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# BWFA Advisor

FINANCIAL PLANNING ♦ INVESTMENT PLANNING ♦ TAX PLANNING

Baltimore–Washington Financial Advisors, Inc.

## The Perils of Do-It-Yourself Financial Planning



Perhaps you've heard Suze Orman, the omnipresent financial personality of our era, tell audiences that no one is better qualified to manage their money than they are. "Whether you want to believe it or not, you and you alone have the best judgment when it comes to your money," Suze writes in [The 9 Steps to Financial Freedom](#).

By Annette Simon, MBA



Suze's message appeals to people, and I run into folks

every day who have taken her words to heart. Like most people in the Baltimore-Washington area, these people are well-educated and well-read. They assume personal finance isn't rocket science, and anyone who reads *Money* magazine should be able to stay on top of their own investments. Why pay a financial advisor to help with something that is mostly common sense?

But, in my years of working with clients, I've found that few people truly manage their own finances well. Most have made costly mistakes that an experienced financial advisor could have helped them avoid. The most common errors include:

**Making emotional decisions about investments.** Successful investing requires steadfast adherence to a consistent long-term strategy. Buying trendy, hot stocks out of greed has cost countless people dearly in recent years. Falling in love with stock picks and holding on long after they should have been sold has also hurt many investors. How many of Enron's stockholders do you suppose clung to a belief that the company would turn around and they would be richly rewarded for their investments in it?

**Selecting the wrong savings vehicle.** Should you be invested in mutual funds? Individual stocks and bonds? Folios? Annuities? Is cash value life insurance a good investment? Are 529 plans superior to UGMAs or Education IRAs for college savings? Simply reading the financial press won't help clear up the confusion; too many of the articles are written by agents and brokers who make their living by selling one or more products. Every week there's another new product pitched as the solution to every problem.

**Failing to take critical actions.** It's hardly news that the tax code is ridiculously complex and that the rules change every year or two. At various points in your life—when you change jobs, get married, retire, or reach specific ages—you may need to make important, often irreversible, decisions affecting your financial future. Failing to decide or choosing incorrectly can be a mistake you'll spend years paying for.

**Underestimating future needs.** It's easy to say that we'll spend less next year or to imagine that we'll live more frugally in retirement. Or that college tuition can't possibly keep rising at such a rapid rate. It's tempting as well to assume that the good old days of the late 1990's will return, and earnings of 20% or more each year will enable us to achieve our goals. Reality isn't always so kind.

Your BWFA financial advisor can save you from these pitfalls and more. We'll charge a fee for our services, but will be worth our weight in gold. We have the experience to understand your complete financial picture and to develop an integrated, ongoing plan to address your needs. We are Certified Financial Planners who work on a Fee-Only™ basis to ensure that your interests come first. So swallow your pride, and watch the benefits accrue as we work together to enable you to achieve your dreams.



Fee **FO** Only™

# Taxes & Tax

## Planning



By Bob Cassel, EA 

whether the tax return was actually correct? Or whether the computer took advantage of the tax laws in your favor?

We have had a chance to review some tax returns that were prepared by well-intentioned Do-It-Yourselfers. In some cases, the results were accurate. On other returns, we found minor mistakes that were not significant enough to warrant a change. In about a third of the returns, we found significant mistakes or misapplication of tax law. By fixing these errors, we have saved the taxpayers anywhere from a few hundred dollars to several thousand dollars in taxes.

There are people who can prepare their own tax returns and come up with accurate results. However, not everyone can. We would like to identify for you those situations in which people should hire a professional to prepare their tax returns. Here is our list. (See if you can find yourself on it.)

1. You have a small business.
2. You want to put a retirement plan in place and need help choosing the correct one.
3. You have investments in stocks or mutual funds. (There are a host of subtle tax issues relating to foreign taxes, U.S. Government interest, and nontaxable income to deal with.)
4. You pay for college or pre-college education expenses.
5. You own stock options or belong to an employee stock purchase program through your employer.
6. Your children (under age 14) have investment accounts.
7. You own a rental property.
8. You are subject to alternative minimum tax or you have an alternative minimum tax credit.

9. You are a schoolteacher with out-of-pocket classroom expenses.
10. You moved into or out of Maryland during the last tax year and need to file more than one state income tax return.
11. Either you will receive a very large refund, or you owe taxes (and possibly penalties) with the return.

