

**YOUR GUIDE TO OBAMACARE** p 59

# Kiplinger's

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FINANCE**

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new annuity choices and  
investment advice that  
may surprise you.** p 46

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**7 Big-Company  
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Money Manager** p 28

**Ditch Cable!  
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OCTOBER 2013

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\*Based on two surveys: The PLANSponsor magazine 2013 Recordkeeping Survey (© Asset International, Inc.), based on defined-contribution plan assets administered and number of participants of recordkeepers, as of 12/31/2012; and Cerulli Associates' *The Cerulli Edge*<sup>®</sup>—Retirement Edition, second-quarter 2013 based on an industry survey of firms reporting total IRA assets administered for Q1 2013.

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KIMBERLY LANKFORD  
[askkim@kiplinger.com](mailto:askkim@kiplinger.com)



### HOLD YOUR BONDS

"Cash in Hand" columnist Jeffrey Kosnett tells income investors not to overreact to this year's struggles in the fixed-income market. Good news: The worst, he says, appears to be over.

► [kiplinger.com/links/holdbonds](http://kiplinger.com/links/holdbonds)

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# Do you have what it takes to finish strong?

Investing for retirement means steering clear of bumps in the road ahead. Yet most people underestimate the income they need to maintain their standard of living in retirement. What's more, retirement for today's investors will last longer than for prior generations.

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# Janet Bodnar

FROM THE EDITOR

## Our Take on Obamacare

**H**ere at Kiplinger, we specialize in giving readers advice they can act on. So we have avoided the wrangling over Obamacare till we could see how the new law will actually affect you. The state exchanges for people who don't have group coverage are scheduled to be up and running during open enrollment starting in October, and right on cue you'll find our story on page 59. Unfortunately, it's still not clear exactly how things will shake out. So I asked contributing editor Kim Lankford, our insurance specialist, for her perspective on some of the unknowns and potential surprises.

Kim notes that each state has its own exchange. Although many exchanges will be run by the federal government, she says, "I don't think people realize how much insurers and premiums will vary from state to state, and even from region to region."

Similarly, insurance premiums will be approved on a state-by-state basis. For instance, says Kim, "it's no surprise" that some New York residents will see rates decline. New York has some of the highest premiums in the country because insurers have been required to charge everyone the same rate, regardless of whether they were young and healthy or older and sick. But in other states, residents could see premiums rise significantly.

For years, Kim has advised readers that individual health insurance was very affordable for most healthy young people—as little as \$100 a month (see "Ask Kim," Sept.). Yet many young

adults still didn't bother to buy it. Now their premiums could be much higher, says Kim, so it's not clear whether they'll sign up.

Subsidies could ease the burden. But with no mechanisms yet in place to verify who qualifies for coverage on the exchanges or who's eligible for premium subsidies, the exchanges will be taking applicants at their word. So it's possible that some people could try to game the system, or that tax issues could arise if they're later found ineligible and have to pay the money back.

People who don't qualify for subsidies probably don't realize that they can still buy coverage directly from insurers outside the exchanges, says Kim. Direct-sold policies give insurers more flexibility to offer smaller networks of health care providers, which can mean lower premiums if you don't mind the restrictions. "There's a whole extra marketplace that people may overlook," says Kim.

Kim has recommended for many years that people who don't have group coverage shop for policies on eHealthInsurance.com, which already functions as a de facto national marketplace. Come to think of it, says Kim, "a lot of money is being spent to teach people to do what we've been writing about all along."

**Retirement advice.** Every year I take our summer interns out to lunch and ask what they've learned during their time with us. I'm always surprised that one lesson rises to the top: the importance of saving early for retirement. "It's



**"A lot of money is being spent to teach people to do what we've been writing about all along."**

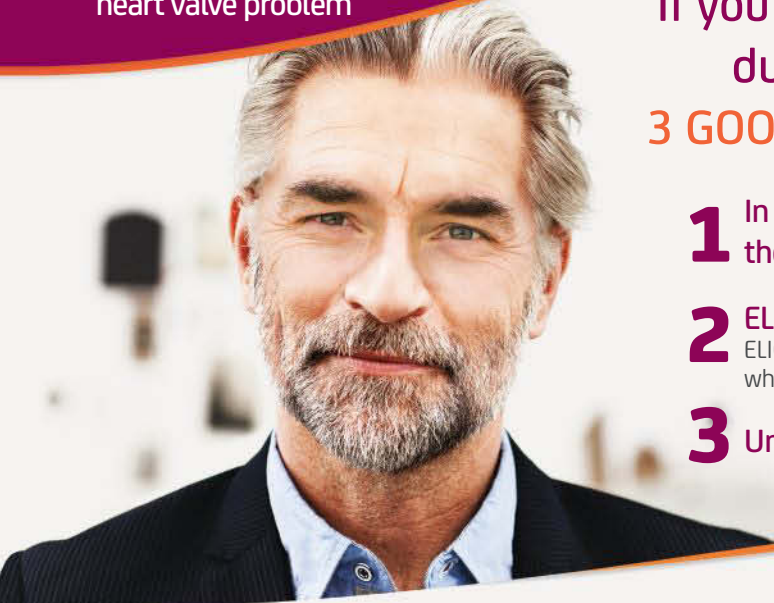
crucial for me to know what to do as a 21-year-old leaving college and getting a real job," says intern Mary Clare Fischer, now a senior at the University of Maryland. "And it's crucial to know what to do later on, when I start tapping various accounts."

For readers in that situation, I recommend our cover story, on page 46. And if you have not yet claimed Social Security benefits, I recommend that on September 23 at 6 P.M. eastern time you log on to a free webcast presented by William Meyer, our partner in Kiplinger's Social Security Solutions. Sponsored by TD Ameritrade, the 45-minute webcast will tell you how to get the most out of Social Security (register at [kiplinger.com/go/social](http://kiplinger.com/go/social)).

And one more piece of advice courtesy of Mary Clare: "Read *Kiplinger's*."

JANET BODNAR, EDITOR  
FOLLOW JANET'S UPDATES AT [WWW.TWITTER.COM/JANETBODNAR](http://WWW.TWITTER.COM/JANETBODNAR).

For people with Atrial Fibrillation (AFib) not caused by a heart valve problem



## If you live with a higher risk of stroke due to AFib, ELIQUIS gives you 3 GOOD REASONS to rethink warfarin.

- 1** In a clinical trial, ELIQUIS® (apixaban) reduced the risk of stroke better than warfarin.
- 2** ELIQUIS also had less major bleeding than warfarin. ELIQUIS and other blood thinners increase the risk of bleeding which can be serious, and rarely may lead to death.
- 3** Unlike warfarin, there's no routine blood testing.

**Ask your doctor if ELIQUIS is right for you.**

ELIQUIS is a prescription medicine used to reduce the risk of stroke and blood clots in people who have atrial fibrillation, a type of irregular heartbeat, not caused by a heart valve problem.

### IMPORTANT SAFETY INFORMATION:

- **Do not stop taking ELIQUIS without talking to the doctor who prescribed it for you. Stopping ELIQUIS increases your risk of having a stroke.** ELIQUIS may need to be stopped, prior to surgery or a medical or dental procedure. Your doctor will tell you when you should stop taking ELIQUIS and when you may start taking it again. If you have to stop taking ELIQUIS, your doctor may prescribe another medicine to help prevent a blood clot from forming.
- **ELIQUIS can cause bleeding which can be serious, and rarely may lead to death.** This is because ELIQUIS is a blood thinner medicine that reduces blood clotting.
- **You may have a higher risk of bleeding if you take ELIQUIS and take other medicines that increase your risk of bleeding, such as aspirin, NSAIDs, warfarin (COUMADIN®), heparin, SSRIs or SNRIs, and other blood thinners. Tell your doctor about all medicines, vitamins and supplements you take.** While taking ELIQUIS, you may bruise more easily and it may take longer than usual for any bleeding to stop.
- **Get medical help right away if you have any of these signs or symptoms of bleeding:**
  - unexpected bleeding, or bleeding that lasts a long time, such as unusual bleeding from the gums; nosebleeds that happen often, or menstrual or vaginal bleeding that is heavier than normal
  - bleeding that is severe or you cannot control
  - red, pink, or brown urine; red or black stools (looks like tar)
  - coughing up or vomiting blood or vomit that looks like coffee grounds
  - unexpected pain, swelling, or joint pain; headaches, feeling dizzy or weak
- **ELIQUIS is not for patients with artificial heart valves.**
- **Do not take ELIQUIS if you currently have certain types of abnormal bleeding or have had a serious allergic reaction to ELIQUIS.**
- **Before you take ELIQUIS, tell your doctor if you have:** kidney or liver problems, any other medical condition, or ever had bleeding problems. Tell your doctor if you are pregnant or breastfeeding, or plan to become pregnant or breastfeed.
- **Take ELIQUIS exactly as prescribed by your doctor and refill your prescription before you run out.**
- **Possible serious side effects include bleeding or a reaction to ELIQUIS itself.** A reaction to ELIQUIS can cause hives, rash, itching, and possibly trouble breathing. Get medical help right away if you have sudden chest pain or chest tightness, have sudden swelling of your face or tongue, have trouble breathing, wheezing, or feeling dizzy or faint.

*You are encouraged to report negative side effects of prescription drugs to the FDA. Visit [www.fda.gov/medwatch](http://www.fda.gov/medwatch), or call 1-800-FDA-1088.*

Please see additional Important Product Information on the adjacent page.

**Visit [ELIQUIS.COM](http://ELIQUIS.COM) or call 1-855-ELIQUIS**

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# IMPORTANT FACTS

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The information below does not take the place of talking with your healthcare professional. Only your healthcare professional knows the specifics of your condition and how ELIQUIS® may fit into your overall therapy. Talk to your healthcare professional if you have any questions about ELIQUIS (pronounced ELL eh kwiss).

## What is the most important information I should know about ELIQUIS (apixaban)?

**Do not stop taking ELIQUIS without talking to the doctor who prescribed it for you. Stopping ELIQUIS increases your risk of having a stroke.** ELIQUIS may need to be stopped, prior to surgery or a medical or dental procedure. Your doctor will tell you when you should stop taking ELIQUIS and when you may start taking it again. If you have to stop taking ELIQUIS, your doctor may prescribe another medicine to help prevent a blood clot from forming.

**ELIQUIS can cause bleeding** which can be serious, and rarely may lead to death. This is because ELIQUIS is a blood thinner medicine that reduces blood clotting.

**You may have a higher risk of bleeding if you take ELIQUIS and** take other medicines that increase your risk of bleeding, such as aspirin, nonsteroidal anti-inflammatory drugs (called NSAIDs), warfarin (COUMADIN®), heparin, selective serotonin reuptake inhibitors (SSRIs) or serotonin norepinephrine reuptake inhibitors (SNRIs), and other medicines to help prevent or treat blood clots.

Tell your doctor if you take any of these medicines. Ask your doctor or pharmacist if you are not sure if your medicine is one listed above.

## While taking ELIQUIS:

- you may bruise more easily
- it may take longer than usual for any bleeding to stop

## Call your doctor or get medical help right away if you have any of these signs or symptoms of bleeding when taking ELIQUIS:

- unexpected bleeding, or bleeding that lasts a long time, such as:
  - unusual bleeding from the gums
  - nosebleeds that happen often
  - menstrual bleeding or vaginal bleeding that is heavier than normal
- bleeding that is severe or you cannot control
- red, pink, or brown urine
- red or black stools (looks like tar)
- cough up blood or blood clots

- vomit blood or your vomit looks like coffee grounds
- unexpected pain, swelling, or joint pain
- headaches, feeling dizzy or weak

**ELIQUIS (apixaban) is not for patients with artificial heart valves.**

## What is ELIQUIS?

ELIQUIS is a prescription medicine used to reduce the risk of stroke and blood clots in people who have atrial fibrillation.

It is not known if ELIQUIS is safe and effective in children.

## Who should not take ELIQUIS?

### Do not take ELIQUIS if you:

- currently have certain types of abnormal bleeding
- have had a serious allergic reaction to ELIQUIS. Ask your doctor if you are not sure

## What should I tell my doctor before taking ELIQUIS?

### Before you take ELIQUIS, tell your doctor if you:

- have kidney or liver problems
- have any other medical condition
- have ever had bleeding problems
- are pregnant or plan to become pregnant. It is not known if ELIQUIS will harm your unborn baby
- are breastfeeding or plan to breastfeed. It is not known if ELIQUIS passes into your breast milk. You and your doctor should decide if you will take ELIQUIS or breastfeed. You should not do both

Tell all of your doctors and dentists that you are taking ELIQUIS. They should talk to the doctor who prescribed ELIQUIS for you, before you have any surgery, medical or dental procedure.

**Tell your doctor about all the medicines you take, including** prescription and over-the-counter medicines, vitamins, and herbal supplements. Some of your other medicines may affect the way ELIQUIS works. Certain medicines may increase your risk of bleeding or stroke when taken with ELIQUIS.

## How should I take ELIQUIS (apixaban)?

**Take ELIQUIS exactly as prescribed by your doctor.** Take ELIQUIS twice every day with or without food, and do not change your dose or stop taking it unless your doctor tells you to. If you miss a dose of ELIQUIS, take it as soon as you remember, and do not take more than one dose at the same time. **Do not run out of ELIQUIS. Refill your prescription before you run out. Stopping ELIQUIS may increase your risk of having a stroke.**

## What are the possible side effects of ELIQUIS?

- See “What is the most important information I should know about ELIQUIS?”
- ELIQUIS can cause a skin rash or severe allergic reaction. Call your doctor or get medical help right away if you have any of the following symptoms:
  - chest pain or tightness
  - swelling of your face or tongue
  - trouble breathing or wheezing
  - feeling dizzy or faint

Tell your doctor if you have any side effect that bothers you or that does not go away.

These are not all of the possible side effects of ELIQUIS. For more information, ask your doctor or pharmacist.

Call your doctor for medical advice about side effects. You may report side effects to FDA at 1-800-FDA-1088.

This is a brief summary of the most important information about ELIQUIS. For more information, talk with your doctor or pharmacist, call 1-855-ELIQUIS (1-855-354-7847), or go to [www.ELIQUIS.com](http://www.ELIQUIS.com).

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## Helping Adult Kids

My wife and I were in our sixties when I received an unexpected and unexpectedly large raise ("From the Editor," Aug.). A significant portion of my paycheck was already going into savings. What were we to do with the sudden increase in income? The solution was to offer our three children allowances of \$100 per week. Each child was to manage the money as an emergency fund to cover unexpected expenses or to pursue an occupation that he or she was passionate about. My elder daughter appears to have used it as an emergency/retirement fund. My son appears to have used it

as a cushion for starting a photography business. My younger daughter seems to have invested the money and hired a financial ad-

### Q READER POLL

#### How much do you plan to save for retirement?

12% \$250,000 or less

12% \$250,000 to \$499,999

27% \$500,000 to \$999,999

49% \$1 million or more

To learn more about how to stretch your retirement savings, turn to page 46.

viser instead of using it to pursue her acting career.

**MERTON CAMPBELL  
CROCKETT  
THOUSAND OAKS, CAL.**

**The expat life.** A slight clarification about Panama's currency. The U.S. dollar is the official paper currency of Panama, and all establishments accept the dollar ("Retire Where You Want," Aug.). Panama mints its own coins (Panamanian balboas), which are identical in size and shape to U.S. coins, and are interchangeable with them.

**BILL MCABEE  
KEYSTONE, COLO.**

Some Medicare Advantage plans will cover health care outside the U.S. As a matter of fact, my plan covers all emergency care worldwide.

**ROBERT J. CATANZARO  
STATEN ISLAND, N.Y.**

**Chill out.** Thank you, Knight Kiplinger, for a dose of reality on today's overheating home market ("My Point of View," Aug.). Where I live, the carpetbaggers have descended with suitcases of cash and begun flipping houses. One recent article glowingly pointed out that total renovations are completed in two weeks' time. I have a master's degree in sustainable interior design. Never have I completed a quality renovation in two weeks' time. Can you imagine what will happen to securitized and collateralized loans when the plumbing starts leaking and the lawsuits pile up?

**MARIE MINNICH  
PALM DESERT, CAL.**

## ONLINE CHATTER

**OUR UPDATE ON FEDERAL** student loans drew these comments ("5 New Rules on Student Loans," Aug.).

"Maybe \$40,000 in student loans for journalism is not such a great idea. Loan awards need to be prioritized for STEM [science, technology, engineering and mathematics] degrees."

"Students need to be very careful when taking out loans. Pick a major that makes sense in the long run. Do whatever you can to minimize college costs. (Can't afford a pricey college? Go to a more affordable one.) Maximize grants and scholarships. Stay at home if you can. And borrow only what you absolutely must."

"It makes good sense to understand how much you'll be required to pay each month once the repayment period starts. 'Know before you owe,' as the Consumer Financial Protection Bureau says."

### ● CORRECTION

*WisdomTree Japan Hedged Equity fund invests in stocks of Japanese firms with a market value of at least \$100 million ("ETF Spotlight," Aug.). ■*

## > LETTERS TO THE EDITOR

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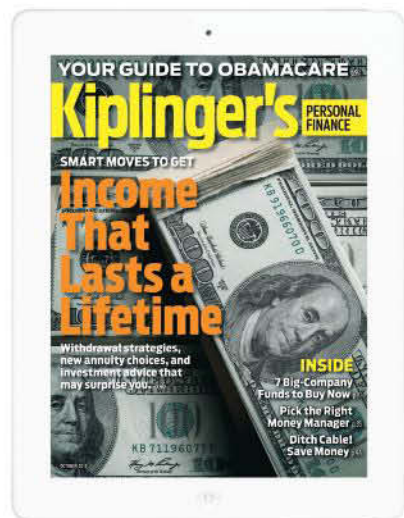
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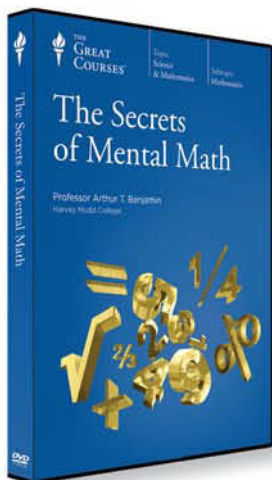


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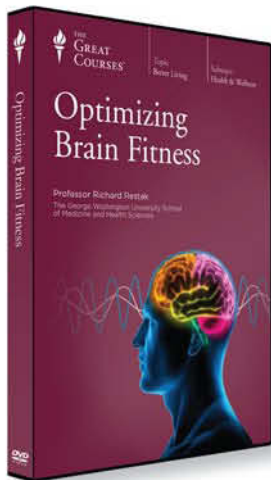


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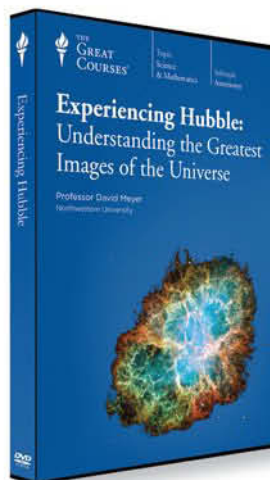
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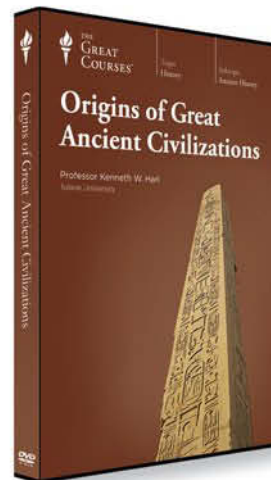
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## AHEAD



## TOPIC A

## DETROIT'S LESSON FOR PUBLIC PENSIONS

**Don't count on getting what you were promised. Start saving on your own.**

### FEW HAVE A BIGGER STAKE IN

Detroit's financial struggles than the employees who made a deal to teach, fight fires or push papers in the municipal building in return for a pension. As the city navigates a bankruptcy filing, workers and retirees worry about "significant cuts" in benefits called for by the city's emergency

manager, who cites a \$3.5 billion funding shortfall, and about the likely restructuring of retirement plans.

The courts will decide how Detroit's pensioners fare. But the debacle should serve as a warning to public workers everywhere: Don't pin your hopes for retirement security on an old-style pension without

saving on your own. "It's a wake-up call," says financial planner Alan Hewitt, a retired Los Angeles firefighter who himself receives a pension.

City bankruptcies are rare. Only 14 cities, towns or counties have filed for bankruptcy protection since 2008, reports *Governing.com*. Resulting pension cuts are even rarer, but they do occur. Ask the residents of Prichard, Ala., where retirees have experienced dramatic benefit reductions (unlike private pensions, public pensions are not backed by the Pension Benefit Guaranty Corp.). An analysis in 2012 of 126 state

and local pension plans by the Center for Retirement Research at Boston College found that the plans on average had just 73% of the funds needed to cover promised benefits—a \$1 trillion shortfall.

States and municipalities are taking steps to put pension funding back on track. Since 2009, 48 states have revised their plans. Changes include raising age and tenure requirements for new hires, requiring all workers to contribute more to their retirement savings, and cutting cost-of-living increases, even for those already retired. Some plans are adding 401(k)-style savings

options to less-generous traditional pensions. Others have become cash-balance plans, in which each worker gets an account (managed by the employer, with a guaranteed minimum return) and, upon retirement, receives an annuity based on the balance.

Funding levels are improving, thanks to reforms and stock market gains. But state and local workers aren't home-free, especially because 30% of them are not covered by Social Security. "Relying solely on your employer is never a good move," says financial planner Jacob Kuebler, in Champaign, Ill., who works with state university employees.

If you can contribute to a supplemental savings plan, such as a 403(b) or 457(b), do so. Given a choice between a savings plan and a pension (or how much to contribute to each), consider that with most pensions, workers employed the longest receive the greatest benefit. So-called defined-contribution savings plans, however, are yours to take with you if you change jobs, and many offer enticements, such as generous matches and shorter vesting periods.

If you're not offered a savings plan outside a traditional pension, set up your own individual retirement account—even if you don't qualify for tax-deductible contributions. Kuebler tells clients to aim for savings equal to 15% of income, which means that if the state requires you to contribute, say, 8% toward a pension, you should sock away another 7% elsewhere.

## INTERVIEW

## ROBO-SIGNING STRIKES AGAIN

**Banks and debt collectors may have illegally sued credit card borrowers.**

*Bill Bartmann is a consumer advocate and president of CFS 2, a debt-collection agency.*

**You say there's a scandal brewing in the credit card industry.**

**What's going on?** It's essentially the same "robo-signing" problem that took place in the mortgage arena a few years ago, when lenders signed off on foreclosure documents without sufficiently reviewing them. Customers are being sued, typically by people who buy delinquent credit card debt from the bank. But because the collection agency frequently relies on incomplete information from the banks when signing off on an affidavit, it may sue an innocent person who has the same name as the debtor. Or it may sue someone for debts that have expired under the statute of limitations or have been discharged in bankruptcy.

