



Financial Foresights

Practical Insights For Your Financial Goals

September 2008

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Hi Everyone,

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

Dave

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Reapplying for Social Security

What if you decide to apply for early Social Security benefits, but a few years into retirement, realize that a higher Social Security benefit would help you increase, and sustain, your standard of living? Fortunately, you're not necessarily locked into your decision to take your retirement benefit early. The Social Security Administration (SSA) allows you to withdraw your benefit application and reapply later if that would be to your advantage.

Why reapply?

Increasing your monthly Social Security retirement benefit is one of the main reasons you might want to withdraw your application and reapply. According to the SSA, most retirees file for Social Security benefits early, often at age 62. But the drawback to claiming benefits early is that your monthly benefit will be substantially less than it would be if you wait until full retirement age, or longer, to collect. For example, if your full retirement age is 66, your monthly benefit at age 62 will be approximately 25% less than it will be if you wait until your full retirement age of 66 to collect, and 43% less than if you wait until age 70. (Source: SSA chart, Effect of Early or Delayed Retirement on Retirement Benefits)

Your Social Security retirement benefit is a steady source of inflation-adjusted retirement income that also provides built-in survivor protection for your spouse.



Once you have a clearer picture of your retirement income needs, you may decide to withdraw your initial application and reapply when you're older, so that you may receive a higher monthly Social Security benefit (adjusted annually for inflation) for the rest of your life. In addition, if you're married, your spouse will generally receive the greater of his or her own

retirement benefit or your monthly benefit (including any cost-of-living increases) in the event of your death, so increasing your retirement benefit may translate into more survivor protection for your spouse.

You may also wish to withdraw your Social Security application if you decide to work and your income is enough to reduce or even eliminate your Social Security benefit, or if your Social Security income is increasing your tax liability.

How do you do it?

You can withdraw your initial benefit application by filing Form SSA-521, "Request for Withdrawal of Application" at your local Social Security office. However, there is a pretty big catch. If you withdraw your application after you begin receiving benefits, you're required to return--in a lump sum--all of the money that Social Security has paid you over the years. But any interest or investment earnings you've received as a result of saving or investing those benefits is yours to keep. If you paid taxes on the benefits you're now paying back, you may be eligible for an income tax credit or a deduction. You can find more information about the tax consequences in IRS Publication 915, Social Security and Equivalent Railroad Retirement Benefits.

There's so much to consider

Not everyone will come out ahead by withdrawing an application for retirement benefits, then reapplying--you'll need to consider your own financial circumstances. Obviously, the requirement to pay back benefits will limit the number of people who can take advantage of this opportunity. And even if you can afford to pay back your benefits, you must be willing to accept the risk that if you die, you or your spouse may not recoup the amount you've paid back. But reapplying for benefits may be worth considering if you need to maximize your lifetime income and provide higher survivor's benefits for your spouse.

Where to Stash Your Emergency Cash

Multiple choices

Many experts suggest having 3 to 6 months' income in your emergency fund. When planning how much to have and where to keep it, consider all your potential emergency resources, such as a health savings account, insurance, an emergency-only credit card, or a home equity line of credit. You may also be able to combine options--for example, an interest-bearing checking account that replaces a credit card for minor emergencies, plus a higher-yielding account for the rest of your emergency cash.



If you're contemplating putting your cash into a mutual fund, be sure to obtain and read its prospectus (available from the fund) so you can carefully consider its investment objectives, risks, charges, and expenses before investing.

A financial cushion can improve your ability to survive bad times, but right now that cash may be earning a relatively low interest rate. However, try to think of it as you might insurance: your emergency fund is designed to be there when you need it. Here are some possibilities that balance safety with liquidity:

Interest-bearing checking accounts

Deposit accounts are federally insured up to \$100,000, so they're as secure as it gets. Bank deposit balances are insured by the Federal Deposit Insurance Corporation (FDIC); credit union balances are insured by the National Credit Union Administration. Lower costs often permit higher yields on online accounts, and minimum balances for online accounts also are typically low. However, depending on the institution, your access with an online-only account may be somewhat less convenient than you're used to; for example, the number of deposits or check-writing privileges may be limited. An ATM/debit card linked to a checking account is convenient, but if the temptation to use it for a "retail emergency" proves too great, it could end up pulling the stuffing right out of your financial cushion.

