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Third Quarter 2013

Top Income-Earners Drive U.S. Economic Growth

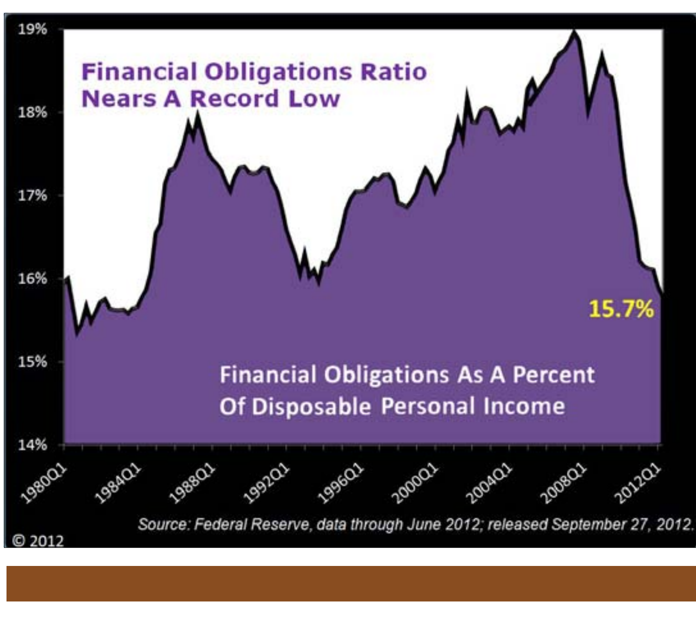
Have you been surprised by the slow but steady growth in the U.S. economy over the last three years and the accompanying doubling in U.S. stock prices in major indexes of the broad stock market? The explanation for these two very positive economic developments may lie in the distribution of income and spending in America, specifically in their skew toward wealthier individuals. To be clear, it's not the top 1% of wealthiest Americans driving the recovery but the top two income quintiles, the middle class — the top 40%.

The top two income quintiles account for 61% of total spending in the U.S. economy, according to statistics released in September 2012 by the U.S. Bureau of Economic Analysis. The bottom two quintiles account for just 22% of total spending.

The top 40% of income earners in the U.S are in good enough financial condition to spend at a level sufficient to fuel slow growth, and recent economic reports indicate that this is likely to continue. Consider the following:

Auto Sales are recovering from the dismal period in 2008 and 2009. Because car sales collapsed during the recession, rising demand for new cars is likely to continue. "Cars have a limited useful life," says Fritz Meyer, an independent economist, "and the age of the fleet should propel new sales in the months ahead."

Housing Starts have rebounded strongly since the recession. The U.S. population increases by about three million a year, according to the U.S. Census Bureau. As a result, the nation needs about 1.5 million housing starts annually, Meyer says. In the years leading up to the recession — the housing bubble of 2005 and 2006 — housing starts soared to nearly two million. After the bubble burst and the recession took hold, housing starts plunged in 2009 to a low of about 400,000 annually. Since then, however, a recovery has pushed the rate to about 700,000 housing starts. Mortgage Bankers Association forecasts, along with the long-term population growth trend, support the case for a continued recovery in housing.



Household Balance Sheets are about as strong as ever. The Federal Reserve's financial obligation ratio, which measures

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Many Women Face Special Challenges As Retirement Nears

Women often find themselves at a disadvantage when it comes to providing for their retirement years. Data shows women tend to live longer than men do, to earn and save less, to bear the financial brunt of divorce and widowhood, and to spend more time and money taking care of family members.

Life expectancy is increasing for both men and women. But women outlive men by an average of five years, according to the Centers for Disease Control and Prevention. Once a U.S. woman reaches age 65 she is likely to live to the age of 85. That makes women far more likely to outlive their assets.

Advocates debate the reasons behind income disparity, but the fact is that women earn 77 cents for every dollar men earn, according to the U.S. Census Bureau. That means women have fewer dollars to put toward retirement savings, and earn less in Social Security benefits.

Historically, women save less money than men. They usually make less, first of all, and thus are more likely to depend on their spouse's earnings for savings. Women also spend more time and money helping ill family members than do men.

For all of these reasons, losing a spouse, whether through divorce or death, can have a more drastic impact for a woman than a man.

