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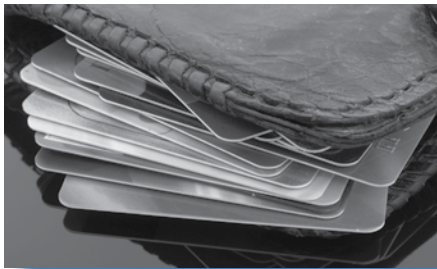
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Control: Self and Debt

Recently, the Federal Reserve put out a scary figure: Americans have accumulated almost \$1 trillion in credit card debt (or what they term “revolving credit”) and that figure has helped catapult the U.S. overall savings rate into negative percentage territory.

Many people, according to the research literature, are unable to control this form of debt since people view paying it off as a sort of “self-denial.” Well, it may appear that way, but it is



not: paying off high-interest credit card debt now is actually going to allow you to spend more in the future. Isn't that what we look forward to doing as future consumers?

Where do you stand in the U.S. credit card economy gamut? Well, simply compare your credit card debt to the average American balance: almost \$9,000. Maybe it's not you who has that kind of debt, but it might be an adult child or friend. Here are some ideas:

While a \$9000 debt is not so staggering to most people, the more important item to remember is that the credit card companies want consumers to continue

Saving . . . and the Intention To Do So

Most research on the psychology of saving tends to compare groups of savers and non-savers and not give much consideration to their INTENTIONS.

So what happens when the researchers look at the relationship between saving INTENTION to actual savings?

The research finds that three factors come into play: time horizon, usage of certain expenditure control techniques and perceived “ease” of expenditure control. In several recent tests (the 2007 DNB Household Survey and a questionnaire survey held in 2005), two groups of respondents were compared: those who planned to save and implemented the intention (the “plan-and-do” group) and those who planned to save but failed to realize the plan (the “plan-in-vain” group). The data support the significance of time horizon and control techniques while the third factor (perceived “ease” of expenditure control) received mixed support.

The successful savers differed from the failed savers in “time horizon”: the time they said was most important to them tended to be further in the future. The successful savers also used effective techniques to control their spending, such as setting up an automatic transfer of funds into a saving vehicle. All techniques used by the successful savers had one thing in common: they made the saving process partly automatic and less dependent on will power.

Of particular note: the researchers predicted that people who THOUGHT saving would be easy would turn out to be more successful at saving, assuming that their confidence stemmed from having good self control, but actually, perceived easiness of saving was not related to saving success or failure.

paying it off slowly: if one were to pay the minimum amount (usually pegged at 2 percent of your balance) each month with a percentage rate of, say 16 percent, it would take almost seven years to pay it off and the total payments would amount to almost \$15,000 for the principal and interest (paying it off at about \$180 per month).

While the current “common” advice is to pay off the debt with the highest interest first, it might be a good idea to

get a few successes under the belt and pay off some smaller debts first, even if the interest rates are lower.

If the debt is cumbersome and cannot be alleviated by cutting expenses, then more income might be a solution.

Also consider the advantages and disadvantages of switching from “unsecured” to “secured” debt — what happens when you switch credit card debt to your home mortgage through, for instance, an equity credit line. ■ ■ ■

Questions & Answers

Q. I have a retirement portfolio worth about \$500,000. About \$100,000 of that amount is nondeductible contributions. If I withdraw, say, \$50,000, could I consider that amount part of that nondeductible \$100,000 and pay no taxes?

A. Sorry, but "No."

The IRS thought about that, so any money that is taken out of an account where pre-tax and after-tax money is mixed, the withdrawal is considered to be a combination of the two. In other words, since 80 percent of all your money in the IRA is in deductible amounts, you will be required to pay taxes on \$40,000 of your withdrawal or distribution. Even if you have separate accounts for your IRAs, the *pro rata* requirement still applies, since you must include the amounts of all your traditional IRAs when calculating taxes on withdrawals or distributions.

Q. If you were to pick one important thing for a parent to do when it comes to helping their kids get into their chosen college, what would it be?

A. No doubt it would be to file early for your college's free money and the all-important FAFSA form (by the way, that stands for: Free Application for Federal Student Aid).

Many colleges require that you fill out not only the FAFSA, but also their finance office's application. Every college has its own deadlines, so be sure you check them out well in advance. We hope you are talking about a high school junior or senior at this time of the year, since the deadlines are way past for the 2008 - 2009 school year.

You may also want to check out the potential of filing both those applications ON LINE, since it saves so much time and energy. Last year, ninety-four percent of families who filed a FAFSA did so on line.