Here are some other circumstances that may indicate you need professional tax planning help:

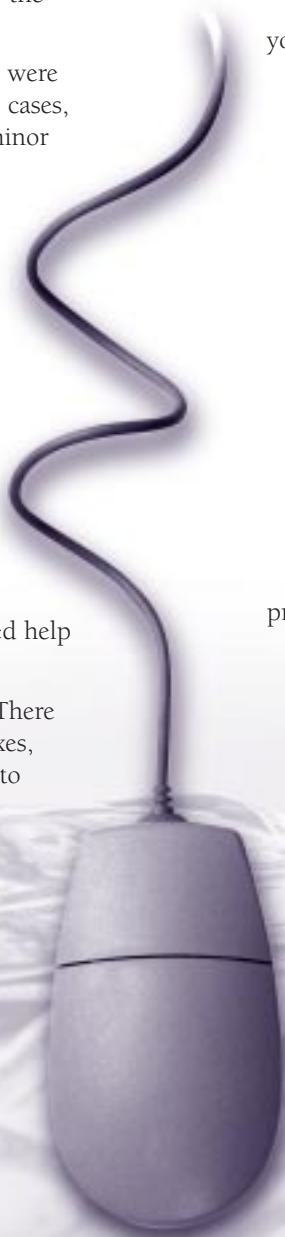
1. You pay, or should pay, estimated taxes.
2. You are a high income individual subject to phaseouts.
3. You switched from the tax preparation software you used for the previous tax year to a different program and you did not properly identify carryover items such as IRA cost basis, capital loss carryovers, depreciation expenses on business equipment or rental properties.
4. You are not using any tax preparation software at all (i.e., you are preparing your tax return by hand).
5. Tax terminology sounds like Greek to you.

What advantages does a BWFA professional tax preparer bring to bear?

1. The experience and knowledge to identify and apply tax savings opportunities
2. The experience and instinct to know when to dig deeper into your records in order to avoid problems with the IRS
3. The ability to identify and help you address general financial non-tax issues

We have observed that most people would prefer to prepare their own tax returns, save a little money, and get the job done with a minimum of effort. However, our experience tells us that at least two thirds of the people who choose this approach do not achieve these objectives.

If you find the process of preparing your own tax returns frustrating, or if you are simply unsure of your results, we are here to help. Give us a call.



# Investment Management



By Saxon Birdsong,  
MBA

## What to Watch in 2002 Trends in How We Acquire Goods

One of the most important steps in successful investing is distinguishing meaningful trends from overpriced hype, fads, and “noise” in the marketplace. In this newsletter, we note that one of the more significant changes going on is how goods are

bought and sold. In the paragraphs below, we have identified issues related to this theme which we have incorporated into our “investment attitude”. As always, we appreciate any feedback you might have on our observations.

**WE CAN'T IGNORE MICROSOFT** because of the enormous impact they have in technology and our economy. Microsoft's new Windows XP will matter most in 2002. It's a vital phase in Microsoft's plan to weave all of its products into the fabric of the Internet. How they do this is likely to provide an important model for how billions of dollars in annual software sales occur. Note the clear parallel here with Gateway: increase profit margins by cutting out retail stores, many of whom rely on software sales.

Microsoft's Passport service is also worth watching. It is a Net-wide identification system and could make Microsoft the gatekeeper to trillions of dollars of electronic commerce transactions. Consumers and businesses will demand more secure payment systems (see below) as activity expands. In this regard, we note that AOL reported that Internet sales were \$11 billion in the fourth quarter alone, up 72% over last year.

**COMPUTER SECURITY IS HOT.** Heading the list of concerns are massive security flaws in software which allowed thieves to see users' credit card numbers and other flaws which allowed remote users to take control of computers. Ongoing threats of viruses and potential massive disruption to Internet communications by terrorists are also issues which will impact the way investment dollars flow and the way consumers and businesses interact.

The Liberty Alliance is an important development which will take shape in 2002. It includes a host of major companies—AOL Time Warner, Bank of America, Sony, General Motors, United Airlines, RealNetworks, eBay, Nokia, Vodafone, American Express, and more—who have joined forces to

form an alternative .NETwork. Their primary concern is that Microsoft may end up handling their e-commerce transactions. How this works—if it works—will have a variety of long-term implications for how we are connected to one another and how business is done.

