Mike Chadwick's

# Money Matters

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## The Pension Issue!

The term pension can have several meanings which I'll define for you to help you better understand the endless stream of technical terms those in the financial world seem to enjoy manufacturing. This conversation comes from two perspectives - the one of the employee and the one of the business owner. The first and most common meaning of the term pension is an income that is paid to a worker (typically paid monthly) for services given to the employer after separation from service (hopefully that separation is retirement, not disability, layoff, firing, quitting, outsourcing, moving, etc.) Think of today's retirees Social Security retirement checks - a form of a pension plan. Most retirees today have some form of pension they are living on, as well as social security. Some were wise enough to have private investments, savings, real estate, etc. to help supplement pensions during the golden years. My concern moving forward is that many employers have dissolved the pension plan in favor of "cash balance plans." The cash balance

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### Inside This Issue



## Life Insurance 101

This is a topic for mass debate - schools of thought reign supreme here just like in the old school of what car company do you prefer - Ford, Dodge or Chevy. This is a much more important topic than just bragging rights, it is the future of families. This has been a sad month for us as we lost two clients - young clients. I'm sad to say we lost a 43 year old woman and a 32 year old man this month - unfortunately both had children. There are now three little girls without parents and an infant boy without a father. The life insurance policy is like a modern miracle - it comes to life just when it is needed and gets the job done that no other financial vehicle in the world can do. I'm going to define the various insurance policies, what they do and don't do and how you should position them in your world - if at all. This is all factual information - verifiable with financial models and not debatable. Read carefully and act accordingly since this is something you can't mess up and fix later on. The life insurance decision is one based on wants not needs. You don't need any - the government says you need the life insurance benefit social security provides - $255.00 (what a joke.) The government says you need auto insurance - to protect someone else, not our own family (another joke in our lawsuit driven society - they need to change the laws!) Here are the types of policies and what

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plan comes in many different flavors and names but some of the one's you'll recognize include 401(k), 403(b), 457, SIMPLE, SEP, Keogh, SAR-SEP, IRA, Profit Sharing, Money Purchase, etc. All these plans are versions of a pension plan but have very different formulas for calculating benefits and contributions. These plans allow a certain number of dollars to be contributed each year, up to some specified maximum and whatever is there in the end, so be it. With the cash balance plan whatever the employee puts in, and perhaps some type of match if the employer feels benevolent, plus any growth or minus any losses will be what is available to the participant upon retirement. This is a far cry from the traditional pension plan (I'll refer to these as Defined Benefit plans from now on) where after working for a certain number of years you could count of some type of income that along with social security was enough to live comfortably on. The contribution formula for Defined Benefit plans is whatever is necessary to assure that the plan will have enough money to fund the benefits promised to workers based on a formula. The contributions allowable here are much higher than any cash balance plan and result in significant tax savings and higher costs for the employer. Many corporations today don't offer Defined Benefit Plans as they realized as early as the early 80's that these plans were too costly, hurt quarterly earnings and decided to shift retirement responsibility to the employees. Today most government, state and municipal employees have a defined benefit pension plan. These too will be going by the wayside as time unfolds - unless of course you'd like to see your income and property taxes quadruple to fund them. Some private employers still have them too but the trend is moving away from them. The baby boomers, generation X, Y and future generations need to realize that the way our parents and grandparents lived during retirement isn't going to be the same for us. Many promises being made today for our futures - including Social Security - are in danger of not coming to fruition. It is ultimately up to each of us, not the employer or the government to be sure we've got a safe and steady future planned. We're all given that opportunity the only question is have we taken advantage of it.

## Business Owner's Perspective

If you own a business, regardless of size, you should consider some type of pension plan. Most business owners I see have most of their assets in the business - necessary to make it run. The pension can be a wonderful tool to help you save income taxes, prepare for your future and reward your employees. If you are the owner of a business without any employees you can set up any type of retirement plan (as long as you've got earned income) and receive tax deductions of as little as $1.00 and as much as $100,000 or more for a defined benefit plan. If you have many employees you may still have a pension plan but need to be sensitive to the type of pension plan you choose. The pension will have certain costs associated with it for your employee's - you cannot discriminate – if you're making contributions for yourself, you'll likely need to make contributions for the employees. Small employers are well served by pension plans as they give you much needed tax deductions, reward employees with money you would have otherwise paid in income tax and help you secure your future.

