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**Commentary:**

## ***The Roller Coaster Is On the Upcycle***

In the last issue of *The Advisory* we focused on the Trend Tool, provided commentary from a noted Fund Manager and Economist, and provided a working description of ETFs (Exchanged Traded Funds).

These topics turned out to be timely as the equity markets continued the progress that began in mid-March. We made EFT purchases for some investors in both the Domestic and Global Equity markets based on the Trend Tool. Also, we began the process of diversifying away from the U.S. Treasury Bond Market, again based on signals from the Trend Tool and other external events.

The diversification transactions have just been completed. Since I'm sure some of you may be wondering what it is that we did and exactly where a good percentage of your funds are now invested I will attempt to define the reasoning behind the moves and the choice of ETFs.

The primary driver of the move away from U.S. Treasuries is based on the expectation the enormous debt funding requirements of our Government will, sooner or later, lead to a significant rise in interest rates, which will, in turn, cause a decline in the price of existing bonds.

The following paragraph from an article in *The Wall Street Journal* summarizes this perspective very well:

"The U.S. government is going to flood the market with newly-minted Treasuries this week — \$200 billion, which will make this the busiest week in 24 years. As of July, the gross supply of Treasury security issuance had come to \$1.25 Trillion, up from \$434 billion last year and \$350 billion at this juncture of 2007. With the yield on the 10-year note still south of 4.0%, this attests to the offset from intense deflationary pressures, though the deteriorating fiscal performance and outlook have generated a super-steep yield curve and, for the time being, established a higher floor for longer-dated yields."

It was announced that an additional \$75 billion in 10-, 20- and 30-year Bonds will be issued in August. The Treasury Department has stated that they may tilt toward TIPS (Treasury Inflation Protected Securities) but details are not available. What all this means is that even though inflation is still quiet there likely will come a time-probably in the near future- when it will start to rise rapidly.

The Treasury auctions in late July were characterized as having lackluster demand as indirect buyers ( i.e. Foreign Central Banks) stayed away. This is another big risk to holding this type of debt, the effects of which our Trend Tool will not be able to see before they happen, which could prove painful.

***Commentary (continued on page 2)***

## Commentary (continued from page 1)

### Reasoning:

1. Most of our investors are at the stage of life when Preservation of Capital is their primary concern. Some would like Growth Opportunities when appropriate.
2. Earnings on the S-T Treasuries and Bond Index Funds averaged around 4%, depending on the allocation. Not bad for the past year, but price erosion had begun affecting total returns.
3. An available tool to provide some protection against sudden declines is Diversification across several Fixed Income sectors.
4. ETFs are tailor-made for this type of diversification: they are easy to buy, have no trading limitations, and are inexpensive to hold compared to Managed Mutual Funds.
5. If possible, use existing Hedging Techniques within the ETF universe. Precise Hedges are not available without using Options and Futures beyond our current expertise.

Conclusions: Develop an ETF-based Fixed Income Portfolio with a Hedge if available. Customize the holdings for those investors who want equity exposure (substitute Equity ETF's for a portion of the Core Fixed Income holdings.)

### 100,000 Portfolio-Allocations

#### Core Fixed Income Portfolio

FPRXX (Prime Fund Capital Reserves)	\$ 9,000	9%
HYG (High Yield Corporate Bond Fund)	\$10,000	10%
EMB (Emerging Markets Bond Fund)	\$10,000	10%
LQD (Investment Grade Corp. Bond Fund)	\$20,000	20%
IGOV (Intl Treas. Bond)	\$10,000	10%
TIP (TIPS Bond Fund)	\$10,000	10%
MBB (MBS Bond Fund)	\$20,000	20%
SHY (1-3 Year Treas. Bond Fund)	\$10,000	10%
VXX (VIX Short-term Futures ETN)	\$ 1,000	1%

**\$100,000 100%**

**Please Note:** We've kept a cash component of up to 20,000 FPRXX and SHY, which can be transferred if opportunities arise to the Equity positions in the Growth Portfolio. The VXX position in both Portfolios are meant to provide a partial hedge to declines in the Equity-related positions. They are not meant to fully hedge but simply provide a cushion against severe changes. Thus far they have performed as expected.