**Why is this coming to a head now?** Thirteen state attorneys general allege

that banks, including Bank of America, JPMorgan Chase, Citigroup and Wells Fargo, sold loans to debt buyers with sloppy practices. Separately, the California attorney general filed suit against Chase for debt-collection abuses against as many as 100,000 customers. The Office of the Comptroller of the Currency is also investigating Chase. For the past two years, the Consumer Financial Protection Bureau has been

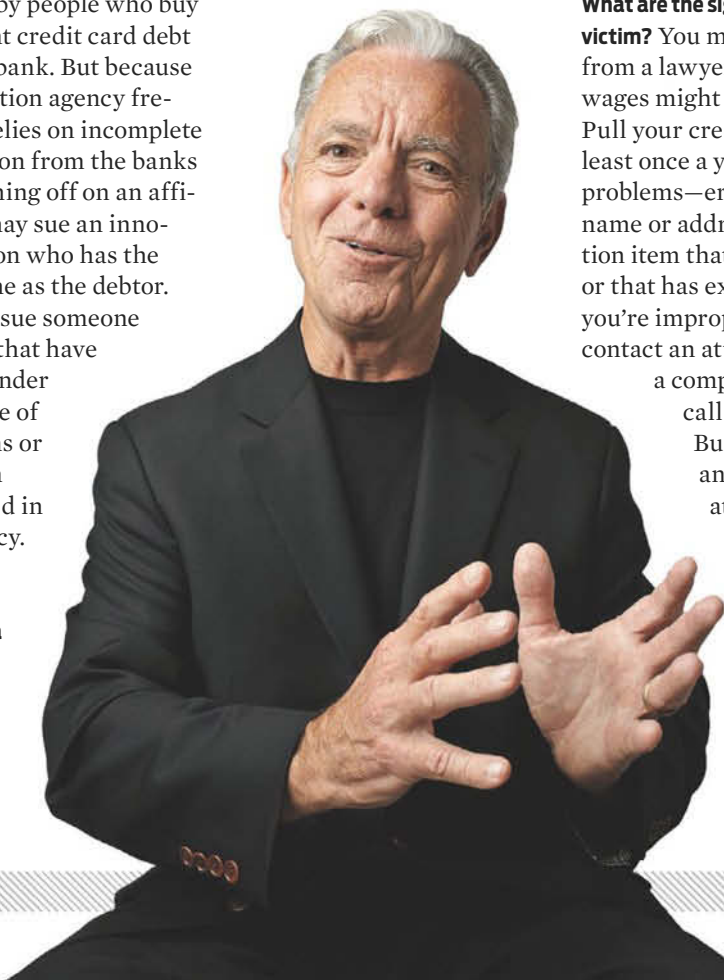
collecting data on this issue. I've never seen a problem attacked by so many groups simultaneously. It's a big deal, and it'll hit the banks' bottom line.

**How many people might be affected?** Judging by the volume of lawsuits and reports on how many of them rely on flawed information, I think the number of customers affected could reach the tens of millions.

**How could so many faulty documents find their way into lawsuits?** It has become easier and less expensive for lawyers to sue thousands of people at once. Thus debt collectors found that they could afford to sue all of their debtors, even those with small balances.

**What are the signs that you're a victim?** You may get a letter from a lawyer or your wages might be garnished. Pull your credit reports at least once a year to spot problems—errors in your name or address, a collection item that you don't owe or that has expired. If you're improperly sued, contact an attorney. To file a complaint, you can call the Better Business Bureau and your state attorney general's consumer protection office. Or submit a debt-collection complaint on the CFPB's Web site.

**LISA GERSTNER**







#### BORROWING

## GET YOUR OWN ANGEL

Find a lender via a social network site and repay a cut of your income later.

**WHEN NATHAN SHARP** TOOK out a loan to launch his price-tracking site, Nifti.com, he didn't agree to pay back principal plus interest. Rather, he's paying 2.5% of his salary for ten years to backers he met through the money-lending platform Upstart. The arrangement includes guidance from his sponsors. "It made sense from a financial and mentorship perspective," says the Boston-based Sharp.

Borrow now and repay a cut of your income later: It's a new trend as student debt overwhelms starting salaries. Borrowers with Upstart pay up to 7% of their income for a decade, capped at five times the original loan amount. If their salary falls below \$30,000, they get a pass, with skipped years added to the repayment term.

Upstart, based in Palo

Alto, Cal., is one of several such platforms. States are getting into the act, too. Oregon's Pay It Forward, Pay It Back is slated to start in 2015. In exchange for paying no tuition or fees, graduates of state schools will pay a proposed 3% of income for 24 years. California and Pennsylvania are considering similar plans.

Such loans sound affordable, but as income grows, they can cost a lot more than traditional student or other loans. "Borrowers aren't going to starve because of these loans," says Jonathan Frutkin, CEO of Cricca Funding, a crowd-funding consulting firm. "But they may hinder saving for vacation, buying a house or putting away money for retirement." A better bet: Focus on affordable college options in the first place.

**SUSANNAH SNIDER**

#### WHAT'S THE DEAL?

## EXPECT HIGHER HEALTH DEDUCTIBLES

But funding a health savings account can help cut your expenses.

**HEALTH SAVINGS ACCOUNTS** have been slow to catch on, with good reason: To qualify, you must enroll in a high-deductible health insurance plan. For 2013, that means a deductible of at least \$1,250 for individual coverage or \$2,500 for a family.

Soon, though, you may not have another choice. Among large and midsize companies, 10% now offer a high-deductible plan as their only option, and 44% are considering moving in that direction in the next three to five years, reports a survey by Aon Hewitt, a human resources consultant.

Employers are turning to these plans in an effort to cut costs, says Aon Hewitt's Maureen Fay. And if you're healthy, they can be cheaper for you, too, because premiums are often lower than those for traditional plans. But if you need medical care, you could be hit with steep out-of-pocket costs.

An HSA allows you to make pretax contributions to a fund designated for those expenses. The money grows tax-deferred, and qualified withdrawals are tax-free. Plus, you can sock away a bundle. In 2013, you can stash up to \$3,250 for individual coverage or up to \$6,450 for family coverage. If you're 55 or older, you can

contribute an additional \$1,000. That's a lot higher than the \$2,500 limit on contributions to a medical flexible spending account. And many employers will kick in to your HSA or match contributions.

As is the case with an FSA, you can use money in your HSA for deductibles, co-payments and other expenses not covered by insurance. But unlike with flex accounts, you don't have to spend all the money by year-end. You may leave the money in your account until you need it, and take it with you if you change jobs.

**SANDRA BLOCK**

#### EXCERPT FROM *The Kiplinger Letter*

## BETTING ON THE NEXT FED CHIEF

Potential successors to Federal Reserve chairman Ben Bernanke include Bernanke deputy Janet Yellen and former Treasury secretary Larry Summers. Both embrace the Fed's role in promoting jobs and a stimulative fiscal policy. But their styles differ markedly. Summers leads through sheer force of will. Yellen is deliberative and inclined toward consensus. Senate confirmation would be harder for Summers. Our money is on Yellen. ([www.kiplingerbiz.com/ahead/fedchief](http://www.kiplingerbiz.com/ahead/fedchief))

## SAVING

# RATES CREEP UP ON FIVE-YEAR CDs

Before you lock in, make sure the early-withdrawal penalty isn't onerous.

**RATES ON CERTIFICATES OF** deposit are finally starting to tick up. Internet banks have recently been offering five-year CDs yielding 2%, compared with an average of 0.69% for all five-year certificates. The average

was about 3% in 2008.

Even marginally higher rates are tempting for yield-starved savers. But if rates are headed higher still, shouldn't you wait to lock in? "It's too early to say whether we've turned a

corner," says Ken Tumin, of DepositAccounts.com. To take advantage of today's higher rates without getting stuck, go for the highest-rate CD with the lowest early-withdrawal penalty.

For example, iGObanking.com is offering a five-year CD yielding 2.05% with an early-withdrawal penalty equal to 180 days' interest. Say you invest a chunk of savings, and after a year you find that market rates are more competitive. Even after the penalty, your yield would be 1.03%. The highest rates for one-year CDs and

online savings accounts are currently about 1%, so you have nothing to lose. If rates stay where they are or drop, you're ahead of the game; if they rise, you can pull the money out and reinvest.

You could make out even better with a reduced penalty, even if the rate is lower. Ally Bank's five-year CD yields 1.5% with a 60-day early-withdrawal penalty. Pull out the money after a year and your yield would be 1.25%. **JESSICA ANDERSON**

## MONEY & ETHICS // KNIGHT KIPLINGER

### Is a CEO-Led Buyout Ethical?



**Q**

I work for a publicly traded company that is struggling, depressing the share price. Now our longtime CEO and several senior executives have joined with a private-equity firm in a bid to take our company private.

They're offering shareholders—including me and a lot of my fellow employees—a modest premium over the recent share price. Our board of directors seems inclined to accept it, but I think the whole thing smells. What do you think?

**A**

I'm with you. The buyout bid might turn out to be a fair price, but the CEO and other brass have a serious conflict of interest. As employees of your company, they have a duty to fix the problems and boost its value for everyone—even if it takes a while and causes some pain and volatility in share price along the way.

But as participants in the buyout bid, they have a contrary interest in paying as little as they can for the stock. They hope to share in a huge gain from engineering a fast turnaround and, ironically, possibly taking the company public again in an IPO. Key question for the CEO: "If you have a great plan for saving our company, why haven't you done it already?"

An even bigger issue is why your board is going along with this. If the members have any guts—and independence from your

CEO—they should demand his resignation (and that of his fellow execs on the buyout team) as a precondition for considering the buyout offer. Then, while interim leadership runs the company, the board should solicit competing bids and also explore a turnaround plan as a public company.

Too many publicly traded companies have been taken private for too low a price in recent years, enriching the new private-equity owners at the expense of the former stockholders, especially small investors. Big institutional shareholders—university endowments, pension funds and mutual funds—should side with the small shareholders and push back against sweetheart deals like this.

HAVE A MONEY-AND-ETHICS QUESTION YOU'D LIKE ANSWERED IN THIS COLUMN? WRITE TO EDITOR IN CHIEF KNIGHT KIPLINGER AT [ETHICS@KIPLINGER.COM](mailto:ETHICS@KIPLINGER.COM).

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## CALENDAR 10/2013



### ▲ TUESDAY, OCTOBER 1

Open enrollment for employer health plans begins. Review changes to your plan and fund flexible spending accounts. Today is also the deadline for the new health insurance exchanges to open. See page 59 for details.

### TUESDAY, OCTOBER 8

As temperatures cool, check the Department of Energy's short-term energy outlook at [www.eia.gov/forecasts/steo](http://www.eia.gov/forecasts/steo) to anticipate and budget for your winter heating bill.

### TUESDAY, OCTOBER 15

Time's up if you requested an extension on your 2012 taxes. If you converted a traditional IRA to a Roth last year, this is your last chance to undo the change.



### THURSDAY, OCTOBER 17

Observe Get Smart About Credit Day by testing your credit-score

smarts at [kiplinger.com/links/creditquiz](http://kiplinger.com/links/creditquiz).

### TUESDAY, OCTOBER 29

Anniversary of the 1929 stock market crash. Huge October drops also occurred in 1987 and 2008. Bargain hunters, note: Historically, the month marks the end of the worst six-month period for stocks. **KAITLIN PITSKER**



### ✧ DEAL OF THE MONTH

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KNIGHT KIPLINGER &gt; My Point of View

## Fewer Buyers for Cheaper Gas

**E**ver since the OPEC oil embargo 40 years ago, U.S. consumers have responded predictably, like rational economic beings, to every big swing in the price of gasoline. When it spiked, we drove fewer miles, switched to fuel-efficient vehicles, used mass transit more. But when the price declined for a long stretch, we went back to our old gas-guzzling ways. Every prediction of the permanent demise of, say, big SUVs, powerful sports cars, and commuting in pickup trucks proved premature.

Will the next time be different? Is it possible that even if gasoline prices decline consumption *won't* go up? I think it's a good bet, and we probably won't have to wait long to find out.

My colleagues in the Kiplinger Business Forecasting Group have made a bold prediction that by 2016 the price of petroleum will fall by 20% to 30% from recent averages of about \$95 a barrel. That would take a gallon of gasoline down by a similar amount, to an average of \$3 a gallon.

That slide will be a boon to consumer budgets, and I have a hunch that this time around drivers won't respond by boosting their use of gasoline. Instead, they'll shift the money into other purchases or savings—unless governments take advantage of the price decline to raise gasoline taxes.

**An oil boom.** High gasoline prices in recent years were the result of tight supplies and surging global demand, especially in fast-growing emerging economies. Conversely, the long price slide we are predicting will be the product of soaring oil production and slowing global demand. Oil production will keep booming—everywhere from Iraq to Canada, and from offshore areas of Africa and South America to our own United States (up 30% just since 2008).

At the same time, oil consumption will continue to decline in the Western nations. In the U.S., we're using 11% less petroleum

today than in 2005, because of urbanization, reduced driving, stricter federal fuel-efficiency standards, a new vogue for small cars and hybrids, and the use of biofuels (ethanol and biodiesel).

Outside of the advanced nations, gasoline use will continue to rise, spurred by a growing middle class wanting to own cars. But governments in countries with fast-growing economies, such as China and India, will reduce their fuel subsidies, impose clean-air rules and perhaps push electric cars, restraining the public thirst for gas.

Overall, the rate of growth in global gasoline demand will slow, and demand will probably be more than matched by higher petroleum production, which will ultimately lead to lower prices.

**Conservation habit.** But today, unlike a decade ago, energy conservation is firmly entrenched in business practices and the public psyche. Not only do we use less for transportation, we also have more-efficient industrial processes, lighting, home appliances and electronics design. The conservation habit is driven not just by a desire to save money, but also by mounting concern about the effects of coal and oil usage on the environment, whether it be local air quality or global climate change.

Natural gas will be abundant and cheap, too. While booming production has its own issues—such as possible air and water pollution from the extraction process—natural gas burns more cleanly than coal and oil in power plants and more cleanly than gasoline and diesel in vehicles (as compressed or liquefied natural gas).

Some possible downsides: Lower prices for gasoline and diesel will lessen the demand for clean biofuels and slow the adoption of all-electric cars, whose high prices continue to turn off car buyers. Yes, there are always trade-offs in free markets. ■

COLUMNIST KNIGHT KIPLINGER IS EDITOR IN CHIEF OF THIS MAGAZINE AND OF THE KIPLINGER LETTER AND KIPLINGER.COM.



**Is it possible that even if gasoline prices decline, consumption *won't* go up? I think it's a good bet."**





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### SAFETY INFORMATION

The most common side effects to Fluzone High-Dose vaccine include pain, swelling, and redness at the injection site; fever, headache, fatigue, and muscle aches. Other side effects may occur. Fluzone High-Dose vaccine should not be given to anyone with a severe allergic reaction to any vaccine component, including eggs or egg products, or to a previous dose of any influenza vaccine.

Tell your doctor if you have ever experienced Guillain-Barré syndrome (severe muscle weakness) after a previous dose of influenza vaccine. If you notice any other problems or symptoms following vaccination, please contact your health care professional immediately. Vaccination with Fluzone High-Dose vaccine may not protect all individuals.

For more information about Fluzone High-Dose vaccine, talk to your health care professional and see complete Patient Information on the adjacent page.

You are encouraged to report negative side effects of prescription drugs to the FDA.  
Visit [www.fda.gov/medwatch](http://www.fda.gov/medwatch) or call 1-800-FDA-1088.

Visit [Fluzone.com/highdose](http://Fluzone.com/highdose) to find out where to get Fluzone High-Dose vaccine and for more information.

**Patient Information Sheet**  
**Fluzone® High-Dose**  
**Influenza Virus Vaccine**

Please read this information sheet before getting Fluzone® High-Dose vaccine. This summary is not intended to take the place of talking with your healthcare provider. If you have questions or would like more information, please talk with your healthcare provider.

**What is Fluzone High-Dose vaccine?**

Fluzone High-Dose is a vaccine that helps protect against influenza illness (flu).

Fluzone High-Dose vaccine is for people 65 years of age and older.

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**Who should not get Fluzone High-Dose vaccine?**

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- ever had a severe allergic reaction after getting any flu vaccine.
- are younger than 65 years of age.

Tell your healthcare provider if you have or have had:

- Guillain-Barré syndrome (severe muscle weakness) after getting a flu vaccine.
- problems with your immune system as the immune response may be diminished.

**How is Fluzone High-Dose vaccine given?**

Fluzone High-Dose vaccine is a shot given into the muscle of the arm.

**What are the possible side effects of Fluzone High-Dose vaccine?**

The most common side effects of Fluzone High-Dose vaccine are:

- soreness, pain and swelling, redness where you got the shot
- muscle ache
- tiredness
- headache

These are not all of the possible side effects of Fluzone High-Dose vaccine. You can ask your healthcare provider for a list of other side effects that is available to healthcare professionals.

Call your healthcare provider for advice about any side effects that concern you. You may report side effects to the Vaccine Adverse Event Reporting System (VAERS) at 1-800-822-7967 or <http://vaers.hhs.gov>.

**What are the ingredients in Fluzone High-Dose vaccine?**

Fluzone High-Dose vaccine contains 3 killed flu virus strains.

Inactive ingredients include formaldehyde and octylphenol ethoxylate.

Manufactured by:  
**Sanofi Pasteur Inc.**  
Swiftwater PA 18370 USA





## GAME PLAN

# “My wife and I are retired and need money from our mutual funds. What will we pay in taxes?”

**DEPENDING ON YOUR INCOME,** you might not have to pay any taxes on your gains. The on-again, off-again 0% long-term capital gains rate for taxpayers in the 10% and 15% tax brackets has been made permanent—and that could benefit a lot of retirees.

In 2013, married couples who file jointly qualify for the 0% capital gains rate if their taxable income is \$72,500 or less; for single filers, the cutoff is \$36,250. Rates for taxpayers in higher brackets range from 15% to 23.8%. Taxable income is what's left after you subtract personal exemptions (worth \$3,900 each in 2013 for you, your spouse and your dependents) plus your standard or itemized deductions from your adjusted gross income. If you don't itemize, note that seniors 65 or older qualify for a larger standard deduction than younger taxpayers (\$14,600 for married couples who are both 65 or older; \$7,600 for single filers).

**Gains must be long-term.** To qualify for preferential treatment, you must hold your shares of stocks or mutual funds more than a year before you sell. Short-term gains (on assets held a year or less) are taxed at your



ordinary income tax rate.

In addition, the shares must be held in taxable accounts. Profits in tax-deferred retirement accounts, such as traditional IRAs, aren't taxed until you take withdrawals, but at that point you'll pay taxes at your ordinary income tax rate (see “Make Your Money Last,” on page 46).

**Your gains could lift you into a higher tax bracket.** When you sell stocks or funds, the profits will increase your taxable income. To pay no taxes on the sale, you'll have to calculate the amount of gains you can take before your income

exceeds the threshold.

Let's say your adjusted gross income (AGI) is \$60,000. Assuming you're both 65 or older, your standard deduction and exemptions will knock your taxable income down to \$37,600. That means you can realize up to \$34,900 in long-term gains—boosting your total taxable income to \$72,500—without paying taxes on the profits. If you take more gains, the 0% rate won't disappear; you'll just owe 15% on gains that exceed \$34,900.

**Capital gains could increase taxes on Social Security benefits.** Your AGI plays a critical

role in how much, if any, of your Social Security benefits will be taxed. If your “provisional income” (your AGI plus 50% of your Social Security benefits plus any tax-free interest) exceeds \$44,000 on a joint return, it's likely that 85% of your benefits will be taxed. As you consider taking profits, remember that capital gains are included in the calculation, even if they're tax-free, because they're part of your AGI, says Mark Luscombe, federal tax analyst for CCH, a leading publisher of tax information. If you have provisional income of \$44,000 or less, less than 85% of your benefits will be taxed. Alternatively, if you're a recent retiree, taking advantage of the 0% tax break to generate tax-free income could enable you to postpone filing for Social Security, which can lead to higher lifetime benefits.

Mark Joseph, a certified financial planner with Sentinel Wealth Management, in Reston, Va., is concerned that many taxpayers who qualify for tax-free gains may not know the break has been made permanent. “It's not often you get a gift from the IRS,” he says. “When you do, you definitely want to open it.” **SANDRA BLOCK**





JAMES K. GLASSMAN &gt; Opening Shot

## Spotting Winners at the Mall

**T**he greatest mutual fund manager of the 20th century once explained a secret to his success: “I began my search for new selections in the usual fashion. I headed straight for my favorite source of investment ideas: the Burlington Mall.”

Those are the words of Peter Lynch, manager of Fidelity Magellan in its heyday, from 1977 to 1990, when the fund racked up an annualized return of 29%—twice the rate of Standard & Poor’s 500-stock index. In a series of books that Lynch wrote after he retired, he said that if individual investors would put the “power of common knowledge” to work, they could gain an edge over professionals. Look around you and, as the subtitle of Lynch’s *One Up on Wall Street* put it, “use what you already know.”

Lynch went on: “I stumble onto the big winner in extracurricular situations, the way you could: Taco Bell, I was impressed with the burrito on a trip to California... Dunkin’ Donuts, I loved the coffee; and recently the revamped Pier 1 Imports, recommended by my wife. In fact, Carolyn is one of my best sources. She’s the one who discovered L’eggs.”

**Egg-cellent.** Carolyn found the pantyhose in an ovoid plastic container, sold in supermarkets, and Peter invested in the manufacturer, Hanes Corp. “It turned out to be a six-bagger,” he wrote, meaning that Lynch’s investment in Hanes sextupled in value before the company was acquired. Lynch essentially was making the same point that Yogi Berra once did: “You can see a lot just by looking.” And nowhere is looking a more powerful tool than in retailing.

We all go to the equivalent of Burlington Mall, which is located in Burlington, Mass., and we all have opinions about where we get good quality, selection and service. We can see which stores have a lot of foot traffic, and which have imaginative merchandising and appealing prices. Do such

attributes translate into strong profits? Not always. But looking is the starting point.

Unfortunately, many of the best retailers, including Neiman Marcus, Toms Shoes and J. Crew, are privately owned. But that leaves scores of smaller retail chains for you to ferret out.

**MICHAEL KORS HOLDINGS (SYMBOL KORS)** is a good example of what you can find. Based in Hong Kong but with corporate offices in New York City, Kors designs men’s and women’s apparel and accessories—high-end but not outrageously priced—and sells them in more than 200 of its own retail stores around the world, as well as in more than 2,000 department stores. If you shop at Kors, you know that the chain’s merchandise has caught fire in recent years—especially its terrific women’s clothes, shoes and logo-heavy handbags. They’re sold in what my fashion-editor daughter calls “stores that are all polished chrome and mirrors, very glam and eye-catching.”

When the company went public on December 15, 2011, Michael Kors, along with private-equity investors, scored a windfall. But Kors remained with the firm as its chief creative officer. John Idol, the highly regarded CEO, stayed, too. The stock has soared, rising from a close of \$24.20 on its first day of trading to \$69 today (all prices are as of August 2). But even if you missed investing in a near-three-bagger, Kors is still attractive. Revenues rose 68% for the fiscal year that ended March 30, and earnings jumped from 78 cents to \$1.97 per share. The stock’s price-earnings ratio, based on estimated profits, is 27—perfectly reasonable for a company growing so fast.

