

FINANCIAL MUSINGS

Gerri A Harrison CFP EA

What about that tax stimulus payment?

It has been hard to miss the talk about the payment that the federal government is sending to individuals. Lets separate fact from fiction.

You are eligible to receive between \$300 and \$600 if single or between \$600 and \$1200 if married filing joint if you meet the income limits. First you must have at least \$3000 of earned income. For this purpose only earned income includes wages, pensions and social security. For a single individual your adjusted gross income must be below \$75,000; for MFJ that amount is \$150,000.

You must file a tax return to receive a stimulus payment. If you have parents or grandparents that normally are not required to file they must file a special 1040A stimulus tax return. This can be done on the IRS website or I am doing them for \$20.

The payment received is not taxable income. It is actually an advance on a 2008 tax credit. If you do not qualify based on 2007 numbers, but do qualify based on 2008 numbers you will receive a payment, but not until you file your 2008 tax return.

If you receive too large of a payment in 2007 you will not be required to pay it back on the 2008 tax return. It is yours to keep.

A dependent is not eligible to receive a tax stimulus check.

In addition to the base amount you receive \$300 per child for each child under the age of 17 claimed as an exemption on your tax return. In the case of divorced parents, whoever claimed the exemption on the 2007 tax return will get the \$300. However, if the other parent claims the child on the 2008 tax return



they will get the \$300 then.

When will you receive the payment? If you had a refund on 2007 tax return and the refund was direct deposited, your stimulus check will also be direct deposited. If you had your refund mailed to you or you owed IRS, you will receive a paper check. The schedule is based on the last 2 digits of the primary taxpayer's social security number:

Direct deposit 5/2 00-20, 5/9 21-75, and 5/16 76-99.

Paper checks: 5/16 00-09, 5/23

Now, what to do with that payment?

The purpose of the payment is to stimulate the economy. The hope is that you will spend it on manufactured goods. This will cause inventory levels to decrease and manufacturing plants will be able to increase production, purchase new equipment and hire new employees.

Think about your situation. Is spending this money on a big screen TV the most effective use of the money? With the recent

increases in the basic costs of living, you may need to be more financially responsible.

The money can be put to great use paying down that credit card debt. It can be put into the bank to have as an emergency fund in case of a job layoff. It can be used to cover the higher cost of gasoline and groceries over the next several months.

In this recession, and yes I be-

lieve we are in a recession, you need to do everything possible to improve your financial situation. You just do not know what is coming in the next few months.

Maybe do what the government wants and spend it, but spend it wisely. Replace that ancient refrigerator or washing machine that is ready to break down. Fill that freezer and pantry with food. Start back to school shopping. Spend wisely. Spend carefully.

Volume 3, Issue 2
June, 2008

My business works because of you and people like you. If you are happy with the service that I provide for you please consider recommending me to your family, friends, co-workers, neighbors and others. I am looking to expand both my financial planning practice and income tax practice.

Inside this issue:

Credit cards, parents beware 2

Early retirement. Think about health care. 2

How can I owe taxes, my account has lost thousands? 3

Getting that loan in a bad credit environment 3

The confusion about charitable contributions 4

Your help is needed 4

Is a Roth right for you? 5

Do not overpay for insurance 5

Think of it as a spending 6

Credit cards, parents beware!

Soon millions of high school seniors will graduate and head off to college. Once they get there they will be inundated with the new opportunities. And they will be inundated with credit card companies trying to sign them up for their credit card. Studies show that college students generate a lot of revenue for credit card companies. In the billions.

College students start by saying they will get it only be for emergencies. For many it does not take much before they are charging basic needs. Then they are subsidizing a lifestyle that they may not be able to afford. They are charging dinners out, new snowboards, trips to the local mall and spring breaks in Florida.

