



Horton Financial Services, LLC

Insights about financial choices

Volume 2, Issue 2
March—April 2004

Financial Choices

TM

In this issue:

Lead Story: Boomers' Security

Baby Boomers are frightened by remarks by Federal Reserve Chairman Alan Greenspan, and they should be concerned about their Social Security benefits.

Frankly, I have been concerned about Social Security benefits for the last forty years, which led to a practice of planning for retirement with clients without social security, and programming it into the scheme of things once benefits begin paying. This method worked out well for most clients.

2003 ECONOMIC COMMENTARY

The domestic equity markets closed 2003 dramatically higher, and year-to-date returns for 2004 are giving clear indications that we are well on our way to recovery from the difficult down market we endured between 2000 and early 2003.

Results for 2003 are especially encouraging when we consider that the year included more corporate scandals, the discovery that many mutual fund companies were providing preferential treatment to large clients, and the ups and downs of our war against terrorism at home and abroad. This recovery is a tribute to the underlying strength and resilience of our economy and the companies and people who drive it.

Under the current system, Social Security is projected to pay out more in benefits than it will collect in the year 2018. The "pay-as-you-go" system will need to either increase contributions, reduce benefits, or some combination of both. Ideally, we would have more workers making contributions into the plan, but the trend is fewer workers to retirees.

The average monthly retirement benefit is currently \$880. A person retiring at 65 that lives twenty years receiving this amount (without adjustments) has a net-present-value of \$133,342, about



Raymond C. Horton, Sr.

55% of the current maximum benefit's net present value of about \$242,440.

It is a sizeable potential asset to either receive or lose. We should plan without it, and if we get it, there will always be good uses for the extra income.

Tax cuts, productivity, increased sales, inflation under control, prime interest rates remaining low, job growth beginning to appear, and consumer confidence all seem to be working together for the U.S. economy to provide the economic recovery.

Could it be better? Absolutely! The massive and growing deficit is worrisome, but in theory the tax cuts will stimulate future growth to deal in large part with the deficit. At least, I hope it will work that way. Some say tax hikes.

While 2003 was a good recovery year in capital markets; don't expect 2004 to be quite as strong.

- Boomers' Security
- U.S. Economy
- By the way...
- Asset Allocation
- Did You Know?
- The Unholy Triangle
- SEC Disclosure Plan
- Hot Ideas!
- Costs of Health Care
- IRA Distributions
- Time to Re-balance?
- Our Practice
- Jobs
- The Cost of Dying
- For CPAs Only

"In the end, it pays to have the best in the beginning"...
Anonymous

Points of Interest.....

- What is Social Security worth to you?
- The recovery is real
- Lower mutual fund fees
- Allocating your assets
- Not so trivial facts
- Don't be a victim of The Unholy Triangle
- Is SEC on right track?
- Some thought-provoking ideas.
- Highest cost health care
- Considering an IRA distribution?
- A strategy for growth with a fund portfolio.
- Points favoring Variable Annuities.
- Jobs are growing
- It can cost a lot to die
- CPE for CPAs

By the way...

A research analyst, Lucas Garland, at Lipper, Inc., a firm that tracks the mutual fund industry, predicts lower mutual fund fees in the wake of investigations about some funds giving preferential treatment, particularly with respect to market timing, to some of their larger shareholders. Currently, fees average 1.48 percent on stock funds.

Asset Allocation

“Asset Allocation” isn’t a new concept for diversifying and potentially strengthening one’s investment portfolio, but more of an evolutionary concept. The latest trend is to own a mutual fund designed specifically for the strategy whose assets are other mutual funds, whose assets, in turn, are equity and debt holdings of hundreds of U.S. and foreign businesses.

The particular mutual fund is managed toward the strategy you have chosen, such as Conservative, Moderate, Growth, or Aggressive models. In any given model, you may be participating in ownership of up to 2,000 companies. This type of fund requires exceptional management to continually research and adjust its holdings in the effort to stay true to the fund’s objectives.

Did You Know?

- That one of every seventeen U.S. citizens visits a Wal-Mart store daily?
- That Federal Reserve Chairman Alan Greenspan’s former occupation was as a saxophonist in the Big Band era?
- One-third of Fortune 500 companies have founding family members in their current management structure?
- European Americans (Caucasian) will become a minority race in the United States by 2050?
- The American male, on average, lives 22 months after retirement, regardless of age at retirement?
- Seventy-five percent of the U.S. population will suffer from a heart attack, stroke, or cancer during their lifetimes?
- Pope John Paul II declared it “immoral” to remove feeding tubes from people in a vegetative state?
- That an Individual Retirement Arrangement (IRA), can form and own a Limited Liability Company?
- More than 2,300,000 persons in the United States have become disabled in automobile/vehicle accidents since 1997?
- Federal transfer taxes at death are diminishing, but increases in state death taxes will offset a part of the reduction?
- In a survey of 300 Chief Executive Officers (CEOs), 45% said they will hire new employees in 2004?
- The National Association of Securities Dealers recently mandated Broker-Dealers send “breakpoint” letters to clients?
- In the absence of a Qualified Sick Pay Plan, continued wages paid to a disabled employee may actually be dividends?
- The accumulation of wealth depends more upon discipline than it does upon income?

