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Fee-Only Financial Advice

PUT YOUR GRATITUDE INTO ACTION!

by Kathleen M. Rehl, Ph.D., CFP®

Be not simply good. Be good for something.

- Henry David Thoreau

When good things happen to us, we naturally feel a sense of gratitude. For example, we can be thankful for our family, a comfortable home, nice friends, meaningful employment, good health, life in a free country, a pretty sunset, and much more. Indeed, when we stop to count all of our "blessings," we would likely say we've received lots for which we are thankful.

I believe that just *being* thankful – feeling grateful for what I've been given – is a good first step. But the next step beyond just *feeling* gratitude is to be **ACTIVELY** grateful rather than just **PASSIVELY** grateful. For me, being actively grateful means I need to do something as a way of acting out my gratitude. This moves me to give to others, just as I have received. My giving is an **ACTIVE** response to all the good I have already been given and will be given in the future.

Active gratitude can certainly include writing a note of thanks to my neighbor who invited me to a nice party or giving a little of my time to visit a friend who is sick. Opening my purse is another way I can actively say "thank you" for the good I've experienced. It's simply healthy for me to give. Indeed, giving isn't so much about the receiver who benefits from my gift – it's more about me as the giver. I really give because

expressing gratitude makes me feel good. And I am healthier for doing it.

Charitable giving allows me to express my gratitude in a very real and tangible way. I know that my gifts are making a difference in the lives of others.

For example, I've directly seen the results that my financial gifts have made in the lives of students attending Capital University in Columbus, Ohio. My husband and I established a special "Rehl Family Scholarship Fund" years ago, following the tragic death of our daughter. Through giving, our healing process was facilitated, too. This became yet another gift . . . to us. The letters and conversations we've had with many of our scholarship recipients are very heartwarming. Yes, this has been a great emotional return on our financial philanthropic investment.

It's true that a lifetime of giving pays rich dividends for the giver. Helping another person is a very meaningful way for me to turn passive gratitude into active gratitude.

At Rehl Financial Advisors, we assist our clients in expressing their gratitude by making charitable gifts, both currently and in their estate plans, to organizations that are special to them. These include a wide variety of important causes: religious organizations, environmental agencies, children's camps, health and medical research, world hunger relief, homeless shelters, community service groups, refugee resettlement efforts, senior services, animal protection agencies, cultural arts organizations, youth groups, and many more.

You may want to talk with your Cambridge Advisor about the best ways through which you can actively express your gratitude. During the holiday season this can be especially meaningful. And the more you practice active gratitude, the more you'll find you have to be grateful for. Try it! You'll like it! ■■■



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HEALTH SAVINGS ACCOUNTS: BENEFITS FOR THE SOLE PROPRIETOR

by Susan A. Schreiner

The Medicare-reform law passed at the end of last year created new, tax-favored health savings accounts (HSAs) for people too young for Medicare. The accounts are new enough that many people have not heard of them, and they have not yet been tested by the courts and the IRS. However, they are an exciting addition to both financial and retirement planning and may prove to be of significant benefit to you if you are a sole proprietor.

Almost anyone not entitled to Medicare (i.e., under age 65) who has a qualified, high-deductible health plan can participate in an HSA. However, if you are a dependent for another taxpayer, or are covered by more than one health care policy, you are not eligible.

A qualified high-deductible health policy is one with a deductible of at least \$2,000 per family or \$1,000 for an individual. There are limitations on the out-of-pocket expenses: they cannot exceed \$10,000 for a family or \$5,000 for an individual, and not all expenses qualify.

You can annually contribute to an HSA the amount of the deductible. The limitations for 2004 are \$2,600 for individuals and \$5,150 for families. If you are over age 55 you can contribute an additional \$500 per year.

This is a great way to either pay the majority of your medical expenses tax-free (as opposed to the 7.5% AGI requirements for itemizing medical expenses) or to save extra tax-deferred money for retirement and the increased medical expenses we all face as we age. You can deduct your HSA contributions regardless of whether you use itemized or standard deductions and regardless of your income. Your earnings on the account grow tax-deferred and are tax-free when distributed, but only if they are used for qualified medical expenses. Like an IRA, if you withdraw the

money for unqualified reasons, you face full taxation plus a 10% penalty. After age 65, the account acts like an IRA – you can withdraw money without a penalty, and the funds are taxed at your marginal tax bracket.

To invest in an HSA, you first need to purchase a high-deductible health insurance policy that carries the qualifications listed above. Second, you need to search for an appropriate HSA. Some companies like Blue Cross / Blue Shield and Assurant (formerly Fortis) can offer both, but you need to carefully think over your investment options and the expenses within the account, as well as any limitations to coverage. You can also set up an HSA separately. A website called

eHealthInsurance.com is one place to begin searching for a place to open an account. Your investment options range from variable and fixed-interest rate accounts to some mutual funds.

As HSAs become more popular, investment options should become more numerous.

Here is an example of an HSA in action: a 37 year-old sole proprietor with a \$1,200-a-year premium and a \$2,000 deductible can write off \$3,200 a year; (the premiums for a small business are now 100% deductible and the \$2,000 goes into an HSA). If this account is not used for medical reasons by age 65, and the investments earn 8% after expenses, the business owner will have an additional \$190,000 toward his or her retirement. If there are medical expenses, the expenses will be paid with tax-free money. Either way, if you have the additional money to save, this is a great

opportunity for lowering your tax bill and protecting your future. ■ ■ ■



"The limitations for 2004 are \$2,600 for individuals and \$5,150 for families. If you are over age 55 you can contribute an additional \$500 per year."



