



# BWFA Advisor

BALTIMORE-WASHINGTON FINANCIAL ADVISORS, INC.

Fee-Only Retirement & Estate Planning, Investment Management, & Tax Services



By *Saxton Birdsong,*  
MBA

## Expect More from Your Advisor

We all know just how tough it is to find truly good professionals. Whether it's a doctor, dentist, or attorney, it's hard to know if you have a good one until you have worked with that person for a while. Your financial advisor can make this process a little easier.

People expect a financial advisor to provide expert advice about investments, retirement planning, insurance, and taxes. At BWFA, we believe a financial advisor should do all those things and much more. An advisor should act as a leader, marshaling a team of professionals to address the full array of your financial needs.

You will often have needs that fall outside the expertise of your financial advisor, but still have a significant impact on your finances. These could include buying and selling real estate, obtaining a mortgage, creating wills and trusts, and addressing long-term care issues for you or a loved one. In each of these cases, your financial advisor can add value by ensuring that you work with high-quality professionals and that the services you receive fit in with your overall financial plan.

Over the years, we have had the opportunity to work with many other professionals. Because we are fee-only and have no fee-sharing arrangements, we refer our clients only to those

professionals whom we have found to be highly competent and who consistently provide good service.

You will see in this issue of our newsletter we have called upon some of these professionals. In the Retirement and Estate Planning section, we worked with Arlene Saks-Martin, a geriatric care manager, to create a meaningful article on planning for long-term care. In the Investment section, we spoke with Donna Barkman of Coldwell Banker in Ellicott City and Tim Rhodes of Coldwell Banker in Bethany Beach to bring you different perspectives on the real estate market.

And now BWFA is expanding its professional network by asking clients to provide us with information about exceptional professionals with whom they have done business. This can include any type of professional, from architect to caterer to web developer. If you have an experience you would like to share, or are looking for a professional referral, please contact us.

For those consumers who do not yet have a financial advisor they are comfortable with, we urge them to contact the National Association of Personal Financial Advisors (NAPFA) at 1-888-333-6659. NAPFA does more than any other professional organization to ensure the competency of its members, and to steer consumers to experienced, fee-only financial professionals who can provide the independent financial advice consumers are looking for.

## What's Happening at BWFA?

**Greg Milsom**, who worked in our financial planning department as a paraplanner, has left our firm to pursue other opportunities. We wish him success.

Replacing Greg is **Henry Becker**, who joined us on February 18. Henry brings tremendous experience and energy to the financial planning department. He has spent his career in the financial

services industry, including working as an Individual Retirement Consultant with TIAA-CREF and as a Financial Advisor with the Government Employees Benefit Association. Henry is also in the final stages of earning his Certified Financial Planner (CFP) designation. He and his wife Tracy live in Laurel and are expecting their first child in June. You can learn more about Henry by reading his bio on our website at [www.bwfa.com](http://www.bwfa.com).



# Retirement & Estate Planning



By Kim Anderson, 

## Planning for Long-Term Care Needs

The issues associated with long-term care are not as far off as we might like to think. Indeed many of us have already had to confront these issues as they relate to our parents or other loved ones. And inevitably we will need to face them for ourselves.

Fortunately, Arlene Saks-Martin, a local geriatric care manager, has some guidance for all of us.

First of all," she says, "don't delay in making decisions about your long-term care wishes." You need to determine where you would ideally like to receive care, at home or in a facility, what type of facility you would prefer, and under what circumstances you would want to enter a facility. And, you need to make these decisions known to your family. "One of the most important things to people of all ages is their right to choose. In order to have that opportunity, it is important to make these major decisions before it is too late." It can become a terrible burden on family members if they have to make these decisions for you without any guidance.

In order to make the best choices in terms of long-term care, you need to get educated. There are a lot of misperceptions out there about what is available. According to Ms. Saks-Martin, many older people say, "I'm not ready to move into a retirement community. I'm not old enough and I don't want to be around all those old people." It is important to understand that there is a wide variety of facilities to meet the varying needs of older people today, from independent living to nursing home care. "People can still come and go as they please, if they are able. They are just adding safety, security, and supervision, if needed."