The message is clear: Retirement planning is a vital necessity for women. We recognize the challenges you may face, and we can help you overcome them.

Ron Dickinson

How To Bridge A Retirement Shortfall

Suppose you've scrimped and saved for retirement but you still haven't met your goals. Or perhaps an illness or a business venture that went south has exhausted your discretionary funds. Or maybe you just didn't count on costs rising so quickly. In any event, you're standing on the precipice of retirement, but you don't think you'll have enough to live comfortably for the next 20 or 30 years. These four practical suggestions might help:

1. Relocate to a less expensive home. According to the Social Security Administration, housing is the largest component of living expenses for people over age 55, accounting for 35% of the cost pie. One of the best ways to save money during retirement may be to downsize your home. Do you really need that rambling four-bedroom colonial in which you raised your kids? You probably do not.

And it's not just size that matters. You might consider moving to a location where the climate is agreeable and the costs are lower than what you're currently paying. Just don't forget to factor in state income taxes and other taxes. For the adventurous, a move out of the country could be an option.

Here's another thing to add to the equation if you're considering relocation—it's usually less expensive for people to live together than alone. A recent study by the Pew Research Center, based on 2011 Census Bureau data, reveals that the number of Americans living in multi-generational family households increased 4.9 million from 2007 to 2009. You could move in with your children, pay your share of the housing costs, and still come out ahead.

2. Refinance your mortgage. With interest rates at historic lows, now's a good time to refinance an existing mortgage if you don't plan on moving anytime soon. If you can cut your monthly bill by hundreds of dollars or more, it won't take too long to recoup the refinancing costs.

3. Figure out your bottom line. Budgeting isn't exciting, but making realistic projections of your likely expenses in retirement can be crucial. Frequently, costs for life insurance and spending on children will disappear as you move closer to traditional retirement age, only to be replaced by travel expenses or other new costs.

4. Go to work part-time. Being "retired" doesn't mean you have to quit working completely. The job market for seniors has been improving, with the Bureau of Labor Statistics showing a 5.6% unemployment rate for those 55 and older in February 2013, compared with 6.1% the year before. Getting a paycheck, even a relatively small one, can remove some of the pressure and supplement your income from investments, Social Security, and distributions from retirement plans.

Finally, take stock of your situation while you're still employed full-time. Planning ahead is the best solution for bridging a potential retirement shortfall. ●

Want To Shift Income? Give It Away

With three key tax provisions that took effect in 2013 raising the ante for high-income earners, you may be inclined to look for ways to shift income-producing assets to family members in lower tax brackets. That can be effective, as long as you're comfortable with the trade-offs.

By now, you know about the tax changes affecting those in upper-income brackets. There's a higher top rate for income—now 39.6%, up from 35%, which applies to single tax filers with income above $400,000 and joint filers above $450,000. There also has been a tax hike on capital gains and qualified dividends, with the usual maximum 15% rate for long-term capital gains and qualified dividends jumping to 20% for tax filers above those same income thresholds. And, finally, there's the Medicare surtax, a new 3.8% tax that applies to the lesser of net investment income or the amount by which your modified adjusted gross income exceeds $200,000 for single filers and $250,000 for joint filers.

What is the end result? If you earn enough, you might be forced to pay a combined 43.4% tax rate on some of your income, and that doesn't even count additional state or local income taxes.

To lighten this heavier tax load, there are several possibilities, including sophisticated trust arrangements. But by far the simplest—and potentially one of the most effective—ways to shift income is to give outright gifts to your children or to other low-taxed family members. Not only will the earnings from property you give away be taxed to your offspring—instead of to you in your higher tax bracket—but you also may be able to reduce or eliminate the 3.8% Medicare surtax.

Suppose you're in that combined 43.4% tax bracket and you shift $10,000 of annual taxable income to

13 Of The Best Midyear Tax Moves For '13

Now that you've put your 2012 tax return to bed, it's time to focus on 2013. Because of tax rate increases for upper-income taxpayers and a new surtax on investment income, it is especially important to get an early jump on tax planning. If you wait until the end of the year, it may be too late.