The best retailers, like the best handbags, don’t come cheap, so look to buy on dips.

**LULULEMON ATHLETICA (LULU)**, the Vancouver, Can.-based purveyor of gloriously colored yoga outfits that has a cultlike following, took a huge dive, from \$82 to \$61, during a two-week period in June—after the CEO resigned on the heels of the embarrassing



**As Yogi Berra once said: ‘You can see a lot just by looking.’ And nowhere is looking a more powerful tool than in retailing.”**

# Independent Research Report Reveals:

## Vanguard's Best and Worst Funds

By Dan Wiener

I'm Dan Wiener, founder and editor of *The Independent Adviser for Vanguard Investors*. And if you're like me, and you want to make as much money as possible from your Vanguard investments—I can help.

After years of researching mutual funds and reporting on the financial industry, I can say that Vanguard is the best mutual fund company for individuals to invest in. Vanguard has a long history in offering high-quality funds to the public, without the hype and flash other fund companies find necessary in the competitive mutual fund industry. However, there are things that they don't and won't tell you about. So I'm telling you.

### Best Funds, Worst Funds

Vanguard offers more than 150 mutual funds, which can make choosing the right one a daunting task. And, let's face it, Vanguard's funds come in all forms. Some are very good funds, others average and some are downright toxic!

Knowing which funds to choose... and which to avoid... requires investors to really dig out the facts hidden beneath the hype.

*"Indexing is a great business—but it's a lousy investment!" - Dan Wiener*

### Vanguard Secrets Exposed

**"Indexing is a lie and your trust could cost you plenty... Indexing doesn't work for you. It works for them"**



Dan Wiener

Like any company, Vanguard only accentuates the positive... and buries the negative in a hole so deep it hopes you'll NEVER find it. Their management isn't going to tell you the truth. But I will.

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- The 7 worst mistakes Vanguard investors are making today—and how to avoid them.
- And much more!



Which means that I can—and do—call them like I see them. When I see an underperforming fund, I say so.

Quite simply, you cannot safely hold on to any fund just because "it's a Vanguard fund."

I'm going to reveal Vanguard's worst funds, then I'm going to pull back the curtain and show you Vanguard's best... the funds my regular readers use to make their Vanguard experience 128% more profitable than the average Vanguard investor.

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As the old saying goes, "You can't tell the players without a scorecard." And you'll get a starter scorecard **RIGHT NOW** when you download this free report.

## “Lululemon and Michael Kors have the power of quality and personality, helping them ward off competitors.”

revelation that a fabric used in Lululemon clothes was too easy to see through. The stock, which has recovered to \$73, still isn't cheap, at 36 times estimated earnings for the fiscal year that ends next January. But analysts expect earnings to jump a robust 29% the following year, suggesting that the stock is reasonably priced.

Lululemon and Michael Kors have the power of quality and personality on their side, helping them to ward off competitors and allowing them to charge premium prices. That description also fits **TUMI HOLDINGS (TUMI)**, which sells the luggage it makes through 114 company-owned stores and another 1,700 distribution points in 75 countries. Tumi went public in April 2012 at \$18, soared to \$26.50 on its first day of trading and is now at \$25. The stock's price-earnings ratio—29, based on estimated 2013 earnings—seems reasonable, given that analysts expect earnings to rise by 25% next year.

As for what my own eyes have seen, the world has two great luxury retailers. The first is **HERMÈS INTERNATIONAL (HESAY)**,

which has perfected the art of charging high prices by limiting the supply of hugely desirable items. With 25 stores in the U.S. and another 300 in other countries, the Paris-based company charges \$10,000 and up for its Birkin handbags, and the waiting list for these and other hot products is often more than a year. The company swatted away the 2007–09 recession like a pesky mosquito. Revenues have doubled since 2007, and profits rose from 288 million euros to 740 million euros (about \$979 million).

Hermès's American depositary receipts trade on the pink sheets—the non-Nasdaq over-the-counter market—which means volume is limited. Still, your broker should be able to buy the stock for you, either here or on the bourse in Paris.

A bonus of owning the stock, which goes for \$35, is that you'll receive the most gorgeous annual report you'll ever see.

My second favorite is Loro Piana, the Italian maker of fine scarves, sweaters and other apparel, with 17 stores in the U.S. and hundreds of others around the world, including ten in China. The family that owned Loro Piana sold it in July for \$2.6 billion to **LVMH MOËT HENNESSY LOUIS VUITTON (LVMUY)**, the largest luxury retail conglomerate in the world. LVMH owns the eponymous leather-goods and wine makers, as well as retail brands such as Céline, Thomas Pink, Pucci, the Sephora cosmetics chain and many more. LVMH, whose ADRs trade for \$37, has been accumulating shares of Hermès and now owns nearly 25% of the firm.

Let's go downscale a bit to Zara, whose success is evident once you step into a store. The shoppers who jam its stores can, says my daughter, “get on-trend items that look chic and expensive, with a sleek, tailored European cut, but you're spending an average of less than \$300 for three or four pieces.” Zara is the flagship chain of Spain's **INDUSTRIA DE DISEÑO TEXTIL (IDEXY)**, or Inditex Group, which is also introducing Massimo Dutti, another superb, more upscale chain, to America. Of Zara's 1,763 stores, 44 are in the U.S. Inditex's ADRs trade for \$27.

Another consumer favorite is **DESTINATION MATERNITY (DEST)**, which owns A Pea in the Pod and other chains (a total of 606 stores) for expectant mothers. At \$30, the stock is well priced and delivers an above-average dividend yield of 2.5%. **WILLIAMS-SONOMA (WSM)**, the cream of the kitchen-gadget purveyors, charges premium prices and offers superb service—plus extravagant catalogs and a great Web site. The stock fetches \$61 and yields 2.0%. Also providing a welcoming experience for consumers is **HOME DEPOT (HD)**, the best of the big-box stores. I recommended the stock in the December 2012 issue of *Kiplinger's* at three-fourths its current price of \$80, and I still like it.

Take my advice, or better yet, look for your own winners. Just remember that when you go to the mall, keep your eye out for stock bargains, too. ■

JAMES K. GLASSMAN IS THE FOUNDING EXECUTIVE DIRECTOR OF THE GEORGE W. BUSH INSTITUTE IN DALLAS. HE OWNS NONE OF THE STOCKS MENTIONED.



■ LULULEMON HAS ATTRACTED A CULTLIKE FOLLOWING.



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# Pick the Right Money Manager

We walk you through the choices and tell you how to vet them. **BY NELLIE S. HUANG**

## YOU'RE TIRED OF GOING IT ALONE.

Who do you call? Since 2008, when nearly every investment category suffered declines, people have been clamoring for good advice. Some seek just a little guidance, while others want to leave virtually all of the decision-making to a professional. But with so many money managers offering their services—from banks to brokers to online sites—picking the right one is harder than ever. How do you find an adviser who's right for you and your family? // On the following









## ❖ Saying Goodbye

## Know When to Fire Your Adviser

YOU HIRED YOUR ADVISER TO GET YOU to the financial finish line. If you're not on course to meet your goals, it's time to find a new one. But there are other signs the relationship isn't working. Read on.

■ **YOU'RE OFF TRACK.** Meet face-to-face with your adviser annually for a checkup. Figure out whether you're making progress. Have any goals changed? Is everything moving ahead as planned? Keep in mind that managers will have some bad years—if so, they should explain why they stumbled.

■ **HE SPEAKS IN GOBBLEDYGOOK.**

If you don't understand your adviser, that's a sign he may not be a good fit for you. Says Barry Glassman, a McLean, Va., adviser: "We get clients all the time because their former adviser made them feel dumb or talked over their heads."

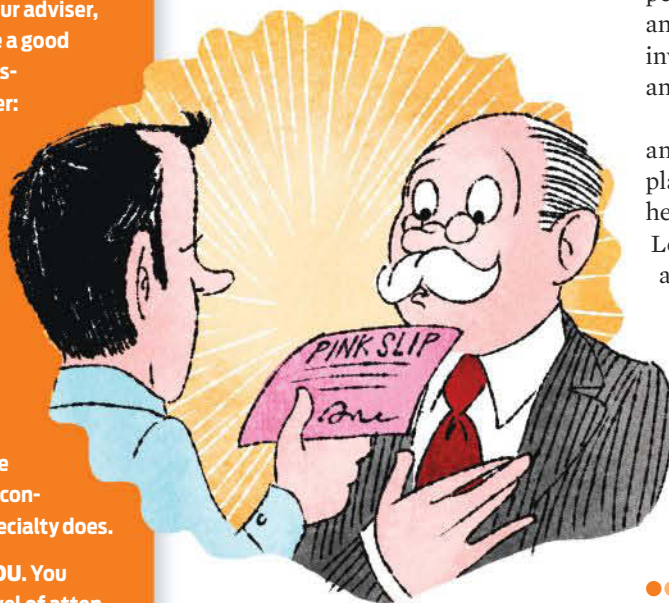
■ **YOUR NEEDS CHANGE.**

Maybe you're getting divorced, or you're getting more interested in income rather than growth. If your adviser's realm of expertise doesn't match your needs, consider finding one whose specialty does.

■ **HE'S JUST NOT INTO YOU.** You should expect a certain level of attention. If you call your adviser and don't hear back within 24 hours—even if it's just to say, "I got your message"—that could be a sign that you're not a priority.

■ **YOU'RE JUST NOT INTO HIM.** Sometimes you simply don't connect. That's a problem, says Michael Prendergast, of Altvest Personal Wealth Management, in New York City. "You have to trust this person. Otherwise, you might not share some things, and then he or she might guide you in the wrong direction."

pages, we'll tell you how. Whether you want a one-time checkup on your financial life or an ongoing relationship with a money manager, we'll lay out the many types of companies you can go to and tell you what kinds of services you can expect, how much you can expect to pay in fees, and the minimum amount you'll need to bring to the table. (You might be surprised to learn that some firms will let you through the door with a pittance.) Then we'll tell you how to drill down within the firms to find a good adviser and what questions to ask when you interview a prospective money manager. We list the kinds of investment managers in order of the minimum amount of money they require, starting with those that demand the least.



●● **ONLINE OUTFITS**

The Web is exploding with sites that offer a variety of services, from tips on stock trades to full-service guidance from a financial planner.

Some Web sites, such as Covestor, TD Ameritrade's thinkorswim and Ditto Trade, allow you to follow or mimic the moves of a manager or a top trader. Other firms, such as Jemstep and FutureAdvisor, offer recommendations on mutual funds and exchange-traded funds based on your

personal circumstances. You plug in data from your brokerage and 401(k) accounts, for example, and the Web services review your account holdings, flagging funds that have high expense ratios or that have lagged the broad market over time.

Some online outfits, including Betterment, Hedgeable and Wealthfront, will manage your money for less than 1% a year. Betterment creates portfolios that contain only ETFs. Plug in your goals (say, "I need \$2 million in 20 years, and I have \$200,000 now") and answer a few risk-tolerance-related questions, and Betterment sets your allocations to get you to your goal. Once a portfolio is established, Betterment periodically rebalances it to keep the allocations in line with the desired percentages. You can start with \$100 and pay 0.35% a year (as long as you invest \$100 a month); invest \$100,000 and you'll pay 0.15% annually.

Some sites, including LearnVest and NestWise, link you to a fee-only planner who comes up with a comprehensive financial and investment plan. LearnVest's services cost \$399 to start and \$19 a month; NestWise charges \$250 upfront and about \$48 a month thereafter. At LearnVest, a budget-starter program costs \$89 to begin and then \$19 a month. The service allows you to connect to a planner, who will help you organize your finances and start an investing program.

●● **FINANCIAL PLANNERS**

Planners do far more than manage your investments. They'll give you advice on saving for retirement and for your kids' college education. They can do estate planning and point you toward accountants who will prepare your taxes. They can discuss the wisdom of trading up to a bigger, more expensive house.

In Monterey, Cal., fee-only planner Gifford Lehman and his three associates at Integrus Wealth Management manage \$165 million for 75 clients. He doesn't require an asset minimum to

# Ask the Right Questions

**YOUR AIM: TO FIND AN ADVISER WHO** shares your values. Use the questions below as a starting point to assess potential advisers. They should ask you some questions, too, about your family, your goals and your risk tolerance. Consider meeting with advisers from a variety of firms—say, a fee-only financial planner, a rep from a national brokerage firm and, if you can afford it, a bank adviser—before settling on one.

**How will you make money from this relationship?** You want a fee-based or fee-only adviser who isn't going to make money by selling you specific products. If an adviser stands to earn a commission by, for example, selling you an insurance product, "there is a conflict of interest," says Gifford Lehman, a Monterey, Cal., fee-only adviser. That doesn't make a broker, who may get paid on trades you make, a bad adviser—you may save money with a commission-based arrangement. And it doesn't mean a fee-only adviser has no conflicts. The key is to ask the question and make sure you feel comfortable with the answer. A reasonable annual fee: 1% of assets or less. But that doesn't include fees on underlying investments, such as mutual fund expenses.

**What standard do you work under: fiduciary or suitability?** Advisers who work under the *fiduciary* standard (typically fee-only financial planners) must act in their clients' best interests at all times. Those who work under a *suitability* standard (typically brokers who earn commissions) have a lower legal standard to fulfill: They must steer you toward investments that are deemed "suitable." Ask every prospective adviser this question, no matter the type of firm. Vanguard advisers, for instance, work under the fiduciary standard. But at Charles Schwab, you may come across some representatives who work under the suitability standard and others who work under the fiduciary standard.

**What's your investment philosophy? How do you manage risk? How do you make buy and sell decisions?** No matter how little you

know about investing, if an adviser can't explain his process to you in a way that you understand, don't hire him. And he should be able to explain what he's doing so that you can decide if you feel comfortable about it. Will he invest your money in individual securities or in funds? What kinds of moves is he considering now, given today's environment, and how will that affect the portfolio?



**What's your ten-year track record, after fees? What risks did you take to get that return? What added to and detracted from returns in each calendar year, especially in 2008?** These are fair questions, but be prepared: Some advisers won't answer them. They'll tell you that the Securities and Exchange Commission has rules about how an adviser can discuss performance. That's true. Some may aggregate account returns. That's what Altfest Personal Wealth Management, in New York City, does for prospective clients. It shows combined results for all accounts, after fees, for every calendar year since 2000 and compares those results with Standard & Poor's 500-stock index and a blended benchmark with 65% in stocks and 35% in bonds.

If a potential adviser balks at giving you an answer, ask for a sample of investments she might put you in today, given your risk tolerance, goals and time horizon. Looking back over the past decade, year by year, how would that portfolio have performed? Past performance is no guarantee of future re-

sults, but seeing how the model performed during strong and weak markets will give you an idea of how comfortable you might be with the adviser's investment strategy.

**Where's my money kept? Who's your accountant?** A good manager won't actually touch your money—he will ask you to send it to another financial firm, such as Charles Schwab, for safekeeping. For instance, Burke Financial Strategies, in Iselin, N.J., uses Raymond James as its custodian. As for the adviser's auditor, if you don't recognize the firm's name, ask why, says Elliot Weissbluth, of HighTower Advisors, a financial-services firm in Chicago.

**Who's on your team? I'd like to meet them.** Some advisers have a team of associates. In some cases, those associates will spend more time with you than the adviser, so it's important to meet them. "If they're not hard-driving people, I would walk," says Edmond Walters, a former adviser in Conshohocken, Pa. You want a staff that's been around for years, too. The reason: continuity, for you and your financial plan. The team may provide the research and analysis behind investment decisions, so frequent changes in personnel could hamper your portfolio.

**What happens if you retire or pass away unexpectedly?** Don't dance around this topic. A good planner will have a ready answer. Ask Barry Glassman, a McLean, Va., adviser, and he'll say: "We have two other client advisers and a robust research team. Moving forward, we will add resources to boost the firm's presence without me."

**Who's your typical client?** You don't want to be the smallest account with any adviser. "You're not going to get enough attention," says John Burke, of Burke Financial Strategies. You also don't want to be the only retiree among a host of young savers. "Matching the client with the right team is important," says Charlie Mueller, of Northern Trust. Some advisers have experience working with business owners; a 35-year-old might relate better to an adviser who's digitally savvy.

become a client, but his fee structure works best for investors with at least \$1 million. He charges between 0.5% and 1% of assets annually, depending on account size. (That fee is on top of any underlying fees for the investments he chooses.) In addition to the usual investing advice, Lehman offers estate and tax planning.

Just because a firm is big doesn't mean it requires a big minimum. Edelman Financial Services, based in Fairfax, Va., has more than 17,000 clients, \$8.5 billion in assets under management and offices in 14 states. Some planners at Edelman will accept accounts of as little as \$75,000, but the fees will be 2% of assets per year, compared with 0.75% annually for an account of \$1 million to \$3 million. Other big firms offer advice in small increments: Garrett Planning Network, a nationwide group of independent planners, can put you in touch with one of its more than 300 fee-only advisers, who charge hourly rates of \$150 to \$240 and can help on an as-needed or ongoing basis. Their target audience is beginners, middle-income earners and do-it-yourselfers. It typically takes eight to 12 hours to devise a comprehensive financial and investment plan.

Then there are brokers-turned-planners. Take John Burke: For 22 years, he was an adviser at big brokerage firms—Merrill Lynch and Morgan Stanley—plying their recommended funds and stocks. Now, he's a financial planner and has his own firm, Burke Financial Strategies, in Iselin, N.J. Instead of making money on commissions, as he once did, he earns a fee based on the assets he manages. And his clients get more than just investment advice—they get comprehensive financial planning, too. The firm is tied to the Raymond James brokerage, but Burke says he doesn't earn commissions on products he sells. His fee is 1% of assets under management annually. He works with clients who have more than \$1 million, but two associates in his office—one is a certified financial planner and the other

is a certified public accountant—take on clients with \$200,000 to \$1 million in assets. "If you exclude people with less than \$1 million, you exclude most of America," says Burke.

#### ●● DISCOUNT BROKERS

Many discount brokerage firms offer tiers of advisory services—and each level typically has its own minimum. But the fees are generally 1% or less per year, depending on the amount of assets you have with the firm. To give you an idea of the array, we'll go through the levels offered at Fidelity, Schwab and Vanguard.

At Fidelity, if you have \$50,000, you can invest in model portfolios at annual fees of 0.25% to 1.7% of assets. But if you want someone to actively manage money for you,

you'll need a minimum of \$200,000 in assets (or \$50,000 in a retirement account), and you'll pay between 0.55% and 1.5% annually, depending on how much money is in your account.

At Schwab, you have to decide how customized you want to get—and how much of the work you're willing to do. On the low-minimum end, \$25,000 gets you a professionally managed portfolio of funds or ETFs. You'll pay 0.2% to 0.9% of assets annually, depending on how much money you

#### ✦ KipTip

## 5 Must-Have Credentials

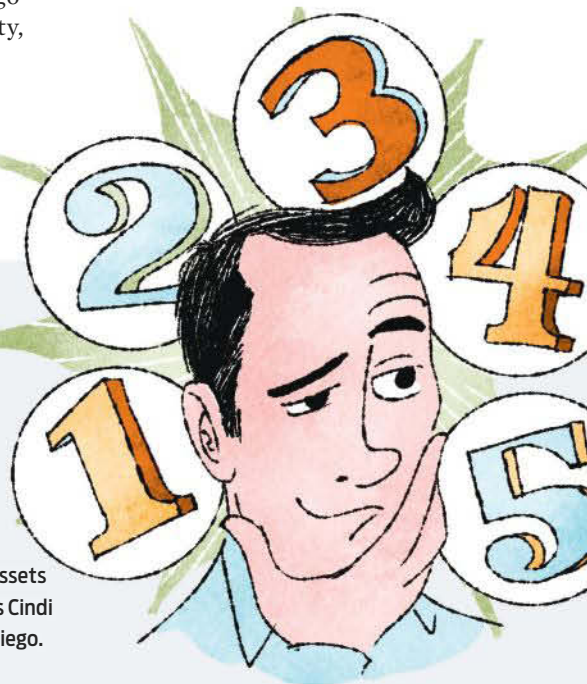
### 1. A DECADE OF THE RIGHT

**EXPERIENCE.** Focus on someone who has experience with clients who have assets and goals that are similar to yours, says Cindi Hill, a former financial planner in San Diego.

**2. A CLEAN RECORD.** Check the disciplinary record to make sure the adviser hasn't had any run-ins with regulators or the law. Advisers who manage more than \$110 million in assets must file Form ADV, a Securities and Exchange Commission document that contains a treasure trove of details about an adviser's business, including a firm's disciplinary record (lower asset thresholds apply in New York and Wyoming). Search by firm name at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov) to find the Form ADV. Smaller firms are regulated by state authorities, but you can check on those firms at the same site. Brokers are regulated by the Financial Industry Regulatory Authority (Finra). Check their records at [www.finra.org/investors/toolscalculators/brokercheck](http://www.finra.org/investors/toolscalculators/brokercheck).

### 3. A TRANSPARENT FEE STRUCTURE.

Some money managers charge a fee for services—a flat fee, an hourly rate or a percentage of assets managed—and are called fee-only advisers. On the other end of the spectrum are commission-based brokers, who make money on the products you buy or sell. But these days, many brokers, such as John Burke, of Burke Financial Group, who is also a certified financial planner affiliated with Raymond James, forgo commissions and charge clients a fee for their services instead. And some fee-only or fee-based advisers may make commissions on some products they sell you. That's why it pays to ask your adviser whenever he recom-





have, plus the fees of the underlying funds. On the high end: \$500,000 gets you into the firm's Private Client program (in which a broker creates a plan and makes recommendations and you carry them out) or the Advisor Network program (you get assigned one member of a prescreened group of independent advisers, with average experience of 20 years).

Vanguard, of course, is known mainly as a purveyor of low-fee mutual funds and ETFs, but it does offer brokerage services as a convenience to its clients. The fund sponsor and brokerage combination also offers a full range of financial advice. It takes \$500,000 in assets to become a client of Vanguard Asset Management Services (the figure can include 401(k) money you have with Vanguard in

mends a new product: Are you being compensated in any way if I buy it?

**4. A CFP, CFA OR CPA DESIGNATION.** There are more than 100 different financial adviser certifications and designations. But only three truly matter. A Certified Financial Planner (CFP) has to complete 18 to 24 months of study, pass a rigorous ten-hour exam, and work for three years as a financial planner or do a two-year apprenticeship with a CFP professional before earning the designation. A Chartered Financial Analyst (CFA) has to pass three six-hour exams and have four years of qualifying work experience to earn the title. A Certified Public Accountant (CPA) knows his or her way around tax planning. Money managers will also have licenses that required them to pass tests.

