



BWFA Advisor

Baltimore-Washington Financial Advisors, Inc.

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



By Saxon Birdsong, MBA

We Get Help From Our Clients

In any service business like ours, the most valuable information business owners can get is how their clients feel about them and the job they are doing. Knowing this, three years ago we formed a Client Advisory Board that agreed to provide us with candid comments about our business. In exchange for lunch each quarter, Board members listen to us and the issues we face, provide feedback, and keep us “client focused.”

Our last meeting, in August, provides a good example of how the Board assists us. We asked Board members to comment on whether we should ask our Investment Management clients to sign new Service Agreements. Over the years, as our business and service agreements have changed, we have not gone back to existing clients and asked them to sign new agreements. Therefore, the agreements we have on file vary somewhat from client to client. Since we expect a visit from Federal Auditors relatively soon, we believed having all new agreements in place would speed their review of our firm (a very time-consuming process) and allow us to get back to the matters of our clients more quickly. We understood that asking clients to sign new Agreements would place a bit of a burden on them. At the very least, we would ask them to use their own time to read and digest a two-page document that is packed with information. As you can imagine, this would be fairly unpleasant.



The opinions of our Board members on this issue varied considerably. However, one specific comment made the most sense, “Who do you care about inconveniencing more—your clients or the auditors?” While we prefer not to inconvenience anyone, sometimes it’s impossible. With the opinion of our Board in mind, we decided it was more important not to inconvenience our clients, and we chose to live with the old Agreements and the impact, if any, this will have.



Our Client Advisory Board has benefited us in many ways, mostly by acting as our clients’ advocate. The Board enables us to see things more clearly through our clients’ eyes and is one of several tools that helps make BWFA unique in the marketplace.

To learn more about our Client Advisory Board, please visit our website at www.bwfa.com. Select the About button on the left side of the screen, scroll to the bottom of the page, and select the fourth bullet, Client Advisory Board. If you are a client and would like to sit on our Board, please send me an email at sbirdsong@bwfa.com.

What’s Happening at BWFA

New Director of Client Services

We’re pleased to announce that Jesse Sternberger has joined our team as Director of Client Services. In this role, Jesse will concentrate on developing new business for BWFA through our existing referral networks. He brings with him more than 35 years of experience in the financial services industry as well as broad management experience in the areas of administration, sales and marketing. Prior to joining BWFA he was the managing director for marketing/public relations for the trust department at Chevy Chase Bank. If you don’t find Jesse in the office, you can try to reach him at the Argyle Country Club golf course.

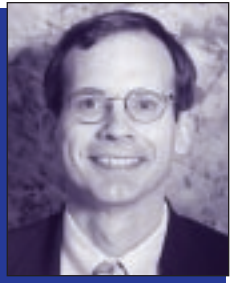
New Planning Department Manager

We also welcome Mark Stinson, CPA, on board. Mark has taken charge of our financial planning services. We were fortunate to steal him away from AXA Advisors, where he worked as a financial consultant. Earlier professional experience includes corporate accounting for Baltimore-area manufacturing firms. Mark, his wife Karen and their four sons live in Marriottsville, Maryland. You can’t miss Mark when you see him; he’s the thin one. He’s a Sprint triathlete and expects to participate in his second event early in October.

Retirement & Estate Planning



Which Financial Plan is Right for You?



**By Mark Stinson,
CPA**

to meet the distinct needs of our clients at different stages of their lives. The purpose of this article is to explain which plan is right for you.

The Pre-Retirement Plan

If you are more than five years from retirement and do not have complicating issues, such as significant employee stock options or your own business, this plan is likely to be for you. At this stage of life, clients find that there are tremendous demands on their resources, including buying a home, raising a family, and putting children through college. Additionally, there is saving for retirement, paying taxes, and protecting assets and loved ones with insurance. The Pre-Retirement plan helps ensure clients get the most from the resources they have.

Our Pre-Retirement Plan identifies what you are doing right and what you are doing wrong. It outlines specific recommendations in investments, insurance, retirement savings, education funding, and basic estate planning. We will also cover any other area that may be of concern to our clients, such as whether to refinance a mortgage. Questions the pre-retirement plans typically answer are:

- Have I selected the best investments?
- Do I have the right kind and amount of insurance?
- How can I reduce my taxes?
- Am I on track in saving for retirement?
- How should I fund my child's college education?
- Can we afford to do what we want to do?

