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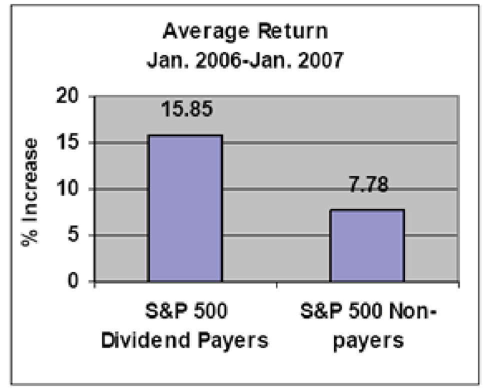
THE FINANCIAL NEWSLETTER OF FINARC, LLC

The Power of Dividends in a Portfolio

It wasn't so long ago that many investors regarded dividends as roughly the financial equivalent of a record turntable at a gathering of MP3 users--a throwback to an earlier era, irrelevant to the real action.

But fast-forward a few years, and things look a little different. Since 2003, when the top federal income tax rate on qualified dividends was reduced to 15% from a maximum of 38.6%, dividends have acquired renewed respect. Favorable tax treatment isn't the only reason, either; the ability of dividends to provide income and potentially help mitigate market volatility also is attractive to investors. As baby boomers approach retirement and begin to focus on income-producing investments, the demand for high-quality, reliable dividends is likely to increase.



Source: Standard and Poor's

Why consider dividends?

Dividend income has represented roughly one-third of the monthly total return on the Standard and Poor's 500 since 1926. According to S&P, the portion of total return attributable to dividends has ranged from a high of 53% during the 1940s--in other words, more than half that decade's return resulted from dividends--to a low of 14% during the 1990s, when investors tended to focus on growth.

If dividends are reinvested, their impact over time becomes even more dramatic. S&P calculates that $1 invested in the Standard and Poor's 500 in December 1929 would have grown to $57 by September 2005. However, when coupled with reinvested dividends, that same $1 investment would have resulted in $1,353. (Bear in mind that past performance is no guarantee of future results, and taxes were not factored into the calculations.)

Dividends can be especially attractive if the market is producing relatively low or mediocre returns. If a stock's price rises 8% a year, even a 2.5% dividend yield can push its total return into the double-digit range; in some cases, dividends could also help turn a negative return positive. Also, many dividend-paying stocks represent large, established companies that may have significant resources to weather an economic downturn.

The corporate incentive

Financial and utility companies have been traditional mainstays for investors interested in dividends, but other sectors of the market also are beginning to offer them. For example, investors are stepping up pressure on cash-rich technology companies to distribute some of their profits as dividends. In June 2007, the number of companies offering dividends was 3% higher than the year before, according to S&P, though increases in the amounts paid have been slowing in recent years.

Dividends are by no means guaranteed; a company's board of directors can decide to reduce or even eliminate them. However, a steady and increasing dividend is generally regarded as one sign of a company's ongoing health and stability. For that reason, most corporate boards are reluctant to send negative signals by cutting dividends.

Look before you leap

Investing in dividend-paying stocks isn't as simple as just picking the highest yield. Some dividends, such as those paid by real estate investment trusts (REITS) and master limited partnerships, don't qualify for the 15% maximum tax rate, and a portion may be taxed as ordinary income. If you're investing for income, consider whether the company's cash flow can sustain its dividend. Also, the 15% rate is scheduled to expire at the end of 2010, and there is no guarantee dividends will continue to receive favorable tax treatment.

If you're interested in a dividend-focused investing style, look for terms such as "equity income," "dividend income," or "growth and income." Also, some exchange-traded funds (ETFs) track an index comprised of dividend-paying stocks, or that is based on dividend yield; be sure to check the prospectus for information about expenses, fees and potential risks, and consider them carefully before you invest. A financial professional can evaluate the role dividends might play in your portfolio.

Income in Retirement

You've worked hard your whole life, anticipating the day you could finally retire and enjoy your golden years. Well, that day has arrived. There's still work to be done, however--you'll need to carefully manage your assets so that your retirement savings will last as long as you need them to.

Review your portfolio regularly

It's commonly said that retirees should value the safety of their principal above all else. For this reason, some people shift their investment portfolio to fixed-income investments, such as bonds and money market accounts, as they approach retirement. The problem with this approach is that if returns don't keep up with inflation, an investment portfolio may not enjoy the growth needed to fund today's longer retirements.

So while there are good reasons to invest more conservatively as you grow older, consider maintaining at least a portion of your portfolio in growth investments.

Choosing a sustainable withdrawal rate

A key factor in determining whether your assets will last for your entire lifetime is the rate at which you withdraw funds. The more you withdraw, the greater the likelihood you'll exhaust your resources too soon.

On the other hand, if you withdraw too little, you may not enjoy your retirement as much as you could. It's vital that you estimate an appropriate withdrawal rate for your circumstances, and determine whether you should adjust your lifestyle and/or estate plan.

An appropriate withdrawal rate depends on many factors, including the value of your current assets, your expected rate of return, your life expectancy, your risk tolerance, inflation, your expenses, and whether you want some assets left over for your heirs.

Studies have tackled this issue, resulting in the creation of tables and calculators that can provide you with a range of rates that have some probability of success. A financial planning professional can help you with this.

Which assets to draw from first?

Most retirees have assets in accounts that are taxable (e.g., CDs, mutual funds), tax deferred (e.g., traditional IRAs), and tax free (e.g., Roth IRAs). Given a choice, which type of account should you withdraw from first? The answer is--it depends.

