WEALTH MANAGEMENT

STERLING WEALTH MANAGEMENT

Planning through the generations

William R. Lewis

Sterling Wealth Management

16 Chestnut Street

Montrose, PA 18801

570-278-1858

www.swmpa.com

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What is Wealth Management?

- Wealth Management is the sum of activities necessary to accumulate, protect, and transfer wealth.
- The wealth management approach to financial planning helps us make important decisions about investments, retirement, insurance, taxes, and transferring assets to heirs.

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Defining the Wealth Management Process

- Gather Data
- Analyze Existing Positions
- Present an Action Plan
- Implement Plan
- Ongoing Review and Reporting

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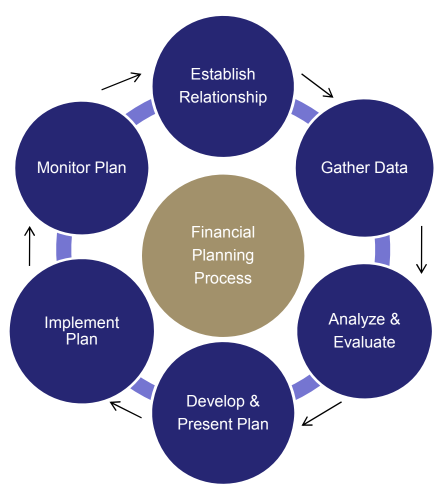
The Planning Process



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Things to Consider When Developing a Financial Plan

- Inflation
- Taxation
- Medical Care
- Portfolio Adjustments
- Retirement Projections
- Projected Income Needs
- Longevity Assumptions
- Social Security
- Return on Investments

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What's Most Important to You?

- One benefit of planning is that it gets you thinking about what is really most important to you.
- Your concerns over your finances are likely more specific than "I want more money."
  - What is the "why" behind your goals?
- What is meaningful to you may not always be quantified in dollars and cents.

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Important, Tangible Goals

- Some of the items that are important to you are going to be less tangible, like:
  - Family
  - Community Service
  - Leaving a legacy
- These intangible items can be reframed in terms of quantifiable financial planning goals, like:
  - Protecting your family by having adequate insurance
  - Leaving behind a legacy with a properly structured estate plan
  - Giving back to your community with a charitable trust

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Accumulation Planning

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What is Accumulation Planning?

- Accumulation planning refers to the strategies involved in the:
  - ✓ Determination of your investment needs.
  - ✓ Creation of an asset allocation based upon those needs.
  - ✓ Selection of suitable investments based on your financial goals and risk tolerance.

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Determining Your Financial Needs

Before any course of action is determined it is important to get an understanding of your financial needs and attitudes. Assessment of your needs typically includes:

- Personal assessment-your age, health, occupation, mortgage, marital status, children, and your potential retirement date.
- Financial assessment-debts, savings, outstanding financial obligations, tax situation.

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Determining Your Financial Needs

- Financial attitude assessment-How comfortable do you feel with the market? What would be the consequence of losing some of your capital?
- Financial goal assessment-Are you looking to retire early? Buy a second home? Put children through college? Leave money to your heirs? Gift money to charity?

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Determining Your Financial Needs

The assessment of your financial needs and objectives determines your portfolio's "balancing point." While no single portfolio can meet the needs of every investor; these assessments point to one of five basic asset allocation strategies:

Conservative	Capital Preservation	Moderate	Growth	Aggressive

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Asset Allocation

Once your financial needs and attitudes have been determined, your assets can be distributed among a variety of investment categories, a process generally referred to as **asset allocation**.

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What is Asset Allocation?

- Asset allocation is a disciplined, long-term financial strategy for distributing wealth amongst various investment categories (stocks, bonds, money markets, real estate, etc.) based on your investment goals, time horizon, and risk tolerance.
  - These categories are divided into smaller ***asset classes***, such as large-, mid-, and small-cap growth and value, emerging markets, corporate and government bonds, international equity, and several others.
- Asset allocation attempts to reduce overall investment risk, create more reliable investment returns, and improves the risk/return tradeoff of your portfolio.

Note: There can be no guarantee that any particular yield or return will be achieved from any investment. Investors should note that diversification does not assure against market loss and that there is no guarantee that a diversified portfolio will outperform a non-diversified portfolio.