The Retirement Plan

If you are within five years of retirement or have recently retired, the Retirement Plan has been designed for you. Retirement is a significant life transition and with it come numerous questions and concerns, such as: How much can I spend in retirement? Will I be able to maintain my standard of living? How do I generate income from my investments? Do I need long-term care insurance? The Retirement

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This is accomplished by developing year-by-year financial projections and using sophisticated analytical tools (Monte Carlo simulations) to "test" different scenarios and help clients identify the best course to follow. In addition, we provide specific recommendations in the areas of Estate Planning, Long-term Care Insurance, Taxes, and Investments. Questions the Retirement Plan typically answers are:

- When can I retire?
- Will I be able to maintain the lifestyle I desire in retirement?
- How should I invest my assets in retirement?
- What can I do to reduce taxes?
- Do I need long-term care insurance?
- Should I revise my wills?



The Estate Plan

If you have substantial wealth, the Estate Plan is the most appropriate for you. Clients with estates above \$1.5 million frequently require techniques and planning beyond basic wills. BWFA will identify which techniques are most appropriate and help clients put the proper techniques in place. In some cases, the preparation of legal documents (wills, trusts, etc.) will require the client to employ an attorney, at additional cost. BWFA will work with the client and the attorney to ensure satisfactory execution of the estate plan. Our Estate Planning service has three objectives:

- To help clients minimize federal and state estate taxes
- To establish how assets will be handled when the clients are no longer able to manage them
- To organize clients' assets and affairs in a way that makes settling affairs easier for their heirs

Financial Plan Reviews

In a clear, concise and cost-effective manner, our financial plans help our clients achieve their goals at each stage of life. Of course, goals, objectives, markets and tax laws change. That is why we recommend a Financial Plan Review biannually. The purpose of the reviews is to determine if our clients are meeting their financial objectives and if modifications or revisions to their Plans are necessary. The Financial Plan Review answers the question: Am I still on target to reach my financial goals?

Investment Management



By Rob Williams



Investor Behavior Hurts Investment Returns

The biggest risk mutual fund investors face in earning a decent return may be their own behavior. A recent study by Dalbar, a financial industry research group, examined real investor returns over a nineteen-year period. It concluded that, "Investment return is

far more dependent on investor behavior than fund performance." Comparative returns show that the results of this "behavior" are truly threatening to the average investor's portfolio.

Average Annual Return for period January, 1984 to December, 2002

S&P500 Index	12.2%
Average equity fund investor	2.6%
Long-term corporate bond index	11.3%
Average bond investor	4.2%
Inflation	3.1%

You would think that investment returns below the inflation rate would be as bad as it could get, but the real results are probably worse. This study did not even consider the high commission costs caused by rapid buying and selling of mutual funds, nor did it consider the tax impact of selling funds held for short periods of time.

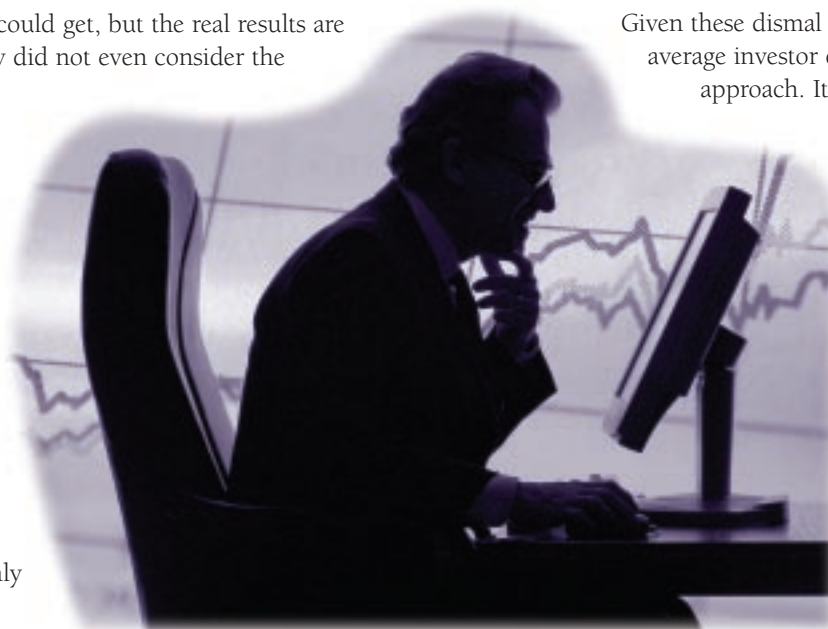
And many investors did trade mutual funds rapidly. The average holding period for a stock fund was only 29.5 months, while the average holding period for fixed income funds was only