The 401(k) and 403(b) have the option of employer contributions and employee contributions to bring the total contribution for the plan, per person up to $42,000.00. For employers who are knocking the cover off the ball they can also establish a defined benefit plan where the contribution limits are only dictated by how much retirement income we can fund for in the formula - $170,000 for tax year 2005. This type of plan can actually allow income tax deductions in excess of your income - that is not a misprint - reread it. You'll actually have no taxable income with the right situation and implementation of the defined benefit plan. You can also put life insurance in many pension plans - having uncle Sam and aunt Rell pick up a third or so of your premiums is always a good thing.

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# Noteworthy News ! ! !

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Our deepest condolences to the Clarke & Gagnon families on the passing of Holly - a young soul. She leaves behind 3 young ladies who are now being cared for by a loving uncle and family.

Our deepest condolences to the Lindquist family - a tremendous loss of a young 32 year old soul - leaving behind mother and a two year old son.

Congratulations to Carol Baumann on her recent retirement - time to enjoy the golden years and spoil the grandchildren.

Congratulations to Janaura Sarra Bishop on her recent purchase of the business she's been running, Infotree Web Services.

Congratulations to Paul & Sharon Ezzo on their retirement and move to Pennsylvania. Enjoy the Amish countryside.

Congratulations to Laurie Danaher on graduating and getting a job as a nurse at UCONN medical center.

Congratulations to Paula Ruth on her recent retirement from the state.

Congratulations to Dave & Denise Pasquallichio and the crew at Nuchies on 30 years in business - January 5th will mark the 30th year of operation.

Congratulations to Bob Nilsson and the A.N. Designs crew on their new building in Torrington.

Congratulations to Lew & Jill Hutchinson and the Invisions crew on their new building in Middlebury.

Congratulations to several members of our financial planning family who have recently been visited by the stork. There are many rugrats currently in incubation across the region ready to terrorize their parents in 2005.

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they do and don't do. Term insurance, as the name implies it is intended for a specific term in time, typically one, five, ten, fifteen, twenty or thirty years. The price can be level or increasing periodically - as the policy renews. This is great for needs that are finite - paying for a loan, transferring a business, protecting a college education, etc. Term is initially very cheap but ultimately unaffordable when you'll statistically need it. Now there is Universal life - it combines term insurance costs with a "side fund" which will accumulate over time. There are some moving parts here where the policy can dissolve (we call it explode) as you age based on what you are putting in, how the insurance and administration costs rise and what the interest rates are. Riders can be added to these policies to guarantee they'll never expire or they'll be paid for at a certain point or all at once. Be careful here - use only top rated companies and use conservative assumptions. Variable Universal Life is very much the same but the investment options are yours to choose. The same warning applies - choose solid companies with a history of doing the right thing - choose smart investments here too - they'll make or break you. Now there is Whole Life - as the name implies good for your whole life. No moving parts here - premiums are fixed, cash value is fixed and death benefit is fixed. Two types of firms issues these policies - stock and mutual - stick with the mutuals. If dividends are paid (mutuals only) they'll increase overall policy values. All of the non term policies can have "riders" that add various benefits - always add waiver of premium and typically avoid AD&D (accidental death & dismemberment). The decision of what type of policy to use is predicated by how long you want to have it and what your exit strategy is - how will you ultimately spend your money and pass your estate on to the next generation. Most people need both types and the wealthy need permanent. Call the office to have this conversation

## Money Quiz

Congratulations to Barb Donias who won lasts month money quiz. After working hard and getting the answer correct, she hasn't claimed her prize, please call. The actual income in 2002 & 2003, both in 2003 dollars was $43,318 & $43,381. Not much of a change as the price of energy and food storm ahead.