**5. GOOD REFERENCES.** After an interview, ask the adviser for at least two references from existing clients with profiles similar to yours—and call them! Also ask an adviser for retirement-income plans for current clients or samples of such plans. Are the plans logical, do they make sense, and do you understand them? If not, ask questions until you do. If you're not satisfied, walk away.

an employer-sponsored retirement plan). Being a VAMS client means that you will have an ongoing relationship with a dedicated team of two salaried Vanguard employees—a financial planner and his or her associate. They'll manage your investment portfolio, allocating your money to a mix of Vanguard mutual funds and ETFs, and help you with other aspects of your financial life, including dealing with such issues as when to take Social Security or how much long-term-care insurance you need to buy. Annual fees range from 0.2% to 0.7% of assets.

#### ●● FULL-SERVICE BROKERS

If you have \$10,000, you can open an account at, say, Morgan Stanley, a prototypical full-service brokerage. You'll work with a broker, who, for a fee of up to 2% of assets annually, will provide guidance on mutual fund investments. But to get more-comprehensive advice at Morgan Stanley—from an adviser who offers a range of services, from investing guidance to retirement and estate planning to banking services—you need at least \$100,000. Fees are negotiable and may include commissions on investments, asset-based advisory charges or both. At Merrill Lynch, you'd need at least \$250,000 to access that level of service.

But there is no minimum at Edward Jones, says Danae Domian, an adviser with the St. Louis-based firm, which has 10,000 offices in the U.S.—many of them one-broker shops in small communities. Charges depend on the type of investment products you buy and can include ongoing asset-based fees to manage the portfolio, as well as transaction costs or annual expenses of mutual funds. For that, clients will get advice that “spans 90% of their financial needs,” says Domian, including paying for a child's education, preparing for retirement, generating income in retirement and estate planning.

As is the norm with brokers, the financial advisers at Edward Jones are held to the suitability standard, which means they must recommend

investments that are suitable for their clients. By contrast, most fee-only financial planners have a fiduciary responsibility to their clients. That requires that they act in their client's best interest at all times.

#### ●● BANKS AND TRUST COMPANIES

Technically speaking, a trust company is not a bank. A trust company is authorized to engage in trust powers—that is, you give assets to a legal entity (the trust) and permit a third party (the trust company) to hold and manage the assets on behalf of a beneficiary (you). But some trust companies, including Chicago-based Northern Trust, are also banks and offer full banking services, too. And some large banks, such as BNY Mellon and J.P. Morgan Private Bank, offer investment advice, financial planning and trust services. So does Vanguard, the mutual fund company.

Because the big banks and trust companies cater to wealthy individuals, we lumped them together. The minimum for full-service financial planning and investment advice is high: It's \$2 million at BNY Mellon and Northern Trust, for example. Wells Fargo asks for \$5 million. But Vanguard's minimum for trust services is just \$500,000.

Big bucks can buy you lots of services. At Northern Trust, in exchange for annual management fees of 0.20% to 0.85% (depending on the amount of assets you have with the firm and the kind of trust accounts you set up), plus costs attached to investment products, the firm will act as your fiduciary steward for every aspect of your financial life, making sure that your best interests are always the top priority. Whether it's your investments, your banking needs, natural gas reserves under a plot of land you own in Nebraska, the yacht you want to buy, or the art collection you plan to auction off at Christie's, the firm has your back. Some additional fees may apply for specific services, of course. Being rich, apparently, can cost a fortune. ■



JEREMY J. SIEGEL &gt; Going Long

## What Keeps Me Awake Now

In early 2011, I wrote a column titled “What Keeps Me Awake,” in which I outlined unfavorable events that could derail my bullish outlook for stocks.

Now that the Dow Jones industrial average is more than 3,000 points higher, it’s time to revisit that question.

In 2011, fear of another debt crisis was a major concern for investors. The Lehman Brothers bankruptcy was still fresh in their minds, analyst Meredith Whitney was predicting a municipal bond collapse, and the European debt crisis was heating up. Just six months later, Standard & Poor’s downgraded the credit rating of the U.S., another move that shocked investors.

Fortunately, we have largely navigated through those troubled waters. With households and businesses paying down their debts, and prices for stocks and real estate on the rise, an imminent debt crisis is now unlikely. Despite Detroit’s bankruptcy, no other locality of that size has failed to pay its obligations.

The European debt situation has also improved substantially. And even though the ongoing European recession has been long and deep, there are some signs of recovery. Even the U.S. budget deficit has shown remarkable improvement, with the deficit for the fiscal year that ends September 30 projected to be \$642 billion, down more than 50% from \$1.3 trillion in fiscal 2011.

Nevertheless, there are real deficit problems down the road as retirement demands on Social Security and, especially, Medicare soar. But those problems will not affect today’s bull market.

**Inflation trends.** With the Federal Reserve and other central banks flooding the world with money, many people are concerned that inflation will threaten the U.S. economy. But the Federal Reserve can reduce its balance sheet and absorb the excess reserves it has created by requiring banks to hold higher reserves. I do think that

inflation will trend a bit higher than the Fed’s official 2% target, but inflation in the range of 2% to 4% has not been bad for the stock market in the past.

One risk I did not note earlier was the country’s poor growth in productivity, which measures the output of the economy per hour worked and determines the standard of living. Productivity growth averaged only 0.6% in 2011 and 0.7% in 2012, with the first half of 2013 not much better. That’s considerably below the 2% average the economy has recorded since 1970.

The fall in U.S. educational achievement could be one cause, as well as the long periods of unemployment many Americans have experienced as a result of the recession. I still believe we will emerge from the slow growth in productivity. Nevertheless, it’s crimping corporate profits.

Two additional risks could strike the market at any time. I still worry about a terrorist attack, especially one involving nuclear material. A nuclear strike would be catastrophic not only because of the lives lost but also because of the costly security measures needed to prevent another one.

To terrorism I would add a new concern: a pandemic caused by a pathogen we cannot contain. We have had a number of fleeting epidemics in recent years, and even when the threat is not high, behavior can change radically. Yum Brands, which owns Kentucky Fried Chicken, says that fears of bird flu kept Chinese away from its restaurants in droves earlier this year, even though the disease could not be transmitted through cooked chicken.

I am hopeful that anti-terrorist surveillance as well as the creation of vaccines will mitigate these risks. They may temporarily deflect us from our upward path, but they will not change my forecast of increasing economic growth and higher stock prices. ■

COLUMNIST JEREMY J. SIEGEL IS A PROFESSOR AT THE UNIVERSITY OF PENNSYLVANIA’S WHARTON SCHOOL AND THE AUTHOR OF *STOCKS FOR THE LONG RUN* AND *THE FUTURE FOR INVESTORS*.



**I still believe we will emerge from the slow growth in productivity. Nevertheless, it’s crimping corporate profits.”**

STOCKS»

# Divide and Conquer

Stocks that split tend to deliver solid gains. We look at three that have split and three that might. **BY KATHY KRISTOF**

**THERE ARE NO SURE THINGS IN THE** stock market. But the odds of making a market-beating profit turn in your favor if you buy companies that split their stock.

In theory, a split has no impact on a stock's value. When a company with, say, one million shares outstanding trading for \$100 per share splits two for one, it ends up with two million shares selling for \$50 apiece. The company is still worth \$100 million, and your piece of the firm is worth the same amount after the split. Nor does a split affect a stock's valuation. A stock with a price-earnings ratio of 10 will still sport a P/E of 10 after a split.

Nevertheless, companies that divide their shares tend to outpace the market for nearly three years after a split, says Neil Macneale, editor of the newsletter *2 for 1*. Seventeen years ago, Macneale started investing his retirement account in 30 stocks that had announced splits. He would buy one new stock each month and sell the oldest, reporting his recommendations in his newsletter. From 1996 through 2012, his portfolio beat the market 13 years out of 17. Over the ten-year period that ended July 31, Macneale's picks returned 13% annualized, according to the *Hulbert Financial Digest*, compared with 8% annualized for Standard & Poor's 500-stock index.

Macneale's strategy is to invest in companies that have already announced splits. However, you could also try to handicap which stocks are likely to split by searching for those that have soared beyond \$100—a level that often turns off amateur investors—and then checking to see whether

the firm has a history of splitting its shares. Here's a look at six attractive stocks—three that have already split and three that seem ripe for splitting. Share prices are as of August 2.

## ●● SURE SPLITS

**AMERICAN STATES WATER (AWR)** has been keeping taps flowing in several Southern California communities since 1929. The San Dimas, Cal.-based utility has also been generous to shareholders, increasing dividends every year for the past 59 years. This year, the company, which operates regulated utilities through its Golden State Water unit, also announced a two-for-one split that was set to take effect in September.

Given that much of American States' business is regulated, it's not surprising that analysts expect modest earnings

growth—2% annually over the next few years. But they may be underestimating the company's potential. In May, American States won approval from California regulators to hike rates by an average of 3.4%. And on June 12, it announced that it will buy assets of the Rural Water Co., which brings it into the agriculture-rich San Luis Obispo area. At \$65, the stock sells for 22 times estimated 2013 earnings and yields 2.5%.

Like trains? Then you'll love **WESTINGHOUSE AIR BRAKE TECHNOLOGIES (WAB)**. The Wilmerding, Pa., company, which does business under the name Wabtec, makes and services all sorts of locomotive parts and rail electronics. Profits have doubled over the past two years, as countries around the world have expanded and updated their transportation systems. Wabtec's backlog continues to grow, with Australian rail systems placing large orders this spring. The company recently hiked its dividend by 60%, to 16 cents annually, and split its shares two for one in June. At \$59, the stock sells for 19 times estimated 2013 earnings, a reasonable P/E in light of estimated earnings growth of 15% annually over the next few years.

**FLOWSERVE (FLS)**, which split three for one in June, helps cities everywhere deliver safe drinking water at reasonable prices. Analysts expect the Irving, Tex., maker of pumps, valves and other fluid-handling gear to benefit as both the U.S. and developing nations make infrastructure upgrades. That should lead to annual profit growth of 15% over the next few years.

S&P Capital IQ analyst Stewart





Scharf lauds Flowserve for its “disciplined approach” to deploying capital. The company, he says, aims to return 40% to 50% of average profits over two-year periods to investors in the form of dividends and share buybacks. He expects the stock, recently \$57, to hit \$65 in a year.

#### ●● POTENTIAL SPLITTERS

Many investors worry that the move to cloud computing could disrupt old-line technology suppliers, such as **INTERNATIONAL BUSINESS MACHINES (IBM)**. But Big Blue has transformed itself from a maker of large, mainframe computers to a service company that helps Main Street deal with the rapid pace of technological change. IBM's second-quarter earnings were up 8% from the same period in 2012 and handily beat analysts' earnings expectations (after adjusting for a \$1 billion write-off in the latest quarter related to layoffs). At \$195, the stock trades for 12 times estimated 2013 earnings and is at roughly the same level it was in

1999, right before IBM's last split.

Another century-old industrial giant, **3M (MMM)**, is also within spitting distance of the price at which it last divided its shares. The St. Paul, Minn., company, which makes everything from light bulbs to cleaning supplies,

says it is aiming to hike profits by 9% to 11% per year over the next several years. Analysts think it's got a good chance of hitting that mark. At \$118, the stock sells for 18 times estimated 2013 earnings and yields 2.1%.

**WHIRLPOOL (WHR)** hasn't split since 1986, but its stock price hasn't been this high—and its prospects haven't looked this good—in decades. The appliance maker's earnings more than doubled in the first half of 2013 compared with the first half of 2012. The benefits of previous cost-cutting, coupled with rising demand for its washers, dryers and cooktops thanks to the resurgence of the housing market, also prompted the company to raise its earnings forecast for all of 2013.

Analysts expect profits to rise by an average of 28% annually over the next several years. At \$138, the stock sells for 14 times estimated 2013 earnings and yields 1.8%. Raymond James analyst Sam Darkatsh says he expects Whirlpool shares to hit \$145 within a year (assuming no split). ■

#### ✿ KipTip

## The Scoop on Splits

**FOR INFORMATION ABOUT SPLITS, SEE THESE RESOURCES.**

**NASD publishes a list of upcoming splits at [www.nasdaq.com/markets/upcoming-splits.aspx](http://www.nasdaq.com/markets/upcoming-splits.aspx).**

**The newsletter *2 for 1* ([www.2-for-1.com](http://www.2-for-1.com)) is \$20 a month, but editor Neil Macneale's blog is free.**

**RightLine.net offers a service that predicts which stocks are likely to split. One month's report costs \$60; a year's subscription costs \$500.**

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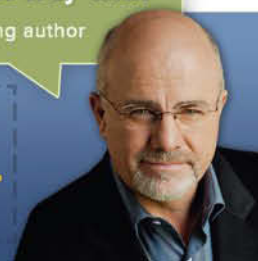


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# Our Seven Favorite Large-Company Funds

Shares of big firms look cheap compared with their small-company brethren. That makes these standouts especially attractive now. **BY NELLIE S. HUANG**

**SMALL COMPANIES HAVE BEEN LEADING** the performance derby lately, and that's one reason it may be time to turn your attention to the big guys. Over the past year, the Russell 2000 index, a measure of small-company stocks, returned 40%, walloping the large-company-oriented Standard & Poor's 500-stock index by 12 percentage points. On the basis of price to expected earnings, large-capitalization stocks are now 20% cheaper than their small-cap brethren, says strategist Ed Yardeni.

Value discrepancies can last for long periods. But in a world with so many real and potential risks, including a dysfunctional Congress, creaky European economies, a slowdown in China and raging conflicts in the Middle East, why not favor the stability of large firms when you can buy their stocks at discounted prices?

With that in mind, we present our list of the best actively managed big-company U.S. stock funds. The funds are listed in alphabetical order (results are through August 2).

## 1. DODGE & COX STOCK

Because of its contrarian approach to stock picking, this venerable value fund can be streaky. During the 2008 disaster, it trailed 91% of its rivals in the large-company value category. But the fund rebounded vigorously in 2009, with

a 31.3% return. That beat 86% of its peers, and it has done well since.

The nine managers who run this \$46 billion fund, a member of the Kiplinger 25, have been on the job an average of 15 years. The one with the longest tenure, John Gunn, arrived in 1977. Since then, Stock has returned an annualized 12.9%, an average of two percentage points per year better

than the S&P 500. Dodge & Cox Stock charges annual fees of 0.52%, an unusually low expense ratio for an actively managed fund.

The managers are highly disciplined. They avoided overvalued tech stocks in the 1990s. In 2000, when the tech bubble burst and the S&P 500 sank 9.1%, Dodge & Cox Stock climbed 16.3%. But the managers' penchant for bargain

prices led them to load up on financial stocks in 2007, which contributed to the fund's 2008 implosion. This apparent inflexibility can try the patience of the fund's shareholders, but over the long term the D&C approach pays off.

## 2. FIDELITY CONTRAFUND

Will Danoff is a model of consistency. A growth-stock specialist, he has run Contrafund since 1990. Over that time, the fund, a member of the Kiplinger 25, delivered an annualized return of 13.2%, an average of 3.4 percentage points per year better than the S&P 500.

Of course, Contrafund has gone through slumps. It lagged the S&P 500 for four straight years from 1994 to 1997, for instance. Around that time, Contra held a hefty 700 stocks. Danoff says he realized that the potential extra returns from the 300 smallest positions weren't big enough to justify holding them in the portfolio. So he trimmed the number of companies down to 400. At last

■ FIDELITY CONTRAFUND'S WILL DANOFF FAVORS GROWING COMPANIES.



report, the fund owned 327 stocks.

Perhaps the biggest knock on Contra today is its gargantuan size: The fund holds \$94 billion in assets. That could make it difficult for Danoff to manage the fund efficiently (see “When to Dump a Fund,” Sept.).

### 3. MAIRS & POWER GROWTH

Fund managers Bill Frels and Mark Henneman love Minnesota. They have invested nearly two-thirds of the fund’s \$3.3 billion in assets in firms that are based in their home state, and the bet has paid off handsomely. Including the first seven months of 2013, their fund, another member of the Kiplinger 25, has outpaced the average large-company growth fund in five of the past six calendar years.

Frels, who joined the fund in 1999, and Henneman, who arrived in 2006, look for well-managed companies with growing businesses that are trading at attractive prices. The average market value of the fund’s holdings is \$17 billion, but the managers can invest in companies of any size. Among the 46 firms in the portfolio, some are large (for example, Johnson & Johnson, with a market capitalization of \$254 billion) and some are small (such as NVE Corp., a firm with a \$237 million market cap that uses nanotechnology to store and transmit data).

### 4. PRIMECAP ODYSSEY GROWTH & 5. PRIMECAP ODYSSEY STOCK

We like funds with low expense ratios and modest minimum investment requirements, and both of these funds fit the bill. Their annual fees amount to 0.67% and 0.66%, respectively, and the funds require just \$2,000 to invest (or \$1,000 in an IRA). But that’s not the only thing working in their favor.

The funds are run in a similar fashion by five managers from Primecap Management Company, an investment firm in Pasadena, Cal. The managers hunt for companies that have promising growth prospects but that are temporarily out of favor. Odyssey Stock can invest in companies of any size, but it focuses mostly on large companies (they accounted for 83% of the fund’s assets at last report). Odyssey Growth puts more of an emphasis on a firm’s potential to generate above-average earnings growth and thus is a bit more inclined to invest in midsize concerns. It recently had 16% of its assets in small firms as well. That makes Growth a bit more volatile than Stock.

### 6. T. ROWE PRICE EQUITY INCOME

Brian Rogers, who is also the chairman of T. Rowe Price Group, has run Equity Income since the fund launched in 1985. Through the years, his strategy of finding large, high-quality firms

that pay dividends has paid off handsomely. Since the fund’s inception, it has returned 11.2% annualized. That beat the S&P 500 by an average of 0.4 percentage point per year. (That may sound skimpy, but over the 27.5-year period, a \$10,000 investment in Equity Income would be worth \$18,000 more than one in Vanguard 500 Index, which tracks the benchmark.)

At last word, Rogers had about 20% of the portfolio in financial-services stocks, including Bank of America. But the fund’s sterling performance over the past year was also driven by health care companies, such as Johnson & Johnson and Thermo Fisher Scientific.

### 7. VANGUARD DIVIDEND GROWTH

This fund, another member of the Kiplinger 25, has set the gold standard for investing in dividend stocks.

Manager Donald Kilbride, of Wellington Management in Boston, seeks high-quality companies with good growth prospects. More important, he looks for outfits that have a proven willingness to increase dividends and that he thinks will boost payouts by at least 10% annually over the next five years. Since Kilbride took over Dividend Growth in early 2006, the fund has returned 8.4% annualized, well ahead of the S&P 500’s 6.2% annualized return. The fund yields 2.2%. ■

## KEY NUMBERS FOR OUR FAVORITE LARGE-COMPANY FUNDS

Low fees, modest minimums and solid long-term returns are hallmarks of our picks. Although it’s important to know how a fund performed during a downturn, keep in mind that every bear market is different. Dodge & Cox Stock, for example, performed superbly during the 2000–02 bear market.

Fund (symbol)	Total return*				Down markets		Expense ratio	Min. invest.	Top three holdings‡
	1 yr.	3 yrs.	5 yrs.	10 yrs.	2007–09†	2011‡			
Dodge & Cox Stock (DODGX)	38.6%	18.4%	8.0%	8.4%	–62.4%	–24.1%	0.52%	\$2,500	Capital One • Wells Fargo • Hewlett-Packard
Fidelity Contrafund (FCNTX)	25.6	17.0	8.6	10.5	–48.2	–16.9	0.74	2,500	Google • Berkshire Hathaway • Apple
Mairs & Power Growth (MPGFX)	36.1	19.0	11.3	9.6	–51.9	–20.9	0.70	2,500	Valspar • 3M • Medtronic
Primecap Odyssey Growth (POGRX)	38.5	18.8	12.0	—	–51.5	–22.9	0.67	2,000	Seattle Genetics • Roche • Amgen
Primecap Odyssey Stock (POSKX)	32.4	16.9	9.6	—	–50.2	–18.2	0.66	2,000	Roche • Charles Schwab • Johnson & Johnson
T. Rowe Price Equity Income (PRFDX)	30.9	16.1	8.7	8.3	–57.5	–20.4	0.68	2,500	AT&T • Apache • Chevron
Vanguard Dividend Growth (VDIGX)	25.7	17.4	9.7	9.7	–42.3	–12.0	0.29	3,000	Microsoft • McDonald’s • Johnson & Johnson
S&P 500-STOCK INDEX	<b>28.1%</b>	<b>17.4%</b>	<b>8.7%</b>	<b>7.9%</b>	<b>–55.3%</b>	<b>–18.6%</b>			

\*Total returns through August 2; three-, five- and ten-year returns are annualized. †Returns, including dividends, from October 9, 2007, through March 9, 2009. ‡Returns, including dividends, from April 29, 2011, through October 3, 2011. —Fund not in existence for the period. §As of June 30. SOURCE: © 2013 Morningstar Inc.



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BONDS >>

# Why You Still Need TIPS

Treasury inflation-protected securities will safeguard your buying power. **BY JOHN F. WASIK**

**TREASURY INFLATION-**protected securities are the go-to income investments if you want to protect principal from the ravages of inflation. But there's a problem: TIPS can lose money and can do so surprisingly quickly.

The downside of TIPS came to light over the spring and early summer, when global credit markets sank in response to suggestions by the Federal Reserve that it might cut back its easy-money policies. TIPS tumbled, too. From May 2 through June 24, a Barclays index of U.S. TIPS with maturities of at least one year plunged 9%.

**How they work.** Introduced in the 1990s, TIPS are Treasury bonds that are linked to the consumer price index. Interest is paid twice a year, and the bonds' principal value increases with inflation and decreases with deflation. When the bond matures, you receive either the inflation-adjusted principal plus interest or, in the event of deflation, the original principal plus interest.

In recent years, investors have poured money into

TIPS and other Treasury bonds as a hedge against turmoil in Europe and other parts of the world. Investors also worried that the Fed's massive bond-buying program would spark inflation. Because of the strong demand, TIPS prices rose, and their yields, which move in the opposite direction, turned negative. (A negative TIPS yield means your return will be less than the change in consumer prices.)

But when chairman Ben Bernanke suggested that the Fed might soon back away from its bond purchases, the fixed-income market—including TIPS—went into a tizzy. Not only did investors flee TIPS under the threat of higher rates, but inflation was nowhere to be found, a terrible combination for TIPS holders.

Some good news did come out of the bond rout. As prices fell, yields on ten-year TIPS became positive for the first time in a year and a half. As of August 2, the real, or inflation-adjusted, yield on ten-year TIPS is 0.42%. That means if you were to buy a ten-year TIPS today, your

annual return over the holding period would be roughly the inflation rate plus 0.42 percentage point.

So are TIPS bargains now? To see whether TIPS make sense, experts look at the so-called break-even rate. That's the difference between yields on TIPS and yields on regular Treasuries, recently 2.6 percentage points on bonds with ten-year maturities. Annual inflation would have to average more than 2.6% for investors to earn more on TIPS than they would on regular Treasuries. Over the past year through June, consumer prices climbed 1.8%, but inflation has averaged about 3% annually for most of the past century.

Most investors should hold TIPS. Think of them as a way of hedging against future erosion of your purchasing power—with some volatility along the way, to be sure, but with less volatility than many other inflation hedges, such as gold.