High-yield savings accounts

Savings accounts typically offer higher interest rates than checking accounts. Again, some of the best rates may be available online. However, make sure you find out whether the yield quoted is an introductory rate and what minimum balance is required to get it. Also, some high-yield savings accounts require that a certain number of purchases be made using a linked credit or debit card--hardly appropriate for an emergencies-only fund.

Money market savings accounts

A money market savings account (MMA) may offer higher interest than a checking or even a regular savings account, but also may have some restrictions on access; for example, it may limit the number of transfers, withdrawals, or checks, and may require a higher minimum initial deposit or balance. (On the other hand, such constraints may force you to think twice before accessing that money without good cause.) MMAs generally invest in short-term commercial loans, CDs, and government securities.

Money market mutual funds

Money market mutual funds may offer higher

rates than checking or savings accounts. Even though they may invest in similar types of securities as money market savings accounts, don't confuse the two. An investment in a money market mutual fund is not insured or guaranteed by the FDIC or any other government agency. Although the fund seeks to preserve the value of your investment at \$1 per share, it is possible to lose money by investing in the fund. If you're in a high tax bracket, consider municipal money market funds, which offer the federal tax advantages of muni bonds. A fund that concentrates on munis from your state also may offer state tax benefits.

Laddered cash equivalents

Certificates of deposit (CDs) or short-term Treasury bills provide less liquidity, but a laddering approach could improve your access while still limiting to some extent your ability to raid your fund without a good reason. For example, you might buy six CDs; the first CD matures in one month, the second in two months, the third in three months and so on up to six months. When the first CD matures, you could buy another six-month CD; you'd do the same with each succeeding CD at maturity. That would make some cash available once a month, and laddering lets you adapt to changing interest rates. A similar strategy could be used with short-term T-bills, available in maturities of 4, 13, 26, and 52 weeks. However, be aware that if you need to sell or cash in a CD early, you may have to pay a substantial penalty that could wipe out any incremental yield. In the case of a brokered CD sold before maturity, you also might suffer a loss. Also, interest rates could affect the value of a T-bill sold before it matures.

Short-term bond funds

Sometimes used as an alternative to a money market fund, short-term bond funds have typically offered higher yields with relatively modest increased risk (though they also are not FDIC-insured). However, recent credit market conditions have underscored their hazards. Short-term bond funds may be more stable than long-term funds, but some investors have been surprised at losses resulting from their fund's exposure during the past year's credit turmoil to investments considered relatively safe.

Whatever you use for your cash stash, have a plan for replenishing it after the emergency has passed.

Saving for College with a 529 Prepaid Tuition Plan



Though not as popular as its ubiquitous cousin the 529 college savings plan, a 529 prepaid tuition plan may be of interest to you as a tax-advantaged way to save for college. A prepaid tuition plan, like a college savings plan, is a type of 529 plan, and enjoys all the tax benefits offered by these types of plans.

Yet a prepaid tuition plan operates very differently from a college savings plan. Knowing the difference can help you choose which type is right for you.

Locking in tuition costs

The main benefit of a 529 prepaid tuition plan is the ability to "lock in" tuition costs. As its name suggests, a prepaid tuition plan allows you to prepay tuition; that is, you purchase tuition now for use in the future. There are generally two ways to do this.

Under the more common contract-type prepaid tuition plan, the plan promises to cover a predetermined amount of tuition expenses in the future based on the amount you contribute today. Alternatively, with a unit prepaid plan, you purchase a certain percentage of units or credits, and the plan guarantees that whatever the percentage of costs such units cover now, the same percentage of costs will be covered in the future.

Example: *One hundred tuition credits are required to fund one year of tuition at State University today. Under a unit prepaid plan, you purchase one hundred credits for \$5,000. When your child enters State University in the future, the \$5,000 you spent today will cover an entire year's worth of tuition, even if costs for one year have risen to \$20,000 by then.*

Tax advantages

Prepaid tuition plans offer the exact same tax advantages as college savings plans--contributions grow tax deferred and withdrawals are completely tax free at the federal level when used to pay the beneficiary's qualified education expenses. At the state level, whatever tax benefits a particular state offers to college savings plan participants--for example, an income tax deduction for contributions and/or tax-free withdrawals from the plan--are also offered to prepaid tuition plan participants.

Who offers prepaid plans?

States may offer prepaid tuition plans for the public colleges within their borders. Typically, states require that the account owner or the beneficiary be a state resident when the account is opened. Currently, 13 states offer prepaid tuition plans--Alabama, Florida, Illinois, Kentucky, Maryland, Michigan, Mississippi, Nevada, Pennsylvania, South Carolina, Tennessee, Virginia, and Washington. In addition to states, private colleges can offer their own prepaid tuition plans. Currently, there is one private prepaid tuition plan made up of a consortium of over 270 private colleges, called the Independent 529 Plan (www.independent529plan.org).

