Weekly Commentary
December 7, 2009

The Taxes

Ten Year End Questions You Need to Ask About Your 2009 Tax Situation – <u>Before the End of the Year.</u>

"It was as true... as taxes is. And nothing's truer than them."
Charles Dickens

For many investors, this may be a confusing and uncertain time. After a wild start to the year, the investment markets seem to be stabilizing – for the moment. We may not be back to the previous high-water marks, but a number of stock market benchmarks are up significantly from the lows we saw in March. On the flipside, economic news remains decidedly cautious. One can naturally be caught wondering how things can be getting "better" when unemployment is at ten percent.

Unfortunately, confusion and uncertainty will not delay tax season. As the Dickens quote above relates, little is more certain than tax season. Before you know it, you will be pulling together forms and statements to prepare your 2009 return.

We would like to give you a head start.

<u>Our experience tells us that many tax savings opportunities are missed because proper planning is put off until it is too late to make a difference.</u> In other words, there are decisions you can make in the last month of 2009 that most likely will not be available in April. For example, we are currently holding quarterly review meetings with many of our wealth advisory clients. We help them look for strategies that may take advantage of this year's investment volatility as well as tax law changes. Once we identify potential opportunities, we work with their tax professionals to implement changes.

Below is our 2009 checklist of our ***10 Questions for End of Year Tax Planning***. We use this tool during our client meetings.

Please look these questions over and let us know if you would like to talk about them. We could meet in-person or speak by phone. If you choose not to meet, we hope you find these questions useful as you complete your own tax update.

Most importantly, please don't put this review off until it is too late to make a difference. By working together with a professional financial advisor and your tax professional, you may find more choices for tax savings than you previously thought existed. Many of our clients have saved thousands of dollars in taxes with these strategies.

Checklist - 10 Questions for End of Year Tax Planning

General Income Planning – consider your salary, bonuses, retirement plan payouts, job changes or any other events that may have important financial implications.

1. **Will my taxable income in 2009 be significantly higher than it was in 2008?** If so, have I had the proper amount of taxes withheld or made quarterly payments that will allow me to avoid potential underpayment penalties? Are there investments or deductions I may qualify for that can reduce my tax liability?

2. **I expect my income to be lower in 2010.** Is there a way to defer earned income into future years? (Also consider the reverse scenario of taking more income this year.)

Investment Planning – review how your investments have performed so far this year and consider any significant taxable events that may occur between now and the end of the year.

3. **So far this year, are my capital gains higher or lower than they were in 2008?** Should I realize capital losses to offset gains or potentially ordinary income? For investments I prefer to hold for the long-term, have I considered tax swapping strategies for realizing capital losses? Do I have carry-forward losses from 2008? Should I realize losses in 2009 with the goal of reducing my 2010 income?

4. **Do I need to be on the lookout for income surprises?** Do I own any mutual funds, partnerships or hedge funds that may make taxable distributions before year end? If so, do any opportunities exist to avoid or defer these distributions? Should I consider looking for alternatives or offsets to these investments to avoid this problem in future years?

Retirement Plans and Planning – the rules for making IRA and retirement plan contributions and distributions for individuals and businesses change regularly, you should be sure you understand these changes and how they affect your current and future taxes.

5. **Am I maximizing my company and personal retirement planning options for deferring income and growing my nest egg?** Am I taking maximum advantage of the company match in my 401(k) plan? Which is better for me a Roth or traditional IRA? What are my contribution limits? Am I entitled to any "catch up" opportunities for making contributions to any of these plans? In 2010, will I need to consider converting my traditional IRA into a Roth IRA? Can I do a Roth conversion and potentially offset the resulting tax with a parallel strategy? Many can, call us to see if there are programs that may be a fit for your situation.

6. **I am older than age 70 1/2 and would normally have to take Required Minimum Distributions (RMDs) from my IRAs.** The RMD requirement has been suspended for 2009, should I take one anyway? What is the deadline for taking my distribution? How much would it be this year? Will it increase in 2010? Should I take more than the minimum? Is there a benefit to consolidating IRAs, rollovers and other retirement plans?

7. **I am self employed (or work in a small company).** Are there retirement savings plans designed specifically for me? Will they allow me to defer greater amounts of income than traditional plans?

