



Financial Foresights

Practical Insights For Your Financial Goals

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Hi Everyone!

I hope you enjoy this month's edition of my newsletter.

Dave

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2008 Tax Filing Season: New and Noteworthy

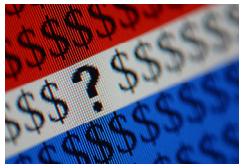
What You Don't Know Can Hurt You

How much of your company's stock should you hold?

Will the Estate Tax Stay Repealed for 2010?

In 2001, a law was passed that gradually phased out the federal estate tax through 2009, and repealed it altogether in 2010. That law,

however, "sunssets" or expires in 2011 and reinstates pre-2001 tax law levels (with an exemption of \$1 million and a top tax rate of 55%). Since 2001, the economic and political climate in the United States has changed significantly. The federal budget deficit has ballooned, the financial markets have been in turmoil, and most importantly, power has shifted to the Democrats. So, the question is: just how likely is it that 2010 will be an estate tax-free year?



Chance of repeal?...virtually zero

Of course, anything can happen, but President Obama has made it clear that he believes the estate tax should continue in some form or other. And in the Senate, Finance Committee Chairman Max Baucus has firmly stated "...repeal isn't going to happen." With increased Democratic majorities in both chambers of Congress, it seems highly likely that some action will be taken soon to head off the one-year sabbatical scheduled for 2010.

Future of the estate tax

Several bills have been introduced in Congress in the intervening years since 2001, some calling for full repeal, others for reform. Reforms that have been proposed include:

- Raising the exemption and/or lowering the tax rates
- Making the exemption "portable" between spouses (allowing surviving spouses to use any unused portion of the deceased spouse's exemption)
- Replacing the estate tax with an inheritance tax (transferring the transfer tax burden to heirs)

- Replacing the step-up in basis rule with a carryover basis rule (also transferring the tax burden to heirs in the form of capital gains tax)

President Obama has endorsed the following reforms:

- Freezing the estate tax at 2009 levels (\$3.5 million exemption and 45% top rate)
- Indexing the exemption for inflation
- Disallowing or limiting valuation discounts

Planning for continued uncertainty

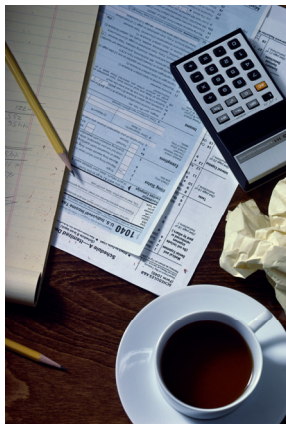
All indications point to the estate tax remaining for the foreseeable future. While the uncertainty that continues to surround the exact components of the estate tax may tempt some individuals to do nothing or wait and see, it may be wiser to review your plans now to ensure that they can withstand the winds of change.

Creating a flexible estate plan is the key to avoiding the pitfalls of future tax law changes, as well as changes that may occur in your personal life. A flexible estate plan uses language and provisions in wills and trusts that maximize the ability to pass estate assets free of estate taxes. And other tools, such as disclaimers and powers of appointment, can allow heirs or trustees to respond to circumstances existing at the time of your death.

Beyond tax

Remember that dealing with estate taxes, no matter what the future may hold, is just a piece of your estate plan. An experienced financial professional can help you identify strategies that may help you achieve your overall estate planning goals.

2008 Tax Filing Season: New and Noteworthy



Not everyone qualified for a stimulus payment in 2008

Rebate payments were phased out for individuals with adjusted gross incomes exceeding \$75,000 (\$150,000 for married couples filing joint returns), and certain individuals didn't qualify (for example, individuals who could be claimed by someone else as a dependent).



A worksheet for calculating the recovery rebate credit is provided on pages 62 and 63 of the instructions for the IRS 2008 Form 1040.

The tax filing season is often a period of high anxiety, and this year brings an additional challenge: a series of legislative acts last year ushered in multiple changes. The good news, though, is that most of those changes work in your favor. So, whether you're completing your own IRS Form 1040 or relying on a professional tax preparer, here are a few new wrinkles to keep in mind.

2008 stimulus payment redux

Remember the economic stimulus payments issued by the federal government last year? Individuals who filed 2007 federal income tax returns, and had \$3,000 or more of income (including amounts received from Social Security and certain veterans' benefits), generally qualified for a stimulus payment of up to \$600 per individual (\$1,200 in the case of married couples filing jointly), with an additional \$300 for each qualifying child under the age of 17.

That stimulus payment you may have received in 2008 was actually an advance payment of a credit against your 2008 taxes, based on your 2007 information. When you complete your 2008 return, you determine the amount of credit you're entitled to (calculated in the same manner as the economic stimulus payment was in 2008, except that your actual 2008 tax figures are used) and subtract the amount that you received as a stimulus payment last year. If the credit is more than you received as a stimulus payment, the difference is claimed as a "recovery rebate credit" on your 2008 income tax return. If the credit is less than the stimulus payment you received last year, you don't have to pay back the difference.