In fact, there are many more choices among long-term care facilities for people who are still active and healthy. In what is known as a continuing care community, people will find all three levels of care: independent, assisted and nursing. Charlestown in Catonsville, Maryland is a well-known example. These facilities will have very active retirement communities, but will also be able to provide increasing care if needed. "If you wait until you become infirmed and disabled to select a facility, you may not have the same opportunities."

So how do you determine the best options available to you? There are a number of resources to help you. Retirement Living Magazine provides a guide to the facilities in our area and lists other resources that may be necessary, such as elder care attorneys and geriatric care managers. It also provides pertinent articles to people facing these decisions. In addition, the Maryland Department of Aging can provide you with a list of licensed continuing care communities and assisted living facilities. Finally, you may want to hire a geriatric care manager. A care manager will conduct an initial assessment for a flat fee. Then he or she will work on an hourly basis, using their extensive knowledge of the facilities and resources in the area to help you find the best match for your needs. That may mean coordinating in-home care services or finding an appropriate facility. You can get a list of care managers in your area by going to the Mid-Atlantic Geriatric Care Managers website.

A large consideration in making any of these decisions will be cost. There is a wide variation in the costs of facilities and care services, some of it quite expensive. If you want to ensure flexibility when it comes to choosing a facility or care option, you may want to consider long-term care insurance. At BWFA, we always include long-term care analysis as part of a comprehensive retirement plan. This allows us to determine if long-term care insurance is appropriate for you.

Making decisions related to long-term care can be difficult. "However," Ms. Saks-Martin says, "starting early can ease this process and help ensure that you have the most choices available to you." When it's time to get started; make sure you turn to the many resources that are out there, especially geriatric care managers. Their expertise can help ensure the best match for your needs.

### Long-Term Care Resources

Mid-Atlantic Geriatric Care Managers –  
[www.gcmonline.org](http://www.gcmonline.org)

Maryland Department of Aging – (410) 767-1100

Retirement Living Magazine – (800) 394-9990

# Investment Management



By Bob Ray

## Is Real Estate the Next Bubble?

Investors who rode the performance wave of technology stocks in the late 90's only to see the bubble burst in March of 2000 are probably wondering whether or not real estate is the next bubble. Real estate has not

quite achieved the returns of tech stocks, but many homes in the Baltimore-Washington region have jumped 25% in the last three years and vacation homes in prime markets have doubled in the last five years. So the comparisons are not without merit.

The performance has been terrific, but does this mean we are in a bubble? If so, how can we take advantage of current real estate values?

### Is Real Estate Really Overvalued?

Stock experts in the 90's claimed that there was no bubble. As tech stocks ran up in value, analysts abandoned traditional methods of profitability analysis, because these firms had no current profits. Instead, they tried to substitute measures that would predict future profitability. Federal Reserve Bank Chairman Alan Greenspan viewed this as "irrational exuberance." Mr. Greenspan's comments were early, but he was right nonetheless. As for real estate, Mr. Greenspan pointed out in congressional testimony last summer that investors cannot buy and sell real estate as efficiently as they can stocks and bonds. So it's harder for bubbles to occur in real estate.

History supports this notion. According to Fannie Mae, the nation's largest residential real estate investor, annual home prices, on a national basis, have not declined since the Great Depression. However, regional downturns have occurred, such as in the oil patch of the early 80's, the rust belt in the mid-80's, and California and New England in the early 90's. The first two events occurred due to regional recessions; the last occurred due to overbuilding. Economists do not expect either a national or regional recession. Since there is a low inventory of homes for sale in the Baltimore-Washington area, one would assume that housing is not overbuilt. So the conditions for a bubble do not appear to exist.

Donna Barkman of Coldwell Banker in Ellicott City says that conditions have been right for a boom in real estate. She points out that there is very little land for sale and a low inventory of homes. In addition, low interest rates have allowed people to buy more expensive new homes while maintaining similar mortgage payments. She says that the market is not as strong today as six months ago due to the uncertainty surrounding the

war. But she feels that buyers will be ready later in the spring. As rates rise, buyers may have more negotiating room, but she doesn't see housing prices retreating.

