Altfest
personal wealth management℠

Spring 2009

THE ALTFEST ADVISORY LETTER

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The New United States of America

BY LEWIS J. ALTFEST

What will our country look like after the current recession is over? Let's go beyond timing to discuss the characteristics of our economy overall and consumers in particular once we have recovered. There are likely to be significant changes that will make us a stronger and more competitive country.

Perhaps the biggest changes will have to do with consumers. They will go back to saving the old fashioned way, putting cash in assets instead of counting on price appreciation of their home and existing stocks to do it for them. The drop in consumption resulting from the focus on savings and governmental policies to be discussed below will result in a one–time, modest to moderate decline in standard of living. However, some people won't even notice it as such, instead looking at it as more effective supervision of their household leading to a more sustainable standard of living. For a time people will take cheaper vacations, keep their car longer, buy less clothing and eat in less expensive restaurants. And, with productivity gains by business which average 1.5 – 2.0% per year steadily raising our standard of living, before too long it will exceed prior peaks.

People who are close to retirement or have already had the going away party will have decisions to make. Those not yet retired may choose between maintaining the separation date and

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Deciding When To Convert to a Roth

BY DAWN BROWN AND TOM FREDRICKSON

Converting a traditional IRA to a Roth IRA, which provides tax-free retirement income, is becoming an increasingly attractive option for many people because of new tax wrinkles.

The main considerations for deciding whether to convert continue to revolve around your expected investment return, time horizon and tax situation. Please consult your Altfest advisor about how these matters might affect your decision.

Now, changes in the tax laws governing conversions offer new opportunities but also add complexity to deciding when to make a conversion.

What is better: converting this year and paying income tax on the conversion when the market is down, or converting next year, in 2010, and taking advantage of a temporary option to defer taxes and stretch them out over 2011 and 2012?

For some, the decision is easy. Any individual or couple whose modified adjusted gross income (MAGI) is more than $100,000, is not eligible to convert this year, so 2010 becomes the default option.

For someone whose MAGI is $100,000 or less this year, the decision is more difficult.

Take for example Sam and Sandy Saver, a New York City couple in the 25 percent tax bracket that converts a $60,000 IRA. Assuming their portfolio grows by at least a reasonable amount of 6 percent or 8 percent in the next year, they would save more than $1,000 in taxes by converting in 2009 compared with 2010. The greater the rise in the market, the better it is to convert this year. Why? Because the Savers pay the tax before their account becomes more valuable. This more than offsets

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Our Shorter Name and Fresher Look

We have some news for you. After 26 years, we have decided to freshen our look and update our name.

We are shortening our name to what we find many people call us today, Altfest. Altfest will be followed by what we do – Personal Wealth Management. We believe Altfest Personal Wealth Management more accurately reflects our business, and you will be seeing it on our letterhead, newsletters and other communications as well as on our web site in the weeks ahead.

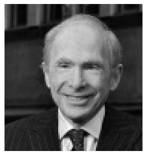
We are also happy to inform you of our new web site where you'll find additional information you can use, including analysis of recent market events like the latest Lunch with Lew podcasts and newsletter articles. We have also had blog and group chat capability built on the site and we are looking at how we can use these tools to add to our communication and keep you informed, particularly during the recessionary environment.

While our look and name are new, the most important things remain the same – our people, our commitment to the Altfest family of clients, and our focus on delivering the highest level of investment advisory and financial planning services.

We hope you like our new look. You know we are always here for you.

Altfest News

LEWIS J. ALTFEST, PH.D., CFP®, CFA, CPA



Lewis Altfest was featured in the January issue of Money Magazine, in the article "Secrets of America's Top Advisors." In addition to other media appearances, Lew discussed various aspects of the current investment environment with the *Chicago Tribune* in January, *New York Times* in February and *USA Today* in March.

KAREN C. ALTFEST, PH.D., CFP®

Karen C. Altfest appeared on ABC News to offer some advice on how to negotiate a severance package. Her article, "A Delicate Time", which focuses on the needs of widows, was published in the March issue of *Financial Planning* magazine. (Please call us if you would like a copy of the article.) Karen also spoke at the NYC Women's Investment Group on how to take care of yourself in today's economy.

PAUL PALAZZO, CFP®, COA

Paul Palazzo spoke at a March meeting of the American Association of Individual Investors (AAII) on value investing.

ANDREW ALTFEST

Andrew Altfest was part of a panel discussion on managed investment opportunities at the Managed Investment Solutions Workshop in February.

NANDINI U. WAMORKAR, CFP®

Nandini Wamorkar appeared in *Financial Advisor* magazine, in the February article "A Glimmer of Hope", where she discussed corporate bonds.