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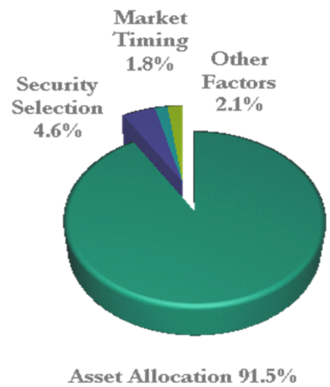
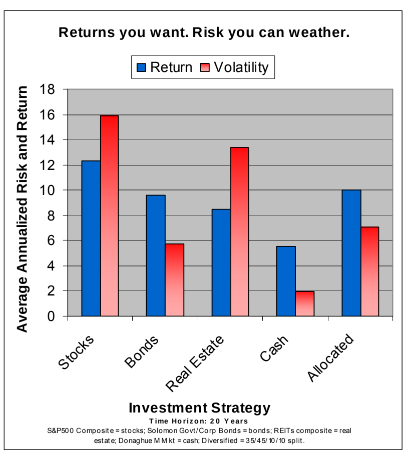
Why Asset Allocation?

- You've heard the warning not to put all your eggs in one basket. Asset allocation extends that logic to your investments.
- Asset allocation involves strategically positioning your portfolio among asset classes according to your risk tolerance and goals.
- A Brinson, Singer, & Beebower study suggests that asset allocation is the primary determinant of ***variation in portfolio returns*** (see right).



An Asset Allocation Example



- **Stocks, Bonds, or Cash?**
  - How about all of the above?
  - Over the past 20 years, a well-allocated portfolio would have given nearly 90% of the return of an all-equity portfolio, with less than half as much volatility.

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Investment Selection

Once an asset allocation approach has been determined, we implement the plan through the selection of specific investment vehicles to fill each asset class. Depending on your portfolio type and your risk tolerance, we will recommend a combination of investments that will help you to pursue your long-term financial objectives. Choices of securities for you investment portfolio may include basic securities and alternative investments.

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Basic Securities

Basic securities, also referred to as traditional investments, include:

- Stocks
- Bonds
- Annuities
- Stock Options
- Mutual Funds
- Individually Managed Accounts

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Alternative Investments

An alternative investment is any investment other than a stock or bond. Alternative investments can include:

- Real Estate Investment Trusts (REITs)
- Futures
- Options
- Tax Credit Programs
- Commodities
- Hedge Funds

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Alternative Investments

The benefits of alternative investments can include:

- Diversification
- Liquidity
- Tax efficiency
- Lower portfolio volatility

Note: Alternative investments involve significant risks which are described in the applicable confidential offering memorandum. Qualified investors should not invest in any alternative investment unless the investors are able to sustain the loss of all or a significant portion of investment capital. Investors should be aware that they will be required to bear the financial risks of this type of investment for a substantial period of time, since many of these investments are illiquid for several years. In making an investment decision, investors must rely on their own examination of the person or entity creating the securities offered and the terms of the investment including the merits and risks involved.

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Accumulation Planning Wrap-Up

Whether you are investing for retirement, college, or another objective, you are faced with the task of quantifying your goal, developing an asset allocation strategy and choosing the most appropriate investment vehicles for your wealth. In the midst of this complexity, we are here to partner with you to help you to pursue your financial hopes and dreams.

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Retirement Planning

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You should consult a tax or legal professional regarding your individual situation.

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What Is Retirement Planning?

- The process of evaluating your current financial situation and creating an accumulation and distribution strategy to help support a desired lifestyle.
- Successful plans can maximize growth, optimize tax-efficient distributions, and allow you to pass on retirement assets to the next generation.

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Most Common Retirement Questions

- Will I be able to maintain my lifestyle?
- Will my income keep up with inflation?
- Will I be able to meet all my expenses, including health care?
- Can I retire now or should I wait?

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Why Do You Need a Plan for Your Retirement?

- Retirement is typically the longest life event you will ever face,
  and it generally dominates other financial goals.
- Average life expectancy in the U.S. for males is 74.8 years
  and 80.1 years for females.
- Increased longevity means that your retirement years can
  span decades.

Looking at Current Trends

- Census figures indicate that only 1 in every 10 Americans today is financially prepared to retire when they reach age 65.
- Life expectancies continue to increase. For a 65-year-old couple,
  the odds that one spouse will live until age 90 are over 50%.
- Social security benefits will replace only 16% of the income of married couples earning $50,000–$100,000 and only 9.5% of the income of married couples earning more than $100,000.
- Over the past 30 years, inflation has averaged about 5%.