Students have little or no income. They cannot afford to pay the balance in full so they begin incurring finance charges. The interest rate goes from that introductory rate of 2.99% to 18.00%. Month after month those balances grow. Suddenly that eighteen year old is on your doorstep telling you he has \$10,000 in

credit card debt that he cannot pay.

Think that your child will not be able to get a credit card? After all, he does not have a credit score and he has only a part-time job earning \$100 a week. That does not matter. The credit card company is counting on you bailing your child out if he gets in trouble. They know if they can get him hooked now they may have a customer for life.

You teach your kid about alcohol and drug use. You keep track of when term papers are due and where school assignments are. Your child will now be responsible for all this.

Make sure you have a frank discussion with him about credit card use. Explain interest rates, grace periods, carrying balances, and effects on credit scores. Make sure your student understands the ramifications of getting himself in trouble.

Who is going to be responsible for paying the bill. If you as the parent are willing to pay the

bill, what restrictions does the card come with? Is it only to be used in emergencies or can a preset amount be spent each month? Who is going to receive the bill? What are the consequences of not using the credit card responsibly? What credit limit do you



They can be so tempting

want to place on the card? Are you willing to bail a child out if he needs help or is he on his own?

For most, student loans are a must to get through college. They will need to be paid back upon graduation. As your child graduates he may now have a car payment and rent to pay. Do not let your child get in a position of having credit card debt hanging over him too. Your child may have to pay higher interest rates for credit, have difficulty renting an apartment or finding desired employment as a result of what he does to his credit in college.

Early retirement? Think about health care.

.Many know the magic age of 59 1/2 when you can start withdrawing money out of retirement accounts without incurring the 10% early withdrawal penalty. Do you know what is magic about the age of 63 1/2 when you are considering or being forced into early retirement?

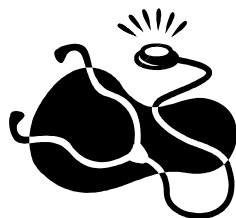
One of the primary concerns of early retirement is health insurance. Many, if not most, private companies are no longer covering retiree's health insurance costs. Medicare will not kick in for health costs until you turn 65.

The age of 63 1/2 is magic because of COBRA. If you leave employment with a company of more than 20 employees they are required to cover you for health insurance purposes under COBRA laws for 18 months. This gives you the bridge until Medicare kicks in.

COBRA laws require the employer to cover you, but does not require the employer to pay for that coverage. Chances are very good that

you will be required to pay the full amount of the premium plus up to a 2% administrative fee. This can cause sticker shock for some, but you will find it is cheaper than purchasing an individual policy.

If you are lucky you will have a spouse whose health insurance plan can cover you. Maybe you can work part-time for a company that provides benefits to part-time workers. You could even start your own small consulting business to qualify for small business health care rates. There are professional organizations that you belong to that may offer health insurance options.



If you must purchase an individual policy consider your options carefully. You may be used to having a plan with a low deductible and low co-pays that covers everything.

The expense of this type of plan will probably be cost prohibitive.

It might be a more effective use of your medical dollars to have a high deductible plan that

more effective use of your medical dollars

does not cover basic costs, but will cover catastrophic costs. Ideally you will combine this with a health savings account.

A health savings account is an account that you set up to pay for medical costs. What you contribute to the account gives you a current tax deduction. What is in the account grows tax-free. Monies can be withdrawn tax-free as long as they are withdrawn to cover qualified medical expenses. You can only pair an HSA with a high deductible plan that meets specific qualifications.

The key is to have some type of insurance. Even a broken arm or short term stay in the hospital would jeopardize your long term retirement savings with no insurance. And think about what a heart attack or serious car accident could do? Do not gamble and go without health insurance, even for a short period of time. The results could be devastating.

How can I owe taxes, my account has lost thousands?

I heard it several times during the past tax season. How can I owe tax because of my investments when the account has lost thousands of dollars? Even when the stock market is dropping you can have taxable income.

