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"The price of discipline is always less than the pain of regret." - Nido Qubein

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Financial Update

Ideas and Action Steps for Achievers

Speculating on the Future of the Federal Estate Tax

What's the future of the federal estate tax? All we know is that no one knows for sure; it's all speculation. So, let's take a look at what could happen. There are five possibilities: (1) Congress could extend current tax law (commonly referred to as the "Bush tax cuts"); (2) Congress could do nothing, essentially turning the calendar back to 2001; (3) Congress could compromise, agreeing on something between the 2001 tax rules and the rules that apply in 2012; (4) Congress could enact new estate tax reform; or (5) Congress could repeal the estate tax altogether.

Note: *Only a few of the estate tax laws that are affected are discussed here.*

Congress could extend current tax law again, probably for two years

That would mean the top gift and estate tax rate would remain at 35%. The generation-skipping transfer (GST) tax (this is an additional tax that's imposed on transfers to beneficiaries who are two or more generations below you) would also remain at a 35% tax rate. The gift and estate tax exemption (may also be referred to as an exclusion) would remain at $5,120,000 (plus any adjustment due to inflation) plus any deceased spousal unused exclusion amount (DSUEA).

The DSUEA is the amount of the gift and estate tax exemption that the first spouse to die does not use. This amount can be transferred from the estate of the first spouse to die to the surviving spouse. This is referred to as portability. Portability would remain.

The GST tax exemption of $5,120,000 plus any adjustment due to inflation would remain. There is no DSUEA for the GST tax (i.e., the GST tax exemption is not portable between spouses).

The smart money is on this possibility. It has been Congress's tendency of late.

Congress could do nothing

Congress could allow all or some of the provisions that sunset to expire, reverting to the 2001 tax rules. The top gift and estate tax rate would be 55% with a 5% surtax on estates that exceed $10 million but do not exceed $17,184,000. The GST tax rate would also be 55%. The gift and estate tax exemption would be $1 million. And, the DSUEA would no longer apply. The GST tax exemption would be $1 million indexed for inflation (estimated so far to be $1,360,000).

Some analysts have proposed letting the Bush tax cuts expire as part of a plan to balance the budget over time.

Congress could compromise

Congress could pass a compromise bill that would set the top tax rate to 45% and the exemption amount to $3.5 million. Whether portability would expire or be extended is anyone's guess.

President Obama supports this option. His 2013 budget plan would return the gift and estate tax, and the GST tax, to 2009 levels; the top tax rate would be 45%, the exemptions would be $3.5 million (but only $1 million for gift tax purposes), and portability would be made permanent.

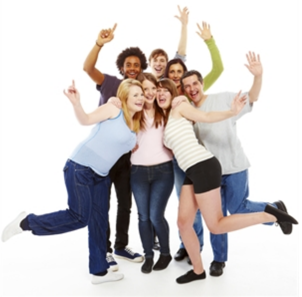
Congress could enact estate tax reform

Many believe that permanent and comprehensive estate tax reform is needed. However, the political landscape is probably not currently amenable to this option. Besides, permanent tax reform does not really mean that it will be permanent (it could, of course, be modified or repealed by future legislation).

Congress could repeal the estate tax altogether

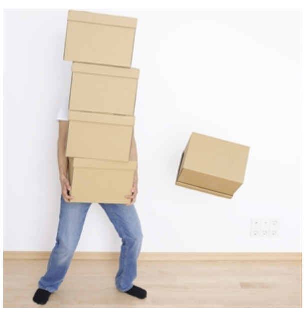
The arguments for and against the repeal of the estate tax continue to wash in, like ocean waves. The tide was high for repeal a few years back, but the current economic and fiscal situation may have slowed its momentum, and the tide seems to be ebbing.

Ways Parents Can Help Their Boomerang Kids



A financial strain

Parents naturally want to help their children during hard times, but in some cases, the financial strain of another adult (or two or three) in the house can be too much of a financial shock. If your adult child needs to move back home, discuss how long your child plans to stay and how he or she can contribute financially to the household.