We will accept questions from readers and reprint selected answers in this column. Send your question(s) to us; we'll answer as many as we can.

Financial Notes Worth Noting

Some Advancements in the Social Security Financing Outlook; But Deficits Continue

The Social Security Board of Trustees recently released its annual report on the financial health of the Social Security Trust Funds. While the key dates for program costs exceeding tax revenues and Trust Fund exhaustion remain unchanged, the 2008 Trustees Report shows improvement in the projected long-term financial status of the Social Security program from last year -- particularly in the latter half of the long-range projection period. This improvement is principally the result of methodological changes for projecting certain aspects of immigration.

- The projected point at which tax revenues will fall below program costs comes in 2017 -- the same as the estimate in last year's report.
- The projected point at which the Trust Funds will be exhausted comes in 2041 -- the same as the estimate in last year's report.
- The projected actuarial deficit over the 75-year long-range period is 1.70 percent of taxable payroll -- down from 1.95 percent in last year's report.
- Over the 75-year period, the Trust Funds would require additional revenue equivalent to \$4.3 trillion in today's dollars to pay all scheduled benefits.

"Social Security is at a crossroads. We face enormous challenges to shore up the system," said Michael J. Astrue, Commissioner of Social Security. "I . . . look forward to working with the next administration, since the challenges that face the Social Security system will undoubtedly require a bipartisan and multi-year effort."

Other highlights of the Trustees Report include:

- Income including interest to the combined Old-Age and Survivors, and Disability Insurance (OASDI) Trust Funds amounted to \$785 billion (\$656 billion in net contributions, \$19 billion from taxation of benefits and \$110 billion in interest) in 2007.
- Total expenditures from the combined OASDI Trust Funds amounted to \$595 billion in 2007.
- The assets of the combined OASDI Trust Funds increased by about \$190 billion in 2007 to a total of \$2.2 trillion.
- During 2007, an estimated 163 million people had earnings covered by Social Security and paid payroll taxes.
- Social Security paid benefits of \$585 billion in calendar year 2007. There were almost 50 million beneficiaries at the end of the calendar year.
- The cost of \$5.5 billion to administer the program in 2007 was a very low 0.9 percent of total expenditures and the combined Trust Fund assets earned interest at an effective annual rate of 5.3 percent in 2007.

The 2008 Trustees Report is posted at www.socialsecurity.gov/OACT/TR/TR08/.



Quotable Quotes

Money is better than poverty, if only for financial reasons. -- **Woody Allen**

College is part of the American dream. It shouldn't be part of a financial nightmare for families. -- **Barbara Mikulski**

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Legacies: Leaving More To Your Heirs Than Physical Assets

There have been lots of stories, recently, in the general media about people who leave substantial assets to heirs with certain strings attached. One article in the *Wall Street Journal* talked about the perceived need identified by a multimillionaire to ensure that his children not be provided with vast sums of money as soon as he met his end. He created trusts that provided his estate to his heirs in stages, so that they would not “become complacent” or any of the other adjectives he might have given for lazy and satisfied with receiving large sums of cash from him.

Through these techniques the multimillionaire was certainly sending a message to his heirs that he expected them to “work” for a living and not to simply depend on his hard work and cash for their living expenses. These types of techniques have been around for years and are easily available through various estate planning techniques.

Besides sending the message of “you are not getting all my money right now,” it also implicitly sends a message of the need to create one’s own wealth and not simply depend on the “capacity,” “luck” or “means” of another.

But something that hasn’t received a lot of press is the idea of legacy bequests: letting your children and grandchildren know, in no uncertain terms, what you hold to be important, dear and cherished in your life.

A legacy, according to a dictionary definition, refers to any gift by will, especially of money or other personal property, or (and here is the definition in the context of the present conversation), something transmitted by or received from an ancestor or predecessor or from the past, as in “the legacy of ancient philosophers.”

So, what we are discussing here is ideas, concepts and, yes, maybe even behaviors, that you cherish and want to ensure that your progeny understand as important and worthwhile.

How do we do that? Well, first, we actually do it all the time as parents and grandparents, aunts and uncles, older sisters and brothers: by example, we show and provide a “role model” for our heirs and descendants. By the way we respond to certain ethical dilemmas and actions, by the way we treat our children and grandchildren after witnessing a burning question in their lives or, even on a

television show or in a play that we see together or when commenting about the behavior of others that we know or famous people in the news.

We are constantly informing our heirs, in explicit and less than explicit ways, how we feel about race, creed, religion, moral attitudes and other ethical and life-affecting attitudes.

