Registered Investment Advisor Firm

©ISSUE VI, VOL. III – *Bud Heng – Registered Adviser (925) 360-6819*

JUNE – 2014

Congratulation Graduates!

For the graduating class of 2014, let me be among the first to say congratulations!

For those graduating from college, you have overtaken the class of 2013 and will now hold the distinction of graduating with the most debt, averaging $33,000. This has more than doubled since 20 years ago. The good news is, the class of 2015 should beat you, amassing even greater debt upon graduation.

The problem with entering the workforce with too much debt, people tend to have a smaller net worth, high credit card and auto loan debts, while having about the save level of mortgage debt.

The mortgage debt can be a good thing to the extent that buying a home means you're contributing to your neighborhood and generally buying things necessary to maintain your home. However, qualifying for that mortgage will be more difficult, while wage growth has become stagnant.

Still even with the college debt, it remains a good choice to attend college where you have a chance to develop skills that will allow for a higher paying career. But if the debt keeps increasing while wages stay the same or start to drop, it may become a different story.

For those high school graduates, you will undoubtedly be hearing any number of speeches at your graduation designed to motivate you and send you onto your future endeavors. If I were to be addressing your class, this would be my message to you:

"You are embarking on a future that is pretty much unknown. You will have moments of joy, sadness and worry, but along the way there will be steps that you can start right now to make sure you have a much better chance of having a wonderful financial future regardless of what life throws at you.

You should develop three critical habits:

- *Save as much as you can for as long as you can. From your paycheck, always pay yourself first. If you get a job with a 401(k), especially one that has an employer matching contribution, make sure you take full advantage, as that path will get you to your goals much more quickly. Develop a savings habit that you can stick with for the rest of your working life.*

- *Don't be afraid of investing aggressively in your investment choices. Even though today you might be feeling worried about your future, whether you'll find a job, keep a job or make enough money to pay your bills. Those worries will naturally drive you to keep enough cash on hand to handle your expenses, but those same worries can keep you from investing aggressively. You can afford to be an aggressive investor meaning you should have more of your investments in stocks than in bonds or cash. Your investing fears you will have in your 60's will not be like the investing fears you have right now. Recessions will happen, markets will go down. There will be market corrections over and over again. If you invest too conservatively, you run the risk of missing out on the gains when markets go up. It pays off to be in the market over the long-term.*

- *Make time work for you! Many of you will run off to begin your life adventure, maybe travel the world, volunteer for worthy causes, etc. But remember this, you only live once and will have one shot at retirement. Do not wait to find time to grow your wealth, get to it now. For example, Jill at age 22 decides to begin investing for her future and saves $2,000 per year for the next 15 years and then stops saving. At age 65, Jill's retirement account would be about $550,000 assuming an 8% annual compounded rate of return. Jack decides to start at age 35 and saves $2,000 per year for the next 30 years, and at age 65, Jack will have about $245,000. Jack invested for twice as long as Jill and ended with up less than half the amount. Jill used time and compounding returns to a far greater advantage. Image what Jill's account would be worth if she hadn't stopped after just 15 years?*

Thank you, I wish you all only the best, now get out there and get a job!"

DIY or Hiring Competent Help?

I occasionally get asked "how can I make sure I'm doing the right thing with my retirement account" by those who have decided they want to or believe they can, manage their investment accounts on their own – a Do-It-Yourselfer (DIY) manager.

The first thing I tell them is that without knowing more about their personal circumstance, their goals and objectives, I could never provide them with sound advice, and anything I offered would be nothing more than they could can get from a monthly publication of *Money* magazine or

Kiplinger's. Even though those publications tend to run promotions like "the only investment you need to own for the next ten years," there is no obvious consideration as to your personal circumstance, so any advice must be weighed in that context.

Without getting into particulars, I'm always willing to listen and provide a macro-view of the investing process and based on questions, I'm able to assess their concerns and sometimes render a "second opinion."

Investment management is not a set-and-forget process. It requires a considerable amount of time and attention if you ever expect to achieve certain defined goals and objectives.

