November/December 2006

WEALTH MANAGEMENT ADVISOR

Building the better trust

How to head off unintended problems down the road

Expecting a baby? Expect financial challenges

Take advantage of your employer's retirement plan

Tax-wise investing with municipal bonds

CFSE
WEALTH MANAGEMENT INC.
Registered Investment Advisor

Fairbanks Professional Center
1400 W. Fairbanks Ave.
Suite 202
Winter Park, FL 32789
Phone: (407) 629-7008
Facsimile: (407) 629-7516

Fifth Third Center
999 Vanderbilt Beach Road
Suite 601
Naples, FL 34108
Phone: (239) 598-3146
Facsimile: (239) 514-3783

Celebration Place IV
215 Celebration Place
Suite 170
Celebration, FL 34747
Phone: (321) 939-0915
Facsimile: (321) 939-0918

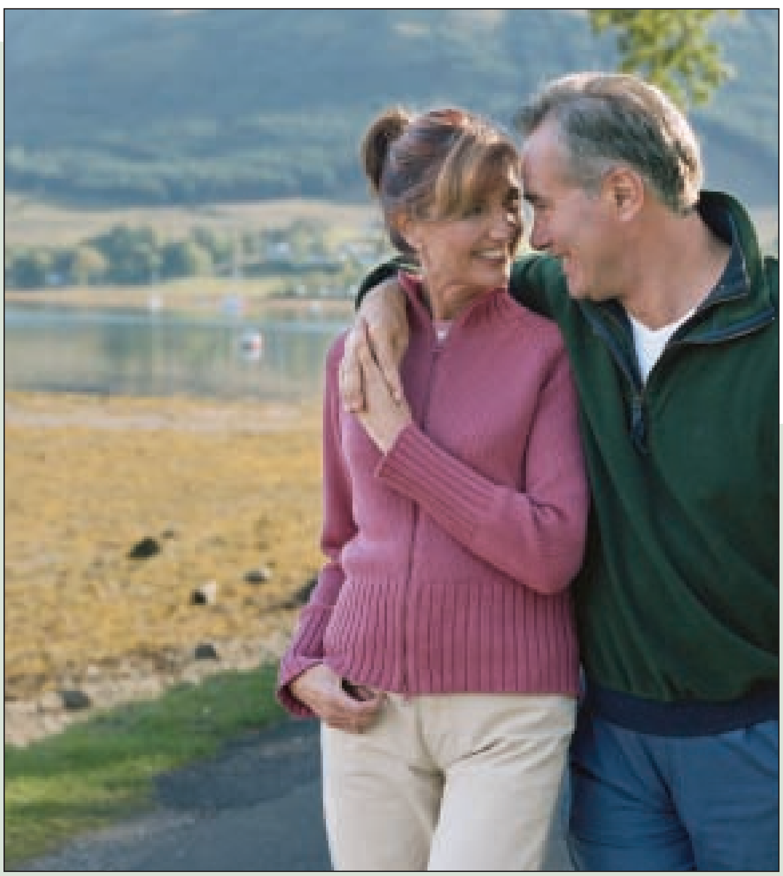
Urban Center Two
4890 Kennedy Blvd.
Suite 110
Tampa, FL 33609
Phone: (813) 286-2477
Facsimile (813) 286-2577

Building the better trust

How to head off unintended problems down the road

Trusts are used to accomplish a wide variety of estate planning and financial purposes. They may be designed to reduce income or estate taxes, avoid probate, provide asset protection for beneficiaries, or simply direct where assets should be placed and remain for a period of time — perhaps even for generations.

As important as it is to focus on your trust goals, it's equally important to keep the rules governing a trust's operations in mind when drafting your trust document. Once a trust has become irrevocable, its flexibility is limited to the provisions already specified in the trust document. It's vital, therefore, to carefully consider today any provisions — including trustee appointments — that might cause issues down the road.