Conditions have been even better for vacation real estate. Properties on the Atlantic Coast have appreciated between 50% and 100% in the last ten years. This price appreciation was first fed by strong demographics as baby boomers entered their retirement years. The strong stock market and the quick profits from technology stocks helped turbocharge values. Then low interest rates fueled the market in the last few years. Tim Rhodes of Coldwell Banker in Bethany Beach, Delaware points to the low supply of high-end homes near the beach and strong demand holding prices firm. However, further back from the beach, new housing starts have increased the available supply. A weak economy could lead to falling prices in this area.

Realistically, the declines in the equity markets to date and the inevitable rise in interest rates will rein in the real estate market. Already we are seeing weakness in new home sales on a national basis. However, strong demographics and moderate economic growth reduce the likelihood of a substantial decline in real estate values. Here at BWFA, we are not in the housing bubble camp absent a deep recession. But we are a nation at war and in these turbulent times a recession cannot be ruled out.

### Should We Take Advantage of the Real Estate Boom?

BWFA is a strong proponent of diversification of assets and we are constantly rebalancing client portfolios to reduce concentrations in sectors that have performed well recently and allocating the funds to sectors that have underperformed. Should our clients trim their real estate holdings and allocate the funds to the equity markets? In theory, yes.

There are circumstances where it might make sense to trim our exposure to this sector. Homeowners who are looking to downsize as they enter retirement might want to do so now to ensure they sell in a strong market. Investors in vacation properties may also feel that locking in capital gains that could be used against capital losses in the stock market would allow for the efficient transfer between asset sectors. But, for most of us, our primary residences and vacation homes are more than investments. They fulfill a primary need for shelter, and we have emotional attachments not found in the stock markets. We are not prepared to trade them for short-term financial gains. In addition, real estate has historically been an excellent hedge against inflation. For most of us, simply holding our real estate is the best course of action.

# Tax Services



By Bob Cassel, EA 

## The Best Tax Breaks You Can Find

With the recent appreciation in real estate values, many of us have significant gains in our personal residences and other properties. Fortunately, our tax laws provide special tax breaks for gains in real estate, especially compared with other types of assets.

The biggest break comes when we sell our homes. Some of you will remember the old rules about rolling over the gain from the sale of one house into another house of greater value within two years and the one-time exclusion available to people age 55 and older. **Please forget these rules. They are obsolete.**

Under current law, if you sell a principal residence that you have held for two years, you are able to exclude up to \$500,000 of gain if you are married (\$250,000 if you are single). You can do this every two years for your whole life. You do not need to roll over any gain into the purchase of a replacement home, and the exclusion of gain is available to anyone of any age. If you have held the property for less than two years, your gains will be taxable.

The new law means that most people will be able to avoid paying tax on the gains in their home. However, there are still some circumstances that will require special planning. If you fall into one of these scenarios, we suggest a visit with your friendly tax advisor (after April 15, please).

**A couple, contemplating marriage, both own a principal residence in their own name.** Once a couple is married, if either spouse sells their principal residence and excludes gain, then the couple is not permitted to exclude gain on the sale of another home for two years. Be careful here; this takes some careful planning.

**A person who owns multiple homes.** It is now possible to convert a rental property or second home back into a principal residence (by living in it for two years) and then sell it and exclude almost all of the gain. (You'll have to pay some taxes on the depreciation you've claimed since 1997.)

**A retiree who purchases a second home with the intention of retiring there.** Many pre-retirees will find themselves in a large home, wishing to downsize someday. If the couple purchases a second home now with the idea that they may someday retire there, they could end up losing the ability to avoid gains on their current residence. Properly planning the timing of the sale can avoid this problem. As long as the person has lived in the home for any two of the last five years prior to the sale, they can avoid the taxes.

**A person who has owned their home for less than two years.** If you sell your home before meeting the two-year ownership test, you may still be eligible for a partial exclusion if the move was due to job relocation, health reasons, or other "unforeseen" circumstances. You may also be able to offset gains with capital losses on your investments.

The new rules are not very complicated, but they have some tricky spots. When you are planning something as important as the sale of your home, especially if it has appreciated dramatically in value, you should at least make sure you've considered the tax consequences.

Tax breaks are also available on real estate other than your primary residence. Techniques such as installment sales, like-kind exchanges, and charitable remainder trusts can help you defer or avoid taxes on your business or investment properties. We will discuss such techniques in the next issue of our newsletter.