You are being smart. The market is down, but you are staying in and riding it out. So many others are panicking and getting out. Since people are wanting out, the fund manager needs to have cash to pay those shareholders. So—the fund manager must sell some of his holdings to raise cash. By doing so, the fund manager may generate capital gains from the stocks he sells.

Later in the year those gains are required to be distributed to the remaining shareholders cre-

ating taxable income. If this is a tax-deferred account that tax is delayed until money is taken from the account.

What can you do to offset this income? If losses are occurring, it may be time to shift from one asset to another. Move from Mutual Fund A to Mutual Fund B.

This allows you to claim the loss that you have in Mutual Fund A. You cannot sell Mutual Fund A and go back into Mutual Fund A within 30 days without creating a wash sale. With a wash sale the loss is disallowed.

I want you to take time to note here that I am not advocating getting out of the market. What I am advocating is called “harvesting your tax

losses”. You are going from one investment to another. You will still be in the market when the upswing starts. You are not trying to time the market. Mutual Fund A and Mutual Fund B should be similar funds to ensure that you remain properly allocated. Now, however you have a \$5000, \$7000 or whatever tax loss that you can use to offset the capital gains that are going to be distributed.

You need only be concerned about this if you have investments being held in taxable accounts. If all your investments are in IRAs, 401(k)s or 403(b)s you will not be paying current tax on the distributions anyway.



Hang in there

Getting that loan in a bad credit environment

One outcome of the subprime mortgage mess is that credit is harder to obtain for just about everyone. Many banks have tightened their requirements for issuing loans.

Think it will not effect you? How about an increase in the rate your credit card company charges you? Many college students will find it harder to get private student loans. Interest rates on home equity lines of credits are often variable and will see increases. Looking to finance an automobile? You may no longer qualify for the best rates.

You need to put some time and effort into your financial habits long before you go looking for that loan. With the new credit scoring system your credit score can go up to 850 and a good credit score is now considered above 740. Check your credit score at www.MyFicoScore.com. There is a fee to obtain your credit score, it is not available free.

One 30 day late payment can significantly effect your score. Pay bills as they come in or pay them online to ensure that they arrive in a timely manner. Many credit card companies are giving the appearance of playing games with their posting of payments to generate late fee reve-

nue.

Reconsider whether or not you should open that store credit card account just to get the 10% discount. Having too many open accounts can be a detriment to your score.

At the same time consider carefully whether or not to close accounts that you do not use often. Creditors like to see a long history of credit. Credit cards that you have had for ten or twelve years are more valuable than the ones that you have had for only a year or two. If you have too much open credit however, gradually close accounts down. Try to do this at least six months prior to applying for a loan.

One of the most important factors affecting your credit score is how much credit you are using in proportion to how much credit you have available. Say you have two credit cards, one that has a \$10000 credit limit and one that has a \$2000 limit. On the \$10000 card is a balance of \$2000 and on the other a balance of \$1000. So right now you are using 25% (\$3000 of \$12000). But if you pay off the \$2000 and close that account you are now using 50% (\$1000 of \$2000).



Think before you sign on the dotted line

Think it will not effect you?

Creditors would like to use a utilization percentage of less than 10%. Pay down balances to get below that percentage. Call your credit card company and ask for a credit limit increase if appropriate. You need to be sure that you will not use this increase.

Once you have improved your credit score as much as possible go shopping for a loan. Do not limit yourself to the local bank where you do business. The credit union down the street may have better rates and offers. A new bank in the area may be willing to cut you a deal to bring in the business. Do not overlook the Internet. Sites such as www.LendingTree.com are available to help you shop around.

What if no bank will give you a loan? Consider alternative sources. Borrow against your 401(k); this should be done as a last resort. Do you have a whole-life insurance policy you can borrow against? Parents or other family members may be an option; you may give a better rate than they can get at the bank. Be sure to formalize the agreement and stick to the terms to prevent hard feelings. Or maybe try your hand at peer-to-peer lending where individuals lend to other individuals. See websites such as www.prosper.com.

