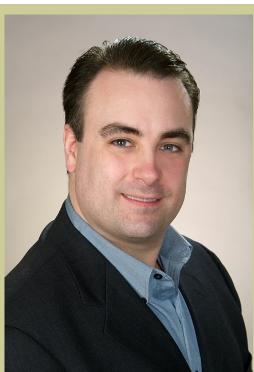
Nicholson Financial Services

Did You Know...?

Fall 2008



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I hope that everyone had a safe, happy and healthy Thanksgiving. I always look forward to the Holidays, but this year even more so as I can not recall a more difficult and draining one out of 15 years as a financial advisor. I have had many, many concerned and even panicked phone calls in recent months. It is to be expected as this environment has been maddeningly irrational. Any investor would have to be officially brain dead to not be concerned. However, I still have not had one client call in a panic and sell everything. I commend you all for such prudence. As I say in my commentary to the right, we couldn't see this coming, but we can think rationally and work our way through it.

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Ask the Experts

RAYMOND JAMES
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A tougher year than we thought...

Going into 2008 it was apparent that we were going to be in for a more difficult environment than we had seen in the prior handful of years. However, none of the forecasts and projections for the year predicted what has happened over the past couple of months. We encountered a "perfect storm" of financial events that caused a market sell off unlike anything that anyone has seen in decades. Should you or I or anyone have seen it coming? I don't think it was possible. Investors and advisors alike make the best decisions they can with the information available at the time. In rare occasions such as this one, some of that information can be flawed. In talking with friends who were, until recently, with Lehman Brothers and Merrill Lynch, they had no idea how deep those companies were into the subprime mess until they learned the fate of their firm's at the same time we all did.

My take on this sell-off is that it had more to do with forced selling by institutions than with individual investors panicking. The credit crisis caused an environment where corporations and other institutions needed to raise cash by any means necessary as they could not borrow as they had been. This meant selling stocks, funds, bonds, loans, etc. for less and less just to get the cash now. I continue to believe that this will be a short-term event. As I look at stocks on a company by company basis, I see many of them with the lowest valuations and highest dividend yields that I have ever seen. Where do you think that all the money that has poured out of the equity markets over the last couple of months is going to go? There are record amounts of cash sitting on the sidelines right now. My belief is that it will go back into the equity markets. Why?
Consider the options. Money markets are paying less 1/2 % or less, CD and bond rates continue to drop, and the Federal Reserve has left the possibility open that they may cut rates again in January. Meanwhile, the dividend of the S&P 500 Index was just recently higher than the dividend yield on the 30 year Treasury Bond for the first time since 1958. Is that logical? I don't think so, but it exemplifies how oversold the market is.

The one thing that all bear markets have in common is that they end...and my belief is that this one will too. The great J.P. Morgan (the man, not the company) once said: "Remember, my son, that any man who is a bear on the future of this country will go broke." I think that is especially appropriate now as more bets have been placed against the US economy and markets in the last year than for it. However, just as Morgan stated so many years ago, I would not want to bet against the people of this country and our ability to recover from a crisis.

I spend a lot of time listening to conference calls, webinars, and the same news media that many of my clients do. I hear many economists and market strategists who are cautiously optimistic about next year. What I do not hear from anyone is that 2009 *could be* one of the biggest "up" years in decades. Would it surprise anyone? The best year in this decade was 2003 as the market dug itself out of the hole it went into in 2002, but 2008 has been worse than 2002. Although it is impossible to predict the future, I believe that this environment has created many opportunities for investors. The chief market strategist at my former firm used to say "the best time to buy stocks is when it turns your stomach to do it." I think that pretty much says it all.

Should You Roll Your 401(k) Money Over to an IRA?

While the investment flexibility that IRAs provide can be a benefit for some people, it may be a drawback for others.

If you're entitled to a distribution from your 401(k) plan (for example, because you've left your job), and it's rollover-eligible, you may be faced with a choice. Should you take the distribution and roll the funds over to an IRA, or should you leave your money where it is?

Across the universe

In contrast to a 401(k) plan, where your investment options are limited to those selected by your employer (typically mutual funds or employer stock), the universe of IRA investments is virtually unlimited. For example, in addition to the usual IRA mainstays (stocks, bonds, mutual funds, and CDs), an IRA can invest in real estate, options, limited partnership interests, or anything else the law (and your IRA trustee/custodian) allows. (Certain investments may not be right for everyone, and some may have adverse tax consequences, so be sure to consult your financial professional.)

While the investment flexibility that IRAs provide can be a benefit for some people, it may be a drawback for others. If you lack investment knowledge and experience, you may be more comfortable with the limited investment alternatives your 401(k) plan provides.

Take it easy

The distribution options available to you in a 401(k) plan are typically limited, usually to a lump-sum payout, or installments payable over a period of years. And many plans require that distributions start if you've reached the plan's normal retirement age (often age 65), even if you don't yet need the funds.