Morningstar analyst Michelle Canavan suggests

investing in TIPS with short maturities, which are less sensitive to rising rates than TIPS with long maturities. Consider **VANGUARD SHORT-TERM INFLATION-PROTECTED SECURITIES INDEX FUND (SYMBOL VTAPX)**, which was launched last October, or its exchange-traded sibling, which trades under the symbol **VTIP**. Both versions show a current negative yield of about 1%. Year-to-date through August 2, the mutual fund version lost 1.1%. Expenses are just 0.10% per year.

Funds and ETFs offer convenience, but if you want a guarantee that you'll get your principal back at maturity, you can buy TIPS directly from Uncle Sam without commission at [www.treasurydirect.gov](http://www.treasurydirect.gov). TIPS are sold in maturities of five, ten and 30 years; the minimum purchase is \$100.

You don't have to rush into TIPS. But if you're investing for the long haul, keep in mind that although inflation has been mild and may stay low for a while, it rarely disappears entirely. ■

## Rising Yields

### THE TIDE TURNS FOR TIPS

Real yields on ten-year Treasury inflation-protected securities recently turned positive. If you buy ten-year TIPS, your return should equal inflation plus the real yield over the next ten years.



As of August 2. SOURCE: U.S. Treasury





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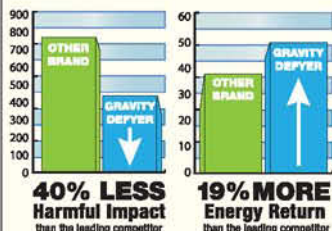


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**SHOCK ABSORPTION STUDY** HPW Biomechanics, 2012  
<sup>\*</sup>Shock absorption: Measurement of max/min pressure (KPa).  
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**Some ideas are so far outside my comfort zone that acting on them would surely give me a stomachache."**

**KATHY KRISTOF** > Practical Investing

## Reader Advice: Good and Bad

**W**hen you write a column about picking stocks, you get plenty of advice about what you should buy. I often find these suggestions wise and enlightening. One of my best-performing stocks, Seagate Technology (symbol STX), was suggested by my editor, for example. Another, KKR Financial (KFN), was a favorite of my son.

Readers have come up with some great calls, too. About a year ago, one reader asked me to look at Eaton Corp. (ETN), an Ireland-based capital-goods maker. At the time, the company was growing nicely, and the stock was selling for just 9 times earnings and yielding a healthy 4%. I told the reader I thought Eaton was a great value and bought some for my personal portfolio (at the time I didn't have any cash in my "Practical Investing" portfolio). I've earned 71% on that holding in just over a year (returns and prices are through August 2).

But I have not always been wise enough to heed readers' advice. One took me to task for selling Lockheed Martin (LMT), which I did last January at \$96, for a 30% gain. I felt vindicated when the stock fell nearly 10% in the days after I sold because of uncertainty surrounding the federal budget.

The fact is, though, that the reader's argument was impeccable and completely consistent with the way I invest—or at least the way I *try* to invest. Lockheed is a strong company that is consistently profitable and pays a generous dividend. That's the kind of stock I generally think you can hold for decades, regardless of short-term market swings. My punishment for failing to heed this wise reader's counsel has been to sit on the sidelines as Lockheed shares soared another 29%, to \$124, since my sale.

But people also give me advice that I can't take—and won't lament forgoing. That's simply because their ideas are so far outside my comfort zone that acting on them would surely give me a stomachache.

For instance, a lot of people made a for-

tune buying gold, which nearly quintupled between 2002 and September 2011. Many gold enthusiasts urged me to jump on the yellow-metal bandwagon.

But I didn't buy a single ounce, nor did I buy funds that track the metal's price or invest in mining stocks. Why? I'm a numbers girl. And no one can provide a good formula for evaluating the right price to pay. Gold is essentially a hedge against fear. When people become worried about the economy or the value of their currency, they bid up gold's price. But are they \$500-an-ounce concerned or \$2,500-an-ounce terrified? I know of no logical way of making that call, so I simply stay away.

**High-P/E aversion.** I feel the same about many popular stocks that sell at absurd price-earnings ratios. Take Amazon.com (AMZN). When one analyst told me in November 2011 that it was a screaming buy at \$192—a price that amounted to about 100 times estimated 2012 profits—I thought he was nuts. Since then, the stock has soared nearly 60% even though Amazon lost money in 2012 and is expected to earn just 86 cents per share this year. At \$304, the stock now sells for 354 times estimated 2013 profits.

Do I regret not getting in at \$192? Not really. (Okay, a little.) But buying Amazon would have put me on pins and needles because I didn't understand why the stock traded at such an exorbitant P/E—and, frankly, I still don't. I would spend my days trying to figure out when sentiment for Amazon might sour. And that would make me miserable and nervous.

I want my investments to make me calm and comfortable, to meet my economic goals without turning me into a neurotic trader. Yes, I sometimes miss out on profits, but I save on antacids. That's a trade I'll make any day. ■

KATHY KRISTOF IS A CONTRIBUTING EDITOR TO *KIPLINGER'S PERSONAL FINANCE* AND AUTHOR OF THE BOOK *INVESTING 101*. YOU CAN SEE HER PORTFOLIO AT [KIPLINGER.COM/LINKS/PRACTICALPORTFOLIO](http://KIPLINGER.COM/LINKS/PRACTICALPORTFOLIO).

# Bond Swoon: How Our Funds Fared

## THE RECENT BOND MARKET

swoon left many investors reeling. From May 2 through August 1, during which bond yields surged, Barclays U.S. Aggregate Bond index sank 3.8%. As a group, the seven bond funds in the Kiplinger 25 fared slightly better, with an average loss of 3.1% (as the table below shows, the one-year results vary widely).

Our two go-anywhere bond funds held up well. **OSTERWEIS STRATEGIC INCOME**, with its strategy of focusing on short-term high-yield debt and convertible bonds that behave a lot like stocks,

eked out a 0.1% gain. And the managers at **METROPOLITAN WEST UNCONSTRAINED BOND** staved off disaster by selling short Treasury bonds (a bet on falling prices) with a small portion of the fund's assets. The fund lost 1.4%.

**VANGUARD SHORT-TERM INVESTMENT-GRADE** surrendered 1.0%. The fund benefited from its focus on short-term debt, typically bonds maturing in one to five years. Manager Greg Nassour says he runs "a high-quality fund very conservatively."

Emerging-markets bond funds took it on the chin,

and **FIDELITY NEW MARKETS INCOME** was no exception, sinking 7.8%. Fears that the end of the Federal Reserve's easy-money policies would lead to higher interest rates around the globe put a strain on emerging-markets debt. Manager John Carlson took advantage of the selloff to add to his position in Hungarian bonds. In volatile, fear-driven markets, he says, "people throw out the good with the bad."

Emerging-markets bonds and Treasury inflation-protected securities got the better of **HARBOR BOND**, which lost 4.6%. Harbor is a near-clone of Pimco Total Return, the largest mutual fund in the U.S. At the end of June, manager Bill Gross had 12% of Harbor's assets in TIPS and emerging markets. For TIPS investors, it was the worst of two worlds: Interest rates jumped while

evidence of inflation was scant. (For more on TIPS, turn to page 40.)

At **DOUBLELINE TOTAL RETURN**, Jeffrey Gundlach and Philip Barach edged the bond market by sticking with their barbell approach to mortgage bonds: They balance government-agency mortgage-backed securities (46% of assets), which have no default risk but a fair amount of interest-rate risk, with non-agency mortgage securities (26% of assets), which have little rate risk but a high amount of default risk. The fund dropped 3.3%.

**FIDELITY INTERMEDIATE MUNICIPAL INCOME**, the lone tax-free fund on our list, fell 3.8%. That compared with a 4.5% decline for the average medium-maturity national muni fund. **NELLIE S. HUANG**

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U.S. Stock Funds	Symbol	Total return*				Added to Kip 25
		1 yr.	3 yrs.	5 yrs.	10 yrs.	
Akre Focus Retail	AKREX	33.2%	22.7%	—	—	Dec. 2009
Artisan Value	ARTLX	23.0	15.4	7.1%	—	May 2012
Baron Small Cap Retail	BSCFX	39.3	18.5	10.8	10.0%	Dec. 2007
Dodge & Cox Stock	DODGX	38.6	18.4	8.0	8.4	May 2008
Fidelity Contrafund	FCNTX	25.6	17.0	8.6	10.5	May 2009
Fidelity Low-Priced Stock	FLPSX	36.7	18.5	11.5	11.6	May 2009
Homestead Small Co Stock	HSCSX	41.6	21.8	16.1	13.2	May 2012
Mairs & Power Growth	MPGFX	36.1	19.0	11.3	9.6	Jan. 2013
T. Rowe Price Sm-Cap Value	PRSVX	34.1	17.8	10.0	11.5	May 2009
Vanguard Dividend Growth	VDIGX	25.7	17.4	9.7	9.7	May 2010
Vanguard Selected Value	VASVX	40.1	18.7	12.7	11.3	May 2005
Wells Fargo Advtg Discovery	STDIX	38.5	21.9	10.8	12.0	May 2012
International Stock Funds	Symbol	Total return*				Added to Kip 25
		1 yr.	3 yrs.	5 yrs.	10 yrs.	
Dodge & Cox Intl Stock	DODFX	33.0%	8.8%	3.6%	11.3%	May 2005
Harbor International Inv	HIINX	22.5	8.7	2.8	10.9	June 2010
Harding Loevner Emrg Mkts	HLEMX	10.3	3.5	1.9	13.9	May 2013
Matthews Asian Gro & Inc Inv	MACSX	17.5	9.2	8.5	13.2	Aug. 2013

Specialized/ Go-Anywhere Funds	Symbol	Total return*				Added to Kip 25
		1 yr.	3 yrs.	5 yrs.	10 yrs.	
FPA Crescent	FPACX	22.4%	12.8%	8.2%	9.2%	Oct. 2008
Merger Fund	MERFX	3.8	2.9	3.5	3.8	June 2007
Bond Funds	Symbol	Total return*				Added to Kip 25
		1 yr.	3 yrs.	5 yrs.	10 yrs.	
DoubleLine Total Return N	DLTNX	2.2%	7.8%	—	—	May 2011
Fidelity Intermed Muni Inc	FLTMX	−1.4	3.0	4.2%	4.1%	May 2004
Fidelity New Markets Income	FNMIK	−0.9	7.2	9.5	10.3	May 2012
Harbor Bond Institutional	HABDX	0.2	3.8	6.8	6.0	May 2004
Met West Unconstrained Bd M	MWCRX	6.1	—	—	—	May 2013
Osterweis Strategic Income	OSTIX	8.3	7.1	8.3	7.4	May 2013
Vanguard Sh-Tm Inv-Grade	VFSTX	1.5	2.5	3.8	3.7	May 2010
Indexes		Total return*				
		1 yr.	3 yrs.	5 yrs.	10 yrs.	
S&P 500-STOCK INDEX		28.1%	17.4%	8.7%	7.9%	
RUSSELL 2000 INDEX†		39.9	18.6	9.7	9.9	
MSCI EAFE INDEX#		28.7	8.9	2.3	8.7	
MSCI EMERGING MARKETS INDEX		4.0	0.9	1.3	13.5	
BARCLAYS AGGREGATE BOND INDEX‡		−2.0	3.3	5.2	4.9	

Through August 2. \*Three-, five- and ten-year returns are annualized. —Not available; fund not in existence for the entire period. †Small-company U.S. stocks. ‡Foreign stocks. §Tracks high-grade U.S. bonds. SOURCE: © 2013 Morningstar Inc.

## FUND SPOTLIGHT

# Europe's Surprising Rebound

Share the wealth with T. Rowe Price European Stock.

**TALK ABOUT ABOUT-FACES. AS WELL AS** the U.S. stock market has performed over the past year, European bourses have done even better. Two years after the near-collapse of the euro, the euro zone's economy is finally on the mend and may emerge from recession by the end of the year. One of the best ways to play the recovery is with **T. ROWE PRICE EUROPEAN STOCK**. The no-load fund, managed since 2005 by Dean Tenerelli, has topped its benchmark, the MSCI Europe index, in six of the past eight calendar years, including 2013.

The 75-stock portfolio holds companies of all sizes from developed European countries. But, says the London-based Tenerelli, "they are not the typical blue chips people see in many other funds." He uses estimates of a company's future free cash flow (the cash left over after the capital expenditures needed to maintain a business) to determine its current value and buys a stock when it's selling below that figure. "I do not focus on growth," Tenerelli says. "But I find a lot of interesting opportunities in slower-growing companies that the market overlooks because they seem boring."

Spanish stocks boosted the fund's results over the past year. These include broadcasters Atresmedia Corp. and Mediaset España, which have surged since Tenerelli began buying them—Atresmedia last spring and Mediaset late last year. Also contributing to the big one-year gain were Scandinavian financials, such as Nordea and Swedbank. **ANJELICA TAN**

## EUROPEAN STOCK FUNDS Ranked by one-year return

Rank/Name	Symbol	Total return through Aug. 2 <sup>**</sup>			Max. sales charge	Expense ratio	Toll-free number
		1 yr.	3 yrs.	5 yrs.			
1. JPMorgan Intrepid European A	VEUAX	44.8%	12.8%	2.3%	5.25%	1.50%	800-480-4111
2. Invesco European Small Company A	ESMAX	42.1	15.6	7.2	5.50	1.69	800-959-4246
3. Putnam Europe Equity A	PEUGX	39.0	12.0	3.2	5.75	1.47	800-225-1581
4. Henderson European Focus A	HFEAX	37.1	10.1	7.7	5.75	1.53	866-343-6337
5. T. Rowe Price European Stock	PRESX	37.0	13.8	5.8	2.00 <sup>r</sup>	1.00	800-638-5660
6. Columbia European Equity A	AXEAX	36.5	11.7	6.4	5.75	1.52	800-345-6611
7. BlackRock EuroFund A	MDEFX	36.4	8.4	1.0	5.25	1.33	800-441-7762
8. Fidelity Europe Capital Appreciation <sup>**</sup>	FECAV	34.7	10.0	1.8	1.00 <sup>r</sup>	0.92	800-544-9797
9. Fidelity Advisor Europe Capital App A	FAEAX	33.8	9.4	1.0	5.75 <sup>s</sup>	1.42	800-544-9797
10. Fidelity Europe	FIEUX	33.7	10.2	2.4	1.00 <sup>r</sup>	0.80	800-544-9797
CATEGORY AVERAGE		32.3%	9.7%	2.7%			

## 20 LARGEST STOCK MUTUAL FUNDS Ranked by size

Rank/Name	Symbol	Assets <sup>†</sup> (in billions)	Total return through Aug. 2 <sup>**</sup>			Max. sales charge	Toll-free number
			1 yr.	3 yrs.	5 yrs.		
1. Vanguard Total Stock Market Idx Inv <sup>@</sup>	VTSMX	\$267.8	30.0%	17.8%	9.1%	none	800-635-1511
2. Vanguard 500 Index Inv <sup>@</sup>	VFIND	145.5	27.9	17.3	8.6	none	800-635-1511
3. American Gro Fund of America A <sup>@</sup>	AGTHX	120.1	32.0	15.8	7.2	5.75%	800-421-0180
4. American EuroPacific Gro A <sup>@</sup>	AEPGX	105.6	21.9	7.1	3.3	5.75	800-421-0180
5. Fidelity Contrafund <sup>@</sup>	FCNTX	98.4	25.6	17.0	8.6	none	800-544-9797
6. Vanguard Total Intl Stock Idx Inv <sup>@</sup>	VTGSX	97.6	21.5	5.9	1.3	none	800-635-1511
7. American Capital Income Builder A <sup>@</sup>	CAIBX	82.5	13.3	10.3	5.2	5.75	800-421-0180
8. American Inc Fund of America A <sup>@</sup>	AMECX	80.7	17.1	12.5	7.9	5.75	800-421-0180
9. Franklin Income A <sup>@</sup>	FKINX	76.1	14.4	10.8	7.8	4.25	800-632-2301
10. Vanguard Wellington <sup>@</sup>	VWELX	75.1	18.9	12.4	8.5	none	800-635-1511
11. American Capital World Gro & Inc A <sup>@</sup>	CWGX	74.5	25.5	10.9	4.8	5.75	800-421-0180
12. Vanguard Emerging Mkts Stock Idx <sup>@</sup>	VEIEX	65.2	3.4	-0.1	0.5	none	800-635-1511
13. American Balanced A <sup>@</sup>	ABALX	62.2	19.7	13.6	8.5	5.75	800-421-0180
14. American Washington Mutual A <sup>@</sup>	AWSHX	62.1	26.5	17.4	8.6	5.75	800-421-0180
15. Fidelity Spartan 500 Index Inv <sup>@</sup>	FUSEX	61.8	28.0	17.3	8.6	none	800-544-9797
16. American Invstmt Co of America A <sup>@</sup>	AIVSX	61.1	27.0	14.7	7.5	5.75	800-421-0180
17. American Fundamental Inv A <sup>@</sup>	ANCFX	58.4	28.7	15.4	7.2	5.75	800-421-0180
18. BlackRock Global Allocation A <sup>@</sup>	MDLOX	56.6	15.2	7.8	5.2	5.25	800-441-7762
19. Fidelity Growth Company <sup>@</sup>	FDGRX	49.5	31.5	20.6	11.1	none	800-544-9797
20. American New Perspective A <sup>@</sup>	ANWPX	47.8	27.1	13.2	7.2	5.75	800-421-0180
S&P 500-STOCK INDEX			28.1%	17.4%	8.7%		
MSCI EAFE INDEX			28.7%	8.9%	2.3%		

<sup>\*</sup>Annualized for three and five years. <sup>\*\*</sup>Closed to new investors. <sup>@</sup>Rankings exclude share classes of this fund with different fee structures or higher minimum initial investments. <sup>†</sup>For all share classes combined. <sup>r</sup>Maximum redemption fee. <sup>s</sup>Front-end load; redemption fee may apply. MSCI EAFE index consists of developed foreign stock markets. SOURCE: © 2013 Morningstar Inc.

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**Total return** assumes reinvestment of all dividends and capital gains; three- and five-year returns are annualized. Returns reflect ongoing expenses but not sales charges.

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**MONEY** // COVER STORY

# Make Your Money Last



**AFTER BOB AND MARGARET LONG RETIRED IN 2007, JUST AS STOCKS STARTED TO TUMBLE, THEY DOWNSHIFTED THEIR EXPECTATIONS.**





PHOTOGRAPH BY LISE METZGER

To make sure your retirement nest egg goes the distance, you need growth as well as income. Rule number one: Don't dump stocks.

BY JANE BENNETT CLARK

**IN 2007, AFTER TEACHING MATH FOR** 34 years at a private school in the Washington, D.C., area, Bob Long was ready to hang up his teaching career and head into a new stage of life. He spent a few months training his successor as head of the math department and, in December, retired at the relatively young age of 61. Bob's wife, Margaret (then 56), had retired a few months earlier from her job in the mortgage industry. The couple were eager to kick back in their new home, in Ocean Pines, Md. // Their timing couldn't have been worse. The stock market entered a downward spiral just as the Longs were tapping into their



retirement savings. They expected their money to last well into their nineties, based on retirement calculators, so they were rattled to see their balance shrink so quickly. “I’m a mathematician,” says Bob. “I learned early on that average returns are nice for the long term, but you do not want to see a drop in the market immediately after retiring.” At one point, he estimates, their portfolio was down 25% from its preretirement balance.

If their timing was all wrong, their response was just about perfect. Rather than bail out of stocks in a down market, they stayed the course (and stopped looking at their brokerage statements). They were conservative in the amounts they took from their retirement accounts. And they dipped back into the workforce. Bob returned to the classroom as a substitute teacher, and both he and Margaret took short-term jobs at the Census Bureau—for fun and pocket money.

The Longs’ restrained approach was rewarded when the market and their nest egg began to rebound after March 2009. But they (and other retirees) can’t be guaranteed they won’t face future challenges. “A lot can change over 30 years,” says David Blanchett, head of

retirement research at Morningstar Investment Management, an investment consulting branch of Morningstar. “The key is to think about where you are now and where you want to be in the future”—and adjust accordingly.

### ●● **DON'T DUMP STOCKS**

At 65, you’d think you could stop worrying about building your retirement stash and focus on preserving it. But with today’s longer life expectancies (a 65-year-old man can expect to live until 84, on average, and a 65-year-old woman can expect to live until age 86), “you have to take on some level of risk if you want to keep up with and beat inflation,” says Nate Wenner, a certified financial planner in Edina, Minn.

To keep the growth engine running, financial planners generally recommend that you have 40% to 60% in stocks at the start of your retirement, with the rest in cash and fixed-income investments to tamp down risk. A more conservative investor might start with 30% in stocks and 70% in fixed-income investments; aggressive investors would reverse it to 70% and 30%.

How you invest within those parameters gets tricky, says Blanchett, given that bond yields remain low by histori-

cal standards (recently 2.6% for the ten-year Treasury bond, for example) and stock prices may be topping out. Aim for a diversified portfolio that includes U.S. and international stock funds, an emerging-markets stock fund and a dash of real estate and commodities. On the bond side, given the low-interest-rate environment, go with short-term bonds, floating-rate bank loan funds and high-yield bond funds (see our suggested portfolio on page 50).

As you get further into retirement, gradually reduce risk by shifting to more bonds and cash. Some investors feel comfortable allocating 30% to stocks even in their advanced old age; others end up with 10% to 15% in stocks and the rest in cash and fixed investments. Only the most conservative investors get out of stocks altogether, says Maria Bruno, a senior investment analyst at Vanguard, and those investors “are very rare.”

Making the adjustments yourself can be a bother; instead, consider putting your money in a target-date fund (if you haven’t already), which adjusts the mix for you. Be aware that funds have different asset mixes and different timetables for adjusting them, called glide paths (see “Aim for the Best Target Fund,” Sept.). For instance, the Vanguard 2015 fund, aimed at people retiring between 2013 and 2017, invests 50% in stocks and 50% in bonds that year and moves to 30% stocks and 70% bonds over seven years. A comparable fund from Fidelity has you start retirement in 2015 with 50% in stocks, 40% in bonds and 10% in short-term funds and moves to 20% stocks with the rest in bonds and short-term funds over ten to 15 years.

