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While we are a little late with our August newsletter, we still felt it was important to send it out. The topics addressed in this month's newsletter provide great guidance on subjects that are important to many of you such as important changes to the home office deduction and updates on personal credit.

*As we have stated in the past, **a Client referral is one of the best compliments a professional services firm can receive** . If you know of anyone that would benefit from the expertise we offer please let us know. There are not many small firms such as ours where you get the experience level, knowledge and understanding*

As your ***CPA Firm*** & ***Trusted Advisor*** , we welcome your comments and encourage you to let us know if there are other topics you would like to hear about. Please visit our Website , Like Us on Facebook , or follow us on Twitter and LinkedIn to get updates and access a wealth of important information.

August 2013

When Is Market Volatility Most Dangerous?

Though a market downturn generally isn't fun for most people, its timing can have a greater impact on some investors than on others. For example, a market downturn can have greater significance for retirees than for those who are still accumulating assets. And it has the most impact if it occurs early in retirement. Why? Because of something known as the "sequence of returns"--basically, the order in which events affect a portfolio.

For retirees, timing is everything

To understand the importance of the sequence of returns, let's look at two hypothetical retirees, both of whom start retirement with a $200,000 portfolio. Each year on January 1, Jim withdraws $10,000 for living expenses; so does Pam. During the first 10 years, each earns an average annualized 6% return (though the actual yearly returns fluctuate), and both experience a 3-year bear market. With the same average annual returns, the same withdrawals, and the same bear market, both should end up with the same balance, right?

They don't, and here's why: though both portfolios earned the same annual returns, the order in which those returns were received was reversed. The 3-year decline hit Jim in the first 3 years; Pam went through the bear market at the end of her 10 years.

	Jim's Return	Jim's Balance	Pam's Return	Pam's Balance
Year 1	-5%	$180,500	15%	$218,500
Year 2	-2%	$167,090	12%	$233,520
Year 3	-1%	$155,519	14%	$254,813
Year 4	3%	$149,885	8%	$264,398
Year 5	7%	$149,677	9%	$277,294
Year 6	9%	$152,247	7%	$286,004
Year 7	8%	$153,627	3%	$284,284
Year 8	14%	$163,735	-1%	$271,541
Year 9	12%	$172,183	-2%	$256,311
Year 10	15%	$186,511	-5%	$233,995

As you can see, Pam's account balance at the end of 10 years is more than $47,000 higher than Jim's. That means that even if both portfolios earned no return at all in the future, Pam would be able to continue to withdraw her $10,000 a year for almost 5 years longer than Jim. This is a hypothetical example for illustrative purposes only, of course, and doesn't represent the results of any actual investment, but it demonstrates the timing challenge new retirees can face.

Weighing income and longevity

If you're in or near retirement, you have to think both short-term and long-term. You need to consider not only your own longevity, but also whether your portfolio will last as long as you do. To do that requires balancing portfolio longevity with the need for immediate income.

The math involved in the sequence of returns dictates that if you're either withdrawing money from your portfolio or about to start, you'll want to pay especially close attention to the level of risk you face. After the 2008 market crash, many individual investors fled equities and invested instead in bonds. Along with actions by the Federal Reserve, that demand helped push interest rates to all-time lows.

However, when interest rates begin to rise, investors will face falling bond prices. And yet if you avoid both stocks and bonds entirely, current super-low interest rates might not provide enough income. Achieving the right combination of safety, income, and growth is one of the key tasks of retirement investing.

Seeking balance

You obviously can't control the timing of a market downturn, but you might have some control over its long-term impact on your portfolio. If your timing is flexible and you're unlucky enough to get hit with a downturn at the wrong time, you might consider postponing retirement until the worst has passed. Any additional earnings obviously will help rebuild your portfolio, while postponing withdrawals might help soften any impact from an unfortunate sequence of returns. And reducing withdrawal amounts, especially in the early retirement years, also could help your portfolio heal more quickly.

Home Office Deduction Rules Get a Remodel

If you run a business out of your home, it's important to understand the associated federal income tax deductions that you might be entitled to. That's especially true this year, with new rules that make it easier than ever for some to claim a deduction.

What's a home office?

A home office is generally a room in your home, a portion of a room in your home, or a separate building next to your home (such as a converted garage or barn) that you use to conduct business activities. In order to deduct associated expenses, though, certain requirements apply.

Basic requirements

Your home office must be used regularly and exclusively as your principal place of business, or as a place where you meet or deal with clients, patients, or customers, in the normal course of your business. If you have a business outside your home, but conduct substantial administrative and management tasks for your business at home (e.g., billing clients, keeping books and records) you may qualify, provided that you have no other fixed location where you could conduct these activities.

The portion of your home used for business purposes (i.e., your home office) must be used *exclusively* for business purposes. You will not qualify for a deduction if the portion of your home is also used for personal purposes. There are two exceptions, however, relating to the storage of inventory and product samples, and the use of part of your home as a day-care facility.