Deciding When To Convert to a Roth

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the disadvantage of paying tax dollars in 2009 instead of leaving them invested for a few more years.

On the other hand, if they think the market is going to decline, the Savers might think they are better off waiting until 2010 to convert rather than paying taxes into a falling market. But Congress allows a measure of protection, enabling people to "recharacterize" their Roth IRA back into a traditional IRA by October 15 of next year and pay no taxes on the conversion because for tax purposes, it never occurred.

Furthermore, after recharacterizing, the Savers could reconvert their now shrunken IRA and pay less in cumulative taxes than they would if they left the previous conversion intact. However, if they convert and recharacterize in the same year, they have to wait until the following year, or at least 30 days, whichever is later, to reconvert back into a Roth. People who converted in 2008 when markets were higher also have this option now to re-characterize and then reconvert. All of these transactions would have to be reported on tax returns.

In our example, the Savers were in the 25 percent income tax bracket both before and after the conversion. What happens if a 2009 conversion would push them into the 28 percent bracket? Would they still be better off converting in 2009? Or would it be better to wait until 2010 when they can stretch out the payments over the following two years?

Our calculations show that if they make the conversion in 2010 and remain in the 25 percent bracket in the following two years, they are better off having waited. Their lower marginal rate of taxation in the future, because of the one-time allowance from Congress to stretch out conversion taxes, makes waiting a better deal than converting in 2009.

We also found that if their account value increases significantly, on the order of 12 percent, they are better off converting in 2009, even if half of their conversion income gets taxed at the higher 28 percent marginal tax bracket. For some people who are not averse to a lot of paperwork, this suggests the possibility of converting in 2009 regardless of the effect on marginal taxation rate and then recharacterizing and reconverting if the high returns don't materialize.

Alternatively, if the numbers work, it's possible to do a partial conversion in 2009 and another one in 2010 to keep the taxes at a lower marginal rate.

Clearly, Roth conversions are no simple matter. Please contact an Altfest advisor if we can be of any assistance in making a decision.

Who Should Consider Converting to a Roth IRA?

- People who lost their jobs or had a pay cut may find their income for this year puts them within the income limits of a Roth;
- Those who anticipate they will be in the same or higher tax bracket in retirement;
- Those who can afford to pay taxes due on the conversion out of a taxable account rather than out of the IRA;
- People who want to be free of the taxable minimum distributions after age 70 ½ in traditional IRAs;
- People who don't need converted funds for at least five years after conversion (any withdrawals taken earlier would be subject to a 10 percent penalty tax if the account owner is under 59 ½, unless they meet one of a narrow list of exceptions);
- People expecting to leave large estates who desire an income-tax exempt source for estate taxes when otherwise a taxable IRA would have to be tapped;
- People seeking "tax diversification": i.e., accounts taxed in different ways to account for unknown future tax rates and provide planning flexibility.
- Starting in 2010, anyone who wasn't allowed to convert in 2009 because of too much income but for whom it otherwise could make sense.

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living on less money, or alternatively postponing that date. Many will choose postponing retirement or working part time for an extended period. Over time working until age 70 will become common. People who have already retired may have to operate in a more frugal manner. For the average middle-income person still working, savings rates at or beyond the 7-8% level that prevailed before the 1990's may be needed.

People regardless of situation may be caught between a current fear of investing large sums in equities and the lower returns in "safe" U.S. Government bonds; the bonds carry the risk of losing significant value because of increased inflation, a distinct possibility after the next year or so.

The situation calls for sophisticated financial planning. Many of our clients who have had this work done by us are likely to be safe despite the recent sharp declines in values, a result of the conservative growth assumptions we made for the 2005-2010 period and the high probability benchmarks we used in determining the plan's chance of success. We deliberately chose less favorable projected returns because of our view of markets and used high probabilities to help protect our clients against negative events such as those that have unfolded recently. Of course if clients wish to return to those same high probability levels, they should be conservative in their spending.

Turning to business, large quality non-financial companies should not have great concerns. Most of them entered the recession with reasonable levels and many had cash on hand. Their actions since then will for the majority create a "lean machine" ready to provide higher profits as demand turns up. Beyond that period greater Government and employee costs and potential inflation may reduce profit margins from abnormally high recent levels but overall profits should gain annually.

Banks and many other financial companies are not in a recession but a depression. Nevertheless, banks are currently enjoying unusually wide profit margins as a result of borrowing from the Government at less than 1% and lending at say 6% which should awaken all but the walking dead. There will be new rules and perhaps a new regulatory authority to make sure that shoddy loan practices and debt leverage don't reappear, at least for a long time.