Planning for irrevocability

The typical living trust is designed to help an estate avoid probate, and to operate in the event of the individual's incapacity. Generally, it's revocable when it's created and during your lifetime, so you can move assets in and out of it and make changes to its provisions. Upon your death, however, it becomes irrevocable. The trust still owns the same assets, plus any that may have "poured over" into it according to the dictates of your will, but they are now governed entirely by your trust document and your trustees' interpretation of that document.

Understand, however, that if you transfer assets as gifts into a trust during your lifetime, such a trust becomes irrevocable as soon as it's created. This applies to a wide variety of trusts, including life insurance trusts, charitable trusts and grantor retained annuity trusts.

To ensure your trust reflects your original wishes, your trust document should provide instructions on how trust investments should be managed and when and how they should be distributed to beneficiaries. But instructions shouldn't be so specific as to hinder the execution of your wishes as circumstances change.

Trust in trustees

It's essential to choose your trustees with care. Consider whether they're likely to act objectively and in the best interests of all of your trust's beneficiaries, because they may be required to mediate conflicts. Conflicts are most likely to occur when the trust's beneficiaries aren't all related, such as a current spouse and children from a previous relationship or when a trust doesn't treat all children equally.

Also consider appointing more than one trustee to prevent the possibility that one won't act fairly on his or her own. Understand, however, that having multiple trustees can lead to conflict among them. Say, for example, you appoint your spouse and a close friend as co-trustees, with both also having certain rights as beneficiaries. Following a conflict, the friend could refuse to let your spouse take income distributions. And the financial services firm overseeing the trust's investments might not allow distributions from the account unless both trustees have approved them.

Naming institutional trustees, such as a bank or trust company, may head off these kinds of issues. Institutional trustees, however, could have their own potential conflicts of interest, such as a lack of independence in making investment decisions. So if you name an institutional trustee, you also may want to give a second trustee power over investment decisions.

Distribution issues

Income distributions are a common source of issues that can, with some foresight, be addressed in a trust document. Requiring a specific amount to be distributed to a surviving spouse, for example, may not be a good idea because it can add to the taxable estate of someone who may not need the income. Instead, it's generally best to leave the distribution of income to the discretion of trustees, understanding, of course, that this additional room for discretion also increases the odds for potential conflict.

Once a trust has become irrevocable, its flexibility is limited to the provisions already specified in the trust document.

If your trust names both income and remainder beneficiaries, how its investments are managed will be an important issue to address in the trust document.

3 common types of trusts

Trusts can serve many purposes and be structured in a variety of ways. Here's a closer look at three common types:

1. Marital trusts. These trusts are used to meet various estate planning goals while transferring assets to the surviving spouse. A bypass trust takes advantage of the full estate tax exemption amount of the first spouse to die. A qualified terminable interest property (QTIP) trust is often used in second marriages to protect the interests of children from a previous marriage. A qualified domestic trust (QDOT) is used when the surviving spouse is not a U.S. citizen.

2. Crummey trusts. Giving beneficiaries a "Crummey" right to withdraw funds, on notice, for a short period of time each year, allows gifts to the trust to qualify for the annual gift tax exclusion. Irrevocable life insurance trusts (ILITs), which you can use to keep life insurance proceeds out of your estate, are often set up as Crummey trusts.

3. Grantor-retained annuity trusts (GRATs). You gift assets to this irrevocable trust and then receive annuity payments for a set term. At the end, the remaining assets pass to the beneficiaries. As long as you outlive the term, the assets (plus appreciation) will be excluded from your estate. A qualified personal residence trust (QPRT) is similar except that you gift your home to the trust and, instead of annuity payments, you receive the right to live in the home for the trust term.

A situation in which a beneficiary is entitled to the trust's investment income but the trust invests solely in non-dividend-paying stock (and therefore the beneficiary receives nothing) must be avoided. On the other hand, if the trust maximizes income by investing entirely in bonds, this could harm remainder beneficiaries by not producing sufficient returns.

It takes a team

With the help of legal and financial professionals, you can anticipate issues that might arise once your trust becomes irrevocable. But it's essential you understand that these professionals can't build the trust without you; your knowledge of the individuals involved — beneficiaries and trustees — will be just as important as their technical skills.