Separate structures

What if your home office is in a separate unattached structure next to your home, like a shed or garage? In this case, the office doesn't have to be your principal place of business, or a place where you regularly meet with clients. However, to qualify for the deduction, you must use that office regularly and exclusively in connection with your trade or business.

Employees can claim deduction

If you're an employee and use part of your home for business, you may qualify for the home office deduction. You'd have to meet all other requirements (i.e., your home office must be used regularly and exclusively as your *principal* place of business), and in addition, your home office must be for the convenience of your employer. You also can't have an arrangement in which you're renting that portion of your home to your employer.

Regular method of determining allowable deduction

Under this method, you determine your actual expenses relating to your home office. Deductible expenses can include both direct expenses and indirect expenses. Direct expenses are costs that apply only to your home office, like the cost of a second telephone line used exclusively for your business.

Indirect expenses are costs that benefit your entire home. Only the business portion of your indirect expenses is deductible as part of the home office deduction (even if you don't claim a home office deduction, some of these indirect expenses may be deductible as itemized deductions on Schedule A of Form 1040). Some examples of indirect costs include rent, deductible mortgage interest, real estate taxes, and homeowners insurance. The business percentage of your home is determined by dividing the area exclusively used for business by the total area of the home. For example, if your home is 2,000 square feet and your home office is 200 square feet, your business percentage is 10% (200 divided by 2,000). In such a case, if you rent your home, you can deduct 10% of your rent as part of your home office deduction.

New simplified option available

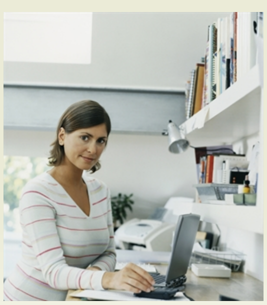
Starting in 2013, a new simplified option is available for calculating the home office deduction. Under this method, instead of determining and allocating actual expenses, you calculate the home office deduction by simply multiplying the square footage of the home office by $5. There's a cap of 300 square feet, so the maximum deduction available under this method is $1,500. You can't use this method if you are an employee with a home office and receive advances, allowances, or reimbursements for expenses related to the business use of your home under an expense or reimbursement allowance with your employer.

Each year, you can choose whether to use the regular or simplified method of calculating the deduction. If you use the simplified method in one year, and in a later year use the regular method, special rules will apply in calculating your allowable depreciation deduction. Additionally, if you are carrying forward an unused deduction from a prior year (because your business deduction exceeded your business income in a prior year), you will not be able to claim the deduction in any year in which you use the simplified method--you'll have to wait for the next year you use the regular method to claim the unused deduction.

Certain limits apply

If the gross income from your business equals or exceeds your regular business expenses, all of the qualifying expenses for the business use of your home can be deducted. But if your gross income is less than your total business expenses, deductions for the business use of your home may be limited. If you use the regular method for calculating the deduction, you can carry forward the unused deduction. If you use the new, simplified option, however, you'll be unable to carry forward the unused deduction.

For additional information, see IRS Revenue Procedure 2013-13.



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Should You Buy or Lease Your Next Vehicle?

After declining dramatically a few years ago, auto sales are up, leasing offers are back, and incentives and deals abound. So if you're in the market for a new vehicle, should you buy it or lease it? To decide, you'll need to consider how each option fits into your lifestyle and your budget. This chart shows some points to compare.

Buying or leasing tips

- *Shop wisely. Advertised deals may be too good to be true once you read the fine print. To qualify for the deal, you may need to meet certain requirements, or pay more money up front.*
- *To get the best deal, be prepared to negotiate the price of the vehicle and the terms of any loan or lease offer.*
- *Read any contract you're asked to sign, and make sure you understand any terms or conditions.*
- *Calculate both the short-term and long-term costs associated with each option.*