Although everyone's situation is different, and not all of these may apply to you, consider these 13 midyear tax strategies for '13:

1. Harvest capital losses. For your 2013 return, the usual 15% maximum tax rate for long-term capital gains is boosted to 20% for single filers with income above $400,000 and joint filers above $450,000. But you still can use capital losses recognized during the year to offset capital gains, plus up to $3,000 of ordinary income that now will be taxed at rates as high as 39.6%.

2. Realize capital gains. Conversely, remember that your capital gains are effectively tax-free up to the amount of your annual losses. That could be particularly valuable now that the capital gains rate is higher for some taxpayers and you also could face the new 3.8% Medicare surtax, which applies to the lesser of your net investment income or your modified adjusted gross income above $200,000 for single filers and $250,000 for joint filers.

3. Avoid the wash-sale rule. If you acquire "substantially identical" securities within 30 days of selling an investment at a loss, the loss can't be deducted on your tax return. Avoid this harsh "wash-sale" result by waiting at least 31 days to buy back the same securities. Alternatives are to buy more of the holding first and wait at least 31 days to sell the original shares or to replace them with an investment that's similar but not identical.

4. Invest in dividend-paying stocks. Qualified dividends still are taxed at a maximum 15% rate for most investors, although a 20% rate applies to those above the same income thresholds for long-term capital gains. To qualify for a favorable tax rate, you must hold the dividend-paying shares for at least 61 days.

5. Arrange an installment sale. Generally, you can defer tax on the sale of real estate or other property if you receive payments over two years or longer. Not only do you stretch out your tax payments, but you also might reduce the effective tax rate if you stay below the thresholds for capital gains and the 3.8% surtax.

6. Contribute to your 401(k). One sure-fire way to lower your tax liability is to increase contributions to a 401(k) plan where you work. For 2013, you can elect to defer as much as $17,500 to your account ($23,000 if age 50 or over). Not only do you avoid tax on the contributions, they can compound tax-free until you withdraw the money during retirement.

7. Convert to a Roth IRA. If you have funds in a traditional IRA, you can convert some or all of that money to a Roth IRA. Future "qualified" Roth distributions won't be taxed. To avoid absorbing a big income-tax hit—due on money you transfer—all at once you could spread out conversions over several years.

8. Transfer IRA funds to charity. For 2013, someone age 70½ or over can withdraw up to $100,000 from an IRA and give it directly to charity without any tax consequences. This tax break, which had expired recently, now has been extended through the end of 2013.

9. Sell the old homestead. The tax law allows you to exclude tax on a gain of up to $250,000 for single filers and $500,000 for joint filers if you've owned and used the home as your principal residence at least two of the past five years. The excluded amount is exempt from the 3.8% surtax.

10. Rent out a vacation home. You can write off certain rental activity costs, plus depreciation, but you must be careful. If your personal use exceeds the greater of 14 days or 10% of the days the home is rented out, deductions are limited to the amount of rental income. Keep summertime personal use below the threshold.

11. Give grads generous gifts. Generally, you can claim a $3,900 dependency exemption for a child graduating from college in 2013 if you provide more than half of the child's support. Figure out the amount of a gift needed to put you over the half-support mark.

12. Install energy-saving devices. The tax credit for energy-saving improvements in a home—such as central air conditioning—is restored for 2013. But the maximum credit of $500 is reduced by expenses claimed in prior years.

13. Adjust your withholding. Finally, due to all the tax-law changes in 2013, you may not be withholding enough income tax from your paychecks. Make the adjustments needed to avoid an "estimated tax penalty" this year. ●

each of three children in the 25% tax bracket and two grandchildren in the 15% bracket. You'll save a total of $11,200 in taxes, this year, next year, and every year until the rules change again. (You will, however, have to watch out for the "kiddie tax," which calls for unearned income above a threshold—$2,000 in 2013—received by a dependent child under age 24 to be taxed at the parents' top tax rate.)

Though transfers to your kids are subject to gift tax, you can use the annual gift-tax exclusion ($14,000 per recipient in 2013) to limit that liability. And the annual exclusion is doubled for joint gifts by a married couple. If there's an excess, it may be covered by the lifetime gift-tax exclusion ($5.25 million in 2013). Similarly, direct gifts to grandchildren are sheltered from the generation-skipping tax by an exemption of the same amount.