On other occasions I get asked "can you guarantee results or that I will never lose money?" I quickly point out that I would never make such a guarantee and if anyone ever does, they should walk away. All investments carry some level of risk and I like to ask "where do you currently have your investments?" I'm typically told "in a savings account so I don't lose money."

This invariable leads to the discussion of "yes, your accounts are typically insured up to the FDIC limits," but "you do realize that the .15% you earned last year in interest means you only lost about 2.25% due to inflation (and inflation is running below historic norms)?" The responses to this economic fact are usually mixed, though typically I hear "yes, but I still have my (pick a number) when I want or need it." All true, except for the "yes" part, telling me they don't understand or are in denial over the devastating effect inflation can have over time.

Is keeping your money in "cash" a wise choice? The answer is yes and no. Yes as an asset class when market conditions dictate or your personal circumstances require extreme liquidity where a portion of your investable assets can and should be in cash. No, when it represents <u>all</u> your investable assets, and it's parked idly over an extended period of time, wasting away to inflation.

Don't believe me - hyperinflation eroded the value (buying power) of the Zimbabwe dollar so badly they were forced to print a 100 Trillion dollar banknote:

So whether you decide to become or remain a DIY investor, you owe it to yourself to become and stay informed – after all, it's your money, your future, your retirement, your legacy.

Rollover IRA Changes

In keeping with the previous month's theme, a change in the IRA rollover rules starting in 2015 could cause issues you need to be aware of. Beginning with distributions in 2015, the IRS will enforce the one IRA-to-IRA rollover-per-12-months rule, without consideration as to if the distributions came from the same or different accounts.

Normally, a plan distribution can be "rolled-over" into the same or another retirement plan within 60 days of the distribution with triggering a taxable event.

The tax code says an "IRA distribution cannot be rolled over tax-free to an IRA if any other IRA distribution received within the preceding 12 months was rolled over tax-free to an IRA." In other words if you do an IRA-to-IRA rollover, you cannot roll over, to any IRA, another IRA distribution received within 12 months after the first distribution.

Presumably the purpose of this rule is to prevent someone from keeping his IRA money continuously outside of the IRA using a series of tax-free rollovers. The IRS has historically interpreted this provision a little more leniently than the actually wording of the code.

This change is the result of a recent case coming out of the Tax Court where an individual withdrew $65,064 from IRA #1. The disposition of these funds were not part of the record, so I assume the funds were spent. Prior to the 60 day period from the date of the withdrawal from IRA #1, another withdrawal from IRA #2 took place in the amount of $65,064. These funds were deposited to IRA #1 within the original 60 day window, completing what the individual thought was allowed under the law. Thereafter, the taxpayer's wife withdrew $65,064 from her IRA (IRA #3) and used those funds to replenish the withdrawal from IRA #2.

There was some dispute as to when the distribution from IRA #3 was "rolled back" into that IRA, but those details did not affect the decision of the Tax Court in this matter.

The Court actually ruled against the taxpayer and the IRS in the case and as a result, the IRS said it would revise its own Publication 590 rule to comport with the Court's ruling.

The once-per-year rule is a trap waiting for the uninformed. For one thing, it's not always clear what a "distribution" is.

For instance, if you request a "cash-out" of your IRA and the IRA provider sends you two separate checks a month apart, the question becomes - is that one distribution or two?

Also, consider someone who has their IRA in six-month CDs. Most banks treat each CD as a separate new IRA, which they close and distribute when the CD matures. If you have multiple CDs in IRAs that close out within 12 months of each other, you won't be able to roll over any but the first one, meaning the remaining funds could become a taxable distribution at maturity.

The best way to avoid getting into trouble with this rule is to always use direct IRA-to-IRA transfers instead of "60-day rollovers." There are no numerical limits on IRA-to-IRA transfers. Direct transfers have always been safer than 60-day rollovers, and now the risks of using rollovers are even greater than before. Make sure you consult IRS Publication 590 if you have any questions.

Davis Investment Group

Davis Investment Group is a fee-based Registered Investment Advisor firm servicing the needs of clients across the United States.

Davis Investment Group custodies all client assets at Charles Schwab & Co. Davis Investment Group's home office is located at 714 Marin Street, Suite #C, Vallejo, CA 94590. The telephone number is (707) 648-2024.

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