Another strategy is to carve out part of the money you would otherwise put in bonds to buy an immediate fixed annuity, which delivers a guaranteed income for as long as you live. “If you buy an annuity with 30% to 40% of your savings, that’s the bond part of your portfolio. Then you can go all in with stocks for the rest,” says Steve

### ✧ **Social Security**

## **Bump Up Your Benefits by 32%**

**TALK ABOUT THE BEST ANNUITY MONEY CAN'T BUY. NOT ONLY ARE SOCIAL SECURITY benefits guaranteed for life, but they are also adjusted for inflation. And you can boost your benefits by 8% a year for every year you delay taking them after full retirement age, until age 70. (Although you can take Social Security at age 62, the benefit is 25% lower than it would be at 66.)**

**Say your monthly benefit is \$2,000 at full retirement age. If you wait until age 70 to take it, you'll get \$2,640 a month (plus all the cost-of-living adjustments you missed while you waited). If you jump the gun and take it at 62, you'll only get \$1,500 a month (and your COLAs will forever be based on the lower amount). The financial impact of the 8%-a-year credit is so powerful, it can make sense to postpone claiming Social Security even if it means dipping deeper than planned into your retirement nest egg.**

**Kiplinger has joined with Social Security Solutions to offer a tool to uncover the most advantageous time to start collecting your Social Security benefits. Visit [kiplinger.socialsecuritysolutions.com](http://kiplinger.socialsecuritysolutions.com) for details on how to get your personalized recommendations.**

# How to Lessen the Tax Bite

ONCE YOU RETIRE, CERTAIN EXPENSES WILL diminish or disappear. You won't spend as much on dry cleaning, for example, and if you're in good shape, you can fire the dog walker. And you'll no longer be saving for retirement—a much bigger expense.

One expense that won't go away is taxes. You may have \$1 million in retirement savings, but the amount available for your retirement income is much less because a portion of the money will go to pay federal and state taxes. This is where having different types of retirement accounts—taxable, tax-deferred and tax-free—comes into play. Depending on the account you tap, along with the type of investment, your federal tax rate could range from 0% to 39.6%. You can keep your tax rate on the low end of the scale by taking tax-efficient withdrawals from your accounts.

**WHAT TO TAP FIRST.** Conventional wisdom has long held that retirees should take withdrawals from their taxable accounts first. That way, you can benefit from low capital gains rates while investments in your tax-deferred and tax-free retirement accounts continue to grow, unfettered by taxes.

In a taxable account, the capital gains rate on assets you've owned more than a year ranges from 0% for taxpayers in the 10% and 15% tax brackets to a maximum rate of 23.8% for taxpayers in the top tax bracket (see "Game Plan," on page 23). To minimize taxes, use your taxable accounts for investments that qualify for long-term capital gains rates or are tax-free. The list typically includes growth stocks, tax-efficient mutual funds and exchange-traded funds, says Christine Fahlund, senior financial planner for T. Rowe Price. If you own individual municipal bonds or muni funds, they also belong in your taxable accounts. In addition, many planners recommend keeping two years' worth of living expenses in these accounts, typically in a money market or other low-risk account.



Next in line are your tax-deferred accounts, which include traditional IRAs, 401(k)s and other retirement-savings plans. Withdrawals from these accounts will be taxed at your ordinary income tax rate (except for any after-tax contributions you made, which will be tax-free). In most cases, you'll also pay a 10% penalty if you take withdrawals before you're 59½. Use these accounts for the portion of your portfolio allocated to investments that are already taxed at your ordinary income tax rate, such as individual bonds and bond funds, real estate investment trusts, and preferred stocks. Many retirees should have stocks and stock funds in their IRA, too.

Last in the queue is your Roth IRA. You may withdraw your Roth contributions at any time, tax- and penalty-free. As long as you're 59½ and have owned a Roth for at least five years, earnings are tax-free, too. Unlike traditional IRAs, you're not required to take minimum withdrawals when you turn 70½. If you don't need the money, you can leave it to your heirs, who will be able to take distributions tax-free.

Because withdrawals from a Roth aren't taxed, Roths are suitable for a wide range of

investments. Income-oriented investments are good candidates for both traditional and Roth IRAs, says Mark Bass, a financial planner in Lubbock, Tex. Fahlund recommends using your Roth for the slice of your portfolio invested in aggressive stock funds, because you'll never be required to take withdrawals—which means you'll have more time for the investments to grow—and you won't have to worry about paying taxes on your profits.

**EXCEPTIONS.** There are a few good reasons to depart from the conventional withdrawal

hierarchy: Once you turn 70½, you'll need to take annual required minimum distributions from your traditional IRAs and other tax-deferred retirement accounts. If these accounts grow too large, the mandatory withdrawals could push you into a higher tax bracket. To avoid this problem, start taking withdrawals from your IRAs before you turn 70½. Mark Joseph, a certified financial planner with Sentinel Wealth Management, in Reston, Va., advises retired clients who aren't yet required to take RMDs (and are likely to be in a higher tax bracket down the road) to look at their other income, such as interest and capital gains from taxable accounts, Social Security and pensions, and withdraw just enough from their tax-deferred accounts to remain within the 15% tax bracket. Additional expenses can be covered by withdrawals from the principal of their taxable accounts first, followed by withdrawals from Roth accounts, he says.

It's also a good idea to take withdrawals for emergency expenses—say, for a new roof or long-term care—from a Roth. You'll owe taxes on money from tax-deferred accounts, which could push you into a higher tax bracket. **SANDRA BLOCK**

Vernon, author of *Money for Life* (Rest-of-Life Communications). Low interest rates are dampening the income you can generate with a single-premium immediate annuity—the meat and potatoes of the annuities world—but there are ways to boost the payouts, such as laddering or buying a deferred-income annuity (see “Add an Annuity to the Mix,” on page 54).

Smart distribution of your assets is only part of the challenge. You also need to adopt a strategy to make your income last for the rest of your life. Many retirees aim to replace 80% of their preretirement income, but it's a good idea to create a budget and test-drive it before you quit your day job (see “Countdown to Retirement,” Sept.). If you can't get by with Social Security, a pension and savings, consider tapping your home equity through a reverse mortgage (see “Insider Interview,” on page 57).

#### ●● **LIVE OFF YOUR INTEREST**

One obvious way to ensure you won't run your portfolio dry is to siphon off the interest, dividends and perhaps the capital gains on your investments and preserve the principal. At current interest rates, you'd need a hefty amount plus a decent guaranteed income to generate a respectable paycheck. A million dollars in a balanced fund or a balanced portfolio with a 3% annual payout (\$30,000) plus a Social Security benefit of \$2,000 a month (for one person) gives you \$54,000 annually. If you're married and you and your spouse each get \$2,000 a month in Social Security, you'd have an annual income of \$78,000.

If you're accustomed to a more lavish lifestyle, that may not be enough, especially considering taxes (for tax-efficient ways to tap your accounts, see page 49). You could supplement the amount by working part-time for the first few years of retirement, postponing the point at which you draw down your principal—at least until you have to take required minimum distributions. The longer you wait to tap

your nest egg, the shorter your time horizon becomes and the less likely your money will run out. Better yet, work a little longer and delay taking Social Security until you hit 70 (see the box on page 48).

#### ●● **RETHINK THE 4% RULE**

For the past two decades, some financial planners have used 4% as a benchmark for how much you can withdraw from your retirement assets and be reasonably assured of not running out of money after 30 years. According to this rule, you would take 4% of your total portfolio in the first year of your retirement and increase the amount each year by the rate of inflation. The benchmark, developed in 1994 by William Bengen, was based on average returns over overlapping 30-year periods, using a model portfolio with a 50% allocation to stocks and 50% to bonds.

But historical averages don't necessarily reflect the conditions you face out of the starting gate, and those conditions can have a disproportionate effect on where you end up. If you start taking distributions from your portfolio at the beginning of a bear market and follow the 4% rule, you could face a higher risk of running out of money after 30 years than if you start tapping your money when the market is healthy, says Martin Schmidt, an adviser at the Institutional Retirement Income Council.

Low interest rates, which are expected to last for at least several more years, make for another game changer. “The returns you earn at retirement are really important to your strategy,” says Blanchett. If you buy a ten-year government bond today, he says, you get 2.6%. That's about three percentage points below the long-term average. “If rates go back to the long-term average, you could be stuck holding a bond paying 2.6% over its lifetime.”

Blanchett and other financial planners suggest that a withdrawal rate of 3% or even 2.5% (with an inflation adjustment) under today's conditions is a safer bet for a 30-year retirement run, but they also agree that a little common sense is in order. Rather than stick to a rigid formula, lower your payout (or skip the inflation adjustment, as the Longs did) when market conditions are against you. Then take it up a notch when your investments are thriving. Blanchett says he still thinks that 4% is an excellent starting point, but to get there requires more active decision-making than it once did. “Historically, it was easy—a slam-dunk. Not so much today.”

#### ●● **LET THE IRS DO THE MATH**

For a different approach, you could take your cue from Uncle Sam and calculate your withdrawals based on the actuarial tables the IRS uses for required minimum distributions (which you have to take anyway from tax-deferred accounts starting at age 70½). This method has you start with

✦ **Kiplinger 25**

## A Portfolio for Retirees

**THIS PORTFOLIO, CONSTRUCTED with mutual funds from the Kiplinger 25, has an even mix of stocks and bonds and is appropriate for retirees looking for both income and growth. You'll need a minimum of \$60,000 to duplicate the portfolio (see page 43 for more details on the Kiplinger 25).**

Vanguard Dividend Growth.....	25%
Dodge & Cox Stock.....	10%
Akre Focus Retail.....	5%
Dodge & Cox International Stock...	5%
Matthews Asian Growth & Inc Inv...	5%
DoubleLine Total Return Bond N.....	10%
Fidelity New Markets Income.....	10%
Met West Unconstrained Bond M.....	10%
Osterweis Strategic Income.....	10%
Harbor Bond Institutional.....	5%
Vanguard Short-Term Inv-Grade....	5%



a minimum payout rate of 3.76%; the percentage goes up each year until you turn 90, topping out at 8.58%. (The IRS life-expectancy tables for a 70-year-old man use an average life expectancy almost twice as long as the one actuaries at Social Security use.)

Here's an example from Vanguard. Say you're 70½ and you have \$500,000 in your IRA. Your first distribution would be about \$18,800. If your account grows at a 3% real rate of return, by age 89 you'd withdraw about \$26,382 in current dollars that year. But there's a catch: At age 90, your purchasing power starts to creep back down. "The question is whether the RMD strategy triggers a drop in the standard of living for someone who lives into his or her nineties," says Vanguard's Bruno.

Add to that the risk that the RMD formula might cause you to take too big a bite out of your savings during a market decline and you'll see that the system, though convenient, is not risk-free, adds Bruno.

### ●● USE THE BUCKET SYSTEM

Another way to hedge your bets against market downturns and other unpleasant events is to position your money in various buckets. With this system, you invest enough money in liquid, conservative accounts to cover several years' worth of basic costs and the rest in short- and intermediate-term bonds and growth-oriented investments, such as stock funds.

To set it up, calculate how much of your essential expenses you can cover with guaranteed income, such as Social Security and pensions. Put enough money to cover the rest of your expenses for several years into safe investments, such as money market funds and short-term CDs. Use a second bucket for discretionary expenses, such as travel, putting that money into short- and intermediate-term bonds. (With current interest rates, you won't get much additional yield over the first bucket, but that will change as rates go up.) The remainder would go into

■ **THE LONGS ARE NOW FULLY RETIRED, ENJOYING A MORE LEISURELY LIFE AT THEIR OCEAN PINES, MD., HOME.**



a third bucket, a mix of stock and bond funds. You replenish the first two buckets by rebalancing and taking profits from the third.

Or use just two buckets, one to cover expenses and the second to nurture growth. Patrick Horan, of Horan Capital Management, in Hunt Valley, Md., encourages his clients to set aside three to five years' worth of expenses in cash and supersafe investments and put the balance—up to 80% of their portfolio—in what he deems to be undervalued stocks. When the stocks hit his assessment of fair value, he sells, using the money to replenish the first bucket. "Most people don't accumulate wealth because they're not taking advantage of growth over time," says Horan.

An annuity also works with the two-bucket strategy: You use the income from an immediate annuity plus Social Security and any pensions to cover your fixed expenses and let your growth investments ride. You'll hedge your bets even further by buying an inflation-adjusted annuity, although you'll receive a lower initial payout.

The bucket strategy does present a couple of problems: Unless you rely solely on guaranteed income, your

portfolio will become increasingly conservative as you sell stocks to replenish the first bucket, skewing the mix, says Tracy Burke, a certified financial planner in Harrisburg, Pa. "At some point, you end up with one big bucket." Also, you may be forced to sell stocks at a bad time, depending on when you need to refill the bucket used for basic expenses. And your bucket strategy may compete with your tax strategy (see page 49). If you decide to use this strategy, consult a financial adviser. In fact, that's good advice to follow before you settle on any arrangement.

● ● ●

So how are the Longs faring, six years after retiring into that disastrous bear market? Quite nicely. Other than an occasional return to the classroom for Bob, the couple are now fully retired. Not only are they enjoying a more leisurely existence (including crafts for her, golf for him), but Bob is back to checking his investments regularly. "Right now, I can keep an eye on the stock market every day. I'm a numbers guy. I'll look just for the fun of it. That uncertain feeling of 2008 and 2009—we don't have that anymore." ■

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\*In determining the funds on the MONEY 70®, the staff of MONEY® Magazine based its decision on each fund's fees, stewardship, experienced managers, and performance. The ending date for performance was 12/10/12. Note: The 11 T. Rowe Price target-date retirement funds are counted as one fund on this list. (The T. Rowe Price Retirement Income Fund is not considered a target-date retirement fund.) From MONEY® Magazine, January/February 2013 ©2013 Time Inc. MONEY and MONEY 70 are registered trademarks of Time Inc. and are used under license. MONEY and Time Inc. are not affiliated with, and do not endorse products or services of, T. Rowe Price. \*\*The same nine funds made MONEY Magazine's 2012 "MONEY 70" list with the exception of the Diversified Mid-Cap Growth Fund; last year, the International Bond Fund was included on the list.  
T. Rowe Price Investment Services, Inc., Distributor.

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# Add an Annuity to the Mix

Use our strategies to lock in higher lifetime payouts. **BY KIMBERLY LANKFORD**

**A NUMBER OF STRATEGIES CAN HELP YOU** stretch your retirement savings over your lifetime. But when it comes to choices you control, only an annuity guarantees that your income—or a portion of your income—will continue no matter how long you live.

You can integrate an annuity into your retirement income strategy in a variety of ways (see “Make Your Money Last,” on page 46). One popular method is to add up your regular expenses (such as housing, food, utilities, insurance premiums and out-of-pocket health care costs) and subtract any guaranteed sources of income (such as a pension and Social Security). Then buy an immediate annuity to provide enough income to fill in the gap. Once you know those costs are covered, you can invest the rest of your money more aggressively—providing extra funds to keep up with inflation, cover emergencies and other large outlays, or leave to your heirs.

The simplest way to provide lifetime income is with a single-premium immediate annuity: You hand over a lump sum to an insurance company when you retire, and it pays you a regular check for life (or for as long as you and a beneficiary live) starting right away. (With a deferred variable annuity with lifetime income benefits, another flavor of annuity usually sold to preretirees, you invest a chunk of money in mutual-fund-like accounts in exchange for a promise of a stream of income in the future.)

Immediate annuities may be simple, but they come with a couple of caveats: Because this type of annuity has fixed payouts that usually aren’t adjusted for inflation, and because you can’t re-

claim the money once you commit it, you should invest only enough to help cover regular expenses and no more. More problematic are today’s low interest rates; now is not a good time to lock in a fixed payout for the rest of your life.

“Because of historically low interest rates, an investor who purchases an immediate annuity now may be solving an emotional dilemma—fear of market risk or fear of loss of income—at the expense of their financial best

interest,” says Tim Maurer, a certified financial planner in Hunt Valley, Md. For example, if a 65-year-old man invests \$100,000 in an immediate annuity now, he’ll receive about \$6,900 per year for life—about \$1,800 a year less than if a 65-year-old had bought the annuity five years ago. Low rates translate into lower payouts because the insurer earns less on its money.

You can combat lower payouts a couple of ways: by laddering annuities or by buying a relatively new product



MARC ROSENTHAL

that guarantees heftier payments if you pick a date down the road to begin receiving them.

## ●● THE ANNUITY LADDER

One way to avoid locking in too much money at low rates is to buy an immediate annuity now with a portion of your savings and invest more in annuities every few years. Payouts will be higher because you'll be older; they'll also increase if interest rates rise.

Michael Ritschel of Colorado Springs retired four years ago as a financial consultant. He receives a small pension and Social Security, but most of his retirement income comes from his own savings. Ritschel, who is 73, has 20% of his portfolio in fixed-income investments and 60% in dividend-paying stocks. He plans to put the rest of his savings in immediate annuities to cover living expenses for himself and

his wife. He recently bought his first annuity and plans to make two more purchases over the next six years. "My goal is to have enough income to cover the necessities and to provide growth with income that will keep up with inflation," he says.

The older you are when you buy an annuity, the higher the annual payouts—assuming interest rates don't fall further. For example, a 73-year-old man who invests \$100,000 in an immediate annuity now could get \$8,820 per year for life; a 75-year-old could get \$9,432 per year for life; and a 77-year-old could get \$10,200 per year for life. If interest rates rise by the time the man purchases the annuities, the payouts will be even higher.

You'll receive the highest payouts if you choose a life-only annuity, which stops paying when you die. (Ritschel chose that version because he already has a universal life insurance policy, with his wife as the beneficiary.) You'll receive a lower annual payout if you buy an annuity that pays out as long as you or your spouse lives. If you're worried that you might both die early, you can choose an option that guarantees payments (to you or your heirs) for at least ten years. A 70-year-old man who invests \$100,000 in a single-life annuity could get \$7,956 per year, or he could get \$6,684 for payouts that continue as long as either he or his wife (also 70) lives. The income would be \$6,588 per year if payouts continue as long as either spouse lives or for at least ten years.

Having the annuities to cover his retirement expenses allows Ritschel to feel comfortable investing his remaining savings more aggressively, because he won't need to sell his investments in a down market to pay his bills.

## ●● DEFER THE INCOME?

Annuities can protect against outliving your income, but you don't really benefit from that protection early in retirement. For that reason, academics and actuaries have embraced products that delay payouts until much later—

### ✦ KipTip

## Where to Shop

### COMPARE PRICES FOR IMMEDIATE

annuities at [www.immediateannuities.com](http://www.immediateannuities.com), which provides payout quotes for many top annuity companies. A 70-year-old man who invests \$100,000 in a single-life immediate annuity now can get annual payouts ranging from \$7,140 to \$8,148, depending on the company. Immediate annuities are generally structured the same, so you can usually pick the annuity with the most generous payout. But be sure to look at the insurer's financial-strength rating, because you may need the payouts to continue for 20 or 30 years. ImmediateAnnuities.com provides three financial-strength ratings for each insurer from which you get quotes. Also look at the ratings in relation to other insurers that are offering similar payouts. You may want to go with an insurer that has a slightly lower payout if it has a much higher financial-strength rating.

typically your seventies or eighties—when you're most concerned about outliving your savings. "If you focus your longevity-risk thinking on those later years, it's less expensive," says Tom Terry, president-elect of the American Academy of Actuaries.

Several years ago, a few insurers introduced "longevity insurance" annuities that paid out beginning when you turned 80 or 85. The payouts were high because many people didn't live that long—and as a result received nothing. But few consumers were willing to take the risk of losing the money if they died before payouts began.

New York Life was among the first to revise the product to allow people to start receiving income much earlier. You may choose to defer the payments for from two to 40 years (although you may have to start taking payments by age 70½ if the money is in a retirement plan subject to required minimum



distributions; see the box below). The longer you defer the payments, the higher the annual income. (You can usually change the date once before payouts begin.) In the meantime, you know the rest of your money needs to last only until the annuity payouts begin. These deferred-income annuities have become popular, with more than \$1 billion in sales in 2012.

If a 65-year-old man invests \$100,000 in New York Life's Guaranteed Future Income Annuity and defers payments until age 70, he'll receive \$10,370 per year for life. If he defers payments until age 75, he'll get \$17,270 per year. Plus, unlike the earlier versions of longevity insurance, you may choose

a cash refund option, which promises that you or your heirs will get back at least as much as you originally invested, even if you die early. But the annual payouts are much lower than they are with the version that stops payments as soon as you die—which can be a good option if you have life insurance or if your spouse isn't dependent on the income. Choose the version with the refund option and you'll get \$8,800 per year starting at age 70 or \$13,840 per year starting at age 75.

In 2003, Barbara and Wallace Tucker, both college administrators, bought a ranch overlooking a small lake in Wolfe City, Tex. They retired there in 2006, when they were both

62. They didn't have pensions and wanted income to help pay their bills, but they didn't know if they would return to work or make other big changes, so they didn't want to tie up too much money in a life annuity. The Tuckers worked with Northwestern Mutual adviser Tom Weilert to convert their retirement savings into income.

Weilert advised them to take one-third of their retirement savings, which had been invested in stock funds, and shift it into a seven-year fixed annuity to help cover their expenses during the early years of retirement. With enough income to pay their bills, they didn't have to sell stocks during the market downturn of 2008. The term on their fixed annuity is nearing an end, so they invested one-third of their remaining retirement savings in a deferred-income annuity from Northwestern Mutual that will provide guaranteed payouts later on.

Nine companies now offer deferred-income annuities, and at least another eight are planning to offer them in the next year or so, says Jafor Iqbal, associate managing director of retirement research for Limra, an insurance research and consulting firm. Fidelity has a marketplace for these annuities in which you can compare versions from four insurers: New York Life, MassMutual, Guardian and Principal (go to [www.fidelity.com/annuities/deferred-fixed-income-annuities/](http://www.fidelity.com/annuities/deferred-fixed-income-annuities/) compare).

Northwestern Mutual has a policy that also pays dividends, which the Tuckers bought. Each year, you can choose either to reinvest the dividends or to receive all or part of the dividends as additional payouts, for extra flexibility. Barbara returned to work in 2011 to set up a nursing program at the Texas A&M Commerce campus, so the Tuckers plan to defer the payouts for several years. Meanwhile, they're reinvesting the dividends. "We'll see what our needs are and whether we'll be self-sufficient without the dividends," says Barbara. ■

## ✱ Strategies

# HOW ANNUITIES ARE TAXED

### THE CONVENTIONAL ADVICE IS TO AVOID

investing in a deferred annuity within a tax-deferred retirement account because the retirement account already has the benefits of tax deferral. But now that more people are buying annuities for their lifetime income guarantees rather than their tax benefits, investing in immediate or deferred income annuities within retirement accounts is gaining popularity.

Taxable annuity payouts are always taxed at your ordinary income tax rate—not the lower capital gains rates. If your annuity is in a traditional

IRA, 401(k) or retirement account in which all of your contributions were pretax or tax-deductible, all of the payouts will be taxed as ordinary income. (If the annuity is in a Roth IRA, all of the withdrawals will be tax-free as long as you've had the Roth for five years and are over 59½.) If you have a deferred-income annuity in a tax-deferred retirement plan and have to take required minimum distributions at age 70½, you may not be able to defer payouts past that age.

If you invested after-tax money in the annuity, the way you take the money can make

a big difference. If you have an immediate annuity or if you choose to convert a deferred annuity into a lifetime income stream (called "annuitizing"), then a portion of each payout is considered to be a tax-free return of principal and a portion is taxable earnings. The principal is returned in equal tax-free install-

ments over the payout period. If you have a life annuity with payouts that stop when you die, for example, then the payout period is the IRS's life-expectancy number for someone your age. Divide your contributions by that life-expectancy number, and you'll owe taxes only on the

portion of each payout beyond that. (If you live longer than the IRS tables anticipate, you'll owe tax on 100% of each payment after you have recovered your investment.)