Expecting a baby? Expect financial challenges

Congratulations, you're about to welcome a child into the world! As if you didn't already have enough to think about, consider this: It costs nearly $280,000 on average to raise a child through age 17, according to the U.S. Department of Agriculture. And that amount doesn't even include big-ticket expenses such as private schools or a college education.

Parenthood will probably pose the biggest financial challenge of your life. But with some planning and fiscal discipline, you can raise a financially prosperous family.

Consider insurance needs

One of your first considerations when expecting a child should be health care costs. Before your baby is born, talk to your company's benefits department — or, if you're self-insured, your insurance agent — to find out what it costs to add a child to your medical coverage.

If both you and your spouse have access to employer health plans, determine which offers the better value for family coverage; it's not necessarily the same one that's best for the two of you alone. Also, many employers offer flexible spending accounts funded with pretax dollars that allow you to save money on unreimbursed health care costs and many child care expenses.

This is also the time to make sure your growing family is taken care of, no matter what happens to you. For starters, make sure that your will and the beneficiary designations on your financial accounts are up to date.

In addition, talk to an insurance agent about the appropriate amount of life insurance protection for you and your spouse. Your agent can help you determine whether term or permanent coverage is best for your situation. Term insurance is generally simpler and cheaper than permanent insurance, though the latter may be more useful for estate planning purposes or to provide income during retirement.

Save early and often

Paying for education is probably the single largest parenting expense you'll face. College costs continue to grow much faster than the rate of inflation — by 5.9% during the 2005-06 school year, according to the College Board.

To work or not to work

If you or your spouse wants to stay at home to care for your child but you worry that you can't give up your second income, think again. Having a job actually may be more costly than you realize.

Your biggest expense will be child care. But consider also the costs associated with work — clothes, gas and car repair or public transportation fares, morning coffees and lunches out — not to mention services such as housecleaning or yard work that you're not home to do yourself.

Of course, there are valid nonfinancial reasons for both parents to choose to work. But if money is what's holding you back from becoming a stay-at-home parent, make sure you're calculating the true cost of employment.

If that pace continues, and with many top universities now costing well above $40,000 per year, it's not unreasonable to think that four years of higher education could set you back a half million dollars or more by the time your newborn turns 18. And if you're thinking about sending your child to private elementary or secondary school, you could be looking at annual tuition bills into five figures annually.

With the cost of education so high, start saving as soon as possible to give your money the best chance to work for you. Consider tax-advantaged education savings options, including 529 plans and Coverdell Education Savings Accounts. These plans enable you to invest after-tax dollars for your child's future education expenses.

Make it work

It's natural to think about money when having a baby, particularly if you've become accustomed to a certain lifestyle. To make sure your child has everything you want him or her to have, you may have to make some new financial choices. Some, of course, will be made for you. With a new baby to care for, you'll probably spend a lot less on travel, entertainment and meals out — giving you more money to spend on daily needs and to save for the future.

Whatever your financial approach to parenthood, remember that you'll find a way to make it work for you. Congratulations on your growing family!

Take advantage of your employer's retirement plan

How — and how much — you can save on a pretax basis for your postwork years depends in large part on the type of retirement plan your employer offers. Several decades ago, defined benefit plans, such as traditional corporate pensions, were the norm. For employees, it couldn't have been simpler: Work a lifetime at one company, and then collect your gold watch and monthly retirement checks.

Defined benefit plans, however, have become less popular in recent years, as many companies have struggled to meet their financial obligations to retirees. Instead, most companies now offer their employees defined contribution retirement plans — often relying heavily on the 401(k) component — which puts the control and responsibility for saving in your hands. It's important, therefore, to understand your options and know how to maximize their benefits.

Tax-deferred growth

The most popular types of plans allowing employees to contribute to their own accounts are named for the sections of the tax code that govern their use:

- 401(k) plans are commonly offered by corporations and other private sector employers.
- 403(b) plans, close cousins to the 401(k), are provided by nonprofit institutions such as schools and hospitals.
- 457 plans generally are offered by state and local government employers.

