Financial Foresight

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Financial Planning: Common Errors and Lost Opportunities

Over the years in doing financial plans for clients, I have come up with a list of shortfalls and missed opportunities that many people are unaware of. These mistakes can cost clients not only time and money, it can put your financial goals at risk. While every client is unique, most plans have one or more of the following issues:

Buying Life Insurance through Work

Unless you are in poor health, you should generally not purchase term life insurance through your employer. Here are three reasons you should purchase your own plan:

1. *The rates are lower.* With your own plan the insurance company is able to screen out high risk clients, giving you a rate that reflects your lifestyle and health. You avoid being grouped with all your coworkers.

2. *Lock in the term.* With your own policy you can lock in a set period of time such as 10 or 20 years. With company plans you will lose your coverage if you lose your job.

3. *Rate lock.* With your own plan rates are set for the term of the policy. With employer plans rates can go up each year due to your age bracket and general rise in rates.

Not Having Disability Insurance

The inability to work could devastate your finances. Disability insurance can be more important than life insurance. If you are disabled, you still have your normal expenses plus new expenses to care for your disability. At age 42, it is four times more likely that you will become seriously disabled than that you will die during your working years.[1]

Not funding a Roth IRA

In my opinion, the Roth IRA is one of the best investment vehicles available. Most importantly, this IRA grows tax free. In addition, prior to retirement, you can withdraw the principal without paying taxes. After age 59½ , you can withdraw the entire balance tax free. Roth IRAs have low fees, investment flexibility, and no required minimum distributions like other IRAs at age 70½. For 2007, you can invest up to $4,000 ($5,000 if you are 50+). Don't wait. You only have until April 15 of this year to fund your 2007 Roth IRA. The maximum contribution for 2008 rose to $5,000 ($6,000 if you are 50+). You can fund a Roth if you have adjusted earned income of up to $166,000 for 2007 and $169,000 for 2008. Check with your accountant to see if you qualify to make a contribution.

Not Funding an HSA if You Qualify

Not only are contributions to your HSA tax deductible, they also grow tax deferred. Withdrawals for health reasons are tax free and penalty free before age 65. (If you withdraw money prior to age 65 for non-health reasons, you will pay a 10% penalty plus ordinary income taxes.) After age 65, you can withdraw earnings for non-health related reasons without the 10% penalty but you will pay normal income taxes. To fund an HSA you need to have a high deductible health insurance plan defined as $1,100 for an individual and $2,200 for a family plan. Contributions may be made of up to $2,900 for individuals and $5,800 for family plans per year. (For those age 55+ you can contribute an additional $800 per year.) Contributions for the previous calendar year may be made up until April 15th. These accounts can be invested for growth or safety.

Not Updating Your Estate Planning Documents

Estate planning documents including wills, trusts, beneficiary forms, and living wills among others, should be reviewed from time-to-time and especially with a change in your family status. Divorce, marriage, children, changes in health, and inheritances are good examples. Do your wishes on your will or trust match up with what you have stated for your IRA beneficiary? Did you set up a trust but not fund it? If you have multiple children/beneficiaries, have you and your spouse or partner thought about what would happen if all the assets went to the surviving spouse? Could some of your beneficiaries be inadvertently left out of your estate? All good reasons to consult with an estate planning attorney.

Not Considering Long Term Care Insurance

The need for long term care can put serious stress on almost any family's finances. Long term care can cost $75,000 or more a year. How long could you pay that bill? Would there be any money left over for your spouse or children? LTC insurance helps you pay for the costs associated with long-lasting or chronic illnesses. Plans are getting very creative and may have some tax benefits.

Not Saving for College

For parents or grandparents looking to save for college, many states offer tax credits for setting up a plan. Vermont offers up to a $500 tax credit for each child. To take full advantage of this credit, a married couple must save at least $5,000 per child within the calendar year. This credit can extend to grandparents and extended family as long as they are the account owner. Many clients are overwhelmed by the estimated cost of four years of school. Even saving $200 per month for 18 years, assuming an 8% annual growth rate, would net $96,017.