Similarly, 401(k) plans often require that a beneficiary take a lump-sum payment shortly after the plan participant dies. This may not be a problem if your beneficiary is your spouse--he or she can roll the funds over to an IRA after your death. But a nonspousal rollover is possible only if your 401(k) plan allows it. And some don't, forcing your beneficiary to take a distribution he or she may not yet need.

On the other hand, you can access the funds in an IRA at any time. You--and your beneficiary after your death--can take out as much, or as little, as you want. While you'll need to start taking required minimum distributions (RMDs) after you reach age 70½ (and your beneficiary will need to take RMDs after you die), those payments can generally be spread over your (and your beneficiary's) lifetime. (You aren't required to take any distributions from a Roth IRA during your lifetime, but your beneficiary must take RMDs after your death.) A rollover to an IRA lets you and your beneficiary stretch distributions out over the maximum period the law allows, letting your nest egg enjoy the benefits of tax deferral as long as possible.

Note: *Distributions from 401(k)s and IRAs may be subject to federal income tax. In addition, a 10% early distribution tax may apply if you haven't reached age 59½. (Special rules apply to Roth 401(k)s and Roth IRAs.)*

Gimme shelter

Your 401(k) plan may offer better creditor protection than an IRA. Federal law currently protects your total IRA assets up to $1,095,000--plus any amount you roll over from your 401(k) plan--if you declare bankruptcy. (The laws in your state may provide additional protection.) In contrast, assets in a 401(k) plan generally enjoy unlimited protection from your creditors under federal law, whether you've declared bankruptcy or not.

Let's stay together

Another reason to roll your 401(k) funds over to an IRA is to consolidate your retirement assets. This may make it easier for you to monitor your investments and your beneficiary designations, and to make desired changes. You may also want to consolidate all of your IRAs. However, make sure you understand how Federal Deposit Insurance Corporation (FDIC) and Securities Investor Protection Corporation (SIPC) limits apply if you keep all your IRA funds in one financial institution.

Fools rush in

- While some 401(k) plans provide an annuity option, most still don't. By rolling your 401(k) assets over to an IRA annuity, you can annuitize all or part of your 401(k) dollars.
- Many 401(k) plans have loan provisions, but you can't borrow from an IRA. You only can access the money in an IRA by taking a distribution, which may be subject to income tax and penalties.
- If you were born before 1936, lump-sum distributions from your 401(k) may be eligible for special 10-year averaging or capital gains treatment. A rollover may make you ineligible for these tax rules.

Ten Gifting Traps You Should Avoid

Lifetime gifting can be a powerful estate planning tool. Transferring property during your life, instead of at your death, has many advantages. Making lifetime gifts can be desirable for personal reasons (e.g., to help your children or other family members) or for financial reasons (e.g., saving taxes). No matter what your reasons for starting a gifting program, there are a few gifting traps you should be aware of.

1. The kiddie tax rules

Beware of the kiddie tax rules when transferring income-producing property to your children. Investment income over $1,800 (for 2008) will be taxed at your marginal income tax rate, not your child's.

The kiddie tax rules apply to children who are: (1) under age 18, (2) age 18 with earned income that doesn't exceed one-half of their support, and (3) ages 19 to 23 who are full-time students with earned income that doesn't exceed one-half of their support.

2. Gifts of retained interests or powers

Be careful when making gifts of property in which you retain some financial interest (e.g., a life estate, right of reversion, or right of revocation) or powers (e.g., the power of appointment). This property may be includible in your estate for estate tax purposes.

For example, say you transfer ownership of your home to your son on the condition that you're allowed to continue living in the home for the rest of your life. You have retained a financial interest in the home, and this interest may be includible in your estate for estate tax purposes.

3. Income taxation of gifts made to a trust

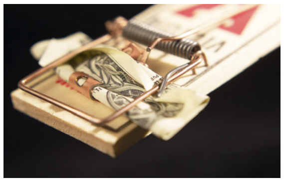
Some types of trusts are taxpaying entities, which are taxed at more compressed income tax rates than individual taxpayers. If you'll be using such a trust, be sure to consider the consequences of paying income tax on trust income at higher income tax rates.

4. Delays in making a gift of life insurance

Do not delay making a gift of a life insurance policy on your life. A transfer of an insurance policy by gift within three years of death results in the proceeds being includible in your estate for estate tax purposes.

5. Delays in planning your estate to meet percentage tests

Do not delay removing certain nonbusiness assets to help your estate meet the percentage tests to qualify for Section 303 (redemption of stock), Section 2032A (special use valuation), or Section 6166 (installment payout of taxes) tax treatment. This technique will work only if the gift is made more than three years prior to your death.