It's been called the new retirement wild card. But it's not inflation, health-care costs, or taxes, though those things certainly matter. What is it that's causing so much uncertainty? It's boomerang kids, and the money their parents spend on them.

The trend

According to the U.S. Census Bureau, there were 6 million young adults ages 25 to 34 living at home in 2011--19% of all men (up from 14% in 2005) and 10% of all women (up from 8% in 2005). Not surprisingly, the percentages are higher for young adults in the 18 to 24 age bracket, with 59% of young men and 50% of young women living with their parents in 2011.

Sociologists have cited a number of reasons for this trend--the recession, college debt, the high cost of housing, delayed marriage, and a tendency toward prolonged adolescence. But whatever the reason, there's no doubt that boomerang children can be a mixed blessing for their parents, both emotionally and financially. Just when parents may be looking forward to being on their own and preparing for their retirement, their children are back in the nest and relying on their income. While the extra company might be welcome, you don't want to sacrifice your emotional and financial health to help your kids.

Set ground rules

If your adult children can't afford to live on their own, establish ground rules for moving back home, including general house rules, how long they plan to (or can) stay, and how they can contribute to the household in terms of rent and chores. As an adult, your child should be expected to contribute financially to the household overhead if he or she is working. Determine a reasonable amount your child can contribute toward rent, food, utilities, and car expenses. You can then choose to apply this money directly to household expenses or set it aside and give it to your child when he or she moves out, when it can be used for a security deposit on an apartment, a down payment on a car, or some other necessary expense.

You should also discuss your child's long-term plan for independence. Does your child have a job or is he or she making sincere efforts to look for work? Does your child need or want to go back to school? Is your child working and saving money for rent, a down payment on a home, or graduate school? Make sure your child's plans are realistic and that he or she is taking steps to meet those goals.

It's a balancing act, and there isn't a road map or any right answers. It's common for parents to wonder if they're making a mistake by cushioning their child's transition to adulthood too long or feel anxious if their child isn't making sufficient progress toward independence.

Turn off the free-flowing money spigot

It can be tempting for parents to pay all of their adult children's expenses--big and small--in an effort to help them get on their feet, but doing so is unlikely to teach them self-sufficiency. Instead, it will probably make them further dependent on you.

If you can afford it, consider giving your child a lump sum for him or her to budget rather than just paying your child's ongoing expenses or paying off his or her debt, and make it clear that is all the financial assistance you plan to provide. Or, instead of giving your child money outright, consider loaning your child money at a low interest rate. If you can't afford to hand over a sum of cash or prefer not to, consider helping with a few critical expenses.

Evaluate what your money is being spent on. A car payment? Credit card debt? Health insurance? A fancy cell phone? Student loans? General spending money? Your child is going to have to cut the frills and live with the basics. If your child is under age 26, consider adding him or her to your family health plan; otherwise, consider helping him or her pay for health insurance. Think twice about co-signing a new car loan or agreeing to expensive lease payments. Have your child buy a cheaper used car and raise the deductible on his or her car insurance policy to lower premiums. Help your child research the best repayment plan for student loans, but don't pay the bills unless absolutely necessary. Same goes for credit card balances. Have your child choose a less expensive cell phone plan, or consolidate phones under a family plan and have your child pay his or her share. Bottom line--it's important for your child to live within his or her financial means, not yours.

Solidify your own retirement plan

Even if your child contributes financially to the household, you may still find yourself paying for items he or she can't afford, like student loans or medical bills, or agreeing to pay for bigger ticket items like graduate school or a house down payment. But beware of jeopardizing your retirement to do this--make sure your retirement savings are on track. A financial professional can help you see whether your current rate of savings will provide you with enough income during retirement, and can also help you determine how much you can afford to spend on your adult child now.