Buying Variable Annuities

This product is often pitched as a great product to save on current taxes. The tax deferral benefit gets more than eliminated by high fees, penalties from the insurance company and the government for early withdrawal, higher tax rates on gains compared to long term gains on stocks and mutual funds, and loss of step up basis for your beneficiaries. Commission rates of 7%

or more can bias a sales agent's judgement and may not be in your best interest.

Buying Equity Indexed Annuities

Agents will promote this as a product that will participate in the upside of the stock market without the downside risk. The problem is that the cost of this insurance along with a host of other fees, higher tax rates on gains, and penalties for early withdrawals or not annuitizing, combined with the steep commission (that can reach 15%) is likely to result in modest performance at best. Meanwhile, your money is tied up for 7 to 15 years. There are better options available for clients looking to avoid risk. With $100,000 to invest, you could buy a 10 year government zero coupon bond for $69,990 today that would mature at $100,000 in ten years. Take the remaining $30,110 and invest in a low cost index focused on dividend paying stocks in the U. S. and internationally. Even if the market only returned 3% per year over those ten years the $30,110 would grow to $47,343. Your total investment would then be worth $147,343. With this strategy you have incredibly low fees, access to your money without penalties, step-up in basis for beneficiaries, clarity, lower tax rates, and the ability to lock in gains before maturity.

Not Reviewing Your Plan or Finances

Many people do not know what they have, what their goals are or how much they are spending. A plan is like a roadmap to help you organize your finances and make sure your goals match up with your strategy.

Not Reviewing Your Credit

It is a good idea to check your credit at least annually to make sure your information is accurate. This may help catch any identity theft issues and may enable you to improve your score. A low score could result in higher interest rates on loans. Go to www.annualcreditreport.com for links to the three reporting agencies.

Not Reviewing Your Home and Auto Insurance Coverage

Have your coverage limits kept up with your home value? Are your deductibles set at the right level? Have you compared your current provider with other companies? Often times, I have had clients save 25% or more while improving their coverage.

Timing the Market

Are you waiting for the perfect time to get into the market? Sure, it would be great to buy low and sell high but the reality is that this is unlikely to happen and the opposite may occur. History always seems to repeat itself with many investors tempted to purchase at the peak of the market and sell at the bottom.

Give yourself peace of mind, save money and taxes, and reduce your risk. These can be achieved by using this list as a starting point. You may be surprised by all of the steps you can take toward making your goals a reality. If you have any questions or would like to discuss any of these topics please contact me directly.

[1] "Why Disability" booklet, by National Underwriter.

Retiring Talk Show Host Reminds Us: Not Only Elders Need Long-term Care

Montel Williams was diagnosed with Multiple Sclerosis in 1999. Earlier this year, CBS reported that this season of his daytime talk show, the 17th, will be the last. The reason is the declining health of the host.

His story is a teachable moment for long-term care planning. The lesson is this: none of us knows when our health will change, and we don't tend to get healthier as we age. Mr. Williams is 51 now, which would mean he was only 42 years old when he was diagnosed. A diagnosis of MS makes it next to impossible to get long-term care insurance (some workplace policies may offer some coverage to employees who are actively at work during a specific enrollment time, even if they are otherwise uninsurable).

Like another famous entertainer, Christopher Reeve, Mr. Williams' health changed for the worse at an age that he had no reason to expect that it would. By all appearances, Williams was someone who was fit, healthy, and physically active. He is a veteran and a graduate from the United States Naval Academy.

Christopher Reeve needed many years of long-term care before he died. While no one can know the future, it is likely that Montel Williams will also need extended long-term care. MS, in William's own words, "…(means) excruciating pain and that eventually I could lose control of my body. " MS is a potentially debilitating autoimmune disease that affects the brain and spinal cord.

Although celebrities may have the resources to weather the financial consequences of extended long-term care, most Americans find the financial implications can be devastating.

As Reeve's story and Williams' situation demonstrate to us, our best intentions to buy long-term care insurance in the future may be derailed by a health change at a relatively young age. There are many Americans who will need long-term care well before age 65, and even before age 50. The causes are many, from brain tumors to car accidents to debilitating illnesses such as MS and early Alzheimer's.

Since illness or injury can strike at any age, purchasing long-term care insurance by age 50 or even age 40 may be a very smart financial decision.

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