BRIAN D. LOWDER, INC.

QUARTERLY NEWSLETTER

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FINANCIAL MARKET OVERVIEW

If you had just returned from a 3-month vacation in an isolated camp in the high Sierra Mountains and called your financial advisor for an update on the financial markets and the current value of your investment portfolio, the response would sound something like this: "Well, I'm sorry to inform you that several tragedies have occurred while you were away. Back-to-back devastating hurricanes have slammed into the gulf states leaving hundreds of thousands of people homeless and the city of New Orleans is completely vacant and under water. The price of oil and has spiked to nearly $70 per barrel from just over $40 per barrel since January of this year. Alan Greenspan has raised interest rates twice since you departed three months ago, the inflation rate is rising and the local real estate market has stopped dead in its tracks – the average annual appreciation rate has dropped from over 20% to less than 2% from August 2004 through August 2005. As you know, September has historically been a poor month for stock market performance. There's more, but enough with the bad news, how was your trip?"

At this point, the color is leaving your face as you pause and ask the awful question, "What was the percentage change in the value of our investment account"? Your advisor would likely answer, "The average percentage change in value of all of our accounts was somewhere between +3% to 5% during the third quarter." Huh?

The third quarter ended with another one-quarter percent increase in the federal funds rate – the eleventh increase since June 2004. The Federal Funds rate has risen from its lowest level of 1% fifteen months ago to 3.75% today. Almost all stock indexes and mutual fund categories ended the third quarter with modest gains, all major stock indexes were up moderately with only the Dow Jones Industrial Average posting a fractional loss during the third quarter of 2005. In retrospect, the stock market performed quite well. Below are sample returns of various asset classes during the second quarter and year-to-date.

3rd Quarter	**Year-To-Date 2005**	**(includes dividends reinvested)**
+ 3.4%	(0.5%)	**Dow Jones Industrial Average**
+ 3.6%	+ 2.0%	**Standard & Poor's 500 Index**
+ 3.9%	+ 3.9%	**DJ Wilshire 5000 (Broad Market)**
+ 4.5%	+ 3.8%	**Large-company stock-Growth**
+ 3.7%	+ 4.1%	**Large-company stock-Value**
+ 5.8%	+ 6.7%	**Mid-Size Stocks – Growth**
+ 6.7%	+ 7.0%	**Mid-Size Stocks – Value**
+ 5.1%	+ 3.8%	**Small-company stock- Growth**
+ 4.0%	+ 5.1%	**Small-company stock- Value**
+11.7%	+ 12.1%	**International (excludes U.S.)**
+17.2%	+ 23.4%	**Emerging Markets**
+ 1.9%	+ 7.5%	**Real Estate**
+ 0.9%	+ 0.7%	**Short-term U.S. Treasury** ***(includes appreciation)***
(0.6%)	+ 0.8%	**Intermediate U.S. Treasury** ***(includes appreciation)***

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The outlook for the investment markets and the overall economic environment seems confusing. Higher oil prices, continued conflict in Iraq and devastating natural disasters doesn't sound like the ideal environment for positive investment returns. One month investors are optimistic and the following month disappointment reappears.

The only explanation I can offer is one you've heard before. The stock market moves in reaction to thousands of pieces of data, news and trading activity each day. Stock prices certainly react to daily news events, but the overall level and direction of the markets are dictated by the likely or probable outlook of the economic environment in about nine to twelve months. The majority of investors, both professional and individual, do not anticipate a worsening environment one year from today. Yes, after reading the newspapers, it is *possible* that the conflict in Iraq worsens, budget deficits grow larger, interest rates move much higher and oil prices continue climbing until we reach the end of the world sometime in 2007. But, it seems more *probable* to us that the difficult times are already upon us, the easy investment returns are behind us and the future appears to offer moderate growth and the absence of devastating declines or spectacular advances.

ROTH 401(K)S AVAILABLE IN JANUARY 2006

Presently, the Roth IRA is the only tax-free retirement-savings plan available, but income restrictions prevent higher-income earners and individuals in their peak earning years from making contributions. Roth IRA contributions are not tax deductible, but the withdrawals made later during retirement are not subject to state or federal income taxes.

Beginning in January, employers can offer a new Roth 401(k) retirement plan as an alternative to the traditional 401(k) plan. This new plan has similar income tax implications as Roth IRAs – no tax deduction allowed for contributions, but future withdrawals are not subject to federal or state income taxes.

With a traditional 401(k) plan, your contributions are excluded from taxable income (i.e. W-2 wages are reduced by the amount of the contribution to the plan) but when you make withdrawals, the amount is taxed as income. With a Roth 401(k) plan, your contributions do not reduce reported wages (i.e. contributions are still reported as taxable income), but money can be withdrawn from the account tax-free as long as the funds have been held in the Roth 401(k) for at least 5 years and the taxpayer is at least age 59 ½. The best advantage of a Roth 401(k) plan is no limits on how high your reported income is for the year. Highly paid individuals get a fair shot at this tax shelter.