### Actions Taken:

1. Sold SHY & AGG, VFISX & VBMFX mid-to-late July. Based on subsequent market moves the timing was good (See page 7).
2. Created two ETF Portfolios: CORE FIXED INCOME and GROWTH GROUP
3. On 7/17 began purchases of ETFs in client NFS accounts.
4. Completed purchases on 7/30 & 7/31. Confirms sent by NFS.

Due to the unprecedented number of trades entered, the process took longer than expected; however we were able to achieve very good executions for all securities.

All trades were submitted with "limit prices," which means that we wouldn't pay more than a specific price per share. If the price rose above that limit the order was not filled.

Additionally, Stop Loss limits have been placed on the equity positions and two over the fixed positions that may be more volatile than the others. A Stop Loss Order will automatically sell out of a position if it drops by a specific amount; in this case 5%.

#### Growth Group Portfolio

FPRXX	\$10,500	10.50%
HYG	\$10,000	10%
EMB	\$10,000	10%
LQD	\$20,000	20%
IGOV	\$10,000	10%
MBB	\$10,000	10%
IVV (S&P500 Index Fund)	\$18,000	18%
EFA (EAFE Index Fund)	\$ 8,000	8%
VXX	\$ 3,500	3.50%

**100,000 100%**



## *A New Look at LTC Insurance*

As financial advisors it is our job to assess each client's risk as it relates to achieving financial goals. We recommend adequate life insurance when appropriate; we allocate investments to provide diversification and spread risk. We also can review health, homeowner's, and auto insurance (although that is not our particular forte).

At any given time all the financial planning can end up worthless when a client is faced with a sudden illness and forced to spend time in a nursing home. The costs are prohibitive and can be up to thousands of dollars per month! (Approximate cost for a stay of 2.5 years:

2007 - upstate NY \$251,473, NY Metro area \$322,919

2013 - upstate NY \$336,998, NY Metro area \$432,743

With costs increasing annually at 5%).

Why are so few people willing to face this financially devastating reality?

For one thing, it can be daunting; so many companies, too many choices, aggressive sales force – it's worse than buying a car! Whom do you trust? How do you recognize the best value for your dollars? And the biggest argument is "what if I don't need it?" All that money gone for nothing!

Reality is that we are living longer. Staying alive, not dying, is one thing. Quality of life is another. We refuse to see ourselves getting older. We think life will go on the way it is today. We do not recognize that we're slowing down a bit, both mentally and physically. Responses like "we'll face that problem when we come to it" or "that's why I had kids, to take care of me in my old age" just lead to disaster.

In a recent survey of Americans with a minimum net worth of \$1 million (not including primary residence), the cost of health care came in second after inflation-eroding assets as their chief concern.

Individuals who reach age 65 have a 40% chance of needing a nursing home for some period in their remaining years. 10% will stay in that facility five years or more. The out-of-pocket cost is expensive now, increasing each year faster than inflation.

LTC insurance is not for the poor. There are government programs to help them. Most folks of modest means with reasonable assets feel the pinch of paying annual premiums and are tempted to self-insure as are the affluent. Both these groups are at risk: the modest means face losing most of their assets, the affluent lose flexibility and impact their legacy.

A client may have saved diligently or recently sold a business to build retirement assets only to be forced to liquidate those funds at an inopportune time to satisfy nursing home bills. His/her portfolio may never recover, jeopardizing lifestyle in later years. Whereas an affluent client may hold on to assets in lieu of passing them on to heirs, thus increasing the value of his estate and potentially resulting in a higher estate tax. In fact, if Congress does nothing in 2010 the estate tax exclusion will return to \$1 million leaving any estate above that amount subject to estate taxes with a top rate of 55%. (New York State has no inheritance tax but it does tax estates of over \$1 million).

