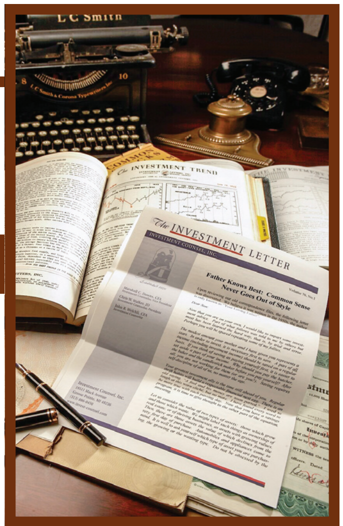
The Investment Letter

Special Edition



Pennies From Heaven?

Money, and particularly investing, is a topic many people fear, as they feel ill equipped to manage it effectively. If you're someone who has recently come into a substantial amount of money, that fear is suddenly magnified exponentially, to the point where it can be crippling. To some extent that concern is justified as mis-steps in managing your newfound wealth can be costly and significantly impact its ability to last.

An individual who suddenly amasses wealth is forced to learn quickly what those who grew their portfolios slowly have learned over 10, 20, 30 years or more of their investing lives. Not only is the learning curve much steeper but the stakes are much higher as well.

Whether it's an inheritance, the sale of a business, lottery winnings, a court settlement or a professional sports contract with a sizable signing bonus - coming into a substantial amount of money can be both exciting and stressful at the same time. While the circumstances under which people arrive at this situation differ, the challenges they face with the windfall are remarkably similar.

To help these individuals we've compiled a list of what we feel are the appropriate steps to take as well as the most common DO's and DON'Ts regarding managing, and most importantly keeping, your wealth. Also, it's important to keep in mind that you don't have to face these challenges alone – in fact not seeking out professional expertise could be a costly mistake.

The Plan

Whether we are professional investors or simply managing our family budget - we've all made mistakes with money. With investing, hopefully our mistakes come early on in our investing lives where the dollars at stake were not that large and were recoverable over the course of many years. If you've accumulated a lot of wealth quickly you may not have the luxury of making mistakes with your newfound millions, as any missteps could be permanent and costly.

In order to grow, and protect your wealth it's necessary to have a plan. Without a plan in place there can be no effective strategy. Without a strategy the tendency to spend and overspend takes over which can easily lead to dire financial outcomes.

Statistics differ on this but one study suggests that lottery winners file bankruptcy at twice the national rate. Other studies claim the number of lottery winners that end up facing bankruptcy is as high as 70%.

Being honest with yourself about your plans for the money is critical. At this point you should be asking yourself questions like what are my needs? My wants? Will I continue to work? Can I afford not to work? What will I be spending this money on? How long does this have to last me?

It's ok to not have answers to all or many of these questions. This is merely to get you thinking about the money in different ways before you do any spending.

To really begin to implement a plan it will be necessary to bring on professionals who can guide and advise you to make the right choices for your particular needs.

The Team

The first call after you've become aware of your windfall should be to a trusted CPA (Certified Public Accountant). They can be found by searching online or through the yellow pages, but a trusted friend or family referral is best. We work closely with a number of excellent CPA's and can also make an introduction.

Why is a CPA important? In most cases taxes are going to eat away a significant portion of your newfound wealth. There are exceptions where that will not be the case, but in most instances, unless you are certain there are no taxes due, a visit to a CPA is in order. A CPA will be able to calculate state and federal taxes from your windfall and can make sure you avoid any interest or penalties from the IRS.

You will likely be visiting your CPA at least annually if you have capital gains or income to report from investments during that tax year. Taxes are a reality and all too often we hear of professional athletes or celebrities who have failed to not only plan for the inevitable call from the IRS but also failed to even consider that taxes may be owed.

Avoiding or delaying taxes is never a good idea – penalties and interest may apply and in some cases tax evasion is even punishable by jail time. A good CPA will keep you informed of your tax responsibility, will make recommendations to minimize taxes and will keep you on the right side of the law.

Second only to taxes, many people dislike investing. Investing can seem complicated and confusing and in some cases it is. This is where a Registered Investment Advisor or RIA can help. An RIA can help manage and execute your investment plan, which they can also help you craft.

Take care to avoid brokers and limit your search to RIAs as they are usually less expensive and are legally obligated to act in your best interest – brokers do not have the same legal requirement.

Perhaps the most important role your advisor can play is taking the emotion out of investment decisions. Humans are wired to fear losses and tend to sell when markets are down and buy when they are high – the exact opposite of the first rule of investing: "Buy low, sell high!"