In all three cases, participants can choose to have a certain percentage automatically withdrawn from their paycheck and invested in the plan. You, not your employer, typically decide how your money should be invested, choosing either from a preselected lineup of investments that may include mutual funds and company stock, or from a virtually unlimited, self-directed securities account.

Contributions to 401(k), 403(b) and 457 plans are tax-deferred — meaning you don't pay income tax currently, but only when you withdraw money — potentially enabling your retirement assets to grow more quickly. And all three plans allow you to sock away up to $15,000 per year, plus an additional $5,000 per year if you're age 50 or older.

Beginning in 2006, the law allows plans to offer a Roth 401(k) alternative. If your company offers it and you choose to participate, you don't receive a current tax deduction for contributions but generally pay no tax when amounts are withdrawn in retirement.

Plans can vary depending on the options your employer makes available. Every plan, for example, offers a different series of investment options. Some employers may even match a percentage of your contributions — a particularly valuable benefit that everyone should try to take full advantage of when it's offered. Employers also may make contributions that aren't tied to employee contributions — for example, a profit-sharing amount subject to vesting rules (which means it can be forfeited if you don't stay with your company for a specified number of years).

Small business plans

If you work for a small company, your employer may offer another type of retirement savings plan, such as a Simplified Employee Pension (SEP) or Savings Incentive Match Plan for Employees (SIMPLE).

SEPs — most common in companies with only a handful of employees — allow employers to open individual accounts on behalf of their eligible employees. For 2006, contributions can equal as much as 25% of an employee's compensation, up to $44,000. Employers are not required to make annual contributions, nor must they contribute the same amount every year. If they contribute a certain percentage to one employee's SEP account, however, they must do the same for every eligible employee in the company.

Defined benefit plans have become less popular in recent years, as many companies have struggled to meet their financial obligations to retirees.

SIMPLE plans come in two varieties — IRAs and 401(k)s. From an employee's perspective, they have much in common. In both cases, an employer opens an account for each eligible employee, who can opt to contribute up to $10,000 annually. Plan participants age 50 or older can contribute an additional $2,500 per year.

An employer may choose to match up to 3% of employee contributions, or decide to contribute up to 2% of compensation, regardless of whether employees make their own contributions. There are a few differences between the two, however. SIMPLE 401(k)s, for example, generally allow loans, while SIMPLE IRAs do not.

Get started today

No matter what type of retirement plan your employer offers, the most important thing is to take advantage of it. And if your employer doesn't offer a plan, consider setting up your own IRA — another excellent, tax-advantaged way to save for retirement.

The bottom line? Invest early and often and use the available tax benefits, and you'll dramatically increase the odds of enjoying a financially comfortable retirement.

Tax-wise investing with municipal bonds

If you're looking to earn tax-exempt investment income, you may want to consider investing in municipal bonds. Municipal bonds, or munis, are debt securities issued by state and local governments for general funding or to fund projects such as schools or highways. These bonds' interest payments generally are exempt from federal income taxes, and in many cases are also exempt from state and local taxes if you live in the state in which the bonds are issued.

Because munis typically are exempt from income taxes, they usually offer lower yields than comparable taxable securities. Even so, these tax-exempt securities may represent the better investment option — especially if you're in a relatively high tax bracket.

A simple formula converts yields on tax-exempt bonds to their taxable counterparts:

Tax-exempt yield % / (1 – your tax rate) = taxable yield %

Say, for example, a muni bond offers a yield of 3.75%, compared with a 5.50% yield for a similar taxable bond. If you're in the 35% federal income tax bracket, the muni bond offers a higher yield, because its taxable equivalent yield is 5.77% (3.75% / 1 – .35 = 5.77%), compared with 5.50% for the non-tax-exempt fund. If your income from the bond is exempt from state and local taxes, the difference could be even greater.