New options have recently appeared that make the pill easier to swallow. Return of premium at death gives the designated beneficiary of the policy a portion or the entire premium paid, less any benefits paid by the insurance company. This option works for clients who are concerned about risk protection but unhappy about paying for a policy they may never use. Two age-based scenarios are offered. One is where younger clients would pay less based on age at death, usually before 65 with a shrinking percentage after that year.

*A New Look at LTC Insurance  
(continued from page 3)*

If a client bought a policy at 45 and dies suddenly at 55 without receiving any claim payments, the policy would pay 10 years worth of premiums to the beneficiary. If that same person died at age 70, the policy would pay 50%, with the rider stopping at age 75. There is an additional cost of 8% over the regular premium for this option.

The other, for older clients, will return all premiums, less any paid claims, regardless of the insured's age, as long as the policy has been in force for at least 10 years. A client who purchases a policy at age 55 and passes away at 70 having made no claims, the beneficiary would receive 15 years worth of premiums. The added premium for a client 55 or older would cost 25% to 34% more with the rider cost increasing as the age at time of purchase increases.

Acceleration of Life Insurance Death Benefit for Qualified Long Term Care services rider is a new twist on a Universal Life insurance policy. While life insurance is recommended for specific goals it can provide funds to cover home health care, a qualified long-term care facility or a viatical payment.

A chronic illness, severe cognitive impairment or inability to perform two ADLs (activities of daily living) for a period of 90 days activates the rider on this policy. Combination plans that pair an annuity with LTC insurance are about to make their appearance in 2010 as a result of provisions of the Pension Protection Act of 2006. LTC insurance benefits paid out of these plans are paid tax-free. This is unprecedented, the first time that contract gains may be paid out tax-free! These new annuities/insurance policies will provide protection against the risk of long term care while providing cash value or income in the event that no LTC services are ever needed and hopefully, at a lower cost.

A Long Term Care insurance policy can be very complicated: the amount of the benefit, the deductible days, waiting period, number of ADLs not performed, benefit limits, inflation factor, in addition to the various riders. Small changes in the policy can affect results many years in the future. These plans need to be considered carefully so as to accomplish the goals intended – peace of mind, comfort, care and reduced risk.

If you do not have LTC coverage it is highly suggested that you give us a call to review the options.



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## *Estate Planning with a New Twist*

The definition of Estate Planning is “the process of preparing for and managing the financial and administrative transitions related to one’s death.”

Being prepared will soften the impact of your passing on your heirs by clarifying your wishes and documenting your assets. It also allows you to provide for the care of an aging parent, a dependent child or a cherished pet.

Estate planning is not just for the extraordinarily wealthy, or moderately wealthy. In fact, with estate tax laws about to change, estate planning is critical for most folks who own a home in Westchester County. Even with the bursting of the real estate bubble, properties in NY, CA, and DC have maintained reasonably high values. The Federal estate exclusion for individuals is currently \$3.5 million and may remain there. But, if Congress makes no changes, the law sunsets and the exclusion returns to \$1 million in 2011. New York State has its own estate tax with an estate exclusion of \$1 million. So, in addition to providing support and care for loved ones, estate planning can create solutions to benefit heirs and reduce the impact of estate taxes. Let’s take a look at a few important parts of the estate planning process.

Your Will is one of the most important documents where you declare who gets what. The purpose of a will is to allow for the distribution of your possessions to the recipients of your choosing. You know that. But what you may not know is what happens if you do not have a will, or if a signed will cannot be found. Each state has its own intestate succession rules that determine the distribution of your assets, which may not reflect your wishes.

In New York State, for example, the surviving spouse is entitled to the entire estate if children or grandchildren do not survive the decedent. If there are children or grandchildren, the surviving spouse gets the first \$50,000, plus one-half of the remaining property.

If no spouse, the estate goes to children, grandchildren, parents, grandparents, great-grandchildren and if there are no relatives, the estate passes to the State of New York, not to your best friend or your favorite charity. Remember, the distribution of assets according to your will does not include accounts with named beneficiaries (IRA, 401k, 403b, TOD, insurance policies). A beneficiary designation supercedes a will. This means that if you state in your will that you want the funds in your IRA to go to your grandson, but on the IRA application you indicated the beneficiary to be your sister, the funds will go to your sister.

