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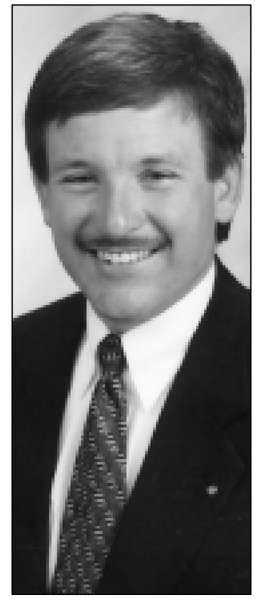
Fourth Quarter Newsletter 2003

Are You Sabotaging Your Investment Goals with Poor Decision-Making?



Experts in behavioral finance – the somewhat new but growing area of study that focuses on the psychology of investing – say such pre-determined factors as our gender, as well as the attitudes we develop about money early on in life, can have a profound effect upon our financial decisions. These factors can determine if and how much we choose to save, spend and invest. Consequently, one it comes to investing, it doesn't always makes sense to "follow your gut." Quite often, attitudes about money and investing are irrational, ill-informed, or emotional responses not based on objectivity.

An experienced financial advisor can do more than just tell you where to invest your money. He or she can also prevent you from making bad investment decisions based on your ingrained beliefs or behavior. As strange as it may sound, many investors continue to make the same mistakes over and over and over. Mistakes we routinely see include: investors who accept advice from splashy financial magazines or friends that have anointed themselves as financial gurus, investors who "save" money by handling their own affairs but fail to consider the cost of the inadequate tax strategies and lower performing investments, business owners who are "too busy" to take the time to evaluate their retirement plans, and investors who have been advised that change is necessary but refuse to make that change because the long-term benefit includes an immediate short-term discomfort (usually involving some sort of capital gains tax).

Bernard Shaw once said, *"Success does not consist in never making mistakes but in never making the same one a second time."* Yet, many investors are never able to achieve financial success because they keep making the same mistakes over and over. Awhile back, University of Wisconsin Professor Werner De Bondt conducted a study by that proves just how powerful of role such "inner forces" can play in the investment process. The study concluded that, left on their own, without the assistance of a professional advisor, most people have a tendency to make poor investment decisions. Many individuals not only lacked an understanding of basic investment principles, they also bought into certain investment myths – such as the tendency to "jump on the bandwagon" and buy stocks that are heading up and sell stocks that are headed down, when just the opposite is the tendency of the experienced investor.

De Bondt's findings also prove that "going with your gut" doesn't pay. His Wisconsin study concluded that when making investment decisions on his or her own, an individual's intuition "often fools us and counsels the opposite." A wiser option, therefore, would be to seek the counsel of a professional money manager, who is trained to recognize damaging investment behavior and point you on a smoother and more profitable path toward your investment goals.

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Estate Planning For Blended Families

Chances are as you look across your Thanksgiving table this November you will be looking at a step-parent, step-child/sibling/cousin or other relation as the result of divorce and remarriage. With 50% of marriages ending in divorce virtually every family now has some sort "step" relative. Has your estate plan carefully considered the myriad of relationships that exist within your blended family?

Although no specific legal documents or investments apply exclusively to blended families, traditional estate planning strategies often need to be adjusted to fit the considerations of a blended family. One of the most important things to consider is the relationship that exists between the children of the first marriage and the stepparent. This is especially critical if the children were older at the time of the second marriage. In these circumstances, there may be a friendly relationship but hardly a parental one. Sadly, at the death of the biological parent, greed that had no rational basis before might suddenly be attributed to the stepparent or the stepchildren leading to nasty family fights and time consuming and expensive litigation.

Here are a few basic strategies to consider when creating an estate plan for your blended family:

The Will: In a traditional family, generally the surviving spouse receives the majority of personal property with perhaps specific bequests to the children. In a blended family, this situation should be addressed more explicitly. Careful planning calls for the biological parent to precisely identify what family items from the first marriage should be left to the biological children. Usually it is left to the parent to create an addendum that will list such items, and far too often, nothing has been done by the time of death.

Also, who is named as executor should be careful consideration. While traditional families routinely name an adult child as executor this may not be the best option for blended families. The relationship between the executor/stepchild and step-parent may suffer irreversible damage as the result of the administration of the estate. Even in cases where the relationship was friendly, the process of estate administration may ruin the relationship completely. This is one situation where it may be advantageous to name a corporate executor. As an unbiased third party, the corporate executor will be able to speak and act from the perspective of the deceased and clarify wishes and direction. This objectivity may defuse difficult situations and allow the survivors not to feel at odds with each other.

Lifetime Giving: If maintaining friendly relationships among survivors is important, to the extent that all parties feel as though they have been treated fairly relationships are likely to remain intact. Lifetime giving presents an opportunity for both the biological parent and the step-parent to work together in participating in the gifting process. Since both parties are involved, resentment that might otherwise develop after the death may be avoided or minimized as children see that their parent has made a reasonable concerted effort to share inheritance through life.

Parents can use "gift-splitting" to accomplish their gifting wishes. Gift-splitting must be used for all gifts made throughout the year. Such gifts, if qualified as present interest gifts, do not have tax consequences so long as they fall under the limits of the annual gift tax exclusion ($11,000 per person or $22,000 per couple). Of course, either parent can make a larger gift and elect to use their unified credit before death. In this case, only the filing of a gift tax return would be required.