If you take deferred annuity withdrawals on your own, instead of locking in lifetime income, all of the early payouts are considered taxable earnings, and payouts after that are treated as a tax-free return of principal. If you withdraw the money in a lump sum, then you owe taxes on the difference between your original contributions and the amount you receive when you cash out.





INSIDER INTERVIEW: ALICIA MUNNELL »

# Fill the Gaps in Your Income

Reverse mortgages and longevity insurance will be critical. **BY JANE BENNETT CLARK**

*Alicia Munnell is the director of the Center for Retirement Research at Boston College.*

## **KIPLINGER'S: WHY THE BIG SHORTFALL IN RETIREMENT SAVINGS?**

**MUNNELL:** People are living longer, so the retirement span has increased. They face rapidly rising health care costs, and given low interest rates, they need a bigger pile of money than they did in the past. At the same time, the full retirement age for Social Security has risen. Medicare premiums are deducted from Social Security benefits, and those premiums are going up. Plus, in a few years, the typical person will be paying taxes on a portion of their Social Security benefits. That's because the income thresholds that determine whether you pay taxes are not adjusted for inflation or the earnings growth that workers experience over time.

**DO LOW INTEREST RATES CONTRIBUTE TO THE PROBLEM?** Interest rates are not that big a deal for low-income people because they don't have anything to invest. As you go up the income scale, interest rates have an increasing effect; the income people get from their money is just smaller. For people who are taking out reverse mortgages and annuitizing the amount, lower interest rates have two effects: On one hand, they can borrow a bigger amount because of the way the loan is structured. But when they annuitize the money, lower rates produce less income.

**WHAT ROLE DO YOU THINK REVERSE MORTGAGES SHOULD PLAY?** For most



■ ALICIA MUNNELL BELIEVES THAT WE NEED TO SET UP A NEW TIER OF MANDATORY RETIREMENT ACCOUNTS.

people, their house is their largest asset. And to date, all the evidence has shown that people really don't tap their home equity until the end of life. They're saving it in case they have a major health event. I think to have anything close to a secure retirement, they need some way to tap their home equity earlier. Moving to a less-expensive house could help, or they could get a reverse mortgage. [Editor's note: Munnell has invested in a reverse-mortgage company.]

#### **HOW FAR ARE WE FROM REVERSE MORTGAGES BECOMING WIDELY AVAILABLE?**

Miles. About 2% of those eligible for reverse mortgages take them. People feel they've spent their whole life paying off a mortgage, and the idea of getting in debt again is not very appealing.

**HOW MUCH INCOME SHOULD YOU TRY TO REPLACE IN RETIREMENT?** The retirement-risk index we put out has calculations for different income groups and factors in whether you own a home or don't own a home, whether you're single or married. We give a range, but my rule of thumb is about 80% of preretirement income.

**IT'S BEEN ARGUED LATELY THAT \$1 MILLION IS NOT ENOUGH TO MAINTAIN A COMFORTABLE STANDARD OF LIVING IN RETIREMENT. IS IT ENOUGH?** It's certainly enough for the average person. I think the point was that for anybody with any moderate amount of wealth, it doesn't provide a lot.

**DOES INVESTMENT STRATEGY MAKE A BIG DIFFERENCE?** Yes, if you're talking about younger people or higher-income people. But the average household has about \$120,000 in retirement savings. It doesn't make sense to spend a lot of time worrying about how that \$120,000 is invested. There are more important levers. One is how long you work. Another is controlling your expenditures as you're approaching retirement—or at least not kicking

up your heels too much when you've paid off your mortgage and your kids are through college. Then you can assure yourself of a more stable standard of living.

#### **ARE MOST PEOPLE WHO WANT TO WORK**

**LONGER ABLE TO?** Even for healthy people, it certainly hasn't been easy in the past four or five years. Then you've got people who have either disabilities or health issues, or their skills are outdated, or their job has gone away. So it's not possible for everybody. But I'm convinced that for people who can, working longer is the best possible thing they can do to ensure a secure retirement.

**“For people who can, working longer is the best thing they can do to ensure a secure retirement.”**

**WHAT DO YOU THINK OF INSURANCE-TYPE PRODUCTS THAT SPEAK TO THE FEAR OF RUNNING OUT OF MONEY?** I'm a great fan of longevity insurance, or advanced-life deferred annuities. You buy them at 65, and they start paying you money at 85. (For details on new types of deferred-income annuities, see “Add an Annuity to the Mix,” on page 54.) I think they would be helpful because people are so fearful. There's a concern that people will use their retirement money to go off on a trip around the world. But I'm absolutely convinced that the greater risk is that they are going to be too cautious. So if we had something that assured people that if they lived to 85, this monthly income would kick in, not only would it provide a signal that people don't have to worry, but it would also tell them that they can

spend their money now because they will have a new source of income later.

#### **ARE ANNUITIES AN OPTION FOR PEOPLE**

**WITH \$120,000?** It might make more sense to use that \$120,000 to support yourself if you have to retire before, say, age 70, and postpone claiming your Social Security benefit (see “Make Your Money Last,” on page 46). In effect, you're buying an annuity through Social Security, which is the cheapest annuity in town.

#### **HOW CAN PEOPLE PREPARE TO PAY THE BILL FOR LONG-TERM CARE, IF NECESSARY?**

I think we need catastrophic long-term-care insurance—something that would make you responsible for the first year of expenses, after which the policy would kick in. That way you would know what you were on the hook for.

#### **YOU'VE SAID THAT THE U.S. NEEDS A NEW MANDATORY TIER OF RETIREMENT ACCOUNTS. CAN YOU TALK ABOUT THAT?**

Our retirement system is simply too small. Social Security is going to replace less, and what people have in their 401(k) accounts is inadequate. So we need an additional tier, initiated by the federal government but managed by the private sector, that would replace about 20% of preretirement earnings. This would be mandatory, in addition to the voluntary 401(k) system. Contributions would come out of the employee's income and be part of the total compensation package.

**WHAT'S YOUR TAKE ON 401(K) FEES?** They are a major issue. If you pay an extra 100 basis points [one percentage point] over a 40-year career, it reduces your pile at retirement by about 20%, so that's a big deal. Boston College recently closed one of its investment choices—which had annual expenses of 43 basis points—to new contributions and replaced it with a similar fund that has annual expenses of seven basis points. That has to be in response to somebody telling them that they're not doing a good job. ■





ILLUSTRATIONS BY BEN VOLDMAN

## HEALTH CARE »

# Get Ready for Obamacare

If you buy coverage on your own, here's what you need to know. **BY KIMBERLY LANKFORD**

### THREE AND A HALF YEARS AFTER

President Obama signed the Affordable Care Act into law, its major provisions are nearly ready for prime time. Beginning January 1, insurers will no longer be able to reject people or charge higher rates because of preexisting conditions; the premiums they charge older people will be capped; most plans won't be able to impose annual or lifetime caps on coverage; and to control the cost of insuring the older and sicker, everyone—including the young and healthy—must have health insurance or face a penalty. In 2014 the penalty is 1% of annual income or \$95 per person (whichever is higher); the penalty increases to 2.5%

of income or \$695 per person in 2016.

If you don't have health insurance through an employer—because you're self-employed or unemployed, you work for an employer that doesn't offer health benefits, or you simply decided to go bare—you may be eligible to receive a subsidy to help reduce your premiums. But to qualify, you have to buy a policy from your state's new health insurance exchange. If you work for an employer that does offer coverage, you can still choose to shop on the exchanges, but you can't get a subsidy if your employer provides "affordable" coverage. *Affordable* means the employee's share of premiums for employee-only coverage is

no more than 9.5% of household income. The employer's plan must also be considered "adequate," which means it covers 60% of the average health care costs in the area (based on a complicated actuarial calculation).

Because of the health care law's new protections, young, healthy people won't get as big of a break on premiums and are likely to pay higher rates than in the past. Older people may pay less, especially if they have health conditions that jacked up their premiums. But the changes will depend on your state's current rules, competition in the marketplace and the level of coverage you have now.

The majority of people, who get



health insurance through an employer, won't see much change in their coverage or how they buy it when they re-up during their employer's open-enrollment season. Employers are unlikely to drop coverage just because the government delayed the requirement to provide insurance until 2015. Rather, expect to see cost-cutting trends continue: increases in premiums, steeper deductibles and co-payments, and shrinking provider networks.

### ●● BUYING ON THE EXCHANGES

Each state will have an exchange (also called a marketplace) where you can buy health insurance and apply subsidies to reduce your premiums. The federal government is running the exchanges in 27 states, and 23 states plus the District of Columbia are running their own exchanges or operating them in partnership with the federal government. The insurers on the exchange, policy details, prices and networks will vary by state, no matter who runs the exchange. You can find

links to your state's exchange at [www.healthcare.gov](http://www.healthcare.gov). In most states, you can buy a policy through your state's new health insurance exchange or outside the exchange, but you can get a subsidy only if you buy on the exchange.

Starting in 2014, all individual health insurance plans must include ten essential health benefits, including coverage for preventive tests, hospitalization, maternity and newborn care, emergency-room care, and prescription drugs. Plans sold on the exchanges must fall into one of five categories: platinum, gold, silver, bronze and a catastrophic policy available only to people under age 30.

Each level must meet certain actuarial requirements. A platinum policy, for example, must cover 90% of average health care costs (based on an actuarial calculation for a "standard population" in your area); a gold plan must cover 80%. But that doesn't translate into a fixed set of deductibles and co-payments at each level. In general, you can expect the highest

deductibles (as much as \$6,000) and more cost sharing (such as higher co-payments and coinsurance) at the bronze level, says Ray Smithberger, Cigna general manager for individual and family plans.

As you climb the metal tiers, deductibles and cost sharing will generally be lower, but premiums will be higher. You'll pay the highest premiums (and get the most coverage) at the platinum level. But the premiums can vary a lot within each metal level, depending on the specifics of the coverage and network. On the Maryland Health Connection, a 25-year-old non-smoker in the Baltimore area would pay from \$131 to \$237 per month for the bronze plan, depending on the insurer. A 50-year-old would pay from \$267 to \$470 per month for the silver plan. Many insurers will offer policies eligible for health savings accounts at all levels.

One of the biggest differences will be the size of each plan's network, says Carrie McLean, director of customer

## How the Law Affects You

### >> PREEXISTING CONDITIONS WON'T MATTER

You can no longer be denied coverage or charged steep premiums because of a preexisting condition—or qualify only for insurance that excludes your medical condition. And you won't have to stay in a job longer than you want to in order to keep your health benefits. If you already have nongroup coverage, you should be able to find a better deal than you have now, even if you don't qualify for a subsidy. So check out the new options as soon as you can on October 1.

When you comparison-shop policies, see what the out-of-pocket costs would be for the types of doctors' visits and procedures you tend to have, how much you would need to pay for your medications, and whether your doctors and hospitals are covered in the plan's net-

work. Do the math to estimate whether it's better to pay extra for a gold or platinum policy that has higher premiums but may have lower out-of-pocket costs.

If you have a policy through a high-risk pool now, find out what will happen to that coverage on January 1. The federal Pre-Existing Condition Insurance Plan will be discontinued on December 31, but some of the state programs may let you keep your current coverage, at least until your policy expires in the middle of next year. Ask your plan about your options, and see the status report at [www.naschip.org](http://www.naschip.org) for more information.

### >> EARLY RETIREES CAN BREATHE EASIER

Many retirees who quit their job before Medicare benefits kicked in have had to scramble to find affordable insurance. That's especially true if they worked for

an employer that doesn't provide retiree health coverage.

In the past, early retirees with preexisting conditions tended to keep their employer's coverage through COBRA, the federal law that requires companies with 20 or more employees to let workers stay on their health plan for up to 18 months. But COBRA coverage can be expensive because you have to pay both your share and the employer's share of the cost (employers typically pay about 70% of the cost for employees).

You'll still be able to keep COBRA coverage after 2014, but you may find a better deal on your own, now that you can't be rejected or charged more because of your health. Also, premiums for, say, a 64-year-old can be no more than three times as much as they are for a 21-year-old, whether you buy coverage on or off the exchanges.

You can get the subsidy only if you buy a policy from your state exchange, and it's a good idea to run the numbers using the tool at your exchange's Web site to see whether you qualify. Even if you earned too much to get the subsidy while working, you may qualify after



care for eHealthInsurance.com. When assessing your options, compare the premiums and out-of-pocket costs for the type of care you tend to use, and make sure your providers are included.

Many companies are also selling policies outside of the exchanges, which could be worth considering if you don't qualify for a subsidy, or you qualify for only a small one. These policies must meet most of the same requirements as those on the exchanges, but they may have different networks and other small variations that can help reduce premiums. Some companies will sell policies on the exchanges in some states and off the exchanges in others. You can buy off-exchange policies directly from the insurers, through a health insurance agent (see [www.nahu.org](http://www.nahu.org)) or on a Web site, such as eHealthInsurance.com. If you already have a policy on your own, you may be able to keep it at the current cost until the policy's renewal date later in

2014 (a few states are requiring people to start new policies on January 1).

### ●● HOW TO GET A SUBSIDY

To qualify, your modified adjusted gross income must be between 100% and 400% of the federal poverty level (400% of the federal poverty level in 2013 is about \$46,000 for an individual and \$94,000 for a family of four). A study by Avalere Health, a health care consulting firm, estimates that 40% of individuals who have nongroup health insurance—and 46% of people who are uninsured—will qualify. (For a definition of modified adjusted gross income, see [kiplinger.com/links/agi](http://kiplinger.com/links/agi).)

The size of the subsidy is the difference between the amount you're expected to contribute based on your income and the cost of the benchmark plan in your state. For example, if your modified adjusted gross income is \$70,650 for a family of four, you're expected to pay 9.5% of your income, or \$6,712, toward the benchmark plan's premiums. If that benchmark

plan costs \$12,500, you'd get a tax credit worth about \$5,790, according to Families USA. (You don't have to do the math yourself. You can calculate your subsidy with the Kaiser Family Foundation's subsidy calculator at [www.kff.org/health-reform](http://www.kff.org/health-reform) or, after October 1, on your state's health insurance exchange Web site.)

You can buy a plan that costs more or less than the benchmark, but your subsidy will remain the same. Anyone with income below 250% of the federal poverty level (\$28,725 for an individual in 2013) can also get a cost-sharing subsidy that reduces co-payments and other out-of-pocket costs, but only for silver plans.

Subsidies come in the form of advance tax credits that reduce what you pay for a policy. When applying for the coverage on the exchange, you estimate your income for the year. The figures will be adjusted when you file your 2014 taxes. If you earn more than you reported, you may have to pay back some of the credit. ■

you leave your job and your income drops.

The subsidy is an advance tax credit—the money will be applied to your premiums immediately when you buy coverage on the exchanges, based on the income you've reported. When applying for coverage on the exchange, estimate what you expect your income will be by the end of the year, including the drop after you stop working.

Compare the cost of buying your own policy with the cost of keeping coverage through COBRA (which doesn't qualify for the subsidies). And compare the coverage and networks. You may want to keep COBRA, even if it costs slightly more, if your doctors and providers aren't covered under the new policies, especially if you're currently undergoing medical

treatment, says Karen Pollitz, senior fellow for the Kaiser Family Foundation.

### » YOUNG ADULTS MAY PAY MORE

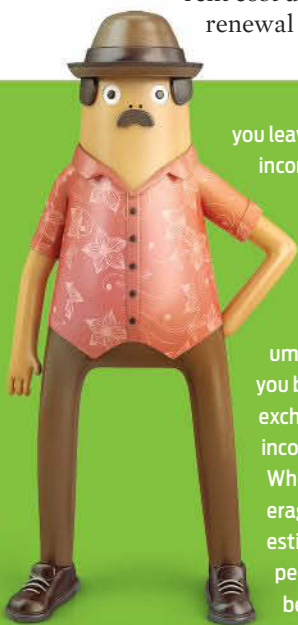
Young adults—and in many cases, parents who were subsidizing them—already got a major perk from the health care law starting in September 2010, when they were permitted to stay on parents' policies up to their 26th birthday. That's true whether or not you live at home, are still in school or are a dependent for tax purposes. In most cases, staying on your parents' policy is still the best deal, especially if they already have to pay for family coverage for younger siblings.

But if you live in another city that isn't covered by your parents' network, or if your parents aren't covering other children and have to pay a lot extra to keep you on their policy, compare the cost of buying coverage on your own. Unfortunately, healthy young adults looking for coverage on their own are likely to face some of the steepest premium increases under the new law. In most states, you can currently find policies for about \$100 to \$200 per month (except in a few high-cost states, such as New York). Those prices are likely to increase, although the new policies

may be more comprehensive. In California, for example, a 25-year-old will pay an average premium of \$250 per month for a silver policy.

Avalere Health estimates that about two-thirds of young adults (age 30 or younger) who are currently uninsured or have nongroup health insurance will be eligible for the subsidies. If you're under 30, you can also buy a special high-deductible catastrophic policy. In California, a catastrophic policy can cost as little as \$141 per month. These policies don't qualify for the subsidies.

If you currently have your own policy—or you buy one before the end of the year—you may be able to keep it at current rates until the year-long policy term is over. Rules vary by state and insurer.





**KIMBERLY LANKFORD** > Ask Kim

## Cut the Cost of Car Insurance

**I'D LIKE TO LOWER MY CAR insurance premiums. What are some of the most common discounts?**

**B.B., MYRTLE BEACH, S.C.**

You'll generally get a discount if your auto and homeowners or renters insurance are with the same company, and you may get an additional discount on all of your policies for adding umbrella coverage. Most insurers give you a break if you are insuring more than one car, or for remaining accident-free for a given number of years.

Most also give a discount for anti-theft devices (such as car alarms, ignition cutoff switches and VIN etchings), anti-lock brakes and special safety features, such as extra airbags. A few insurers, including Farmers and Travelers, offer discounts for hybrids or alternative-fuel vehicles. You usually get a discount for low mileage and might get an even bigger one for installing a tool that tracks the time of day you drive, your mileage, and acceleration and braking rates.

You may get a break for taking a defensive-driver course (although some insurers offer these discounts only to senior drivers or teenagers). If your child is a full-time student and maintains at least a B average in high school or college, a discount of about 15% is typical. Most insurers give you a discount if your child moves more than 100 miles away from home for college and doesn't take a car, but the insurer will still provide coverage while your child is home for vacations.

Several insurers offer discounts for members of the military, and some have special breaks for some professionals (such as teachers) or members of certain groups (such as alumni associations). Most also give you a discount for paying your premium in a lump sum rather than monthly, and for using paperless billing and automatic payments. For Bankrate's recent sur-

vey of the ten largest auto insurance companies, go to <http://tinyurl.com/oxlrj67>.

**Scholarships and 529 plans.** *My daughter was awarded a full scholarship to college, but we've been saving for college for years in a 529 plan. Is there any way that I can get the money out of the 529 without penalty?*

**T.K., ANN ARBOR, MICH.**

You're in luck...again. When you tap a 529 plan, each withdrawal is a combination of contributions (always tax- and penalty-free) and earnings (taxed and usually hit with a 10% penalty if not used for eligible education expenses). But when a scholarship reduces your out-of-pocket costs, you can withdraw up to the amount of the scholarship and owe no penalty on the interest portion of the withdrawal.

**IRA transfers to charity.** *Can anyone transfer money from an IRA tax-free to charity?*

**BOB ROBERTSON, ZEPHYRHILLS, FLA.**

No. Tax-free transfers to charities—capped at \$100,000 annually—are limited to those older than 70½. The transfer lets you count the donation as a required minimum distribution but not report the amount on your tax return. (As the law stands now, this is the last year tax-free transfers to charity will be permitted.) Not reporting the RMD might reduce the portion of your Social Security benefits subject to tax or help you avoid Medicare Part B and Part D high-income surcharges.

If you're under 70½, you can take a taxable distribution, give the money to charity and, if you itemize, claim a deduction for the full amount. If you're older than 70½, you can either make a tax-free transfer to charity or deduct the gift as a charitable contribution, but you can't take both tax breaks for the same contribution. ■

**GOT A QUESTION? ASK KIM AT [KIPLINGER.COM/ASKKIM](http://KIPLINGER.COM/ASKKIM). KIMBERLY LANKFORD ANSWERS MORE QUESTIONS EACH WEEK ON [KIPLINGER.COM](http://KIPLINGER.COM).**



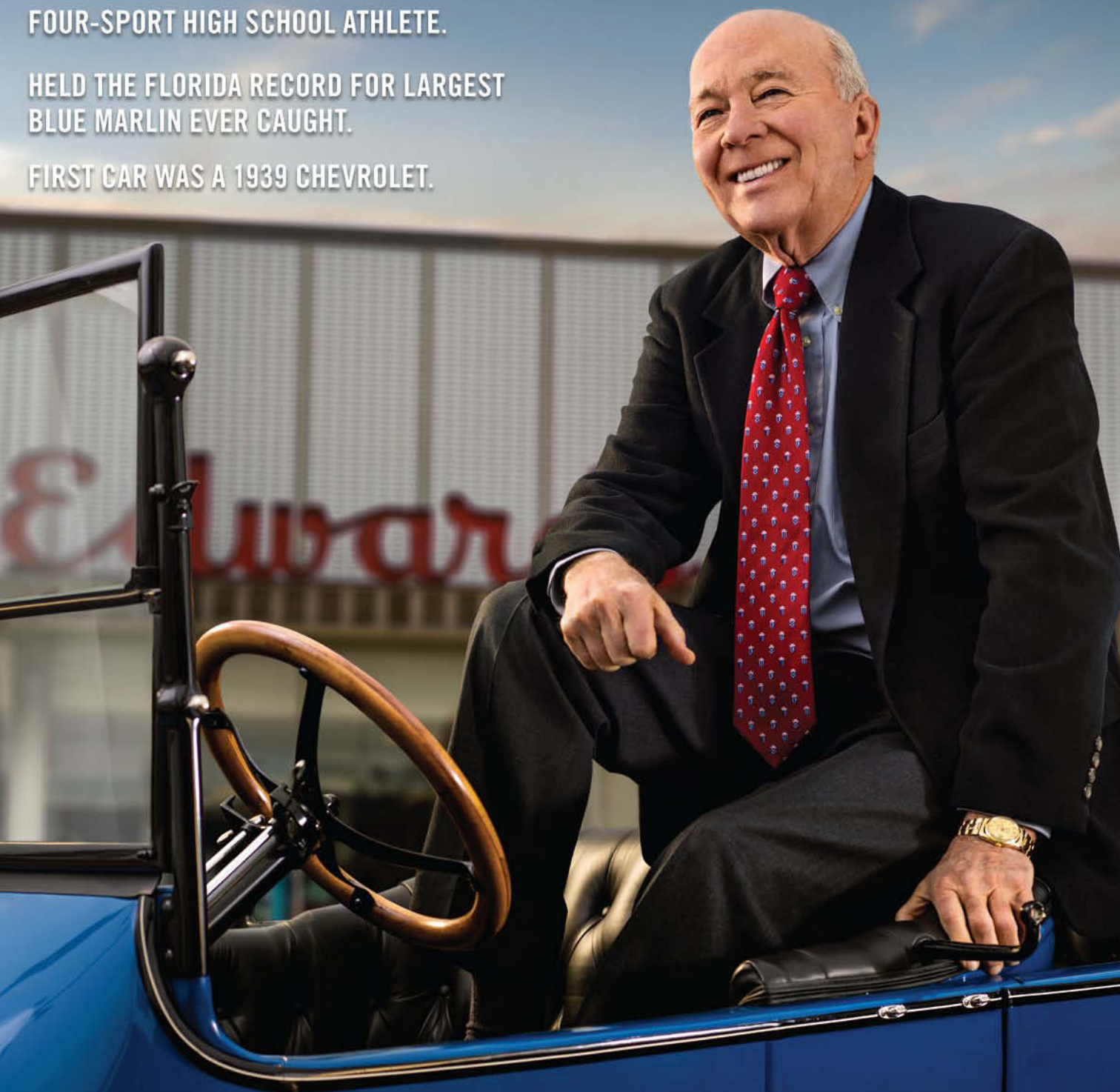
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## CREDIT &gt;&gt;

# Beat a Credit Card Late Fee

**IT CAN HAPPEN TO THE BEST** of us: A credit card bill gets buried in a pile of mail, you miss a payment, and you're smacked with a late fee. Fortunately, federal rules now limit late fees on credit cards to \$25 unless you've missed a payment within the past six months, and the fee can't exceed the minimum payment you owe.