So, if you didn't qualify for an economic stimulus payment last year, or received less than the full amount, you get a second bite at the apple. For example, maybe your 2007 adjusted gross income was too high to qualify for a stimulus payment, but your 2008 adjusted gross income is below the threshold. If you had a child born in 2008, you could also end up with additional recovery rebate credit dollars.

Economic stimulus payments and IRAs

If you had a 2008 economic stimulus payment directly deposited into a tax-advantaged account like an IRA, and subsequently withdrew the funds, you may have received a Form 1099-R showing the amount you withdrew as a distribution. As long as you did not withdraw

more than the amount of your economic stimulus payment from the IRA (and you make the withdrawal by the due date of your return, including extensions), however, you do not have to pay tax or penalties on this amount. (You actually have until the due date of your return, including extensions, to withdraw the stimulus payment amount from your IRA without tax consequences.) Follow the IRS instructions for lines 15a and 15b (Form 1040), Exception 5, or lines 11a and 11b (Form 1040A), Exception 5.

First-time homebuyer credit

If you bought a home on or after April 9, 2008 (or if you purchase a home before July 1, 2009), and you qualify as a first-time homebuyer, you may be eligible for a refundable tax credit equal to 10% of the purchase price, up to \$7,500 (\$3,750 if married filing separately). For homes purchased in 2009, you can claim the credit on either your 2008 or 2009 federal income tax return.

The home has to be your principal residence, and—to qualify as a first-time homebuyer—you must not have had an ownership interest in a principal residence in the United States for the three-year period immediately preceding the purchase. You can't claim the credit if your modified adjusted gross income (MAGI) is \$95,000 or more (\$170,000 or more if married filing jointly), and you're only entitled to a partial credit if your MAGI exceeds \$75,000 (\$150,000 if married filing jointly).

This credit, however, is essentially an interest-free loan. Two years after you claim the credit, you have to start paying it back (generally over 15 years in equal installments). Special rules apply if you sell the home during the repayment period, or if the home ceases to be your principal residence.

Standard deduction for real estate taxes

Even if you don't itemize deductions on your 2008 return, you may be able to deduct at least some of the real estate taxes you paid. That's because, for the first time, individuals who do not itemize deductions will be able to claim an additional standard deduction for real estate taxes paid to state and local governments, up to \$500 (\$1,000 if married filing jointly).

With the number of recent tax changes, it could pay to take a little extra time to review IRS instructions this year. And, as always, if you have questions, talk to a tax professional.

What You Don't Know Can Hurt You

You've probably heard the saying, "what you don't know can't hurt you," but when it comes to your finances, ignorance is not necessarily bliss. It's easy to make bad financial decisions when you lack sufficient information or you are misinformed. By the time you realize your mistake, it's usually too late to correct it. Here are several common mistakes that can be avoided with just a little bit of forethought.

Naming the wrong insurance beneficiary

Life insurance has many benefits. Among them is the fact that death benefits are generally paid directly to the beneficiary you name in the policy without passing through probate. But what happens if the beneficiary you name is unable to accept the death benefit, because he or she is a minor, deceased, or incompetent? In these circumstances, unless you've named an alternate beneficiary, the life insurance proceeds will be subject to all of the expenses and delays associated with settling an estate through probate.

What can you do before it's too late? Review your life insurance beneficiary designations at least annually to be sure the proceeds will pass to the proper beneficiary without the involvement of probate. Also, consider adding at least one contingent or alternate beneficiary in case the primary beneficiary is unable to receive the proceeds.

Selecting the wrong pension option

If you're lucky enough to have an employer-sponsored pension for your retirement, the distribution choices you make usually can't be changed, regardless of whether your circumstances change. Before making your choice, get all of your plan's options from the plan administrator and review them with a financial professional who can help you crunch the numbers. Estimate your retirement income needs, then determine what the best strategy is for you and your family.

What can you do before it's too late? If you're married you're required to take a joint and survivor option, unless your spouse waives his or her rights to your pension. If you elect the single life option, your payments will be larger, but at the expense of a future spousal benefit. If you choose the single life option, make sure

you have plenty of other income or life insurance to replace the pension for your surviving spouse.

Owning assets jointly

Owning assets jointly often can be a good strategy to avoid probate or minimize estate taxes. However, this form of asset ownership also has disadvantages. The joint owner has equal rights to the jointly owned asset, meaning he or she can withdraw from a joint bank or brokerage account or sell his or her interest in the asset without your consent. In addition, adding someone's name to an asset may be considered a gift, subject to possible gift taxes. And, owning assets jointly exposes those assets to the creditors of your joint owner. Finally, with respect to long-term care planning and Medicaid qualification, adding a joint owner can negatively affect your Medicaid eligibility.