Gifting might be the right strategy for your situation. However, keep in mind that by gifting you lose some ability to create a tax efficient and integrated estate plan.

Qualified Plans: Frequently, the largest asset a couple has, qualified plans should be closely examined. In situations where the parent has named the spouse as primary beneficiary and all children equally as contingent beneficiaries, equitable or equal distributions may become an issue. After the death of the parent and once the plan has been transferred to the spouse, the souse can then change the beneficiary of her plan(s) to benefit her own children at a later date. Assuming the account is large enough, this predicament can be avoided by dividing plan assets into several accounts-one for each child and the spouse.

Further, naming a child as a beneficiary is extremely beneficial to the child. With this type of "inheritance" the child can set up a "stretch IRA" and take distribution over their lifetime. Since the child will be taking a significantly smaller minimum required distribution (RMD), the account will continue to grow tax-

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Beware of Financial Magazines and Talk Shows: Don't believe everything you read or hear...

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financial advocate will not engage in market timing and will help investors stick to a well thought out comprehensive plan that takes market fluctuations into consideration. A good financial advocate will not be swayed by glossy magazines or "fast" money investments.

Finding a good financial advocate isn't that hard but will take some diligence. Most financial "planners" base their compensation on products they sell you. Others are compensated in part by commissions and in part by a fee. This arrangement leaves many investors feeling uncomfortable. After all, these planners have a built in conflict of interest-they need to sell you something in order to make a living. How does the individual investor know if what is being sold is really in his best interest? Are these planners really your "advocate"?

Investors looking to avoid this conflict of interest should consider using a strictly fee-only financial advocate like Vigil Trust and Financial Advocacy. Fee-only advocates provide financial advice (estate planning, retirement, investments, etc.) based solely on the client's best interest. Further, many fee-only advocates, like Vigil, base their ongoing fee on a percentage of assets under management. For example, the better Vigil does for the client the more the client and Vigil both earn and vice versa. Compare this approach to financial journalism where the success of a magazine/television show has little to do with the quality of the advice given.

Estate Planning For Blended Families

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free through long-term capital appreciation. When you consider that under the new regulations each child can use his life expectancy rather than the eldest beneficiary's life expectancy, the compounded earnings have the potential to considerably increase the value of the initial gift. If the plan is first transferred to the surviving spouse, a larger MRD will have to be taken until her death, regardless of income need.

But before you rush out and change your beneficiary designations consider these three dangers. First, will the surviving spouse need to access all plan assets in order to generate enough income? Second, will naming children waste the use of estate tax spousal deduction and generate unnecessary estate taxes? Third, will naming grandchildren as beneficiary trigger a generation skipping tax. At the end of the day, it may be best to name a trust as the beneficiary if individuals other than the spouse are named as beneficiaries.

As mentioned, there is no special document that applies only to blended families. In creating your estate plan be careful to consider and share with your financial advocate all of the potential problems that could materialize. Your financial advocate will then assist you in adjusting traditional estate planning tools to help lessen the possibility that an acrimonious relationship will develop between your loved ones.

IRS Announces Additional Pre-Tax Saving Opportunity

Effective September 3, 2003, the IRS will now allow you to use your Health Care Reimbursement Account (HCRA) or Healthcare Reimbursement Arrangement (HRA) to reimburse you for over the counter drugs and supplies. Eligible products include antacids, allergy medicines, pain relievers and cold medicines. Over the counter drugs must be used for the purpose of treating a medical condition. The IRA has not addressed the issue of other over-the counter items like shoe inserts, bandages, hot packs. However, these items may be eligible with a letter of medical necessity from your physician. Ineligible products include dietary supplements and non-prescription wellness drugs like vitamins and herbal remedies.

Unfortunately, the IRA is not allowing HCRA or HRA election changes based on this new provision. In order to qualify for reimbursement all products must have been purchased on September 3, 2003, or later.

Thank You For Referrals

The greatest compliment that we receive is when someone calls and says, "I was referred by (you our client)." This lets us know that we are doing a good job and you trust us enough to refer your family and friends to us for their financial needs.

If you have someone in mind that you think could benefit from learning more about Vigil's services and you would like us to contact them please call or send us their name. You need not worry that we will besiege your referrals with a sales pitch. Our initial consultations are always free and at no obligation.

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Beware of Financial Magazines and Talk Shows: Don't believe everything you read or hear...

Have you purchased a financial magazine that screamed "2003's Hottest Investments" or some other urgent investment advice? Do you regularly tune in to cable television investment programs? Have you ever purchased a particular investment based on advice in a magazine or on television? Following the advice of financial magazines and talk shows is not the greatest idea and here's why.

When investors start building their portfolios around the advice of financial magazines and talk shows what they are really doing is looking backwards at what was hot. Financial journalism is all about doing something different now. This tends to make you think that staying the course will cause you to miss trends. In reality, shifting from fund to fund in search of the "hot" investment is just an attempt at market timing and is a recipe for disaster.

So just how is an investor supposed to know when it's time to make portfolio changes? Ask someone who makes these decisions on a daily basis. A good

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