slightly longer, 34.3 months. This is despite all of the attempts by the mutual fund companies, and the financial profession as a whole, to encourage investors to hold funds for the long haul.

The discrepancy in returns between the average investor and the indexes is easy to explain. The study found that investors continuously make the mistake of trying to "time the market" by buying funds when their performance is hot, then selling these funds when their performance inevitably turns down. The result is that investors do exactly the wrong thing, buying high and selling low.

A secondary cause for this underperformance of the average investor compared to the indexes is certainly the high cost of mutual funds (which is why we recommend that our larger clients use individual securities). But if we assume mutual funds cost an average of 2% per year, then mutual fund expenses still would only account for a small part of the discrepancy.

Given these dismal numbers, what should the average investor do? The study offered one approach. It noted that mutual fund investors who bought and held their funds did the best. Therefore, the results of this study suggest that, if you want to invest in mutual funds, you have to be able to resist the urge to meddle. Otherwise, turn over the reigns of your portfolio to a professional investment advisor. The larger your investments, the more important it is to use a professional.



Tax Services



By **Bob Cassel, EA,**



State Death (Estate) Tax Changes— What Should You Do?

As a result of the Economic and Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), our federal estate tax system has changed greatly. As we noted in our Spring 2004 newsletter, changes in federal estate taxes caused an unexpected reduction in the amount of

estate taxes collected by each state. As you can imagine, the states quickly began revising and even creating laws designed to recoup the lost revenue.

Many people will be affected by these changes. In this article, you will find some guidelines to help determine if you are affected and what you can do about it.

A number of states have already amended their laws, effectively increasing their estate taxes to recover the lost revenue. These include: D.C., Maine, Massachusetts, Minnesota, Nebraska, North Carolina, Rhode Island, Vermont, Virginia, and Wisconsin. Other states have created stand-alone estate taxes, including: Kansas, Maryland, New Jersey, Ohio, and Pennsylvania.

If you live in one of these states and did your estate planning more than a year ago, you probably did not take these tax law changes into account. The language in your wills or trusts may refer to federal estate tax law and may inadvertently cause you to pay more estate taxes at the state level.

In Maryland for example, if your estate documents call for funding a credit shelter trust to the federal exclusion level (currently \$1.5 million), your estate could end up paying Maryland as much as \$64,000 in estate taxes. Any estate valued at more than \$1 million is now subject to Maryland estate tax.

The language in your wills and trusts may have been written at a time when state taxes were less of an issue than they are now. In the past, state laws were in alignment with the federal laws. Now that the states have “decoupled” from federal estate tax laws, the rules of the game have changed.

Single individuals in Maryland with estates over \$1 million don't have very many options to avoid the new tax. One technique is to make gifts during your lifetime, under the annual gift exclusion amount of \$11,000, to reduce the value of your overall estate and thereby either reduce or avoid Maryland estate taxes. Charitable gifts made by your estate will also reduce estate taxes.

Married Marylanders will have a few more planning opportunities. If you are a Maryland couple with a combined total estate valued between \$1 million and \$3 million, you will want to be sure that your estate planning documents are flexible enough to cover both federal and state law.

What Should You Do

If your estate is worth more than \$1 million, we recommend you revisit your estate plan with your financial advisor. To prepare for the meeting you should:

1. compile a current listing and valuation of your assets, liabilities, insurance benefits
2. review your desires for transferring your estates to your heirs
3. review your plans for gifting during your lifetime
4. review changes to your states' estate tax laws

You will then be prepared for a visit with your attorney to make the appropriate changes to your estate planning documents.



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