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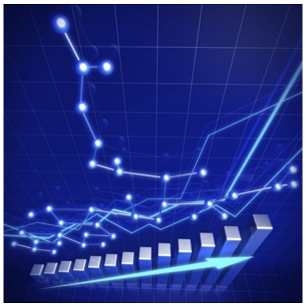
Stock Market Metrics: Playing the Numbers



Fundamental metrics based on the operations of individual companies also can be aggregated and averaged to suggest the state of an index comprised of those stocks.

There are no infallible guides to stock market movements. However, that doesn't stop investors from using various measurements to try to divine the current and future direction of a stock's price or the equity markets as a whole. Here are some common methods (or metrics) for gauging the stock market.

Gauging volatility

The CBOE Volatility Index®, informally referred to as the VIX® and nicknamed "the fear index," measures real-time changes in the prices of a group of S&P 500 30-day options traded on the Chicago Board Options Exchange. When financial markets are stressed, prices of those options tend to rise as investors try to hedge any potential negative impact on their portfolios. The more concerned options traders are about potential instability, the higher the VIX tends to go; conversely, when fears subside, the VIX tends to be lower. How high is high for the VIX? During the worst of the 2008 financial crisis, it spiked to 89 at one point. Since then, it has gradually returned to more normal levels in the teens and twenties.

Moving averages

A moving average reflects a stock's average price or an index's value over a specified period of time (for example, the last 50 days). As a new average for the time period is calculated each day, the earliest day's data drops out of the average. The results are typically depicted as a line on a chart, which shows the direction in which that rolling average has been moving. For example, a stock's 50-day moving average (DMA) shows whether the stock's short-term price has been moving up or down; a 200 DMA smooths out shorter-term fluctuations by using the longer 200-day rolling time period. When a stock's price moves above its 50-day or 200-day average--two of the most popular gauges--technical analysts typically consider it a bullish signal that the stock or index has momentum. Conversely, when the price moves below its moving average, it's considered a bearish signal suggesting that any uptrend could be reversing.

Golden cross/death cross

When the short-term moving average of a stock or index rises above a longer-term average--for example, when the 50 DMA moves upward above its 200 DMA--the situation is referred to as a "golden cross." It shows that the stock's most recent price action has been increasingly positive, suggesting that investors have grown more bullish on the stock. Technical analysts also look for golden crosses with various stock indices--the S&P 500 is perhaps the most popular--to try to gauge the potential future direction of the equity markets.

The so-called "death cross" is the inverse of a golden cross. It occurs when the 50 DMA falls below the 200-day, and is considered a bearish signal, especially when seen in a broad market index such as the S&P 500. Such signals may or may not be valid; there are arguments on both sides. However, many of the automated trading systems that are responsible for a large percentage of all transactions are guided at least in part by such perceived quantitative signals. As a result, an index or stock can experience volatility--either up or down--as it reaches either of these points.

Fundamental metrics

Other stock market metrics rely on the nuts and bolts of corporate operations that are reflected on a company's balance sheet--so-called "fundamental data." Though based on the operations of individual companies, they also can be aggregated and averaged to suggest the state of an overall stock market index comprised of those stocks. The following represent some frequently used fundamental stock metrics.

Earnings per share (EPS): This represents the total amount earned on behalf of each share of a company's common stock (not all of which is necessarily distributed to stockholders). It is calculated by dividing the total earnings available to common stockholders by the number of shares outstanding.

Price-earnings (P/E) ratio: This represents the amount investors are willing to pay for each dollar of a company's earnings. Calculated by dividing the share price by the EPS, it can be used to gauge investor confidence in the company's future. A ratio based on projected earnings for the next 12 months is a forward P/E; one based on the previous 12 months' earnings is a trailing P/E. Like EPS, P/E is considered an indicator of how expensive or cheap a stock is.

Return on equity (ROE): This is a way to gauge how efficient a company is, especially when compared to its peers in the industry. This percentage compares a company's net income (usually for the last four quarters) to the total amount of shareholders' equity (typically, the difference between a company's total assets and its total liability).