Perhaps the biggest changes will have to do with consumers. They will go back to saving the old fashioned way, putting cash in assets instead of counting on price appreciation of their home and existing stocks.

The Government of the future is more murky with battles now going on between Democrats and Republicans and perhaps between President Obama's two sides, as a leftist reformer and a middle of the road pragmatist. Is the large Government spending principally needed to stimulate our economy as people save money or is it a cover for a reversal of all Reagan's policies? More specifically, in a few years Obama may be forced to choose between a difficult large increase in taxes for all, perhaps a consumption tax, and a simpler laissez-faire approach of letting inflation reappear in a virulent form with the dollar declining. My guess is that he, with the prodding of the Chinese and other large foreign holders of dollars, will choose a combination of the two, including some turn-up in Government's role.

One thing seems particularly clear to me. This is not the start of the decline and fall of the United States. We will recover. There may be no V-shaped turn up beyond the economic trough. On the other hand, once things turn up we will make steady progress annually toward our goal which is to remain the most powerful country in the world, with continued growth which will be measured first with a steady stock market recovery and then later on with one for real estate.

Continued Thanks for Your Referrals

The Altfest team would like to thank all of you who continue to refer your friends, colleagues, and family members to us. The majority of our new clients come through referrals.

Referrals are given when clients feel they receive real value from their wealth management team and want to share that benefit with their loved ones.

We at Altfest Personal Wealth Management are committed to providing special attention to each person introduced to us, especially since they come from you, our respected clients and colleagues.

Complimentary Parking Available

We are pleased to inform you that Altfest Personal Wealth Management offers complimentary parking. If you are driving into Manhattan for your scheduled Altfest meeting, you are invited to park your car at the Champion Parking Garage, conveniently located at 425 Park Avenue. The entrance to the garage is located on 55th Street.

Please note, there are two Champion Garages on the block between Lexington Avenue and Park Avenue. This arrangement is for the second lot, located closest to Park Avenue.

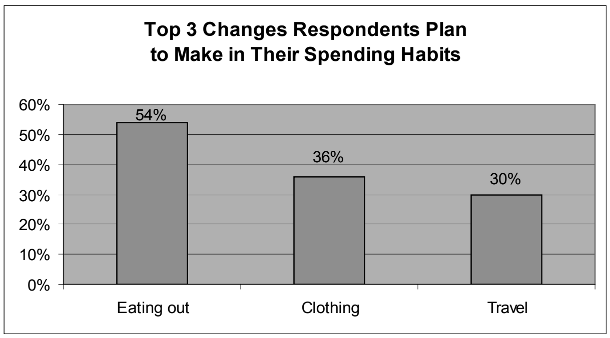
Survey Finds Frugality Is In

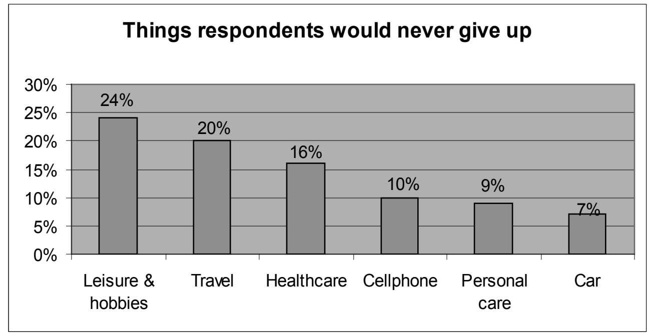
BY KAREN C. ALTFEST

I recently surveyed 151 people to see how spending habits have changed in this difficult economy.

While 64.7% of respondents have already altered their habits, the top 3 changes respondents plan to make in their spending habits are eating out, clothing and travel.

But people said there are some items they would never give up, including leisure activities and hobbies, travel, healthcare, and their cellphone. They said these things were important in order to keep up spirits, maintain contact with the world, and ensure emotional well-being.





It's a sign of today's greater conservative mood that 43% of respondents who might receive a $1,000 stimulus from the government would save it, while 15% would use it to pay off debts, 13% would spend it, and 11.8% would invest it.

Respondents:

- 68% of respondents were 60 years+
- 56. 9 % were female
- 47.7% were married
- 22.9% were retired
- 18.3% have had a salary freeze

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Altfest Personal Wealth Management is a family owned fee-only financial planning and investment management firm celebrating its twenty-sixth year of helping our clients achieve their financial goals. The Altfest Advisory Letter is produced in-house as a client service, to share our thinking on relevant topics.

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