

Too Diversified? Not Diversified Enough? When is Diversification Just Right?

You've probably heard TV commentators refer to something called the "Goldilocks economy." It's an economy that's not too hot (moving so high and fast it's poised for a huge fall) or too cold (meandering with no immediate upside) but just right, which means somewhere comfortably in the middle.

There's also a "Goldilocks" factor to proper diversification, though it depends as much on your own personal factors as well as what's happening in the market. Proper diversification happens when you consider the time it will take to reach your specific financial goals based on your age, risk tolerance and assets, and then use that information to make investment choices that counterbalance each other no matter how hot or cold markets get.

There are plenty of ready-made solutions to diversification on the market. You may have heard about target date mutual funds and target risk mutual funds. Target date funds allow an investor to select a fund that corresponds their current age and their year of their planned retirement, and the portfolio will adjust automatically to fit that profile. A target risk fund isn't tied to a specific retirement date but how much risk you're willing to take on – these funds have been around for years and are directed toward investors who can describe their investment philosophy in a word – aggressive, moderate or conservative.

Is ready-made the right way to go? If it's the difference between saving and not saving, yes. But chances are you can do better with personalized advice. A CERTIFIED FINANCIAL PLANNER™ professional can take a closer look at what you really want to do with your money and help you design a diversified portfolio tailored to the way all of the following factors apply to you:

- Your specific financial goals
- Timeframe
- Current assets
- Risk tolerance

How do you know if you need help diversifying a portfolio? Here are some questions to ask yourself:

How do you view your retirement? Today's retirement ideal is changing. If your health picture is good and you're not quite willing to give up work altogether, it's wise to design a plan for a full- or part-time post-retirement career or extensive volunteer work. Can a product that automatically changes your diversification picture every year foresee the investment performance and tax issues that may surface in a working retirement? Not likely.

How would your portfolio weather a serious market downturn? Based on your retirement scenario, are you diversified enough in various asset classes (stocks, bonds, cash or real estate) that the overall value of your retirement portfolio wouldn't severely suffer if one or more of your asset classes suffered a serious downturn? When the market bubble popped in 2000, many investors who were invested heavily in growth stocks suffered because they didn't have other investments positioned for gains or at least stability against those losing value.

Are you adequately covered for worst-case scenarios? Granted, Social Security and Medicare – for as long as they last – will always offer some degree of safety net to retirees, but have you also planned savings and investments outside your retirement fund to cover possible health and unexpected financial emergencies in your post-retirement years? A planner can help you check your investment diversification as the years go by to make sure you are prepared for any eventuality.

Will you know how to keep fees under control? Targeted investment plans automatically re-allocate your holdings based on your investment timeframe, but they generally charge higher fees to do so. Self-managed portfolios of individual stocks might become fairly costly if you trade often. To get a properly diversified portfolio of investments, you need to understand the various fees and costs associated with them and whether there might be more affordable alternatives. Fees should be reasonable in relation to overall performance.

How will you avoid over-diversification? First of all, what is over-diversification? It doesn't pertain to the overall amount invested, but how that money is allocated. Simply, money spread across too many different kinds of investments can mean that a positive gain in any single one won't make that much of a difference in the overall value of your portfolio. Are there rules of thumb? Some believe you shouldn't own more than 15-20 individual stocks or mutual funds in more than four or five asset classes that don't overlap each other.

When hiring a planner, it's always appropriate to ask what his or her approach to diversification would be relative to your particular situation and why.

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Planning a Move? Make It a Smart One From a Money Perspective

Residential real estate in America is far from a recovery to pre-2005 levels in most markets. But if you're thinking about a move when the economy and real estate markets improve, you've got an important ally on your side right now – time.

Beyond the purchase or sale of a home, people don't think about all the financial planning details that should go into a move. Some of the smartest money decisions can happen before you select a home, or even a city or neighborhood. Such research can be done relatively easily from these resources and many more on destination cities:

- Local newspapers and city magazines, either in print or online
- The destination city's Web site
- The destination state's department of revenue and education Web sites
- Online real estate listings
- Your tax and financial planning professionals
- Utility websites and the American Automobile Association (AAA) daily fuel gauge report (<http://www.fuelgauge.com/sbsavg.asp>) to determine your energy spending

Here are some ideas to incorporate into a money plan for a future move:

Study the destination's cost of living: Most people have a fantasy spot or two in their minds of where they'd like to live. For most, it's all about the weather, the culture and creature comforts. But before you relocate, drill deeper. For starters, onsite or online, it makes sense to study not only rental rates or home prices, but property, local and state tax rates, food and entertainment prices, and given current energy concerns, utility and gasoline prices and whether public transit options are available. And don't just focus on current numbers – read ahead to see where these costs are going.