In summary, individuals who contribute to a Roth 401(k) are willing to pay income taxes now on the amount of their contribution(s) in exchange for tax-free withdrawals later on during retirement. Conversely, individuals who contribute to a traditional 401(k) are able to reduce income taxes today based on the contribution amount, but must pay income taxes later on all withdrawals. In both cases, a 10% penalty is assessed on any withdrawals made before age 59 ½.

The *combined* contribution limits for both plans in 2006 is $15,000 for all individuals plus an extra $5,000 ($20,000 total) for individuals who reach age 50 or older in 2006. If your employer offers both plans, this means you can invest the maximum in one type of plan or divide your contributions between them. However, if your employer matches all or a portion of your contributions, all matching amounts must be placed into the traditional 401(k) plan. Lastly, you cannot move assets between the different 401(k) plans, but after you leave your job you can roll Roth 401(k) balances into a Roth IRA and traditional 401(k) funds into a regular IRA.

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If offered a choice, which is the better 401(k) plan? In most circumstances, the Roth 401(k) plan is the better choice. The regular or traditional 401(k) plan is a better choice if two things happen: Your tax rate during retirement is lower than your current tax rate, **and** you do something that practically no one does – invest the tax savings into a separate account. Let's break it down. First, it does seem logical that your income tax rate will be lower during retirement than it is now – after all, you won't have employment income to report. However, the biggest segment of our population – the Baby Boomers, will begin retiring at age 60 or about 100 days from now. Every year thereafter for about 15 years, more big-spenders will be retiring at a time when our budget and trade deficits are growing at an alarming pace. The only way to fix the deficit problem aside from an economic boom is to raise taxes and tighten spending. That's a scary thought. So, assuming taxpayers will be in a lower income tax bracket during retirement may not be a wise assumption.

Second, the tax savings that result from making a traditional 401(k) plan contribution is rarely saved. A taxpayer makes a 401(k) contribution and that contribution is not reported as W-2 wages. Therefore, income tax is not assessed on this amount. That's a tax saving! But most people don't save and invest the "tax savings" – they simply spend it.

On the other hand, the Roth 401(k) contributor paid income taxes on each of her contributions. However, she will receive her withdrawals tax free during retirement, while the traditional 401(k) taxpayer is paying income taxes on every withdrawal during retirement. And since the "tax savings" of the traditional 401(k) taxpayer were not invested along the way, both the Roth 401(k) and traditional 401(k) taxpayers have the same size portfolio at retirement. However, the Roth 401(k) taxpayer receives his withdrawals free of income taxes and therefore is in a better position. Sound confusing?

There are other considerations in this decision. Since Roth 401(k) contributions are not tax deductible, your paycheck will be smaller and your reported taxable income will be higher. The result for some taxpayers could cause a phase-out of tax deductions, child tax care credit or the AMT (Alternative Minimum Tax) exemption. These issues and others are beyond the scope of this newsletter. The important point is to continue making 401(k) contributions to either plan or you might consider splitting your contributions between the two different plans. Maximizing your retirement plan contributions is more important than deciding which type of 401(k) plan is the best choice.

CHECK YOUR CREDIT REPORT FOR ERRORS & IDENTITY THEFT

Each year, you have the right to get one free credit report from each of the three credit bureaus. Unfortunately, it is very easy and common for errors to creep into this compilation of personal data, credit history and public information. Regular checkups are critically important.

Monitoring your credit report is your best line of defense against credit card fraud and identity theft. To get started, go to www.annualcreditreport.com or call 877 322-8228. You will be given a choice of which credit bureau to start with. Be prepared to verify your identity by answering several questions such as the name of your mortgage lender, amount of your monthly payment, who holds your auto loan and previous personal addresses. If you answer incorrectly, you'll be locked out of the online system and must order by mail. Remember to print out a copy or save it on your computer. Lastly, be advised additional detail about your credit score may be purchased for a nominal fee. If you find an error in your report, contact the credit bureau for details on how to correct. Don't wait until you need to apply for credit or refinance your home.

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NEW PRESCRIPTION DRUG BENEFITS FOR MEDICARE BENEFICIARIES

Beginning in the month of October, private insurance companies and the government will be contacting Medicare beneficiaries (retirees) about Medicare's new *voluntary* prescription-drug program that **begins in January 2006**. The sign-up period for new Medicare Part D prescription-drug benefit begins November 15, 2005 and runs through May 15, 2006. However, if you want coverage to begin on January 1, 2006, you must sign up before the end of this year. If you will turn 65 next year or beyond, you will sign up for Part D when you enroll in Medicare.