Debt/equity ratio: Obtained by dividing a company's total liability by all shareholder equity, this percentage suggests the extent to which the company relies on borrowing to finance its growth.

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Can I convert my traditional IRA to a Roth IRA in 2012?

It may be an excellent time to consider converting your traditional IRA to a Roth IRA. As a result of market volatility, some investors have seen a reduction in the value of their traditional IRAs, meaning that the tax cost of converting may have dropped significantly. Also, federal income tax rates are scheduled to increase in 2013, so converting this year may be "cheaper" than converting next year.

Anyone can convert a traditional IRA to a Roth IRA in 2012. There are no longer any income limits, or restrictions based on your tax filing status. You generally have to include the amount you convert in your gross income for the year of conversion, but any nondeductible contributions you've made to your traditional IRA won't be taxed when you convert. (You can also convert SEP IRAs, and SIMPLE IRAs that are at least two years old, to Roth IRAs.)

Converting is easy. You simply notify your existing IRA provider that you want to convert all or part of your traditional IRA to a Roth IRA, and they'll provide you with the necessary paperwork to complete. You can also transfer or roll your traditional IRA assets over to a new IRA provider, and complete the conversion there.

If a conversion ends up not making sense (for example, the value of your Roth IRA declines after the conversion), you'll have until October 15, 2013, to "recharacterize" (i.e., undo) the conversion. You'll be treated for federal income tax purposes as if the conversion never occurred, and you'll avoid paying taxes on the value of IRA assets that no longer exist.

The conversion rules can also be used to allow you to contribute to a Roth IRA in 2012 if you wouldn't otherwise be able to make a regular annual contribution because of the income limits. (In 2012, you can't contribute to a Roth IRA if you earn $183,000 or more and are married filing jointly, or if you're single and earn $125,000 or more.) You can simply make a nondeductible contribution to a traditional IRA, and then convert that traditional IRA to a Roth IRA. (Keep in mind, however, that you'll need to aggregate the value of all your traditional IRAs when you calculate the tax on the conversion.) You can contribute up to $5,000 to an IRA in 2012, $6,000 if you're 50 or older.

Can I undo my Roth IRA conversion?

When you convert a traditional IRA to a Roth IRA, you include the value of your traditional IRA, reduced by any nondeductible contributions you've made, in income for federal tax purposes in the year of the conversion. But what happens if the value of your Roth IRA subsequently declines, making the conversion a bad deal from a tax perspective? No problem. The IRS lets you recharacterize (undo) a conversion, if you act in a timely fashion.

For example, assume you convert a fully taxable traditional IRA worth $50,000 to a Roth IRA in 2012. You include $50,000 in income on your 2012 federal income tax return. But shortly after the conversion, the value of your Roth IRA declines to $25,000. Now you're suddenly faced with the proposition of paying taxes on $50,000, while your Roth IRA is worth only $25,000.

All is not lost--because of the recharacterization rules, you have until your tax return due date (including extensions) to undo all or part of a conversion if it no longer makes good financial sense. So in this example, you have until October 15, 2013, to recharacterize. (Similarly, if your conversion occurred in 2011, you have until October 15, 2012, to undo the conversion.)

When you recharacterize, you need to withdraw the amount you originally converted, plus any earnings, out of the Roth IRA and transfer it back to a traditional IRA. To simplify the calculation of earnings if you decide to recharacterize, you should consider using a new Roth IRA for each conversion. You might also consider using a different Roth IRA for each separate investment, or class of investments, you plan to make--this way, if one investment goes down but another goes up, you can recharacterize only the Roth IRA that declined in value (you don't need to aggregate your Roth IRAs for this purpose). If you wish, you can always combine Roth IRAs later after the recharacterization deadline passes.

If you convert a traditional IRA to a Roth IRA in 2012 and then recharacterize, you'll have to wait until January 1, 2013, to reconvert those same dollars (and any earnings) to a Roth (or, if later, the 31st day following the recharacterization). However, any other traditional IRA dollars you have can be converted to a Roth IRA without restriction.

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