Sources: U.S. Bureau of the Census; National Association of Variable Annuities; CSIS National Commission on Retirement Policy, 1997; Office of Research and Economic Analysis, Pension and Welfare Administration; Employee Benefit Research Institute; Merrill Lynch Strategic Planning

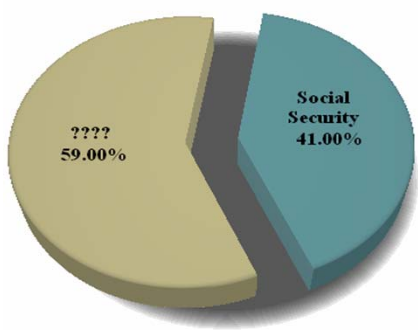
Assessing Current Attitudes

- 48% of Americans are concerned that they have not saved enough.
- 54% of Americans expect to be working full- or part-time after age 65.
- 57% of Americans whose income is less than $25K/year expect to face a financial crisis in the future.

Source: 2004 Merrill Lynch/Nationwide Survey

Social (In)Security

- Many people think social security will cover their retirement expenses. Unfortunately, according to the Social Security Administration, today's retirees can only count on social security for 41% of their income at retirement.
- Where is the rest of the money coming from?



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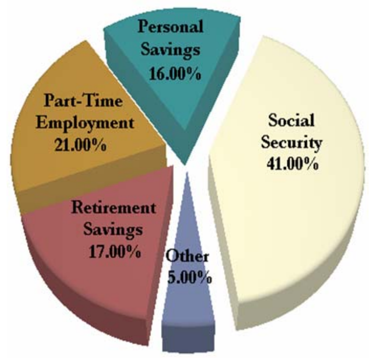
Filling the Gap

- The majority of your retirement income is going to come from **you** and your investments



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Looking at the Options

- The Wealth Management process attempts to coordinate the investments held in your:
  - Personal savings
  - Qualified employer-sponsored plans
  - Individual retirement accounts (IRAs)
  - Executive deferral plans
- The goal is to allow you to accumulate enough money to support your desired retirement lifestyle, and to have money left over to leave to your loved ones.

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Personal Savings

- Personal savings may not fall within a traditional retirement vehicle, but these savings are part of your overall retirement plan.
- Personal saving strategies can help fill retirement gaps not filled by IRAs, social security, and qualified plans.
- Personal savings may include investments in:
  - Annuities
  - Government securities
  - Real estate
  - Stocks and bonds
  - Alternative investments

Qualified Plans

- Qualified plans include employer-sponsored plans, such as 401(k)s and pension plans, governed by the Employee Retirement Income and Security Act of 1974 and years of continuous legislation.
- Plans allow for pretax investments that grow tax-deferred.
- Plans also have contribution limits and strict distribution rules.
- Types of qualified plans include:
  - Keoghs (PSPs/MPPs)
  - 401(k)s
  - Nonprofit 403(b)s/457s
  - Defined benefit plans
  - ESOPs
  - 412(i) plans

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IRA Planning

- IRAs help you save for retirement while allowing you to take advantage of favorable tax incentives.
- IRAs are inexpensive, as well as easy to establish and maintain.
- Many people use IRAs to consolidate retirement assets that were previously held in employer-sponsored plans.
- Types of IRAs:
  - Traditional/rollover IRAs
  - Roth IRAs
  - SEPs and SIMPLEs
  - Spousal IRAs
  - "Stretch" IRAs

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From Accumulation to Distribution

- As you move from the "saving" phase to the "distribution" phase of your financial life, it's important to understand the implications of this change.
- Instead of adding to your assets, you will be spending them. Money's going out the door rather than coming in.

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Distribution Planning

- At the heart of the retirement plan should be an effective withdrawal strategy that will help ensure that your hard-earned assets last and fulfill the needs for which they're intended.
- Distribution options:
  - 72(t)s
  - Beneficiary planning
  - Cash flow analysis
  - Qualified/nonqualified distributions
  - Annuity distributions
  - Multigenerational ("Stretch") IRAs

How We Help You Plan for Retirement

- **Get a comprehensive view** of your various investment accounts.
- **Evaluate your current financial situation.**
- **Create an investment strategy** that suits your risk tolerance and works across all of your investments.
- **Monitor your portfolio and your spending habits** and refine your strategy where necessary.

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Taxation Planning

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What Is Taxation Planning?