Check ahead on insurance: It's particularly important for self-employed business people to check on what individual and group health insurance may cost in a new destination. But everyone should check on what rental, home, auto and even new life insurance policies may cost. On the home or rental insurance front, it's also a good idea to see if there are restrictions on any pets or property insurable in that area. If you are changing employers, you should make sure your former employer keeps you on your health plan through COBRA (Consolidated Omnibus Budget Reconciliation Act) so you will have coverage until you move on to new insurance. It's also a good idea to make sure that insurance will cover you adequately in that new city or state.

If it's a job transfer, compare benefits: If you have the option of moving to a new city through a transfer at your employer – or if you expect that to be the only option for keeping your job – it makes sense to do some casual investigation in your human resources department right now to check moving allowances, whether all current benefits will extend to a new location, or whether there are any improvements over your current benefits after the move.

Talk to your tax professional: If you are moving more than 50 miles farther from your former home than your old main job location was from your former home, your move will meet one of the main requirements that will allow you to deduct expenses related to that move. You'll want to talk to your tax professional about that and other major tax issues you'll face at your new location, and you may also want to go over deductibility of items you may want to give to charity so you don't have to move them.

Check critical amenities: It's important to know the quality of an area's schools (this is important for all taxpayers, not just those with school-aged children), crime rates in various neighborhoods (and if they're improving or deteriorating) and the quality of nearby health facilities. Having access to the best private or public services where you live is always smart money thinking.

Plan your financial services before your move: The financial professionals and services you currently use may or may not be available to you if you move to a new city or state. If you are working with a longtime tax professional, tax attorney or financial planner, see if you can still work with them after you move. There might be a host of reasons those relationships may need to end. Various professionals may need to be licensed or certified to serve clients who live in other states or countries. The time to look for a talented referral is now, not on moving day.

Pack smart: All critical financial data and papers should be organized and ordered so you don't lose key documents. Carry them with you if that's possible. At the same time, if you keep financial data on your computer, do a thorough backup that you can keep in a safe place with all your key documents and files.

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Thinking About Working Abroad? You're Going to Need Detailed Planning

The globalization of the world economy has led employees of all ages to consider working abroad. But as much as overseas employment is a major personal and professional decision, it's also a huge financial consideration.

First of all, just because you're skipping off to work full-time in another country, don't think you've cut ties with Uncle Sam. As long as you are an American citizen or a resident alien, you will be responsible for filing a return with the Internal Revenue Service every year, and the paperwork can be complex.

That's why if you are considering an overseas opportunity, it's a very good idea to meet with a tax professional who has experience working with Americans working abroad to handle their foreign, federal and state tax matters. It's also a good idea to work with a CERTIFIED FINANCIAL PLANNER™ professional with similar experience to keep up with your spending, saving and retirement planning issues while you're focusing on your career in foreign lands.

Here is some general information to consider if you're considering an overseas move:

You may qualify for a tax break: The Internal Revenue Service has rules that prevent U.S. citizens from paying taxes in the United States and the foreign country where the citizen works. The foreign earned income exclusion addresses the most common risk of double taxation on wages and self-employment income earned abroad.

To qualify for the exclusion, there are three tests: you must be able to prove you work in a foreign country, you must be able to prove that foreign income, and you must pass either the "bona fide" or the "physical presence" residency tests in that foreign country. The "bona fide" test is passed if you live in the country for at least one uninterrupted tax year (between January 1-December 31). The physical presence test is usually the one people pick – it's passed if the taxpayer was present in that foreign country for any 330 days which don't have to be consecutive or part of a particular tax year. For tax year 2008, the amount of the exclusion will be \$87,600.

If you work in a country that charges no income tax, the exclusion becomes particularly valuable because once the first \$87,600 is removed the first dollar of taxable income is taxed in the lowest income bracket. That means there's a chance you might pay less tax if you had stayed home and earned all that money in the United States.

You may also qualify for separate housing cost tax credits and deductions that will bring down that overall income deduction.

Meanwhile, the foreign tax credit covers the amount of foreign tax paid on income subject to U.S. taxes after accounting for all your exclusions and deductions.

Why sometimes it's better to work for someone else: Some countries have special laws that govern taxation for self-employed individuals that may result in U.S. expatriates paying special taxes for the self-employed – there may be reciprocal agreements between countries governing such agreements. Self-employed people in particular should seek out help on how best to manage taxes and overall spending issues abroad.

Meanwhile, many multinationals create “tax equalization” packages for employees working abroad that charges employees the tax amounts they would have paid in the states while picking up the entire tax bill in the U.S. and the overseas location. It's important to make sure, however, that employers are figuring in all the potential taxes you'd pay for benefits like an overseas housing and school allowance, relocation fees and other perks related to expatriate work.

Even if you're working for one of the most employee-friendly companies on the planet, it's important that you bring your own tax advisor into the process to make sure all your bases are covered.

Get advice on record-keeping: If you've been lackluster at keeping track of your financial activities while working in the States, it's time to change your ways. Get advice from your tax and financial planning experts on the best ways to sort and keep financial records either physically or on computer. And since you might be tempted to ask more questions about the care and feeding of your finances while you're abroad, ask your professionals what it will cost to have these discussions and whether there's anyone you can talk to where you're going.

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