	Buying considerations	**Leasing considerations**
Ownership	When the vehicle is paid for, it's yours. You can keep it as long as you want, and any retained value (equity) is yours to keep.	You don't own the car--the leasing company does. You must return the vehicle at the end of the lease or choose to buy it at a predetermined residual value; you have no equity.
Monthly payments	You will have a monthly payment if you finance it; the payment will vary based on the amount financed, the interest rate, and the loan term.	When comparing similar vehicles with equal costs, the monthly payment for a lease is typically significantly lower than a loan payment. This may enable you to drive a more expensive vehicle.
Mileage	Drive as many miles as you want; a vehicle with higher mileage, though, may be worth less when you trade in or sell your vehicle.	Your lease will spell out how many miles you can drive before excess mileage charges apply (typical mileage limits range from 12,000 to 15,000).
Maintenance	When you sell your vehicle, condition matters, so you may receive less if it hasn't been well maintained. As your vehicle ages, repair bills may be greater, something you generally won't encounter if you lease.	You generally have to service the vehicle according to the manufacturer's recommendations. You'll also need to return your vehicle with normal wear and tear (according to the leasing company's definition), so you may be charged for dents and scratches that seem insignificant.
Up-front costs	These may include the total negotiated cost of the vehicle (or a down payment on that cost), taxes, title, and insurance.	Inception fees may include an acquisition fee, a capitalized cost reduction amount (down payment), security deposit, first month's payment, taxes, and title fees.
Value	You'll need to consider resale value. All vehicles depreciate, but some depreciate faster than others. If you decide to trade in or sell the vehicle, any value left will be money in your pocket, so it may pay off to choose a vehicle that holds its value.	A vehicle that holds its value is generally less expensive to lease because your payment is based on the predicted depreciation. And because you're returning it at the end of the lease, you don't need to worry about owning a depreciating asset.
Insurance	If your vehicle is financed, the lien holder may require you to carry a certain amount of insurance; otherwise, the amount of insurance you'll need will depend on personal factors and state insurance requirements.	You'll be required to carry a certain amount of insurance, sometimes more than if you bought the vehicle. Many leases require GAP insurance that covers the difference between an insurance payout and the vehicle's value if your vehicle is stolen or totaled. GAP insurance may be included in the lease.
The end of the road	You may want to sell or trade in the vehicle, but the timing is up to you. If you want, you can keep the vehicle for many years, or sell it whenever you need the cash.	At the end of the lease, you must return the vehicle or opt to buy it according to the lease terms. Returning the vehicle early may be an option, but it's likely you'll pay a hefty fee to do so. If you still need a vehicle, you'll need to start the leasing (or buying) process all over.

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I recently incurred a significant amount of credit card debt. How should I begin to pay it off?

The best way to pay off credit card debt is with a single lump-sum payment, which would allow you to get back on solid financial ground quickly, without having to pay additional interest. Sources of funds that can be used for a lump-sum payoff include any substantial windfall, such as an inheritance or employment bonus. However, most individuals find themselves getting into credit card debt due to a lack of funds in the first place, so this may not be an option for everyone.

If you have multiple credit cards that carry outstanding balances, the next best strategy is to prioritize your repayment and systematically pay off your credit card debt. Start by making a list of your credit cards, and prioritizing them according to their interest rates. Send the largest payment possible to the card with the highest interest rate. Be sure to continue making payments on your other cards until the card with the highest interest rate is paid off. You can then focus your repayment efforts on the card with the next highest interest rate, and so on, until they're all paid off.

Another option is to transfer your balances to a card that carries a lower interest rate. Balance transfers can allow you to reduce interest fees and pay more against your existing balance. One of the dangers with this method lies in the fact that an excessive amount of balance transfers can end up having a negative impact on your credit score.

If you own a home and have enough equity, you may be able to use a home equity loan to pay off your credit card debt. The interest on home equity loans is typically lower than credit card interest rates and is usually tax deductible. While home equity loans can be an effective way to pay off debt, you'll need to be careful not to incur additional debt, particularly if you end up having an available line of credit.

Finally, whenever you're attempting to tackle a significant amount of credit card debt, always be sure to pay more than the required minimum payments. Otherwise, you'll continue to carry the bulk of your balance forward for many years without actually reducing your overall balance. You can refer to your monthly statement for more detailed information on the impact minimum payments will have on your credit card balance.

I recently came across an error on my credit report. Is there any way I can fix it?

Good credit is an important part of your overall financial well-being. It can impact everything from the interest rates you'll pay to being a prerequisite for employment. As a result, you'll want to try to fix any errors on your credit report and have them removed as soon as possible.

Your first step should be to contact the credit reporting agency in writing to indicate that you are disputing the information contained on your credit report. The credit reporting agency usually has 30 days to complete an investigation of the disputed information. Once the credit reporting agency investigation is complete, they must provide you with written results of their investigation.

If, during its investigation, the credit reporting agency confirms that your credit report does contain errors, the information on your report either must be removed or corrected.

If the investigation does not resolve the issue, you still have a couple of options. First, you can try to mitigate the disputed information by adding a 100-word consumer statement to your credit bureau file. Even though consumer statements are often dismissed or ignored by potential creditors, it can at least provide you with a chance to tell your side of the story. You can also try to resolve the issue with the creditor that submitted the inaccurate information in the first place. The creditor will be obligated to investigate the disputed issue and notify you of its findings.

If you believe that the error is the result of identity theft, you may need to take additional steps to try and resolve the issue, such as placing a fraud alert or security freeze on your credit report. You can visit the Federal Trade Commission (FTC) website at www.ftc.gov for more information on the various identity theft protections that might be available to you.

Finally, due to the amount of paperwork and steps involved, fixing a credit report error can often be a time-consuming and emotionally draining process. If at any time you believe that your credit reporting rights are being violated, you can file a complaint with the Consumer Financial Protection Bureau (CFPB) at www.consumerfinance.gov.

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