- Taxation planning considers the taxation implications of individual, investment, or business decisions, usually with the goal of minimizing tax liability.
- While decisions are rarely made solely on their tax impact, you should have a working knowledge of the income or estate tax issues and costs involved.
- Even if you delegate tax planning to your accountant, knowing what decisions can affect your tax liability will allow you to take the greatest possible advantage of permissible tax savings.

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Income Tax Planning

- Major goal is to minimize federal income tax liability
- Can be achieved by reducing taxable income through income deferral and shifting
- Other strategies for reducing taxable income include:
  - Deduction planning
  - Investment tax planning
  - Year-end planning strategies

Income Tax Planning

Investment Tax Planning

- Involves evaluating how to best position assets in order to minimize the amount of taxes you have to pay on an ongoing basis
- Requires year-round planning
- Begins with an in-depth understanding of the tax implications of various investments and investment strategies

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Investment Tax Planning

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Gift & Estate Tax Planning

- Giving away wealth, during life or at death, may lead to federal taxes—and possibly additional state taxes. These include:
  - Gift taxes
  - Estate taxes
  - Income taxes
  - Inheritance taxes
- By understanding these taxes and the various strategies you can use to minimize them, you can better protect your assets.

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Gift & Estate Tax Planning

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Life Event Planning

- Some events in life—retirement, for example—come with tax considerations.
- Life event planning focuses on the impact of significant events on your life, as well as on the stages of your wealth management plan.

Life Event Planning

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Who Needs Tax Planning?

While tax planning is a continual process, there are a number of events that should trigger a review:

- Planning for retirement
- Taking retirement distributions
- Buying or selling investments or other property
- Buying or selling a home
- Making large gifts to a relative or to charity
- Starting, buying, or selling a business or business equipment
- Planning for education
- Planning for employee stock options
- Planning for medical or long-term care
- Changing jobs
- Winning the lottery or inheriting large sums
- Birth, death, marriage, divorce of a family member
- Incurring employee business expenses

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Ten Common Tax Planning Mistakes

1. Waiting until the end of the year to begin tax planning.
2. Ignoring the impact of the Alternative Minimum Tax on your financial decisions.
3. Not taking advantage of tax-deferred or tax-free investments.
4. Ignoring the tax implications of life changes, such as the birth of a child, marriage, divorce, selling a home or business, etc.
5. Overlooking the tax-lowering impact of charitable gifts.

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Ten Common Tax Planning Mistakes

6. Not taking into account the impact of estate taxes on your beneficiaries.
7. Not having a succession plan (everyone with a successful business should have one).
8. Not understanding the tax savings opportunities under new tax laws.
9. Not maximizing the tax advantages afforded by retirement plans.
10. Selling property or a business without taking into consideration the capital gain impact.

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Tax Planning Wrap-Up

- The final step is selecting the most appropriate strategies in light of their cost benefits and implementing them.
- Tax planning can involve complex strategies and should be aided by a team of experts, including an attorney, a CPA, and your financial advisor.
  - Having a lead advisor can assure coordination of your tax planning efforts.
- In the midst of this complexity, we are here to partner with you to help you pursue your financial hopes and dreams.

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Estate Planning

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What Is Estate Planning?

- A process that creates a master plan for the management of your property when you are disabled and the distribution of that property at death at the lowest possible cost.
- Common estate planning issues include:
  - Transferring wealth
  - Minimizing transfer taxes
  - Asset protection
  - Charitable gifting

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Transferring Wealth

- Wealth transfer planning involves the smooth transition of wealth to the next generation, or to charities, according to your wishes.
- You decide to whom, how, and when your assets will be distributed, as well as who will manage your estate or business.
- Wealth transfer planning also involves the management of assets and your health care during disability or incapacity.

Transferring Wealth

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Minimizing Transfer Taxes

- A major goal of estate planning is to minimize potential taxes without interfering with your other financial goals.
- If you give away wealth, during life or at death, you may incur federal taxes—and possibly state taxes.
- You can help protect assets you transfer from excessive depletion by understanding these taxes and the various strategies you can use to minimize them.