The confusion regarding charitable contributions

The deduction for charitable contributions is still allowed. You can still take a deduction with supporting receipts. You can still take a deduction for clothing and household goods given to the Rescue Mission, Nearly New Shop or the Salvation Army. You can still give away a vehicle and get a tax deduction.

What has changed about charitable contributions is that you are now required to have evidence to support your deduction. There is not “a standard amount” that can be taken. You are no longer allowed a deduction for cash contributions of any amount. IRS wants you to have a receipt for each contribution.

If you go to church and put loose cash in the collection plate you are no longer entitled to a tax deduction. You must write out a check or use the envelopes that many churches provide. With either of these methods you can request a tax statement at the end of the year showing your contributions for the year.

You cannot claim a deduction for the Girl Scout cookies or Boy Scout popcorn. Money given at the local PTA bake sale or to the Little League kids standing outside of the grocery store is no longer deductible. You have no written receipt supporting the amount spent.

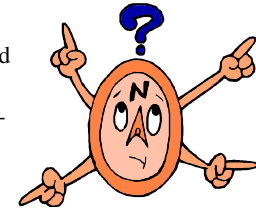
The key is to written proof of the contribution.

With the donation of goods, rules now say that they must be in “good condition” to take a charitable contribution for them. The recommendation is that you take photos of all items before donating them. This can provide you with the proof that they were in good condition.

Be careful about claiming large deductions for charitable goods for many years in a row. Make sure you have a lifestyle that supports the ability to take this deductions. If you earn \$30,000 a year it would be hard to justify that you can afford to give away \$4000 worth of clothing every year. This would cause a “red flag”.

Be aware that if the amount that you give away in “goods” exceeds \$5000 in a year you are required to get an outside appraisal for the value you are placing on the items.

Vehicle donations to charitable organizations are still allowed. The amount that you get to take as a deduction is the what the organization is able to sell the vehicle at auction for. The charitable organization is required to provide you with a receipt reflecting that amount. This means for most individuals the deduction



It is time to end the confusion

will be \$200—\$500 instead of the thousands of dollars that many people were claiming.

You are still eligible to claim a deduction for charitable miles. If you serve on a non-profit or church’s board, travel to Scout meetings or do volunteer work of any type be sure to keep track

of the number of miles that you drive for that activity. You are allowed a deduction of 14 cents per mile.

Many of you know that in 2006 and 2007 you had the ability to contribute up to \$100,000 to a charitable organization from IRA proceeds without having to claim the distribution from the IRA as income. It looks like this is going to be resurrected for 2008. It has not passed as law yet, but the anticipation is that it will happen before year end. Lets just hope it gets passed and you still have enough time to act before the end of the year.

And the good news is they are talking about making charitable contributions an above-the-line deduction. That means even if you do not itemize you would still be able to take a deduction. So—for now keep all those receipts even if you do not normally itemize.

Your help is needed

Yes, gasoline, milk, bread, and heating costs are all on the rise for you. At the same time, you need to be aware that these costs are rising for those that are less fortunate for you. Food pantries are serving more and more people. Soup kitchens are serving a larger portion of the population. Elderly are having to choose either heat, eating and medications. Five and six year olds are coming home to empty houses because single mothers are still at work and cannot afford childcare. The number of children in foster care and in the prison system is growing in leaps and bounds. Drug and alcohol addiction is on the rise.

All around us people are in need.



Everyone needs a little help

And, I know that you are busy with your lives—kids, jobs, after-school activities, cooking dinner and all the other things that we fill our lives with. But—I ask you to consider, what is your purpose in life? What do you want to be remembered for?

What are you projecting when you pass by that red kettle and do not toss in your loose change? What are you showing your kids when you complain about having to buy a bag of stuffing or a canned good for the Thanksgiving basket at school?

