors may consider dollar-cost-averaging now or investing equal amounts of money at set intervals. That way they use volatility to their advantage, buying more shares when prices are down.

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On The Money



"In today's economy, it's important to diversify! Put some of your money under your mattress, put some in a cookie jar, bury some in your back yard..."



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Retirement Planning

Many People Know Little About One Of Their Most Valuable Retirement Assets

By Humberto Cruz, Tribune Media Services

It's one of the biggest, if not the biggest, asset for millions of Americans in or near retirement.

But we have little practical knowledge of this asset - assuming we even think about how to get the most out of it.

I am talking about Social Security retirement benefits, which should be a component of any retirement income plan.

Consider: The average monthly Social Security retirement benefit will be about \$1,153 in 2009. To receive that much inflation-adjusted income for life, a 65-year-old man would have to pay an insurance company a lump-sum premium of about \$204,000 for an immediate annuity based on quotes I found from highly rated companies.

According to a recent online survey commissioned by Fidelity, 56 percent of the 61-year-olds

surveyed didn't know when they would receive unreduced benefits. (The answer is age 66 for anyone born between 1943 and 1954. After that, the age of eligibility rises by two months every year until it becomes age 67 for those born in 1960 or later.)

More than half didn't know we have to file for benefits three months before we want to start receiving them. Almost a third believed incorrectly that Social Security benefits are not taxed (up to 85 percent of benefits may be taxed depending on what other income we have).

More than half didn't know that a surviving spouse could be eligible to receive the Social Security benefit of the deceased spouse if it was larger than the survivor's own benefit.

Also, 45 percent say they plan to start taking

reduced benefits as soon as they are eligible at age 62. The most common reason given was that they need the money.

Such an action would lower their benefits permanently. Perhaps there is another way to bridge the income gap until full retirement age that they didn't consider.

Also, just 22 percent said they knew exactly how much their benefits would be - and 26 percent had no idea. And yet Social Security has been mailing Americans an annual benefits estimate since 1997, and this year the agency introduced an improved benefits estimator at www.socialsecurity.gov/estimator.

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