



In this issue

The New Normal	1
Savings & Budgets	1
Your Credit & CCARDA	2-3
Annual Withdrawal & AMT	3-4

What's a Wealth Hazard?

Basically, it's a risk or a threat to your financial health. They come in all shapes & sizes and very often in disguise.

Which of life's Wealth Hazards are Avoidable, Manageable, and Recoverable?

That's what our new book is all about. Here is what we mean when we talk about life's wealth hazards and how to Avoid, Manage, and Recover from them.

Avoid. To identify risks or threats to your financial health and to take steps to prevent or reduce the early effects of the event. When you attempt to Avoid a wealth hazard, you are on the offensive.

Manage. To address the effects of the wealth hazard and take action to contain it, re-direct it, and eliminate it if possible. When you try to Manage a wealth hazard you are on the offensive.

Recover. Sometimes a wealth hazard is so fast-moving that there is little or no time to Avoid or Manage it proactively. In that scenario, you must react to Recover from its effects. The process of repairing the damage from a wealth hazard may be lengthy or it may be quick. The key question is how seriously it impacted your financial health. While you Recover from a wealth hazard, you are on the defensive.

Wealth Hazards | Avoid | Manage | Recover |

What You Don't Know May Be Hazardous To Your Wealth

2nd Quarter 2009

Volume 11, Issue 2

The New Normal

The image of two children on opposite ends of a playground seesaw often comes to mind these days when you hear or watch the news. Has the market bottomed yet? Are we in a bear market rally? How low will mortgage rates go? Is it time to buy a home? Is it time to sell my home? Is it safe to buy a new car from a bankrupt automaker? Credit card limits are slashed and fees increased. Your plans for retirement are jeopardized or put on hold. Your child's college dreams are now a little more hazy. All this uncertainty drives us crazy. Get used to it, this is The New Normal.

We recently received the following information in one twenty-four-hour news cycle: housing sales are up, home prices are falling more slowly, interest rates are holding steady, and a national weekly magazine declares on its cover that the recession is finally over. Now for the other shoe: a global telecom firm cuts 8,000 jobs, the state of California issues 327,000 IOUs totaling \$1.95 billion against the backdrop of a potential \$26.3 billion budget deficit, and consumer confidence drops again.

How can this be? What's going on here? It's the New Normal; at least, that's what they're calling it this afternoon as we write these words. Our friends, the "dismal scientists" more commonly known as the nation's beloved economists, have been working overtime to explain how economics is still relevant despite not having predicted much of what happened in 2008 and 2009. That's not to say that we expect our economists to possess extrasensory perception, but since we're in need of blaming someone, anyone at this point, we thought we'd start with the folks who always seem to have a model or formula to explain why things happen the way that they do. Most economists now say that what happened was entirely predictable, given what we now know today was occurring in the housing, job, stock, and bond markets. The problem, they say, is that we didn't know what was happening, when it was actually happening; therefore, the result was a surprise to most of us. Therein lies part of the problem with complex markets - whether it's the housing market, or the job market, or the stock market, or the corner market. We've become so accustomed to everything working properly most of the time that we've lost our appreciation for what can go wrong and what can happen when several things go wrong at nearly the same time.

Determine Your Savings Goal and Budget

The most common reason for saving is the "rainy day fund," putting money aside so that if lightning should strike in the form of job loss or health issues, or if any other unexpected need for cash arises, you have quick access and reduce the stress and interruption to your daily life. Most financial planners suggest that you save three months of expenses to be comfortable while you address the event. If you're employed in an occupation that might require re-training or a lengthy job search, you should consider putting away up to six months of savings. If you or a family member have a medical condition that may result in uninsured medical expenses coming due, perhaps saving six to twelve months would be appropriate. Some other goals include saving for retirement, a car, school tuition, a great vacation, or buying your first home. Whatever the objective, the discipline that is required remains the same - you must make periodic payments to your savings plan. Most experts agree that you should have the money deducted from your paycheck so that you don't have the ability to re-direct the funds elsewhere. Pay yourself first.



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The Numbers

- DOW 8,447 up 11.01% since 03/31/09, down 3.75% year to date
- NASDAQ 1,835 up 20.05% since 03/31/09, up 16.36% year to date
- S&P 500 919 up 15.22% since 03/31/09, up 1.77% year to date

A few words from the Editor

Wealth Hazards was established to help people to Avoid, Manage, and Recover from life's wealth hazards. There are too many hazards to list, so our approach will be to share with you examples that you can use to better understand how to apply these principals to the challenges that each of us will face from time to time. If you should have any questions, comments, or concerns feel free to contact us at ask@wealthhazards.com.



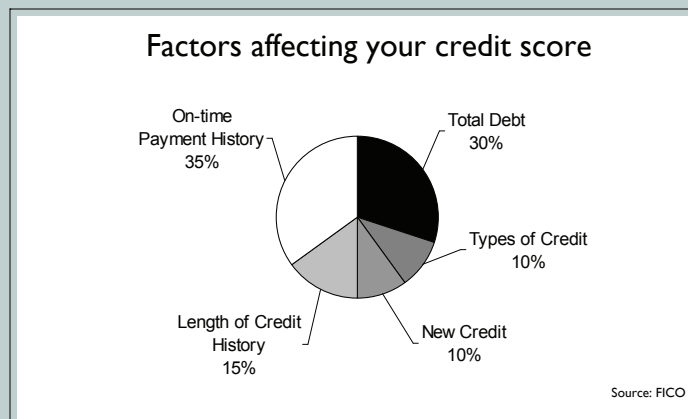
Thomas Hertog, Editor

Determine Your Savings Goal and Budget (continued)

Start to reduce your spending on miscellaneous items you don't really need or want. Begin to track your spending going forward and compare it to the three-month worksheet you created. We hope you'll see a reduction in your spending and an increase in your savings. Watch as your savings grow each month toward your goal. When you review your actual spending versus your budget, resist the temptation to spend a little of your new-found savings. Wait until after you've saved for six months and then reward yourself with a small, affordable, but meaningful gift. As your savings grow, you should consider opening a full-feature savings account that will allow you to move funds into it from your checking and or rewards/cash back credit cards. The easier it is to save, the more money you will actually put aside. Shop for the best interest rate available and consider seeding the savings account with a little extra money if that gets you a higher initial interest rate.