What are you showing when you buy canned goods for the Chow volunteers in the stores?

What do you want to be remember for ?

What are you showing when you donate clothes to the local shelters? What are you showing your kids when you take toys they have out-grown to the local women’s shelter?

Think about these options. They do not take a lot of time. By all means volunteer your time if you can. Show not just by your words, but by your actions the importance of helping those less fortunate. If you cannot afford the time though please help with your wallet. Give up that bottled water for a day and use the money for a cause close your heart. Whether it is time or money you will get so much in return for what you give.

Is a Roth right for you?

Roth IRAs have been around for a while and Roth 401(k)s are over a year old now. Yet many people still do not understand the difference between the traditional versions and their Roth counterparts.

With a traditional IRA and a traditional 401(k) you have tax deferral. If your salary for the year is \$50,000 and you put \$10,000 into a traditional 401(k) you will only pay income tax on \$40,000 for that year.

If you put \$4000 into a traditional IRA and fall within the income limits you can take a deduction for that amount. That means you would be reducing your taxable income by \$4000.

If you are in the 15% tax bracket and put in \$10000 you will be saving \$1500 on your current federal income tax return. Add NYS tax savings to that and you have an additional \$700 in savings for a total savings of \$2200.

Now lets say it is thirty years later. Your \$10000 could have grown to somewhere around \$100,000. And you decide that you want to liquidate the account and take all the money out. If tax rates have not gone up, you will pay \$22000 in taxes for using the tax

deferral option and having saved \$2200 in taxes.

If you take the \$100,000 out over time you will pay even more in taxes since the amount will continue to grow until the account is fully liquidated.

You will pay more in taxes if tax rates have gone up. Think that will happen in 30 years?

With the Roth IRA or Roth 401(k) you will not get that tax savings up front. So in essence you will need to come up with an extra \$2200 to put the full \$10000 into the Roth 401(k).

Now that same \$10000 will grow to \$100,000 just like in our first example. The difference here is that as you take the money out of the Roth IRA you do not need to pay any taxes on the distributions. The full \$100,000 is yours.

There are some additional advantages. If you need to take money out of a traditional IRA prior to age 59 1/2 you will owe income tax as well as a 10% penalty. You can withdraw your contributions from a Roth IRA at any-time with no tax or penalty consequences.



Are you on the right path?

At age 70 1/2 you are required to start taking minimum distributions from traditional plans.

There is no such minimum distribution requirement for Roth accounts.

Social security is taxable if your income is above \$32000 for a MFJ couple. IRA and 401(k) distributions will be counted as income towards that \$32000.

Roth distributions will not count as income towards the \$32000.

If your company offers a Roth 401(k) consider contributing to it. If your company does not offer a Roth 401(k), consider whether or not you should contribute to a Roth IRA before contributing to the traditional 401(k).

If you have traditional plans it is possible to convert them to Roth accounts. You will have to pay current taxes on the converted amount, but not any penalties. From here on the money would grow tax free. With the stock market low right now it might be the ideal time to convert. Before tax rates go up too.

Do not overpay for insurance

Too many people use insurance inappropriately. When you purchase insurance you are trying to protect yourself against catastrophic losses. Your house burning down. A major car accident. A hospital stay.

Whether you are dealing with liability, fire, or collision, you cannot and should not try to insure yourself against every possibility. You need to decide with each of these policies how much you can self-insure and how much protection you need to purchase insurance for.

Take the issue of deductibles. With your house insurance how often have you said, I am not going to file a claim for \$300 because I do not want my insurance premium to go up? So, why do you have a \$250 deductible on your policy? Why not save yourself 25-40% in premium costs by increasing that deductible to

\$1000 or more? You will be protected if the house burns down, but will pay less in each of the next 30 years. If you did try to file multiple claims of \$250 you may find your insurance cancelled and be unable to obtain new insurance at a reasonable rate.