The Unholy Triangle?

Sometimes, unwittingly, people will make the spouse, or a trust the owner of a life insurance policy on the other spouse, and make a third entity, such a business, relative, trust, etc., the beneficiary. On the surface this seems okay, but it isn’t. What happens is that it creates a taxable “gift” from the policyowner to the beneficiary, when the insured is not also the owner. Not good! Under normal circumstances, there is no gift or income tax due on proceeds left to a named beneficiary.

In the case of the “unholy triangle”, the beneficiary still receives the proceeds without tax, but the gift tax burden is assessed to the owner of the policy. This becomes particularly onerous when the beneficiary is an out-of-favor individual or entity with the owner of the policy.

A variation of this scenario is when, in a Community Property State, using only two entities in the policy, the owner/insured and the beneficiary. Let’s say, Bill is the owner and insured under a \$1,000,000 policy and that Judy, his wife, was initially the beneficiary. After a dispute with Judy, Bill changed the beneficiary of the policy to Lucy, the new girlfriend of Bill whom Judy does not know.

Do you think Judy is just a little bitter after Bill’s demise to learn that upon filing the claim form with the life insurance company to receive the million dollars, income tax-free, with which to support herself and their six children’s lifestyle, that Lucy is the sole beneficiary of the proceeds?

Lucy receives the proceeds tax-free. Because Judy and Bill were residents of a Community Property State, and life insurance is regulated by the State, not the Federal Government, Judy is deemed to have been half owner of the proceeds by way of being half owner of the policy, which is further deemed to have been given to Lucy. This results in a \$500,000 taxable gift from Judy to Lucy.

Not only did Judy not receive any of the death benefit, she had to pay Lucy for the privilege of giving her half of the \$1,000,000 death benefit. Bill was quite a guy!

How can this happen, you ask? Believe me, some very smart people get caught in financial traps every day that seem innocuous on the surface. Bill probably changed the beneficiary in anger. Further, while venting his anger, he didn’t plan to die. The moral to this story is to “know what you are doing, or know someone that does”.

SEC Disclosure Plan

The Securities & Exchange Commission is considering issuing a new rule that would require mutual fund companies to disclose their practices and methods for preventing abusive market-timing and other measures favoring larger shareholders within their funds.

Some of the mutual fund companies feel this new rule will arm those bent toward cutting corners with information they need to develop new ways of circumventing the rules.

Hot Ideas !

- Review the beneficiary of your life insurance policies. You may have unwittingly created a future gift tax or disinherited a grandchild.
- Insure the “earning power” of the goose that laid the golden egg.
- Don’t insure for potential small losses; insure for potentially big losses.
- Tax avoidance is legal; tax evasion isn’t.
- A good asset protection device for seniors is long-term care insurance.
- Investors working with a professional do better than those who don’t.
- Set aside time for a “financial discussion” each month with your spouse.

The Spiraling Cost of Health Care

The United States spends a larger share of its gross domestic product (GDP) on health care than any other industrialized country. Expenditures for health care represent nearly one-seventh of the Nation’s GDP (13%), and continue to be one of the fastest growing components of the Federal budget.

The current rate of growth in health care costs exceeds other sectors of the economy. The challenge is to hold costs down while continuing to provide the highest quality health care in the World. New ways to contain costs and obtain high value are needed for consumers and investors.

IRA DISTRIBUTIONS

Think of a number between 13 and 15. Now double it. That is about how many different scenarios there can be in distributions from IRA accounts. Quadruple that number and you come up with the approximate number of questions that could apply to IRA distributions. Simple? No. Tedious? Possibly. Applicable to you? You bet!

Not even your weather-worn, seasoned, Financial Services Professional will have all of the answers on the tip of his silver tongue, but he can work through every situation to an ultimate conclusion in your interest. Even so, the applicable tax advice should come from your CPA.

Don’t assume distributions are pre-ordained specifically for you. The law is pre-ordained, but the possible avenues you may travel within the law are varied, often determined by your particular situation, beneficiary, spouse, taxes, income requirements, required distributions, etc.