This month's challenge is to tell me what the national debt was in 1940 & 1999, in their respective year dollars. The first correct answer will win a free dinner or a free massage, your choice.

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## Identity Protection

Get a copy of your credit report and dispute inaccuracies immediately, contact the following:

| | | |
|---|---|---|
| Equifax | www.equifax.com | 800 685 1111 |
| Trans Union | www.transunion.com | 800 888 4213 |
| Experion | www.experion.com | 888 397 3742 |

Remove your name, phone and mailing address from marketing lists: www.the-dma.org

Stop credit card offers from coming in the mail 888 5OPTOUT

If you're going away, put your mail on hold by calling the postal service 800 275 8777.

Don't carry social security cards or PIN #'s in your wallet or purse. Shred all documents you discard that may have sensitive info on them.

## Sharing Profits ?

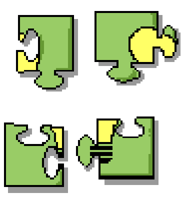
Since the 2003 tax law change giving dividends preferential tax treatment, many corporations are beginning to give more profits back to shareholders. In the last few years dividend payouts have declined to record lows and have recently changed the tide and began climbing upwards. Dividends are an important component of total return, responsible for 4.3 of the 11.31% return of the DOW from 1929 to 2002. This is the right thing to do as when corporations are armed with too much cash that they don't have a good use for they tend to do a few stupid things, namely excessive compensation, excessive cash in low rate accounts and poor capital investments. Here is an industry by industry outlook of what's been going on with dividends in the past few years:

| Sector | Annual Dividends | Yearly Change |
|---|---|---|
| Financials | 51 Billion | 34% |
| Consumer Staples | 21 Billion | 16% |
| Health Care | 20 Billion | 6% |
| Industrials | 20 Billion | 12% |
| Energy | 14 Billion | 6% |
| Telecom | 12 Billion | 11% |
| Consmr Discr. | 11 Billion | 5% |
| Utilities | 11 Billion | 3% |
| Info Tech | 7 Billion | 95% |
| Materials | 6 Billion | 7% |

We're not talking about chump change here. The higher dividends provide a current return to investors regardless of stock performance - current dividend levels of around 2% are well below historical averages. Hopefully, they'll keep heading north.

## Inspirational Quotes

- If you have the ability to reach, the top is always vacant, author unknown
- The fearless are merely fearless, those who act in spite of their fears are truly brave, author unknown
- The greatest pleasure in life is being able to do what someone else told you you'd fail at. I'm a strong enough person to accept failure, but I'm not strong enough to handle not trying, author unknown
- Love is a gift from heart to heart, And it's not restricted to those who are smart, because only when you are in love you can act like a fool without giving a darn, author unknown



## Bypassing Probate

The painful process of getting assets from one person to another can be virtually eliminated with the correct planning. Assuming a couple who both have savings or investments there are two types of accounts that can be transferred without probate. If you have a joint account that is titled "John & Mary Dough, JTWROS (Joint Tenants With Rights of Survivorship)" that account goes right to the other person, skipping go, probate and $200.00. If the account is "John & Mary Dough, TIC (Tenants in Common)" that account needs to go through probate. This sounds bad but is necessary for those with assets to successfully implement estate planning techniques. Now let's look at someone with an individual account. There are ways of using that account to avoid probate, by adding a POD (Payable on Death) or a TOD (Transfer on Death) language to the account. These are essentially beneficiary designations as you have in IRA's and insurance. You can name anyone you like in any percentage you like. These are smart planning techniques that can be used to make your planning as smooth and pain free as possible. If you or anyone you love would like more info, call the office for our probate reduction kit.

If anyone you care about would benefit from receiving this newsletter, tell us who they are and they will be included on our mailing list. I'm sure they'll appreciate you thinking about them and having their best interests at heart.

Name______________________________________________________________

Address____________________________________________________________

City _______________________________State_____________Zip Code_______________

Name______________________________________________________________

Address____________________________________________________________

City _______________________________State_____________Zip Code_______________

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