Raise the deductible on your vehicle insurance and if applicable on your boat, motorcycle, trailer, ATV and anything else. Depending on how high you go you could save \$1000 or more a year in insurance premiums.

A little talked about insurance is PMI. If you put less than 20% down on the house when you took out your mortgage you were generally required to get primary mortgage insurance. Once you have 20% equity in the house, either because of appreciation in value or by paying down the mortgage, you can get PMI cancelled. No

one is going to tell you to do this. It is up to you to notify your lender. The amount you are paying can be several hundreds of dollars per year.

With home equity, credit card, store charge cards, auto loans and just about any other loan you are asked if you want the disability and life insurance protection. These are not good deals and should always be declined. The cost for the protection you are getting is too much.

Instead have a general disability policy and a general life insurance policy that will pay all these outstanding debts in the case of a disability or death.

Before renting a car, check with your automobile policyholder and with your credit card company to see if they cover rental car damages. Oftentimes you already have the same coverage that the rental car company is asking you to purchase and can decline this costly insurance.



Make you are protected

sure

Gerri A Harrison CFP EA

189 Riverside Dr
Johnson City NY 13790
Phone: 607-729-4144
Fax: 607-729-0533
Email: gerriharrison@stny.rr.com

**Look for us at
GerriHarrison.com**



Relax, I am here to help you

I hope you are enjoying Financial Musings. Please feel free to pass it onto a family member or friend. If there is something you would like to see me address please feel free to contact me by email, phone or mail.

Gerri Harrison Financial Services provides financial planning and tax preparation services to individuals and small businesses. "I want to be part of the family. There for the good and the bad. Everyone has a job and serves a purpose in the family. My job is to assist you in achieving your financial dreams and aspirations as well as meeting your financial obligations and concerns. I want to be there to pack your child off to college or pack you off to retirement. I want to be there through the christenings, weddings, illnesses and deaths. Whenever there is a financial matter you have a questions about I want the first thing you think of to be "Gerri will know how to handle it.".

Think of it as a spending plan

You hear the word diet. What do you think? Deprivation. Starvation. Lack of choice. Lack of freedom. Restriction. When people hear the word budget they often think of the same thing—lack of freedom and choice. All things fun must go away.

The key is in your thinking. Do not think in terms of the word budget. Think in terms of a spending plan. With today's rising prices and stagnant income you need to be willing to make choices. That is what a spending plan allows you to do. Life needs to be about trade-offs. Choices that only you can make.

Maybe that Starbucks coffee is what gets you through the day. So—what are you willing to give up to have that \$5 a day for that latte? Are you willing to bring your lunch from home instead of eating out everyday? Are you willing to dry-



It is a balancing act

clean less to reduce bills and hand-wash more items? Are you willing to purchase generics instead of name-brands? Use coupons?

Maybe you are not willing to give up that high speed Internet. Are you willing to trade in that 100 channel cable selection for more basic cable? Are you willing to give up purchasing video games?

Stop mindlessly spending and letting money slip through your hands without knowing where it is going. How often have you started with \$25 in the morning, and it is gone by evening. Yet you have no idea how you spent it. Make informed choices.

To be informed you need to be willing to keep track of where money is going. Use computer software such as Quicken or use a simple manual ledger system. Keep track of all types of purchases. As you learn where money is going you can begin to set and achieve goals.

You may think you have no choices sometimes. But, even with fixed expenses there are options. Maybe you choose an alternative supplier over NYSEG to reduce your gas and electric bill. Maybe you change your long distance phone carrier or go with a different plan with the same carrier to reduce costs. Reduce interest charges by making bi-weekly payments instead of monthly. Downsize your housing to be able to travel more.

The possibilities are endless. Take the first step. Determine where your money is going. Then decide if that is the way you want to use your money. Nothing should be sacred. Prioritize everything. Not according to some financial guru's rules, but according to what is important to you. Remember to plan for today and for tomorrow to keep choices available.