Starting January 1, 2006, Medicare will begin offering coverage for prescription drugs under a new part of Medicare (Part D) and the government will be mailing a handbook, *Medicare & You 2006* to all eligible participants. The handbook will list the drug plans available in your area. The government has approved and will subsidize these plans, but ***private insurance companies will actually provide the coverage***. Anyone who has Medicare Part A and/or Part B can get Medicare prescription drug coverage (Part D). (Medicare Part A covers hospital and other inpatient services. Part B covers doctor visits and other outpatient services, including durable medical equipment).

There are two types of Medicare private drugs plans (Part D plans):

- **Stand-alone prescription drug plans (PDP).** "Stand-alone" plans *only offer prescription drug coverage*. You can continue to get all your other medical services (such as doctor visits, hospital stays) from traditional Medicare. The estimated monthly cost ranges from $32 to $37 per month with a deductible and some cost-sharing for prescriptions.

- **A Medicare private health plan (like an HMO, PPO or PFFS).** You can join or remain in a Medicare private health plan (Medicare Advantage) that provides *all your Medicare-covered services, including prescription drug coverage.* Bundling all coverage into one policy might save costs, but the downside is that some plans may not include your doctors and hospitals in their networks.

Retirees are going to face many choices as some states (including California) may have up to 40 drug-only insurance plans to choose from. In addition, each plan will have a list of drugs that are cheaper under each of their plans, the lists will be different from plan to plan, and some medications might not be covered at all. These lists (of covered drugs) are called formularies.

The first step when choosing a plan is to list the prescriptions you take now on a regular basis and include the purpose, brand name, generic name, dose and cost per month. Use this list to compare and find out if your medications are on each company's list. Unfortunately, insurance companies can change their formularies (list of covered drugs) as long as they provide 60 days notice.

What should retirees do if they have employer-sponsored drug coverage? In general, most retirees with comprehensive drug coverage from former employer-provided plans should stay with what they have as these plans are often more generous than the Medicare plans will be. The way to determine whether your employer-provided plan is better is to watch for a letter (from the government) coming to you stating whether your employer-provided drug coverage is "creditable" or comparable to Medicare's. If it isn't, you should probably sign up for a Medicare drug plan. Even if the former employer's drug coverage is creditable, it means the government has decided it is at least as good as the Medicare benefit. But that doesn't necessarily mean it's the best choice for you.

Once again, comparisons are necessary to make the right decision. If the employer has high out-of-pocket costs (large deductible and co-

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payments) you might want to consider the Medicare drug plans in your area. Remember, before making any changes to employer-sponsored coverage, it is important to clarify your options with the current plan administrator. Giving up drug coverage may mean you won't be able to get it back or risk losing other valuable medical benefits.

What should retirees do if they have been using a Medicare-approved discount drug card? Retirees should confirm whether they have any credits built up on the card and try to use all remaining credits before they enroll in any Part D drug plans. Once they enroll, they cannot use the old card.

Should I keep my Medigap policy? Millions of seniors have purchased Medigap plans, also known as supplemental policies, to cover Medicare deductibles, some prescription-drug expenses and other costs. Please be advised that once the new Part D drug benefit starts, insurance companies can't sell ***new*** Medigap policies *that cover drugs*. Retirees who already have these policies can keep them, but they might be better off shifting to a Medicare plan. Please note, having Medigap drug coverage *does not* protect people from the penalty (described below) if they decide to sign up for the Medicare drug benefit late. Medigap plans without drug coverage will continue to be sold.

Lastly, delaying the decision whether to enroll in a Part D drug plan can be costly. Seniors need to make their decisions by May 2006 or be forced to wait until the next annual enrollment period which is November 2006. In the meantime, for every month the enrollment is delayed, the premium (monthly cost of coverage) increases by 1%. For example, if a senior who is eligible for Medicare Part D waits one year to enroll, he or she will pay 1% more each month of delay increasing the premium cost 12% for each year thereafter. *This penalty does not apply* to those seniors who have prescription drug benefits through a former employer or union retiree plan, *as long as* those benefits are equal to or better (creditable) to the coverage provided under Part D. In other words, if a retiree already has comparable coverage but decides to switch over to Medicare Part D sometime later, no penalties will be assessed.

Contact Us

Brian D. Lowder, Inc.

Brian D. Lowder, CFA, CFP®
Michael Kinnear, MBA, MSFS, CFP®
Clinton Winey, MBA, CFP®
Remette Martinson
Pamela Priest

Address
12780 High Bluff Drive Suite 100
San Diego, CA 92130

Telephone
(858) 794-6800

Fax
(858) 794-6906

Website
www.bdlowder.com

Email
brian@bdlowder.com
mike@bdlowder.com
clint@bdlowder.com
rm@bdlowder.com
pam@bdlowder.com

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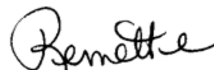
Best regards

Brian Lowder

Clinton Winey

Michael Kinnear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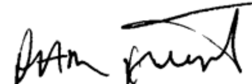
Pam Priest