Gifting, Education Planning and Charitable Contributions – a final area for review falls under the general concept of "gifting". From educational savings plans to outright gifts to charitable contributions, there may be strategies that will allow you to accomplish personal goals while reducing your tax burden.

8. **From a tax planning perspective, is there a more efficient method for funding my children's (grandchildren, other dependents) educational needs?** Should I review or update my 529 plans, custodial accounts or educational IRAs? Do the changes to the 2009 HOPE credit affect our educational planning? I (my spouse) am considering pursuing a new degree, are there tax strategies for advanced funding?

9. **I understand there are annual limitations on the value of gifts I may make to any one individual.** What is the new limit for 2009? Are there advantages to maximizing gifts to certain family members? My children are financially secure, are there tax advantaged strategies for making gifts to my grandchildren?

10. **I am charitably inclined, is it better to gift cash or appreciated securities to my favorite charities?** I don't have a favorite charity at this time, but I have heard about personal foundations and gift funds, how do these work? I own a highly appreciated stock that I would never sell because of the taxes, but could use some additional income, should I consider a charitable trust?

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THERE IS A DIFFERENCE BETWEEN LUCK AND SKILL and knowing when you are just lucky and when you are successful due to skill is of paramount importance as an investor. Let's say you correctly called the flip of a coin five times in a row. What are the odds that you will correctly call the next flip? Correctly calling five coin flips in a row might be considered a "hot streak" and lead you to believe that chances are high you can correctly call the next flip. Well, assuming it is a fair flip, there is, of course, only a 50/50 chance that you will be correct because flipping a coin is a game of known probability. The fact is the coin flip has no memory of your hot streak.

An investor who is on a "hot streak" may or may not be lucky. Let's take John Paulson as an example. He was a faceless hedge fund manager toiling in obscurity until he came upon an idea. He became convinced several years ago that the housing market was a bubble ready to burst. He put his money where his thesis was and he made billions of dollars for himself and his clients, according to a new book, *The Greatest Trade Ever*, by Gregory Zuckerman.

Today, Paulson is the toast of the hedge fund world and his latest "big bet" is that gold prices will continue to rise. This is not a recommendation from us to either buy or sell gold; rather, we want to make a point.

With millions of investors, odds are that some of them will make winning investments numerous times in a row. If these winning investors were, in reality, just lucky, *but they think they were actually skillful*, then that is when the situation turns problematic. The lucky investor may start to think they are infallible and get stubborn when the market turns against them. Eventually, when the lucky streak ends, it will likely mean serious losses for the investor. Only time will tell whether John Paulson got lucky or whether he has substantial investment skill.

The best antidote we know of to the danger of confusing luck and skill is to remain humble. When our investment strategy performs well, we are very thankful. When it doesn't perform well, we try to learn from it. The investment business has an uncanny way of turning hubris into painful losses. We think humility is a safer route.

Weekly Focus – Think About It

"If we become increasingly humble about how little we know, we may be more eager to search."
-- John Templeton

Best regards,

Tony Hartman

P.S. Please feel free to forward this commentary to family, friends, or colleagues. If you would like us to add them to the list, please reply to this e-mail with their e-mail address and we will ask for their permission to be added.

* The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.
* The DJ Global ex US is an unmanaged group of non-U.S. securities designed to reflect the performance of the global equity securities that have readily available prices.
* The 10-year Treasury Note represents debt owed by the United States Treasury to the public. Since the U.S. Government is seen as a risk-free borrower, investors use the 10-year Treasury Note as a benchmark for the long-term bond market.
* Gold represents the London afternoon gold price fix as reported by the London Bullion Market Association.
* The DJ Commodity Index is designed to be a highly liquid and diversified benchmark for the commodity futures market. The Index is composed of futures contracts on 19 physical commodities and was launched on July 14, 1998.
* The DJ Equity All REIT TR Index measures the total return performance of the equity subcategory of the Real Estate Investment Trust (REIT) industry as calculated by Dow Jones.
* Yahoo! Finance is the source for any reference to the performance of an index between two specific periods.
* Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.
* Past performance does not guarantee future results.
* You cannot invest directly in an index.
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