6. Payments for tuition or medical care made to the donee

Payments you make for tuition or medical care on behalf of another are exempt from federal gift tax. However, to qualify, you must make the gifts directly to the educational or medical institution--do not make such payments to the donee.

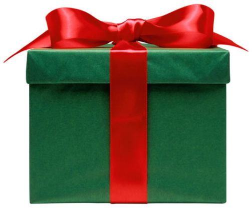
No matter what your reasons for starting a gifting program, there are a few gifting traps you should be aware of.

7. Overlooking gift splitting

For 2008, you can give $12,000 per donee federal gift tax free under the annual gift tax exclusion. There is also a gift-splitting privilege for spouses who qualify that can double the exclusion.

8. "Reverse" gifting if death is imminent

Reverse gifting is a technique where a healthy individual transfers low-basis assets to a dying individual. If the decedent lives for more than one year from the date of the transfer, the basis gets stepped up to fair market value. However, the basis will not get stepped up if the decedent dies within a year of receiving the gift, and should this happen, you may end up needlessly paying gift tax and/or using up your $1 million gift tax applicable exclusion amount.

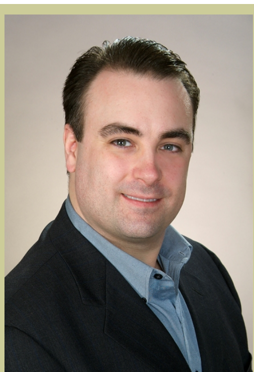


9. Overlooking the benefit of taxable lifetime gifts

Don't assume that lifetime gifts and transfers made at death result in the same tax effect. Paying gift tax on taxable lifetime gifts can result in an overall tax savings because the tax you pay is also removed from your estate.

10. Selecting property that does not attain your tax-savings objectives

There are some types of property that you should avoid giving if you want to enjoy tax savings, such as property that has depreciated in value or is likely to depreciate.



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Ask the Experts

Can I get an estimate of my child's financial aid eligibility before we officially apply for aid?

Yes. Last year, the U.S. Department of Education launched an online financial aid tool to help families better prepare for the cost of college. Called the FAFSA4caster, it's modeled on the government's official aid application, the FAFSA (Free Application for Federal Student Aid). The tool examines a family's financial data and estimates how much aid a student might expect to get. To use the tool, visit www.fafsa4caster.ed.gov.

To complete the FAFSA4caster, gather the following information for you and your child:

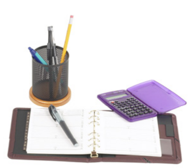
- Social Security numbers
- Federal tax information or tax returns, including W-2 information
- Information on savings, investments, and business and farm assets
- Records of any untaxed income (such as Social Security or welfare benefits)

To get as accurate an estimate as possible, you should answer all the questions on the tool, even if you have to estimate or guess.

Using the FAFSA4caster isn't exactly a quick process, but when you're ready to apply officially for federal aid, the FAFSA4caster will automatically transfer all of your data (that's password protected and saved securely) to your online FAFSA application, saving you the hassle of keying in all your information again. And, if your financial circumstances change, you'll get the opportunity to update any answers on the FAFSA that you originally submitted on the FAFSA4caster.

By providing an advance estimate of federal aid eligibility, the FAFSA4caster can help you forecast how much money you and/or your child may need to come up with to meet college costs--information that can also come in handy in the college selection process. By having an idea of the numbers ahead of time, you can help minimize unwelcome surprises.

When does my child need to submit financial aid applications?



The FAFSA is the federal government's financial aid application. It should be submitted as soon as possible after January 1 of your child's senior year in high school (and after every January 1 in any year your child is seeking aid). Several financial aid programs operate on a first-come, first-served basis, so getting your child's application in early increases his or her chances of securing aid.

Your FAFSA relies on the previous year's tax information. For example, a FAFSA filed in early 2009 would rely on information from your 2008 tax return. Because most parents have not yet completed their federal income tax return in January, one option is to complete an estimated tax return, which can then be used to complete the FAFSA, a practice the federal government considers acceptable.

You can fill out the FAFSA on paper or online at www.fafsa.ed.gov. A paper version takes about four to six weeks to process; the online version takes only one week. The better route is the online application. Not only is the processing faster, but the form notifies you of inputting errors and does the math as you go along. Plus, if you've previously filled out the FAFSA4caster, the government's online financial aid tool, the online FAFSA will be automatically populated with your data.

Along with the FAFSA, some colleges require you to submit one or more additional financial aid forms to determine your child's eligibility for the college's own grants, loans, and scholarships. These colleges may have their own forms, or, more commonly, they require you to complete the College Board's PROFILE application. The PROFILE application can be submitted in the fall, before the FAFSA, but it's a good idea to check with individual colleges regarding their submission rules. Go to profileonline.collegeboard.com to file the PROFILE online.