A good advisor will explain your investments to you and regularly communicate should any changes be necessary in your portfolio. Because investments generate taxes it is important that your CPA and advisor work together on your behalf.

Your circumstances will likely also require the services of a legal counsel. A good lawyer can be invaluable and can help with drafting Trust or other documents to protect your wealth. They can also advise on other questions you are likely to have concerning your wealth.

Legal representation is also necessary in the event you find yourself the target of a lawsuit and we highly recommended that a trusted lawyer reviews any contracts you may have, including those between you and your CPA and investment advisor.

Proper legal counsel can also draft the appropriate documents to make sure your wishes are met when it comes time to distribute wealth to your heirs and/or charities.

Whether or not your unique situation calls for the services of an insurance professional will become much clearer after you meet with your lawyer, CPA and your investment professional.

We cannot stress enough the importance of working with professionals that have your best interests at heart and can help manage the emotional roller coaster that such situations bring about.

In addition there are a few general rules of thumb when it comes to newfound wealth. Each person is unique and our list is not exhaustive, but it is a good start if you find yourself in this situation.

DON'Ts

- DON'T use your newfound assets to leverage yourself by taking on additional debt. Any existing debt should be retired not expanded. Keep in mind that unless you continue to work and earn income, your assets and whatever income they can generate for you are the extent of your wealth.
- DON'T spend excessively. What is and isn't excessive will be determined by having a

conversation with your financial professional.

- DON'T advertise your new status. Flaunting wealth is a surefire way to attract unwanted attention from a broke third cousin you haven't heard from in years to unscrupulous opportunists looking to steal or defraud you.
- DON'T back every business "opportunity" that comes your way. As someone with means, those opportunities will seemingly appear out of nowhere and often are high risk (after all it's not their money!) and poorly planned out. If you are seriously considering investing in a business, whether yours or someone else's, make sure it is vetted by professionals you trust and the risk of this investment is reflected in your overall investment portfolio.
- DON'T forego having a budget. Just because you have more money to spend, doesn't mean it is a never-ending supply. A little budgeting can go a long way in making sure you don't spend more than you have available.
- DON'T make decisions in haste. Take the time to thoughtfully consider any decision that can't be undone. Buying a business, an annuity, real estate transactions or quitting a job are all decisions that should be made with great thought rather than on impulse. You most likely don't know what turns your new wealth will bring. During the first six months to a year, take your time and don't make material decisions that can't be reversed.

DO's

- DO hire a CPA and an Investment Advisor to handle taxes and managing investments for you. Make sure they are carefully vetted and have your best interests at heart. Only consider handling this yourself if you are an expert in these matters. Practicing your skill at managing taxes and investments at this point is not worth the risk.
- DO take some time to think about what your expectations are and whether they are realistic. Mansions and fancy cars are fine, but also consider the upkeep and taxes on such purchases.
- DO be honest about your plan for how you expect to use your investment portfolio. A portfolio that you intend to deplete within 5 years will look and act much differently than one that is being managed to last the life of the owner.
- DO take prudent risk. A common mistake, second only to overspending, is being too conservative with your money. Remember a million dollars is not what it used to be. Many people believe "I'll just spend the interest and never touch the principle." A million dollars invested in "no risk" Certificates of Deposit (CDs) will earn just 2% or $20,000 per year. Twenty thousand dollars per year is less than the US family poverty rate and likely insufficient as a sole source of income. A prudently invested, diversified portfolio, on the other hand, over the long-term, can reasonably expect to return in excess of 6%.
- DO enjoy your wealth within the parameters you have set forth in your plan.

While the above is not meant to be a complete guide to dealing with all the new challenges that arise from newly acquired wealth. It is, however, a general guideline that can help protect that wealth, to the extent possible, from taxes and those seeking to separate you from it.

The above advice is sound but it is not a substitute for meeting with a trusted CPA and investment advisor to establish proper goals, guidelines and strategies to best craft the type of financial strategy that makes sense for you.

Having an influx of wealth is a great problem to have. Unfortunately, it can be as much a curse as a blessing if not managed carefully. Treat your windfall with the same care and consideration you would your other assets and not as 'found money.'

For over 85 years we have been helping and guiding individuals and families that have faced the challenge of managing the "problem" of wealth. Please take advantage of our experience and expertise by scheduling a meeting with Investment Counsel. We can help you successfully transition into this exciting yet intimidating time.

With the proper planning, guidance and the right expectations, this wealth can provide a secure and enduring source of income for a lifetime or longer.