But those events and

those “implicit” opportunities are haphazard and may not ensure that our heirs understand fully what we mean. Our legacy might be better offered to them in hard, fast and specific formats that leave little to the imagination.

How To Transmit Your Philosophical Legacy

As we were doing research for this article, we came across a story of a fellow who was very “close” to his father. After his father’s passing, he was quite disappointed that there was nothing in his father’s belongings that was specifically written to him. He thought for sure that there would be something he could refer to that would be directly from his father’s hand, expressing his theories about life, the pursuit of happiness or something of that nature.

While we are not sure that everyone would enjoy “finding” something like that, we are sure that most everyone who found “a something like that” were it available, would read it and take it to heart.



On Writing Your Legacy

1. Reflect and reminisce. Going through an old photo album might help.
2. Compose a list of life events that taught you something.
3. Write a story about them.
4. Reflect on friends; what are the characteristics? How did you show friendship?
5. List mistakes and what you learned from them.
6. Jot down ideas from happy and sad times. What made them so? How did you react?
7. Write about the future and what you hope it will be like for your children and grandchildren.

Everyday Financial Strategies

Preparing Our Children For Financial Competence

We asked lots of parents regarding how much THEIR PARENTS informed them about financial matters and a whopping 60 percent said that they received NO financial education from their parents. When asked about what they learned in school about handling money, the most they can remember was dealing with how to ensure they got the right change from the cashier — and that was in elementary school!

So, if parents can remember very little about “being taught” by THEIR PARENTS about how to deal with financial matters and yet there are precious few other sources for that information, then guess what? Our kids may be hardly informed at all!

Whether we speak specifically with our children about financial matters, they see, in many instances, how we deal with them. Do we sometimes argue about expenditures? Is one parent in the family a “spender” and the other a “saver?” Do the youngsters overhear conversations about credit, bill-paying, etc? What happens when the subject of how much to contribute to a certain charity comes up? Depending on how they are dealt with, our children learn from those interactions.

How can we, then, as responsible parents, ensure that our children grow up with at least the BASICS about money, saving, investment, etc? Here is a list of ideas that you might consider as you prepare to reach that goal:

1. First and foremost, we need to be open about family finances. Now, this does not mean that children need to be privy to every financial decision that is made in a household, but if they are even slightly involved, for instance, in the family budget process, they will learn about trade-offs and other negotiations that allow family financial matters to get settled. One family we know sat the kids down and, with monopoly money, approximated the family's monthly income and had each child take a turn paying taxes, the cable bill,

the gas and electric bill, the mortgage, groceries, entertainment, etc. Another idea to bring the family into important decisions: does the fancy vacation take place this summer or should that money be set aside for the **ultra-fancy vacation** NEXT summer?

2. Encourage children and grandchildren to save by setting an example and providing incentives.

Work on goal-setting. One family we know works toward putting aside some money every month for a specific family goal, tracking progress, experimenting with different ways to make the goal-reaching more exciting (and fun) and, ultimately, sharing in the goal's fruition when it is achieved.

It is also important to distinguish between saving and investing, compound returns on investment and the important difference between long- and short-term goals like retirement / higher education or the flat screen TV.

3. Allowances are an important way to teach children about managing money. On a small scale (and, usually without disastrous consequences if not done well), the child's allowance is like a paycheck for an adult family member.

Some advisors feel that allowances should NOT be attached to chores or other household activities based on the assumption that children should be required to assist in the activities of a household without having a monetary reward attached to each task. Others theorize that using an allowance as a payment for household duties teaches young people that there is no “free lunch.” Another alternative might be to find some middle ground with a basic

allowance and a “consulting fee” for additional duties over and above the required tasks.



A *Consumer Reports* survey once showed that children who receive a regular allowance were more likely to save money and donate to charity. We leave that decision to you.

4. Teach youngsters about the proper use of credit. Children must understand, as we do, that credit cards do not equate to free money and they

ought to understand how interest accrues when credit cards are not paid off by the end of the grace period.

5. Ensure that your children think about alternatives. For instance, if you have an impassioned spender who wants to buy everything s/he sees, provide an alternative: show the difference between those single pieces of candy and the whole box (usually a substantive difference in price). This is especially apparent at the “big box” stores.

6. Finally, force them to make decisions. “You may have x or y, but not both. Make up your mind.”

Believe it or not, these little humans will grow up, have families of their own and will recollect the money management tools they got from you. Give them your time, a respect for the value of a dollar, the idea that they have to work for what they get and a saving /investing mentality and they will be vastly more likely to grow up as decent money managers.

They may not be particularly thrilled with the ideas now, but they will thank you in the future . . . for sure.