Ongoing Microsoft litigation will continue to impact the business/investment landscape. Nine states have refused to settle with Microsoft in its antitrust case. While a corporate breakup is off the table, Microsoft could still be saddled with penalties that will cost it billions and dampen its competitive ferocity.

**PEOPLE WANT NET MUSIC.** While Napster is effectively disabled, users can still get free music from companies like BearShare and Audio Galaxy. In 2002, we'll find out if they want Net music enough to pay for it. A host of Net music services with names like EMusic, Pressplay, Rhapsody, and RealOne hope to collect monthly fees for digital music. But none of these services offer the versatility of the old Napster system.

The coming year promises the continuing gigahertz chase between chipmakers Intel and Advanced Micro Devices, as they continue to develop the new 64-bit chip. Early reports suggest Intel's next version of Itanium will be powerful enough to propel Intel into new markets: high-end scientific desktops and top-of-the-line mainframe computers. It'll also spell a major competitive threat to Sun Microsystems, whose UltraSPARC computers currently dominate the 64-bit market.

Amazon.com's next profit report in January may help to foretell the future of e-commerce.

For months now, Amazon.com has been forecasting its first quarterly profit number for the quarter ending in December. Analysts disagree and are projecting a .04 to .08 cents per share loss. But analysts have been wrong (they have overestimated losses) in five of the last six quarters.

AOL has the opportunity to make its merger with Time Warner really pay off big by integrating Time Warner's high-speed cable and content (movies and music) services with its

continued on reverse



# Financial Planning

## You Had Better Review in 2002



By Kevin Condon 

The drama of 9/11 and the depressed securities markets of 2000-2001 have in some way affected us all. According to recent press reports, many Americans have begun to reprioritize their lives and review their financial planning assumptions at this time. We assume that this will be no less true with members of the BWFA family. As your advisors, we have been

reviewing plans which we have completed in the last few years with an eye to the sustainability of cash flow when calculated from present depressed market prices. In financial plans completed before July this year, our planning assumptions used a 6% static annual rate of return during retirement and a rate of return as high as 8% before retirement. In the past year, we have actually changed our approach to future rates of return. On annual review, we will be recasting your projections using new assumptions and then calculating the future probability of success of your plan. As you know, we suggest that all planning be reviewed annually. Some of you have disciplined yourselves to do so; others have not. This year, be certain to get a thorough review. Nearly all your planning parameters should be reviewed and many plans will need recasting to take into account the changes of the last 24 months in the world.



Take this opportunity to review with us any significant changes in your life. Besides world events and market downturns, health issues, relocation decisions, retirement cash needs, and other personal issues will also affect the outcome of your financial planning. If it has been more than a year since your original plan was completed or since your last review, please schedule some time to see us during the first quarter. Some data collection may be necessary, especially if we do not do your taxes or manage your investments. However, new iterative projections can determine the probability of success of your current plan much more closely than we were able to with our previous system. The peace of mind that comes from knowing with some certainty if anything needs to be adjusted in order to maintain your current lifestyle is immeasurable.

### You may ask, "Can I save any money?"

In a recent financial planning review, new IRS estate tax tables substantially altered our recommended estate planning strategy for one client. As a result, we were able to eliminate \$13,000 in annual insurance premiums and free up over \$200,000 in insurance cash value for other uses, because our review showed that the death benefit in his policy would not be needed to pay estate taxes.

### WHAT TO WATCH IN 2002, continued

existing Internet services. It could pull this off in 2002, and this would open a whole new chapter in home entertainment and how we do business.

The proposed merger of Compaq and Hewlett Packard is worth watching. If the merger doesn't collapse, it would produce the second largest computer company behind IBM. The new company will need to find a new way of doing business (which neither of them individually has been able to do so far) to

compete in the low-margin PC arena against Gateway and Dell. Everyone will be watching for the creative new approaches these companies might bring to the table in 2002.

I have often thought of how helpful it would be to be able to pay for an independent, objective service which would tell me what to pay attention to, so I could ignore the noise. That way, I'd have more time to fish.