Because the choices are varied, the most appropriate choice for you may possibly elude you unless you know the options available to you. This is a good reason to review your IRA accounts with a professional who can guide you through the steps to accomplish your individual objectives.

Time to Re-balance?

So, you have a mutual fund portfolio or a variable annuity with sub-accounts, and some have won and some have lost. Realizing all securities have ups and downs, you decide to sell the lower performing funds and put that money into the better performing funds. That makes sense, doesn’t it? No.

It is time to re-balance your portfolio. Let’s say you started off with five accounts and an allocation of 20% to each account, but now they are 26%, 23%, 17%, 16%, and 19%. Being the sharp person you are, you have a professional financial services advisor helping you. Your advisor recommends that you re-shuffle the portfolio so that you once again have 20% in each account. You ask, “why”, and get this explanation:

“By selling off the top of the better performing funds, you are taking your profits. By investing your profits in your funds that have declined in value, you are buying more shares at a lower price. If your best funds turn downward, you have already taken your profits. If your worst funds turn positive, you have more shares working for you. If your best funds continue with positive growth, you are still okay. If your worst funds continue with negative growth, your basis per share is lower than when you started, and positioned for later growth.”

The re-balancing strategy, in theory, helps you grow your account. Re-balancing can be set up to occur automatically at intervals you specify within the investment/management company’s service capabilities.



Insights about
financial choices

Volume 2, Issue 2
March—April 2004

Horton Financial Services, LLC
One Texas Centre 415 Texas Av., Suite 333
Shreveport, LA 71101-3540

Phone 318-222-8600 or 888-897-8800

Fax 318-222-4023 or 888-809-2100

Meeting Financial Challenges Every Day!

WE are on the web.
Visit us at www.HortonFinancial.com

About Our Practice

For almost forty years, we have been helping people solve financial problems. The slogan of Horton Financial Services is ***“Meeting Financial Challenges Every Day”!***

Our firm is paid for distributing insurance and investment products, but the nature of our business is ***“planning”***, working with each client, one at a time, to help them achieve certain financial objectives.

We have never focused upon our personal income, but upon doing the right thing for the client, always considering the income a by-product of our service.

We have impacted over 2,000 lives in a positive way over the years, and continue to grow our business one client at a time, typically upon referral from existing satisfied clients and contract holders.

Our pledge to you is that we will always strive to do the right thing for you, and to merit your trust and confidence.

For CPAs Only

A ***“continuing professional education”*** (CPE) two-hour seminar will be presented on “412(i) plans”, William H. Black, Jr., President of 412(i) Plans, Inc., presenting the timely program free-of-charge on Wednesday, May 26, 2004 from 11:00 a. m. until 1:20 p.m. (including lunch) in the first floor conference room of sponsor, Horton Financial Services, LLC, 415 Texas St., Shreveport, LA. **RSVP 318-222-8600.**

Sources include:

- Wall Street Journal
- Fox Financial News
- The Shreveport Times
- Dow Jones
- National Assn of Ins. & Fin. Advisors
- American Health Insurance Assn.
- The Associated Press
- The National Underwriter
- Million Dollar Round Table
- Denver Rocky Mountain News
- Accident Facts
- Editorial knowledge

JOBS

The U.S. Department of Labor reported more than 300,000 new workers were hired in March. This number far exceeded expectations, and turned out to be the largest number of hires in a single month in four years.

The jobs picture in March brought the first quarter total to some 513,000 new jobs, adding more credibility that the U.S. economy is advancing. However, economists want even more evidence to feel the expansion is sustainable.

Often, one of the prices to pay for rapid expansion is a rise in interest rates. We are seeing a little upward movement in interest rates for home mortgages, while some fixed interest rate retirement products are still continuing to drop. My feeling is that rates will bounce around near the basement and rise only slightly by year-end.

Another notable factor in the March jobs growth is that the expansion came from almost all sectors of the economy, signaling a balanced growth, with construction, retail and health care leading the way.

The Cost of Dying

Most of us think we will just leave our assets to our spouse and/or family, and that will be that. Hello??? Surprise! Uncle Sam has a first lien on those assets in terms of Federal Estate and Gift Tax, Capital Gains, and Federal Income Tax.

Since the Estate Tax exemption has been steadily increasing each year, and now sits at \$1,500,000, some of the States have begun increasing their State Death Taxes, seen as an opportunity for the coffers of State Treasuries.

We don't generally give consideration to Capital Gains Taxes at death, but the IRS does. Hopefully, most will be long-term and taxed at the lower rate.

Also, if we have earned income during the year of death, the IRS wants their fair share of that too. It could be your last tax return, but not necessarily.