For retirees who don't care about leaving an estate to beneficiaries, the answer is simple in theory: withdraw money from taxable accounts first, then tax-deferred accounts, and lastly, tax-free accounts. By using your tax-favored accounts last, and avoiding taxes as long as possible, you'll keep more of your retirement dollars working for you.

In practice, however, your choices, to some extent, may be directed by tax rules. Retirement accounts, with the exception of Roth IRAs, have minimum annual withdrawal requirements. In general, your first withdrawal must be made by April 1 of the year following the year you turn age 70½, with subsequent distributions due each December 31. Failure to do so can result in a 50% excise tax imposed on the amount by which the required minimum distribution exceeds the distribution you actually take.

For retirees who intend to leave assets to beneficiaries, the analysis is more complicated. You need to coordinate your retirement planning with your estate plan. For example, if you have appreciated or rapidly appreciating assets, it may be more advantageous for you to withdraw from tax-deferred and tax-free accounts first. This is because these accounts will not receive a step-up in basis at your death, as many of your other assets will.

However, this may not always be the best strategy. For example, if you intend to leave your entire estate to your spouse, it may make sense to withdraw from taxable accounts first. This is because spouses are given preferential tax treatment with regard to retirement plans. A surviving spouse can roll over retirement plan funds to his or her own IRA or retirement plan, or, in some cases, may con-

Income in Retirement (cont)

tinue the deceased spouse's plan as his or her own. The funds in the plan continue to grow tax deferred, and distributions need not begin until the spouse's own required beginning date.

By planning carefully, investing wisely, and spending thoughtfully, you can increase the likelihood that your retirement will be a financially secure one.

Working in Retirement-What You Need

Planning on working during retirement? If so, you're not alone. Recent studies have consistently shown that a majority of retirees plan to work at least some period of time during their retirement years. Here are some things you should consider.

Why work during retirement?

Obviously, if you work during retirement, you'll be earning money and relying less on your retirement savings--leaving more to grow for the future. You may also have access to affordable health care, as more and more employers begin offering this important benefit to part-time employees. But there are also non-economic reasons for working during retirement. Many retirees work for personal fulfillment--to stay mentally and physically active, to enjoy the social benefits of working, and to try their hand at something new.

How will working affect my Social Security benefit?

If you work after you start receiving Social Security retirement benefits, your earnings may affect the amount of your benefit check. Your monthly benefit is based on your lifetime earnings. When you become entitled to retirement benefits at age 62, the Social Security Administration calculates your primary insurance amount (PIA) upon which your retirement benefit will be based. Your PIA is recalculated annually if you have any new earnings that might increase your benefit. So if you continue to work after you start receiving retirement benefits, these earnings may increase your PIA and thus your future Social Security retirement benefit.

But working may also result in a reduction in your current benefit. If you've reached full retirement age (65 to 67, depending on when you were born), you don't need to worry about this--you can earn as much as you want without affecting your Social Security retirement benefit**.**

If you haven't yet reached full retirement age, $1 in benefits will be withheld for every $2 you earn over the annual earnings limit ($13,560 in 2008). A higher earnings limit applies in the year you reach full retirement age. If you earn more than this higher limit ($36,120 in 2008), $1 in benefits will be withheld for every $3 you earn over that amount, until the month you reach full retirement age--then you'll get your full benefit no matter how much you earn. Yet another special rule applies in your first year of Social Security retirement--you'll get your full benefit for any month you earn less than one-twelfth of the annual earnings limit ($1,130 in 2008), regardless of how much you earn during the rest of the year.

Not all income reduces your Social Security benefit. In general, Social Security only takes into account wages you've earned as an employee, net earnings from self-employment , and other types of work-related income, such as bonuses, commissions, and fees. Pensions, annuities, IRA payments, and investment income won't reduce your benefit.

Also, keep in mind that working may enable you to put off receiving your Social Security benefit until a later date. In general, the later you begin receiving benefit payments, the greater your benefit will be. Whether delaying the start of Social Security benefits is the right decision for you depends on your personal circumstances.

One last important point to consider. In general, your Social Security benefit won't be subject to income tax if that's the only income you receive during the year. But if you work during retirement (or you receive any other taxable income, or tax-exempt interest), a portion of your benefit may become taxable. IRS Publication 915 has a worksheet that can help you determine whether any part of your Social Security benefit is subject to income tax.

How will working affect my pension?

Some employers are adopting "phased retirement" programs that allow you to ease into retirement by working fewer hours. Other plans require that you fully retire before you can receive your pension. And some plans even require that your pension benefit be suspended if you retire and then return to work for the same employer. So check with your plan administrator before you make any decisions.
Working during retirement can impact your retirement plan, so consider the implications before making a decision .

Material provided by Forefield Inc.

Late Winter 2008

Volume 17, Issue 1

NEWS

Catherine Friend White was selected as one of the Top Ten Investment Advisors in Boston by the readers of Women's Business for the second consecutive year.

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W. David Malone has been appointed Chair of the Ambassador program at the Newton-Needham Chamber of Commerce. The Ambassador Committee is comprised of volunteers of existing members. These volunteers help new and existing members to take advantage of using the Chamber. Dave is looking forward to raising the bar for the Ambassador program by improving retention rates and developing an efficient and successful blueprint for all Ambassadors to follow. With assistance of great leadership from the Board of Directors and a helpful staff, the Ambassador Committee is hopeful for a successful 2008.

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Catherine Friend White spoke about entrepreneurship and success secrets for women in business to members of TiEWIN, the global network of entrepreneurs. The organization has a membership of 10,000 global entrepreneurs.

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