Beneficiaries are those persons or trusts named specifically to receive the assets in your account. As stated earlier, there are certain accounts that will be distributed according to “beneficiary designation”. These include your IRA, 401k, 403b, TOD (transfer on death) accounts and insurance policies. If you have been widowed, divorced, married or if you’ve changed your mind or a beneficiary has passed away, it is critical to review and update your beneficiaries periodically. Too often an individual passes away and the IRA passes to former spouse or to the estate of a deceased relative.

**Letter of Instruction** is a letter that covers anything and everything not included in your will. You may state your desires for burial or cremation, funeral or memorial service, burial site, music, flowers, pallbearers, etc. You may also make provision to cover the cost of these items. You may direct the distribution of jewelry, furniture, clothing, etc. or the care of your pet. The more specific you are, the easier it will be for those left behind.

**Trusts** have many purposes and there are several types used in estate planning. One of the most common trusts is the *Bypass or Credit Shelter Trust*. Its purpose is to reduce or eliminate federal estate taxes. This trust is typically used by a married couple whose



## Estate Planning with a New Twist (continued from page 5)

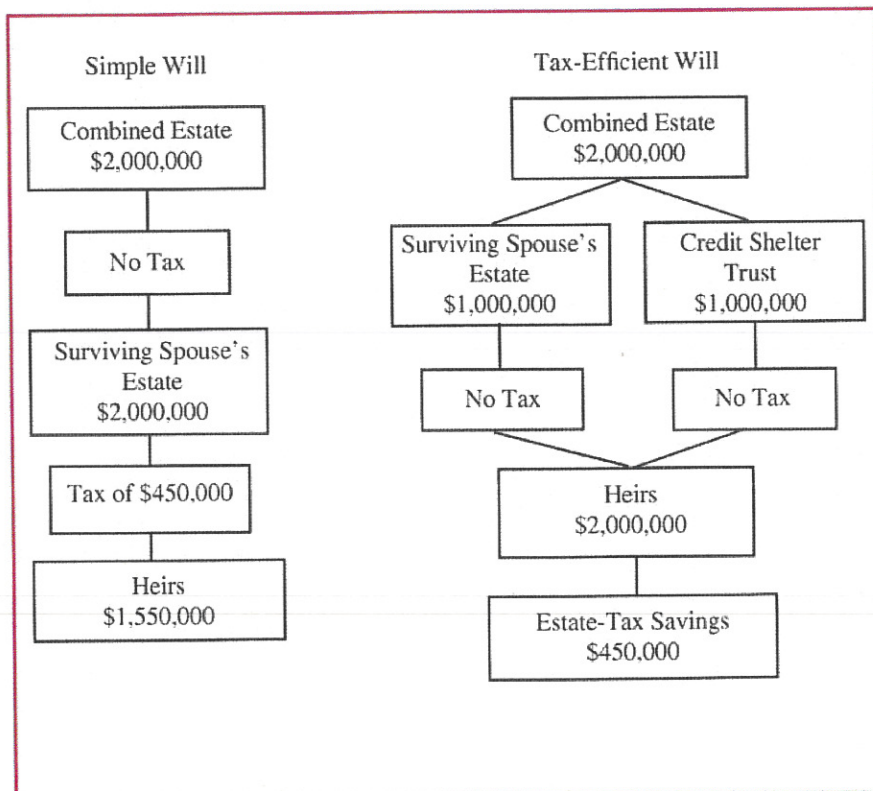
estate exceeds the federal exclusion amount. (Let us interject a note of caution here, this trust must be established while both partners are alive. Once one partner passes on, there is no way to create this protection!)