THE FUTURE OF SOCIAL SECURITY – *Hope for the best or plan for the worst?*

by William D. Starnes, CFP®, MST, ChFC

How Social Security Works

Income is collected for the Social Security program from your payroll taxes (shown as FICA on most pay stubs). Each person pays a flat rate of 6.2% on income up to \$87,900. In addition, your employer also pays another 6.2% for a total of 12.40% of your income. If you are self-employed, you pay the entire 12.40%. This collected payroll tax is used to pay benefits to current Social Security recipients.

Social Security is a “pay-as-you-go” system that pays current recipients out of this year’s collected payroll taxes. If collected payroll taxes (income) exceed benefit payments (expenses), as is currently the case, the excess is added to the U.S. Treasury’s general revenue and spent. In exchange for the excess funds, the U.S. Treasury provides unmarketable treasuries (i.e., IOU’s) that are accumulated in the Social Security “trust fund”.

In about 2017, when the baby boomers begin retiring en masse and claiming benefits, the trust fund surpluses will be needed. This is because the collected payroll taxes will no longer cover the benefit payments. The trust fund surplus IOU’s will then be presented to the U.S. Treasury for payment. Where will it get the money? There are two options: 1) increase revenues by increasing taxes or borrowing from the public; 2) reduce other government spending and direct the saved dollars to pay the IOU’s. Since the second option is not likely to happen, you can see that the trust fund’s only real asset is the government’s power to tax or borrow. So, whether or not there is currently a social security trust fund makes no difference to the future viability of the program.

There is a “trust fund”, but its only asset is its claim on your future financial security.



The Potential Problem

Just as Mr. Ponzi’s investment scheme collapsed when the stream of new investors dried up, Social Security will also become unsustainable when the pool of new workers doesn’t grow rapidly enough to pay the recipients of benefits. Because of the coming surge in the number of recipients (i.e., retiring baby boomers) with a much smaller pool of new workers to support their benefits, Social Security faces a serious funding crisis.

What This Should Mean To You

It is clear that with no changes, *in its current form*, Social Security will soon become unaffordable and eventually unsustainable.

There have been and will continue to be offered many solutions. Because outright benefit reductions would mean political suicide, the changes will be as subtle as possible and deferred as long as possible. Solutions may include increased taxation of benefits, change to the benefit calculation, reductions to the cost of living adjustments, increases in the full retirement age, etc.

The political risks involved in raising taxes, cutting benefits, or both, give a strong incentive to defer action. Because of this and the fact that the young will have far less political clout than the larger group of baby boomers, benefit cuts or increased taxation will likely fall on future Social Security beneficiaries rather than current or soon to be recipients.

In the meantime, you want to closely review your Social Security Earnings Benefit & Estimate Statement each year to ensure that you receive the benefits to which you are entitled – even if reduced. Frankly, I hope for the best . . . that the necessary changes will occur using prudent and fair methods. In the meantime, I will

continue to plan for the worst by continuing to save aggressively. ■ ■ ■

“Frankly, I hope for the best . . . In the meantime, I will continue to plan for the worst by continuing to save aggressively.”



ASK an Advisor

IS TAX PLANNING FOR ME?

by Ken Robinson, JD, CFP®

Q. “Why should I bother with tax planning? I often don’t have enough to itemize deductions anyway, and there are no other tax breaks I qualify for.”

A. Sometimes tax planning is not about finding a new deduction you haven’t used before. It may be a matter of deciding when to take a deduction you already know about. If your itemized deductions are close to the amount of the standard deduction, you may benefit from deduction bunching. You can double up on certain expenses in, say, the even-numbered years, and skip them altogether in the odd-numbered years. What if your itemized deductions come to \$9,600? The 2004 standard deduction for a married couple filing jointly is \$9,700.

Naturally, you’d take the standard deduction on your taxes. But what happens if you make some of “next year’s” contributions in the last month of this year? Suppose that in December 2004, you make your charitable donations of \$500 for 2005 early, and pay the \$1,000 property tax bill that’s not due until January. You’ll have an extra \$1,500 in itemized deductions for 2004. Now the total of \$11,100 (\$9,600 + \$1,000 + \$500) is more than the standard deduction, by \$1,400. If you’re in the 25% federal tax bracket, you’ll save about \$350 on your tax bill.

What happens next year? You’ve already deducted \$1,500 of “next year’s” expenses. So in 2005, your itemized deductions would only be about \$8,100 (\$9,600 - \$1,500). Since this is less than the standard deduction, that’s what you’d take in 2005 . . . exactly as you’d be doing anyway without bunching.

This is what makes deduction bunching work so well. You can always take the standard deduction, no matter how little you may be able to itemize. So you pile on the deductions in the even-numbered years (reducing your tax bill), and don’t pay any more in the odd-numbered years. As an extra benefit, you only have to itemize once every two years.

Deduction bunching can be particularly important for people who receive separation payments (like unused sick or vacation pay) the year that they retire or change jobs. If this happens, you may be pushed into a higher tax bracket for that year. One client who was never able to itemize before is itemizing in 2004, because the sick and vacation payout means that far more state and local income tax is being withheld than ever before. So his itemized deductions are higher than usual, at precisely the time he’s in the highest tax bracket of his life. He’s paying his 2005 property tax early, and making 2005 charitable contributions in December to maximize his deduction bunching.

Of course, you can’t plan to do this with all your deductible items. Some expenses don’t lend themselves to this kind of timing. Consult your Cambridge Advisor to see how deduction bunching applies to your situation.

Most of the time, we have to give something up to save money. We eat in instead of dining out, or buy used cars instead of new. But when you lawfully reduce your income tax, you get to keep the money without giving up anything except a little time spent planning before the end of the year. And you may save enough to make it more than worth your while. ■ ■ ■

