



January, 1<sup>st</sup> 2013

## **Building Personal Financial Guardrails**

With all eyes on Washington where our elected-politicians on both sides of the aisle struggled in striking a deal to avoid the infamous “fiscal cliff” until the eleventh hour, people on Wall Street and the Main Street alike grew very nervous as the clock continued to tick. In the end, the American people are poised to bear the brunt of the compromised deal—which consists largely of tax increases. For the average people like you and I feeling vulnerable, what can we do to protect ourselves, or at a minimum level, reduce the impact of government policies to our daily financial lives?

### **Budgeting**

I cannot stress enough the significance of having a personal or family budget. In essence, a budget, or a spending plan, is the first step toward being financially intelligent and the key to taking control of your financial life by:

- Letting you understand where your money is coming from and going to;
- Identifying (potential) problem areas or problematic spending habits, before they get out of hand; and
- Helping you build confidence in managing your own money as a result.

Similar to our government, a vast number of people “believe” that they do not need a budget, partly because they can keep swiping that credit card. If one is maxed out, they can just roll the balance to another card and keep on spending. But, unlike Uncle Sam, most of us do not have a printing press in the basement (at least legally), and those credit card statements all have a due date!

If you have a budget and actually utilize it, you should not have problem dealing with credit card debts, or better yet, you would owe the credit card company nothing! A good budget lets you know exactly how much you can spend, when to put a purchase on credit, when your bills are due, and total confidence that all of the bills will be paid in full, on time every time. What sounds like a far-fetched dream for our politicians need not be for you. With a few months’ worth of persistence, perseverance, and patience, you can put your financial house in order for good!

This is a particularly good time to create or adjust your budget as there are several changes that are likely to effect it. The payroll holiday did not get extended into 2013, which means most taxpayers will see a 2% decrease in their paycheck (SECA portion of the Social Security tax reverts back to 6.2% from 4.2%). That roughly translates to about \$80 less take-home pay every month for a median income household<sup>1</sup>. If you are consistently overspending (having a deficit), the smaller paycheck will suddenly seem much smaller! On the contrary, by looking at your budget and identifying categories in which you can cut back spending, you should run into little trouble, if any.

One of the new taxes to look out for and incorporate in your budget this year is the Medicare surtax on wages and net investment income for high income earners. While the top marginal income tax rate of

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<sup>1</sup> Income, Poverty, and Health Insurance Coverage in the United States: 2011. U.S. Census.  
<http://www.census.gov/prod/2012pubs/p60-243.pdf>



39.6% applies to married couples making over \$450,000, the Medicare surtax hits households with income at a much lower threshold: \$250,000 for joint filers and \$200,000 for single taxpayers. If you are subject to the new tax, be sure to consult with your tax and financial advisor on ways to minimize the unpleasant surprise.

#### Estate Planning

Regardless of the uncertainty caused by continuously evolving estate regulations, a sound and properly drafted estate plan will provide invaluable and tangible protection to you and your family. Gone are the days where a simple will was enough. Contemporary estate planning that centers around a “living trust” can benefit the estate by reducing taxes, protecting assets, and providing for individuals with special needs. It can also take advantage of the prevailing estate laws and available tax credits.

Other tools in the estate planning suite such as powers of attorney ensure the continuity of business and household operations while you are away or otherwise unable to act. Periodically reviewing your estate plan, making sure that you have the correct beneficiaries listed on your retirement accounts and life insurance policies, and informing your loved ones and professional advisors about your plan enhances the likelihood of your plan being carried out. It also greatly reduces the potential for unnecessary conflict, stress, and tension among family members and heirs.

Intricate family relationships and the non-traditional family units often call for a more carefully thought-out and sophisticated estate plan to ensure fairness and equality. Concerns among these families may include how to make sure the surviving partner is provided for and also insuring children from various marriages end up with equitable inheritances.

#### Use of Roth IRA

With the government’s growing appetite for revenue, taxes are likely to go higher. What better than a Roth IRA that gives you the ability for true tax-free savings and withdrawals? My last letter, *Five Reasons to Go Roth*<sup>2</sup>, explains in detail why I am a supporter.

All I will suggest here is that, if you meet contribution eligibility<sup>3</sup>, stashing up your Roth IRA or 401(k) should be the priority. Even if you are not eligible or your work does not offer a Roth option on your retirement plan, you can still convert assets in a traditional IRA to a Roth easily.

#### Stick to Your Plan

It is never too late to begin a plan, and any plan works only as long as it is being followed and reviewed on an ongoing basis. Make this your top New Year’s resolution and let us help you get started on a sound financial plan.

May the New Year bring you good health and good wealth!

- Henry Yu, CFP®

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<sup>2</sup> [http://www.summaglobal.com/newsletters/2012\\_Q4\\_GoRoth.pdf](http://www.summaglobal.com/newsletters/2012_Q4_GoRoth.pdf)

<sup>3</sup> For details, please refer to the IRS website: <http://www.irs.gov/Retirement-Plans/Amount-of-Roth-IRA-Contributions-That-You-Can-Make-For-2013>