Realize, though, that these are irrevocable gifts, so you're giving up complete control over the property. If you're not comfortable with that, you'll need to consider other options for reducing those higher taxes. ●

Computers For Grandparents: 10 Tips

Older brains stay younger with stimulation, and social media and photo-sharing allows you to stay in touch with your family. But which computer is best for grandparents? Here's some help.

1. Old Computers. If your children offer you a computer, only consider it if it's less than three years old. Prices have dropped on computers and you can probably find one for $1,000 or less.

2. What's It For? If texting, email, web-surfing, and video-chat are all you need, consider a tablet that has the advantage of portability.

3. Mac Or PC? An iPad will be easiest for a novice. But if you're a veteran PC-user, you may prefer a Windows tablet. If you already own an iPhone, stick with an iPad or Mac computer because you already know how to operate it.

4. Screen Size. New tablets and "ultraportable" computers now come in small sizes. Before buying a screen less than 11-inches in diameter, be sure you can read all the text in emails and on the Internet.

5. Set Up. If you're a novice, salespeople at the computer store will help you learn how to set up your new machine. Apple and Microsoft stores often offer classes. Or maybe you can persuade a child or grandchild to help you.

6. App Store. Whether you're seven or 75, the app store has something for you. No matter what your age, make sure you know how to use the app store.

7. FaceTime Or Skype. Be sure to set up a video calling service. Apple FaceTime and Skype are free and easy to use once they're set up, and they allow video calls across the country or across the world for free.

8. Sharing Photos. Ask family members whether they use any photo-sharing or social websites already, such as Facebook, Twitter, or Flickr. They can send you an invitation to see all their photos. With Flickr, which allows you to store and share photos for free, you can set up an account that only family members can see.

9. Passwords. A password-management program would be wise. LastPass.com is free, easy, and secure, but there are many other options.

10. Financial Data. Accessing your financial accounts online can make life simpler, but security is paramount.

If you're not a veteran Web surfer, before posting sensitive information or accessing your accounts, please call our office. We would be happy to help you get the basics set up so you can access your information securely 24/7 from anywhere. ●

Top Income-Earners Drive

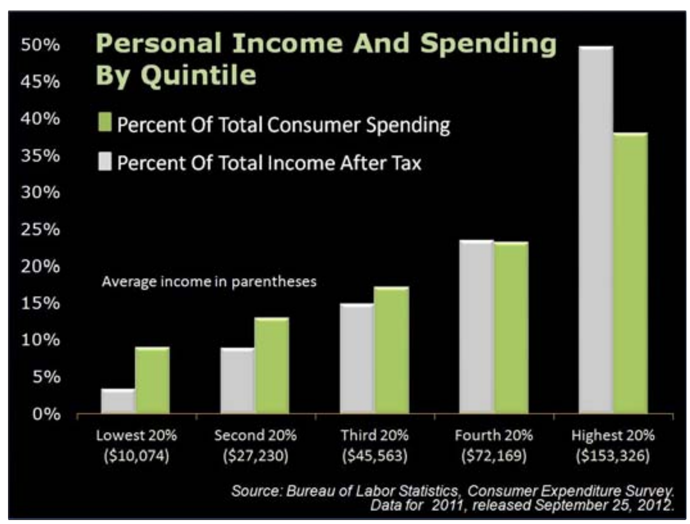
(Continued from page 1)

consumers' fixed expenses compared to disposable income, has fully recovered since the recession. At 16%, households have 84% of after-tax income with which to make purchases.

"Consumers' ability to cover their monthly 'nut' has seldom been better," according to Meyer. "As incomes have recovered, household debt has been reduced and interest rates remain low."

The financial obligations ratio consists of estimated required payments on outstanding mortgage and consumer debt plus automobile lease payments, rental payments on tenant-occupied property, homeowners' insurance and property tax payments divided by disposable personal income.

The data on the top two income quintiles does not address whether wealth in America is more concentrated. But it does debunk the myth that the top 1% controls the American economy. It also shows, unfortunately, that individuals in the lowest income quintile are finding it difficult to meet expenses. Still, it is comforting to know that the nation's economy and the rise in corporate earnings behind the stock market's three-year rebound are driven by a broad demographic group, and their ability to continue to fuel a slow-growth recovery appears fundamentally sound. ●



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