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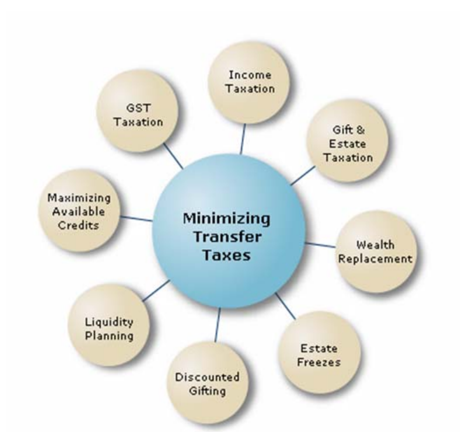
Minimizing Transfer Taxes



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Asset Protection

- If you own substantial assets, creditor protection can be a concern. Creditors can include:
  - The IRS
  - An accident victim
  - Medicaid
  - Business creditors
  - An ex-spouse
- An asset protection plan first identifies potential exposure and then identifies preventative tools and strategies to reduce exposure.

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Asset Protection

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Asset Protection

- Long Term Care

Life Expectancy on the Rise

- The number of years we spend in retirement is increasing
  because of advances in medicine.
- Many illnesses once considered terminal can now be managed
  and are termed chronic.
  - For example, people can live for years with cancer, heart disease, diabetes, or Alzheimer's disease.
- How do we plan for this?

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What Happens as We Age?

- Bodies wear down.
- We need assistance with day-to-day routines.
- We may not be able to live independently.
- Health care expenses increase.

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Logical Assumptions

- Do we think we will live a long life?
  - If we do, chances are we will get sick.
    - If we get sick, chances are we will need care.
- How will this care be paid for?

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The Impact

- If we live a long life, what will be the probable consequences for our *families* and *our finances?*

LTC Is a Family Issue

- More than 70% of care is provided by families (informal care).
- Of that, 67% is provided by children and their spouses and grandchildren.
- How can a loved one's need for care impact a family?

What Is LTC?

- LTC is generally described as providing care and services when a person . . .
  - Is unable to perform activities of daily living
  - Has a severe cognitive impairment
  - Requires custodial, not skilled, care

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Personal Assets/Cash

- Things to consider:
  - The average national cost of care is $75,000 per year.
  - Health care costs are increasing 6.5% per year.
- Will we have enough money to pay for our care?
  - Have we allocated enough funds to pay for our care when we get sick?
  - Can we access these funds without destroying our financial plan or invading principal?

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Charitable Gifting

- Charitable gifting is motivated by both personal and tax incentives.
- Most people donate to favorite charities because they believe in the charity's mission and they gain a sense of satisfaction by contributing to that mission.
- Congress encourages charitable giving through tax legislation that can minimize your income and estate taxes.
- Charitable planning involves selecting gift property and a charitable structure that will target your income, estate planning, and donative needs.

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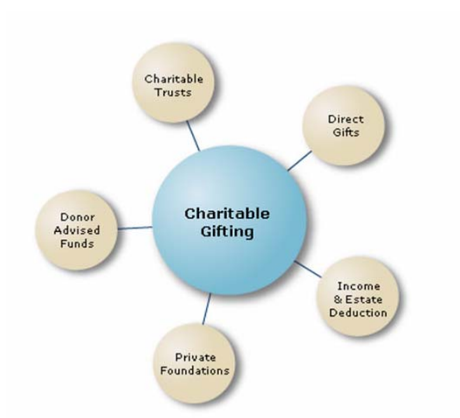
Charitable Gifting



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Who Needs Estate Planning?

- Everyone can benefit from estate planning. If you don't create your own plan, the state has created one for you. But the state does not take into account your and your family's special needs.
- You do not need to be wealthy to have an estate plan. Planning may be more important for smaller and mid-size estates because a misstep may have a greater impact on your heirs.

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Estate Planning Rules of Thumb

- Everyone should have three estate planning documents:
  - A power of attorney
  - A living will
  - A will

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Determining Your Estate Planning Needs

- Before determining any course of action, it is important to consider:
  - How and when you want your wealth to benefit your heirs and your community
  - Your current and future cash flow
  - Your estate's ability to pay taxes and other expenses
  - Who will manage your assets and your health care if you are disabled

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Does Your Current Plan Reflect Your Goals and Needs?

- Do the ownership and beneficiary designations of your property and retirement plans reflect your estate plan?
- Are you taking advantage of the annual gift tax exclusion?
- Are you currently gifting to charities?
- Are your revocable trusts funded?

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Does Your Current Plan Reflect Your Goals and Needs?

- Will your life insurance be received estate tax-free?
- Will your retirement plans force unnecessary income taxes for your heirs?
- Is your business succession plan equitable?
- Do your heirs understand your estate plan?

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Estate Planning Wrap-Up

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Questions and Answers

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