Keep in mind, however, that municipal bonds that are "private activity" bonds aren't exempt from the alternative minimum tax, which, despite recent legislation temporarily slowing its growth, is expected to affect millions more taxpayers in future years.

Anyone can buy municipal bonds directly from the government or through an investment firm, but most investors gain exposure to munis through mutual funds, which tend to be more liquid than the market for individual municipal issues. Funds also provide muni investors with a level of diversification that would otherwise be difficult for all but the very wealthy to obtain.

Before investing in munis or a muni bond fund, keep in mind that these investments carry risk, including the risk that you may lose some or all of your original investment. Any bond investment carries both a default and interest rate risk. The default risk is the risk that the issuer won't be able to make timely payments of interest, dividends or principal as required. The interest rate risk reflects the fact that bond values generally are affected inversely by market interest rate changes. So if rates increase, the value of an existing bond typically decreases.

Mutual funds are sold by prospectus. Investors should carefully read the prospectus before investing. They also should consider carefully information contained in the prospectus, including investment objectives, risks, charges and expenses, before investing. For this and other information, request a prospectus from your financial professional.

Your source for customized investment and financial planning

CFSE
WEALTH MANAGEMENT INC.
Registered Investment Advisor

James W. Ferrell, CPA, PFS, CIMC
President
A Certified Public Accountant (CPA), Personal Financial Specialist (PFS) and Certified Investment Management Consultant (CIMC), Jim is the founding shareholder and President of CFSE Wealth Management, Inc. He is actively involved in local organizations including: Morning Star Charities, Inc. (President), Winter Park Chamber of Commerce, the University of Central Florida Golden Knights Club, Winter Park YMCA (Board of Directors), Entrepreneurship Society at Rollins College (Board of Directors) and is an Inductee in the UCF College of Business Administration Hall of Fame.

Katie Miller, MBA
Vice President - Consulting
A Certified Financial Planner (CFP) candidate with a Master of Business Administration Degree from Rollins College, Katie works as a financial consultant responsible for assisting clients set and achieve their long-term financial goals through investments, tax planning, asset allocation, risk management, retirement planning, and estate planning. Katie is a member of the Entrepreneurship Society at Rollins College and is actively involved in such local organizations as the Winter Park Chamber of Commerce, Orlando Chamber of Commerce, Downtown Orlando Partnership and Camp Boggy Creek.

Please call us today at 407-629-7008 (Winter Park) or 239-598-3146 (Naples) to discuss your needs, or visit www.CFSEonline.com for more information on our services.

Successfully managing personal and family finances means making the right decisions today while considering their implications for the future. At CFSE Wealth Management, we believe financial decisions are not one-time events — as life changes, so must your financial strategy. By working with our experienced team of advisors, you will benefit from the independent perspective necessary to make your financial vision a reality.

We provide a full range of investment consulting and financial planning services including:

- Investment Policy Review/Creation
- Comprehensive Personal Financial Planning
- Tax and Estate Planning
- Asset Allocation Modeling
- Fund Cost Efficiency Analysis
- Manager Search/Selection
- Asset Liability Modeling
- Investment Portfolio Structuring
- Performance Measurement
- Manager Review/Analysis
- Access to insurance and other financial services through our affiliated businesses.

We welcome the opportunity to show you how CFSE Wealth Management can help you with your personal and family financial affairs.

CFSE Wealth Management, Inc. is registered with the Securities and Exchange Commission (SEC) and the State of Florida. Our mission is to provide the highest quality investment advisory, financial planning, estate planning and consulting services in a cost-effective and objective manner. We are part of the CFSE family of professional services firms, including:

- ***Chastang, Ferrell, Sims & Eiserman, L.L.C.,*** the area's largest locally based accounting firm, which offers tax, auditing, review, accounting, and consulting services to a wide range of businesses and individuals. Through membership in NEXIA International, the firm can provide local service throughout the world.
- ***CFSE Business Services, Inc.,*** provides a broad range of strategic, financial and operational advisory services to selected business clients in the Southeast. The firm offers high quality business valuations, capital raising consulting, strategy development, and financial intermediary services.