Each of us is entitled to a tax credit, which is applied to the taxes we may owe on our individual estate. (A taxable estate includes investments, real estate, cars, art, collectibles, bank accounts, limited partnerships, insurance policies, IRA's, 401k, etc.) That amount is currently \$3.5 million. Between married partners there is an unlimited marital exclusion. At death all the assets of one partner pass to the surviving partner and are subject to no estate taxes. (Here is where the trouble lies when the combined spousal estate exceeds the exclusion limit.) At the passing of the second partner, his/her estate must pay estate taxes on all the assets. The family was able to take only one exclusion, that of the second or surviving partner. The first partner lost his/her exclusion by passing all assets to the spouse. That is a very generous move that benefits Uncle Sam. The purpose of the Credit Shelter Trust is to allow both partners to take advantage of this exclusion. Sometimes the benefit might be accomplished by separating assets and not holding everything in joint name; for example, the home and cars in one person's name and the brokerage account and country house in the other's. But the most effective way is to have a trust written delineating the terms, benefits, beneficiaries and disposition of the assets. On the passing of the first spouse, the trust directs the establishment of a separate irrevocable trust into which assets belonging to the deceased spouse can be deposited. The surviving spouse is the primary beneficiary of this trust with the children as secondary beneficiaries. Assets equaling the exclusion amount are put into the trust thus taking advantage of the estate credit and having the individual owe no estate taxes. At the passing of

the second spouse, he/she gets to exclude an equal amount (assuming laws have not changed) thus saving the family thousands of dollars in estate taxes.

Note of caution: folks go through the effort of having a trust written but forget to fund the trust (change title on house or accounts) losing their exclusion!

Another trust frequently used is a *Special Needs Trust* set up specifically for the care of a dependent child (or parent) where the trust assets will not count as personal resources and allow the individual to qualify for Medicaid benefits. More on this in the next edition of *The Advisory*. These trusts are only two examples of the many tools of financial and estate planning. As we do not practice law and cannot advise you on the drafting of a will, trust or other document, you must confer with a competent estate-planning attorney. We can, however, work with you and your attorney, review your beneficiaries, and implement the directives outlined in the trust.



Please Note: The phase-down of the Federal Estate Tax Exclusion is set to expire in 2010 and revert to \$1 million per person