Nuts and bolts

Prepaid tuition plans have a few quirks, though. Here's a summary of ways they differ from college savings plans:

Prepaid tuition plan	College savings plan
Offered by states (limited to your own state's plan) and private colleges	Offered by states--can join any state's plan
Can generally enroll only during open enrollment period	Can join any time
Funds must be used at participating colleges; plan may offer a refund if other college chosen	Funds can be used at any accredited college in the United States or abroad
Certain amount of tuition guaranteed	Returns not guaranteed; could lose money
Money generally for tuition only	Money for tuition, room and board, books, etc.

Is a prepaid tuition plan right for you?

The appeal of a prepaid tuition plan lies in the peace of mind it offers. Instead of fretting when you see college costs rising each year at twice the rate of general inflation, you're insulated from price appreciation. If your child plans to attend an in-state public college (or, in the case of a private prepaid plan, one of the participating colleges), then a prepaid tuition plan may be a good choice. If your child later decides to attend another college, prepaid plans typically have a mechanism to refund your contributions, usually with a predetermined amount of interest, so make sure to learn the refund policy before joining.

A prepaid tuition plan, like a college savings plan, is a type of 529 plan, and enjoys all the tax benefits offered by these types of plans.



Investors should consider the investment objectives, risks, charges, and expenses associated with 529 plans before investing. More information about specific 529 plans is available in each issuer's official statement, which should be read carefully before investing.



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Ask the Experts



What's a credit score and why should I care about it?

Your credit score is the result of a mathematical formula that's applied to all the information in your credit report (both positive and negative) and then compared to millions of other credit reports. The most common credit score is a FICO score, developed by the Fair Isaac Corporation. A variation of the basic FICO model is used by each of the three major credit reporting agencies: Equifax, Experian, and TransUnion.

Your FICO score is based on five categories, each of which accounts for a percentage of your total score:

- Your payment history: 35%
- An analysis of your debt: 30%
- The length of your credit history: 15%
- Recent inquiries/new credit activity: 10%
- Types of credit in use: 10%

The result is a three-digit number between 300 and 850 that estimates your level of credit

risk. The higher the number, the lower the risk.

This number significantly affects your ability to get credit and the terms you're offered. Generally, lenders consider people with scores above 700 to be in good financial health, and worthy of the best interest rates and credit terms. Those with scores below 600 are considered to be financially risky, and may be turned down for credit or offered stricter terms (higher interest rates, lower credit limits, and/or requirements for collateral or a cosigner or both).

To keep your score high:

- Pay your bills on time
- Repair any damage (i.e., overdue payments) as quickly as possible
- Keep your balances on your credit cards low (especially in relation to your credit limits)
- Pay off your debt
- Don't open new accounts you don't need

How do I dispute an unsatisfactory credit card purchase?

If you used a credit card to make what turns out to be an unsatisfactory purchase, you should first seek a refund or a replacement from the merchant that sold you the item. But if you have no luck there, you may have some recourse through the credit card company.

There are some requirements. First, you must have used the credit card to purchase the merchandise for personal (not business) use. Second, if you've already paid the credit card bill on which the sale is listed, the credit card company generally won't help you.

Additionally, the unsatisfactory purchase must have been made either with a charge card issued by the merchant or with a bank's card. If the item was not purchased with the merchant's own card, then the item must cost \$50 or more.

Further, unless you used the merchant's own card, the purchase must also have occurred within your home state or within 100 miles of your billing address. Catalogue sales, Internet sales, and orders placed by telephone may be

considered in-state purchases. State laws may vary, but these purchases are generally protected.

If you're unable to resolve the matter with the merchant, be sure to write the credit card company within 60 days of when the charge first appeared on your statement. Include in your letter your name, account number, information about the unsatisfactory item, and what you've done to try to resolve the matter with the seller.

The card issuer will usually investigate the matter, and you may withhold payment on the unsatisfactory merchandise until the matter is resolved. (Until then, no interest or late fees will be charged.) If the investigation reveals you are right and the merchant is at fault, you won't have to pay for the item or any finance charges on it. However, if the card issuer doesn't believe the merchant is at fault, you'll be expected to pay for the item. If you want to continue the dispute with the merchant, you'll have to do so in court.