Your Credit

The most optimal use of credit occurs when you borrow money when you don't really need to. That is when you've saved enough to pay cash outright. This may seem foolish, but it's an old line from lenders who tell us that people who don't need to borrow as much, because they have more cash to put down, are the most creditworthy clients that they have and get the lowest interest rates and best terms.



When you keep in mind that your credit score is based upon the factors in chart to the right, you can begin to see why not needing to borrow as much is what makes you attractive to lenders. Almost everyone must take out a mortgage on their home, and most people have an auto loan. But while big ticket purchases like homes and autos have a higher price tag than washers and dryers, there are a lot more washers and dryers sold each year than homes and autos.

Purchases of durable goods, those products having a useful life of at least three years, are the driving force in our economy. Financing these purchases has fallen mainly on credit cards and home equity lines of credit.

Many consumers make purchases on an emotional level rather than on a rational basis. This applies to homes and autos as well as furniture, vacations, and clothes. Yes, you do need a roof over your head, but do you really need six bedrooms, five baths, a four-car garage and a swimming pool? Yes, you do need a car to get around, but do you really need three new SUV's with heated/chilled cup holders, a DVD player with surround sound and a half-bath onboard? Probably not. This over-spending is what leads to individual credit problems and on a larger scale, to economic challenges for our nation.



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What's in CCARDA for Me?

The new Credit Card Accountability, Responsibility, and Disclosure Act (CCARDA) signed into law in May 2009 will help to level the playing field for consumers who play by the rules but sometimes find that their credit card companies are treating them like a poor credit risk.

The new law prevents creditors from making rate changes on existing balances without reason or warning unless you are sixty days behind on payments. Any rate change that does occur must be rescinded after six months if all payments are made on time. Monthly statements will need to show how making only the minimum payment affects the time it will take to pay off the balance at the current interest rate.

Statements will need to be written in "plain English" so that consumers can understand all terms and calculations. No one under the age of twenty-one years will be allowed to get a credit card until their income is verified or parental consent is given. All payments will first be applied to higher-interest rate balances instead of the lowest-rate balances. Statements must be mailed to consumers so that they have at least twenty-one days to make their payment on time. While these changes will not protect consumers who make late payments, exceed their credit limits, or violate the terms of their agreements, it will help the majority of people who do pay on time and use their cards responsibly.

Annual Withdrawal Rate

Most planners say that you should aim to withdraw 3 to 5 percent a year of your retirement assets in order to preserve your income-producing principal and to be able to sustain your lifestyle in the event that you live beyond your initial expectations. A withdrawal rate of 3 percent will allow withdrawals for 30+ years and a 5 percent rate allows for 20 years of withdrawals. Normally, your first year withdrawal does not include an adjustment for inflation. The second year and every year thereafter of withdrawals can include the prevailing rate of inflation. For example if your retirement assets total \$500,000 and you withdraw 5 percent or \$25,000 the first year, then you would withdraw \$25,000 plus the rate of inflation the second year. If inflation is running at 3 percent, you would add 3 percent to your \$25,000 and your total withdrawal would be \$25,750. For purposes of this example, we have ignored the investment return on the remaining asset balance, but the benefit to taking only 5 percent a year from your balance is that your investment returns, less inflation, may be very close to a net change of nearly zero, and you could find that your assets last much longer than you expected. You can always spend more than you forecast to spend if you find that your income-producing assets are generating more distributable income than planned.

Alternative Minimum Tax

The Alternative Minimum Tax (AMT) was created to close loopholes that high income taxpayers were using to avoid paying federal income taxes. In 1970, when the AMT was first introduced, it was very specific to those high income taxpayers who employed various tax avoidance strategies. Today, it has broadened to include many ordinary taxpayers who would not be considered high-income earners. The AMT can be triggered by the taxpayer's use of deductions referred to as "tax preference items." These items may include state and local income, sales, and property taxes, accelerated depreciation, medical expenses, miscellaneous itemized deductions, percentage depletion, some types of tax-exempt income, certain kinds of credits, personal exemptions, and the standard deduction. What concerns taxpayers and tax experts alike is not only the tax preference items that can trigger AMT but



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Volume II, Issue 2

Alternative Minimum Tax (continued)

the tax rate itself, which is 26 percent on the first \$175,000. In 2004, the Congressional Budget Office said that "Over the coming decade, a growing number of taxpayers will become liable for the AMT. In 2010, if nothing is changed, one in five taxpayers will have AMT liability and nearly every married taxpayer with income between \$100,000 and \$500,000 will owe the alternative tax. Rather than affecting only high-income taxpayers who would otherwise pay no tax, the AMT has extended its reach to many upper-middle-income households. As an increasing number of taxpayers incur the AMT, pressures to reduce or eliminate the tax are likely to grow."

The AMT is a complex and difficult part of the tax code to understand. If your tax return includes any of the tax preference items detailed above, you should consider using a tax professional to prepare your tax return. The AMT tax is higher than the standard bracket amounts and not paying the AMT could result in penalties and interest being levied against you by the IRS.

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Our mailing address is:

Wealth Hazards, Inc.

4780 Ashford Dunwoody Road

Suite A527

Atlanta, GA 30338

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