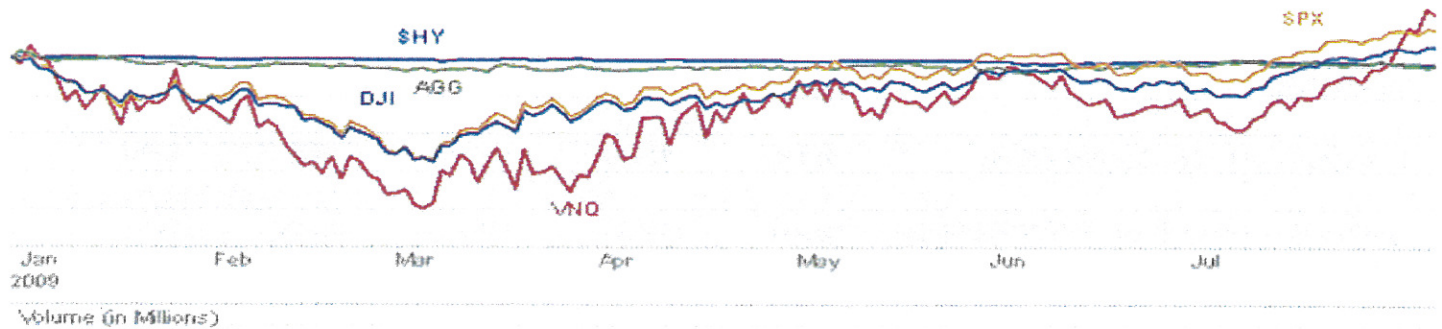


Chart from CNBC



5/1 to Date

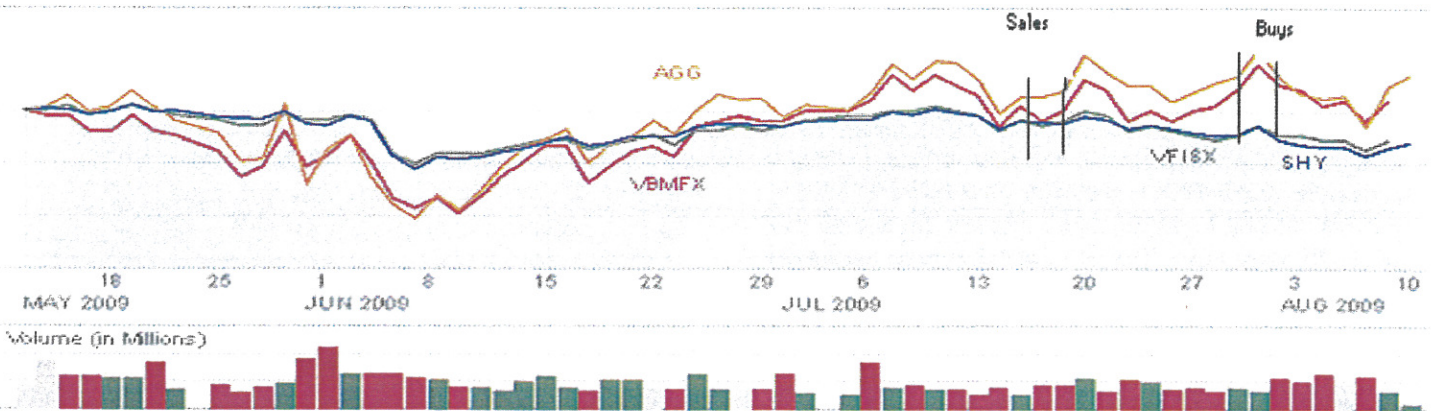
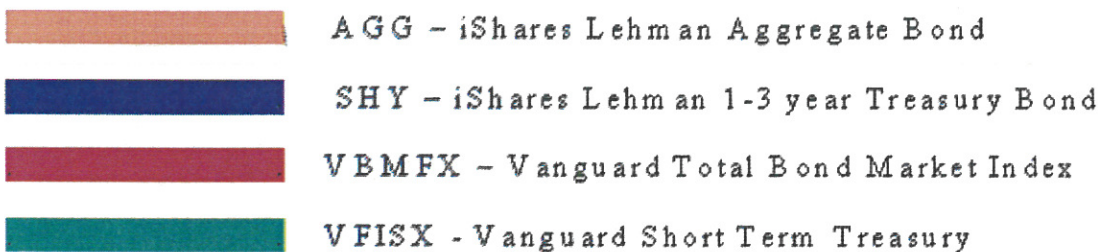


Chart from CNBC





## Market Activity

Market Indicator	Prices			Percent Changes	
	6/30/2008	3/31/2009	6/30/2009	Last Year	Last Qtr
1 Ounce of Gold ( <i>London PM Fixing</i> )	919.50	924.00	942.00	0.5%	1.9%
Technology-oriented Stocks ( <i>NASDAQ Index</i> )	2315.63	1545.20	1838.22	-33.3%	19.0%
Small Company Stocks ( <i>Russell 2000 Index</i> )	698.14	429.00	513.22	-38.6%	19.6%
International, Global Stocks ( <i>EAFE Index</i> )	1957.23	1083.64	1305.82	-44.6%	20.5%
Large Company Stocks ( <i>S&amp;P 500 Index</i> )	1278.38	815.94	918.90	-36.2%	12.6%
Higher Yielding Stocks ( <i>DJ Utilities Index</i> )	506.99	331.27	355.79	-34.7%	7.4%
High Yield Bonds ( <i>M.L. High Yield Index</i> )	837.78	660.73	803.05	-21.1%	21.5%
Tax-free Municipal Bonds ( <i>Bond Buyer Index</i> )	107 9/32	102 14/32	105 10/32	-4.5%	2.8%
Long-term US Gov't Bonds ( <i>Lehman Index</i> )	1766.31	1960.08	1815.44	11.0%	-7.4%
Inflation ( <i>Consumer Price Index</i> )	220.00	212.70	215.70	-3.3%	1.4%

Source: Wall Street Journal, Barrons, and Yahoo Finance. An index is an unmanaged group of securities considered to be representative of the stock and bond markets in general. An index cannot be invested into directly and assumes dividends are not reinvested. In addition, past performance is not indicative of future results.



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