What can you do before it's too late? Consider the ramifications of joint ownership carefully before implementing this strategy. If your intent is to leave the asset to the joint owner, alternatives such as payable on death accounts, trust designations, or life estates may accomplish your goal and protect your interest in the asset at the same time.

Underinsured homes

Imagine this scenario: you just suffered through a terrible fire that destroyed your home and most of its contents. You get an estimate on the cost to rebuild your home and file a claim with your homeowners insurance carrier. To your shock, you find that they are not going to cover the entire cost to rebuild. You thought your policy covered the full replacement cost of your home. However, the policy actually provides extended replacement cost, which offers up to 120% of the policy's face amount--not enough to cover all of the costs to rebuild your home.

What can you do before it's too late? Review your policy at least annually and make sure the face amount is enough to cover the cost to rebuild your home should the unthinkable occur. That means you need to know the approximate cost to rebuild, including any additions and improvements you made to the home. Also, take into consideration increasing costs of materials and labor.



You could make financial decisions that turn out to be wrong because you lack sufficient information or you were misinformed altogether.

Other common mistakes

- *Failing to provide for financial loss due to a non-work related disability*
- *Miscalculating how much life insurance you need*
- *Owning too much company stock in your employer-sponsored retirement plan*
- *Underestimating how long your retirement may last*
- *Overestimating the annual rate of return you'll earn on your investments*
- *Trying to save for your children's college education at the expense of saving for your retirement*



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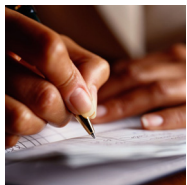
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Ask the Experts



How much of your company's stock should you hold?

No matter how good a company you work for, you should think carefully about how much you should have invested in it. Yes, there are

companies whose employees have become wealthy from company stock that was part of their compensation. But there also are stories about employees of companies such as Enron, Bear Sterns, and Lehman Bros.--people who believed in their employers but learned the hard way that allowing one company--especially a current employer--to dominate their investment or retirement portfolio can have devastating consequences.

According to the most recent Employee Benefit Research Institute statistics (Issue Brief No. 308, August 2007), company stock represents an average of 11% of 401(k) plan participants' assets (though that percentage is less than in previous years). However, few mutual fund managers would allow a single stock--any stock--to represent that much of a fund's portfolio. And a corporate pension plan is actually

prohibited from investing more than 10% of its holdings in the company's own stock.

Ironically, the better your company's stock has performed, the greater the chance that it may have grown to dominate your portfolio. However, even if your company is a good one, working at a company means you've invested your "human capital"--your earning ability--in that firm. If you also have a large portion of your investment capital there, your financial well-being is even more dependent on a single company. If a company's stock is suffering, it might react by cutting jobs company-wide. If yours were one of them, both your human and investment capital would be hit.

And don't forget to consider whether an equity mutual fund you hold also may have invested in your company's stock. You can find out a fund's holdings by checking its annual and semiannual reports. You can use the information to estimate your total exposure to your employer's stock.

What issues might company stock options raise at tax time?

If stock options are part of your compensation package, a significant market downturn can mean special financial pain.

In many cases, people who receive options to buy their company's stock find that during a downturn, the stock's market price is lower than the option's exercise price. Since few would choose to exercise an option that requires paying more than the market price, the option is said to be "underwater"--a situation that was widespread last year. If your options are underwater, it's worth checking to see if your company has considered asking its shareholders to approve repricing the options, or exchanging them for a smaller number of options with a lower exercise price. Some companies are taking such steps to try to retain valued employees.

If you exercised options to purchase your company's stock in 2008, you may face a more complex problem. The type of option and when you exercised it can raise a number of issues at tax time. If you own nonqualified stock options, you'll generally owe ordinary income tax on the difference between the exercise price and the stock's market value as of the date you exercised it. That amount is considered compensation and, if you're an

employee, should be listed on your W-2 form.

If you exercised incentive stock options (ISOs), tax is ordinarily deferred until you sell the stock that you acquired. However, unless you sold the stock in the same year that you acquired it, you have to factor in the alternative minimum tax (AMT). For AMT purposes, when you exercise an ISO, income is generally recognized to the extent that the fair market value of the shares when acquired exceeds the option's exercise price. This means that a significant ISO exercise in one year can trigger AMT liability, even though no income is actually received. This application of AMT could be a real problem if you exercised the options in early 2008 and later saw the value of the stock you received dramatically decline in value. If you are subject to AMT as the result of an ISO exercise, you'll be entitled to a resulting AMT credit that can be used in future years.

The Emergency Economic Stabilization Act of 2008 included some relief for taxpayers who exercised ISOs prior to 2008, and makes it easier to claim unused AMT credit. However, it will be of little help if you exercised ISOs in 2008. For more information, talk to a tax professional.