Some issuers have instituted even more lenient policies. For example, the

pair service. The likelihood of getting the fee erased varies, but you may have a better shot if your card is with one of the larger banks, Heath says. And the odds improve if it's your first late payment. If the lender won't budge, suggesting that you'll close your account might do the trick. (But think twice before closing an account: Reducing the amount of credit available to you could hurt your credit score.)

Regardless of whether you end up paying the fee, make sure you send in at least the minimum payment as soon as possible. Your history of on-time payments accounts for 35% of your FICO credit score—more weight than any other factor carries. Generally, the longer you go without paying, the more potential damage to your score. If you pay the bill within 30 days of the due date, the lender might not report the delay to the credit bureaus. But if you let the bill go longer than that, the card issuer is more likely to inform the credit agencies and turn over your case to its collections department. **LISA GERSTNER**

Kiplinger.com

## RATE UPDATES

For the latest savings yields and loan rates, visit [kiplinger.com/finances/yields](http://kiplinger.com/finances/yields).

Citi Simplicity card doesn't charge a late fee, and the Discover It card cuts first-time offenders a break. But even if your card issuer isn't as forgiving, there's a decent chance it will waive the late fee if you call and ask. "If you've been a good customer, you can flex your muscle," says John Heath, directing attorney at LexingtonLaw.com, a credit-re-

YIELD BENCHMARKS	Yield	Month-ago	Year-ago
U.S. series EE savings bonds*	0.20%	0.20%	0.60%
U.S. series I savings bonds	1.18	1.18	2.20
Six-month Treasury bills	0.07	0.08	0.14
Five-year Treasury notes	1.36	1.38	0.61
Ten-year Treasury notes	2.63	2.48	1.51

As of August 2. \*EE savings bonds purchased after May 1, 2005, have a fixed rate of interest.

• Bonds purchased before May 1, 1995, earn a minimum of 4% or a market-based rate from date of purchase.

• Bonds bought between May 1, 1995, and May 1, 2005, earn a market-based rate from date of purchase.

SOURCE FOR TREASURIES: U.S. Treasury.

## TOP-YIELDING MONEY MARKET ACCOUNTS

TAXABLE FUNDS	30-day yield as of July 30	Min. investment	Web site (www.)
Invesco Money Market Fund Inv (INAXX)*	0.09%	\$1,000	invesco.com
Meeder Money Market Retail (FFMXX)*	0.08	2,500	meederfinancial.com
PNC Money Market Fund A (PEAXX)*	0.05	1,000	pncfunds.com
Delaware Cash Reserves A (DCRXX)*	0.05	1,000	delawareinvestments.com
NATIONAL AVERAGE	0.01%		

TAX-FREE FUNDS	30-day yield as of July 29	Tax. eq. yield 25%/39.6% bracket	Min. investment	Web site (www.)
Invesco Tax-Ex Inv (TEIXX)*	0.12%	0.16%/0.20%	\$1,000	invesco.com
Alpine Municipal MMF (AMUXX)*	0.02	0.03/0.03	2,500	alpinefunds.com
PNC Tax-Ex MMF A (PXAXX)*	0.02	0.03/0.03	1,000	pncfunds.com
American Cent T-F Inv (BNTXX)*	0.02	0.03/0.03	2,500	americancentury.com
NATIONAL AVERAGE	0.01%	0.01%/0.02%		

DEPOSIT ACCOUNTS#	Annual yield as of Aug. 2	Min. amount	Web site (www.)
Evantage Bank (Okla.)†§	1.10%	none	evantagebank.com
AmTrust Direct (N.Y.)†	1.05	\$5,000	amtrustdirect.com
Incredible Bank (Wis.)†	0.91	2,500	incrediblebank.com
Sallie Mae Bank (Pa.)†	0.90	none	salliemae.com
NATIONAL AVERAGE	0.11%		

\*Fund is waiving all or a portion of its expenses. †Internet only. #Deposit accounts include money market deposit accounts and high-yield savings accounts. §Similar yields are available at AmericaNet Bank and Redneck Bank. SOURCES: Bankrate.com; Money Fund Report, iMoneyNet Inc. (508-616-6600; www.imoney.net.com).

## TOP-YIELDING CERTIFICATES OF DEPOSIT

1-YEAR	Annual yield as of Aug. 6	Min. amount	Web site (www.)
Colorado Federal Savings Bank (Colo.)	1.00%	\$5,000	coloradofederalbank.com
Palladian PrivateBank (Ill.)†	1.00	10,000	palladianprivatebank.com
Doral Bank (Fla.)†	0.95	500	doraldirect.com
BAC Florida Bank (Fla.)†	0.95	500	bacflorida.com
NATIONAL AVERAGE	0.24%		

5-YEAR	Annual yield as of Aug. 6	Min. amount	Web site (www.)
EverBank (Ohio)†	2.06%	\$1,500	everbank.com
iGobanking.com (N.Y.)†	2.05	1,000	igobanking.com
Barclays Bank (Del.)†	1.65	none	banking.barclaysus.com
First Internet Bank of Indiana (Ind.)†	1.60	1,000	firsttib.com
NATIONAL AVERAGE	0.77%		

†Internet only. SOURCE: © 2013 Bankrate.com, a publication of Bankrate Inc., 11760 US Highway 1, N. Palm Beach, Fla. 33408 (800-327-7717, ext. 11410; www.bankrate.com/kip).

## LOW-RATE CREDIT CARDS

Issuer	Rate as of Aug. 2*	Annual fee	Late fee	Web site (www.)
First Command Bank (P)	6.25%	none	\$25†	firstcommandbank.com
Lake Michigan Credit Union (P)	6.25	none#	25†	lmcu.org
Simmons First Bank Visa (P)	7.25	none	25†	simmonsfirst.com

## RETAIL REBATE CARDS

Issuer	Rate as of Aug. 6*	Annual fee	Rebate earned Store/Other	Web site (www.)
Williams-Sonoma Visa	13.74%	none	3%/1%	barclaycardus.com
Amazon Rewards Visa	14.24	none	3†/1‡	amazon.com/rewards
Costco True Earnings Card	15.24	none§	1/1&	americanexpress.com

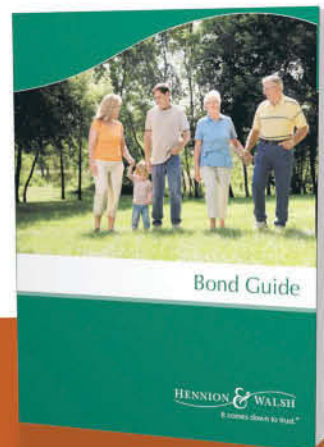
Rates are adjustable. \*If you do not qualify for this interest rate, the issuer will offer a higher-rate card. (P) Platinum card. †\$35 if late more than once in six months. #Must be a credit union member. ‡2 points at gas stations, restaurants, office supply stores and drugstores; 1 point on all other purchases. §Must be a Costco member. &3% on gas (up to \$4,000 annually; 1% thereafter); 2% on restaurants and travel; 1% on all other purchases. SOURCE: Bankrate.com. Banks may offer lower introductory rates.





# Are Tax Free Municipal Bonds Right for You?

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for your free Bond Guide.



## The Main Advantages of Municipal Bonds

Investors are attracted to municipal bonds for three reasons, safety of principal, regular predictable income and the tax-free benefits. Together, these three elements can make a compelling case for including tax-free municipal bonds in your portfolio.

### Potential Safety of Principal

Many investors, particularly those nearing retirement or in retirement, are concerned about protecting their principal. In March of 2012, Moody's published research that showed that rated investment grade municipal bonds had an average cumulative default rate of just 0.08% between 1970 and 2011.\* That means while there is some risk of principal loss, investing in rated investment-grade municipal bonds can be a cornerstone for safety of your principal.

### Potential Regular Predictable Income

Municipal bonds typically pay interest every six months unless they get called or default. That means that you can count on a regular, predictable income stream. Because most bonds have call options, which means you get your principal back before

the maturity date, subsequent municipal bonds you purchase can earn more or less interest than the called bond. According to Moody's 2012 research,\* default rates are historically low for the rated investment-grade bonds favored by Hennion & Walsh.

### Potential Triple Tax-Free Income

Income from municipal bonds is not subject to federal income tax and, depending on where you live, may also be exempt from state and local taxes. Triple tax-free can be a big attraction for many investors in this time of looming tax increases.

### About Hennion & Walsh

Since 1990 Hennion & Walsh has specialized in investment grade tax-free municipal bonds. The company supervises over \$2 billion in assets in over 15,000 accounts, providing individual investors with institutional quality service and personal attention.

### What To Do Now

Call 1-800-318-4850 and request our Bond Guide, written by the experts at Hennion & Walsh. It will give you a clear and easy overview of the risks and benefits of tax-free municipal bonds.



Dear Investor,

*We urge you to call and get your free Bond Guide. Having tax-free municipal bonds as part of your portfolio can help get your investments back on track and put you on a path to achieving your investment goals. Getting your no-obligation guide could be the smartest investment decision you'll make.*

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Without Cost or Obligation

**CALL 1-800-318-4850**

(for fastest service, call between 8 a.m. and 6 p.m.)

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# Cut the Cable Cord

Switching to another video service can save big bucks and reduce hassles.

BY LISA GERSTNER

## THE LONG LIST OF CABLE CHANNELS

that you never watch. The skyrocketing bills—and the battles with your provider's customer-service department to return them to earth. The fees for everything from equipment installation to service calls. // Those are just a few of the reasons why dealing with a cable or satellite-TV provider is so frustrating—and costly. According to the Federal Communications Commission, the average cable bill is \$62 a month, or \$744 a year. And prices can go a lot higher depending on the plan you choose. You could be happier (or at least richer) if you ditched cable and took advantage of the growing options for watching TV shows and movies online instead. // And yet we have





a complicated relationship with our cable providers. A recent survey by CouponCabin.com found that 45% of U.S. adults think that cable TV is a waste of money. But even though the alternatives to paid TV are becoming more compelling, most people are resisting change. About 86% of households with a television set still subscribe to a “multichannel video service,” such as cable or satellite TV, says Bruce Leichtman, president of

Leichtman Research Group. Subscriptions have declined by just one percentage point over the past couple of years. Instead of replacing cable, many customers are *adding* Internet video options to their palette. “It’s more of a supplement than a substitute,” says Leichtman.

That means people are likely spending more money on video than the numbers show. But unless you are addicted to watching *Mad Men* on

Sunday nights or you’re an avid sports fan, you can probably get your TV fix from the Web via streaming video for a lot less money. The usual suspects, such as Netflix and Hulu, continue to provide access to large collections of movies and previously aired TV shows.

And a start-up called Aereo is testing the waters for streaming more TV online. For \$8 a month, subscribers can view programming live from major broadcast networks and local channels and record shows to view later. Aereo is available in a few cities now, and it has plans to expand. The company has clashed in court with broadcast networks about the legality of its business, but so far Aereo has prevailed.

Methods of slinging Web video beyond your PC screen are expanding, too. Google, for example, recently introduced a \$35 device the size of a USB flash drive called Chromecast. Plug it in to any HDTV and you can stream content wirelessly from compatible services, including Netflix and YouTube. Your computer, tablet or smart phone acts as a controller (see the box at left for more on Web-to-TV streaming devices). Video services are also responding to customers’ increasing appetite for viewing programs on their mobile devices by offering smart-phone and tablet applications.

## Stream From the Web to Your TV

**SOME TV SETS HAVE BUILT-IN CAPABILITIES FOR WEB ACCESS, AND MANY BLU-RAY PLAYERS** also have Web access and apps. Or by connecting your laptop to your HDTV with an HDMI cable, you can view anything that appears on your computer screen on the TV. You can also buy an adapter at most electronics stores to use an HDMI cable to connect an iPad or iPhone to a TV.

The devices below connect to your TV to stream content, and many have a broad range of features to choose from. Roku, for example, offers more than 750 channels. With Apple TV’s AirPlay, you need a wireless connection to display what appears on your Apple device on your TV.

SERVICE	PRICE	TOP STREAMING OPTIONS
<b>Roku</b>	Boxes <b>range from \$50 to \$100</b> , depending on picture quality and other features	Amazon Instant Video, Blockbuster On Demand, Crackle, Hulu Plus, MLB.TV, Netflix, NBA League Pass, NHL GameCenter Live, Redbox Instant by Verizon, Vudu
<b>Apple TV</b>	<b>\$99</b>	Hulu Plus, iTunes, MLB.TV, Netflix, NBA League Pass, NHL GameCenter Live
<b>Chromecast</b>	<b>\$35</b>	Netflix, YouTube
<b>Google TV</b>	Boxes that support Google TV range from <b>about \$80 to \$170</b>	Amazon Instant Video, Crackle, Netflix, Redbox Instant by Verizon
<b>WD TV</b>	From <b>about \$60</b> for the basic Play box to <b>about \$250</b> for the Live Hub device	CinemaNow, Hulu Plus, MLB.TV, Netflix, Vudu
<b>Wii</b>	<b>\$130</b>	Amazon Instant Video, Hulu Plus, Netflix
<b>PlayStation 3</b>	<b>Starts at about \$270</b> (PlayStation 4, debuting at the end of the year, is available for <b>pre-order for \$400</b> )	Amazon Instant Video, CinemaNow, Crackle, Hulu Plus, MLB.TV, Netflix, NHL GameCenter Live, Vudu
<b>Xbox 360</b>	<b>Starts at \$200</b> (Xbox One, set for release in November, is available for <b>pre-order for \$500</b> ); to stream video content, you need a <b>\$60 annual Xbox Live Gold membership</b>	Amazon Instant Video, CinemaNow, Crackle, Hulu Plus, MLB.TV, Netflix, NBA League Pass, NHL GameCenter Live, Redbox Instant by Verizon, Vudu

### ●● FIND NEW TV EPISODES

For many, watching TV without paying for it means going back to basics: setting up an antenna to pick up programming on local broadcast stations. Go to [www.antennaweb.org](http://www.antennaweb.org), enter your address or zip code, and the site will pull a list of available TV stations as well as the type of outdoor antenna required to get a signal from each. (Bonus: You may find that your HDTV reception using an antenna is sharper than with cable or satellite.) You should be able to get stations that have strong signals using an indoor antenna (a good one may cost \$40); for weaker signals, you’ll need a good outdoor antenna (\$50 to \$100 or more).



Hulu.com is the hub for viewing TV shows from participating networks online. Typically, you can stream the five most recent episodes of a show's current season free, and programs usually pop up on the site the day after they air on TV. (Fans of Fox shows have to wait eight days after an episode's air date to watch it online—except for subscribers to eligible cable or satellite services.)

Upgrade to the \$8 monthly Hulu Plus service and you'll get access to a wider selection of TV and movies—including full seasons of TV shows—as well as the ability to stream many shows through compatible devices, such as smart phones and the Roku box. If you can't find a show free on Hulu, check the station's Web site (current-season episodes of some CBS shows, for instance, are at CBS.com but not Hulu.com).

If you can't stream a TV show free, look into buying episodes from services such as Amazon Instant Video or iTunes. You may be able to purchase the full season of a show for less. For instance, buying the 22 episodes of *Scandal's* second season in HD on iTunes, at \$3 a pop, would total \$66; buy the full season and you'll pay only \$30. Through Amazon Instant Video, order a TV Pass to get discounted episodes of current-season TV shows as soon as they are released.

Netflix's \$8 monthly streaming service doesn't carry new, current-season episodes of popular network and cable-TV shows (though you'll find previous seasons of many programs). But Netflix has waded into creating original shows, such as *House of Cards* and *Orange Is the New Black*, that have proved popular with viewers. (In fact, the critically acclaimed *House of Cards* is now on sale through other streaming services.) And rather than use the standard model of releasing new episodes periodically, Netflix has made new full seasons available all at once.



#### ●● GET MOVIES ON DEMAND

By watching movies online, you can keep the stacks of DVDs filling your cabinets from getting any higher. To see the newest releases, you'll typically have to rent or buy them individually, rather than use a streaming subscription service. Amazon Instant Video, Blockbuster On Demand, CinemaNow, iTunes and Vudu all have movies that you can rent or purchase on demand.

When you rent a movie, it will be available to you for some period, typically 30 days. You'll usually have one to two days to watch it once you've started it. If you purchase a movie, you can watch it anytime, and you may be able to download it to certain devices. At [www.canistream.it](http://www.canistream.it), enter the name of a movie and the tool shows which services offer the film for rent or purchase and how much you'll pay. If a movie is not available on a service you prefer, you can sign up to get an alert when it arrives.

With the Netflix streaming option, you can access plenty of movies but typically not new and popular ones. If you're a heavy watcher of the latest releases, Netflix's DVDs-by-mail

service may be more cost-effective (though less convenient) than renting movies a la carte from other providers. Redbox Instant by Verizon has a smaller library of older films to stream (no TV shows), but for \$8 a month you also get four DVD rentals from Redbox kiosks, where you'll find newer releases.

#### ●● TRIM YOUR CABLE INSTEAD?

If you prefer not to dump your cable or satellite provider, consider cooling the relationship. If you subscribe to hundreds of channels that you don't watch, downgrade to the basic service. Take stock of whether you're using all the features that your package offers. For example, you could return any cable boxes around the house that you rarely use. If a promotional deal ends and your bill shoots up, call your company and ask whether you can enter a new promotion. Research the offerings of competing services and be prepared to request a price match. Threatening to switch providers may be the prompt the cable company needs to give you a better deal.

A large family may find more value in a cable subscription than

an individual would, says Sam Rosen, of ABI Research, a technology research firm. And the case for cable strengthens if your provider has its own streaming services. HBO subscribers, for example, get unlimited access to the premium channel's content online using HBO Go, and you can stream it to devices such as Apple TV and Roku.

### ●● ALTERNATIVES FOR SPORTS

For an all-around sports enthusiast, a cable or satellite package that includes ESPN and other sports networks is probably the way to go, though you can catch some sports programming on broadcast TV if you install an antenna. At WatchESPN.com, you'll need a paid-TV subscription to access much of the content. But those who use participating Internet service providers can view ESPN3 content through the site, which includes some college athletics, golf, tennis and other sports.

If you're partial to a sport that offers a Web streaming package, you might get by without cable—but you'll often have a hard time catching the home team play because of blackout policies that bar coverage of games in a team's local market. Baseball fan? Subscribe to MLB.TV for \$110 a year and watch live games of any Major League Baseball team

that is not in your region. With the \$130 yearly premium package, you can stream to compatible devices, such as Roku and Apple TV. For National Basketball Association and National Hockey League fans, NBA League Pass Broadband (\$180 early-bird price for the 2012–13 season; 2013–14 prices unavailable) and NHL GameCenter Live (\$169 for a full season in the past) also provide streaming video of live out-of-market games.

In general, DirecTV customers are the only folks who can watch any out-of-market National Football League game live, through the satellite provider's NFL Sunday Ticket package. But if you can't use DirecTV for some reason—say, your landlord won't allow a satellite dish to be installed on your apartment building's roof—you can stream Sunday Ticket online for \$300 in the 2013 season without using regular DirecTV service. ■

## Where to Find TV and Movies Online

**THE SERVICES BELOW ALLOW YOU TO WATCH VIDEO CONTENT FREE, SUBSCRIBE TO A MONTHLY service, or rent or buy movies or individual episodes of TV shows. For video that you can rent or buy a la carte, you may find lower prices than those listed here for older or less popular selections.**

You'll need a speedy broadband Internet connection to stream video without hiccups. Netflix, for instance, recommends a minimum download speed of 1.5 megabits per second to stream its content and at least 5.0 Mbps for HD-quality streaming. You can test the speed of your Internet connection at [www.speedtest.net](http://www.speedtest.net).

SERVICE	PRICE
Hulu	Free for basic service; <b>\$8 a month</b> for Hulu Plus
Crackle	Free
Netflix	<b>\$8 a month</b> for unlimited online streaming; <b>\$8 a month</b> to receive unlimited DVDs by mail (one at a time)
Amazon Instant Video	Rent popular and new movie releases <b>starting at \$4</b> or buy them <b>starting at \$10</b> ; buy recent TV episodes for <b>\$2</b> (\$3 for HD)
iTunes	Rent popular and new movie releases <b>starting at \$4</b> or buy them <b>starting at \$10</b> ; buy recent TV episodes for <b>\$2</b> (\$3 for HD)
Redbox Instant by Verizon	<b>\$8 a month</b> to stream movies online and receive four monthly credits for DVD rentals from Redbox kiosks (where you'll find new movie releases)
Vudu	<b>\$5 or more</b> to rent new movie releases; purchase new movies <b>starting at about \$10</b> ; rent recent TV episodes for <b>\$2</b> (\$3 for HD)
Blockbuster On Demand	Rent new and popular movies that you can stream to compatible devices <b>starting at \$4</b> (\$5 or more for HD)
CinemaNow	Rent new movie releases <b>starting at \$4</b> or buy them <b>starting at \$10</b> ; buy recent TV episodes <b>starting at \$2</b> (\$3 for HD)



# What You Need to Know About Buying a New Car

Use our tips to put yourself in the driver's seat and get the best deal. **BY JESSICA ANDERSON**

**1. Time is on your side.** It's the beginning of the new model year, and dealers are itching to clear space on their lots for the new cars. So now is your chance to get a good price on a 2013 model. For any vehicle you're considering, go to TrueCar.com to compare the average transaction price in your area with the sticker price. Next, head to Edmunds.com, and enter the make, model and trim level to see the dealer invoice price. Click on "Incentives and Rebates" to view current manufacturer offers. That way you'll know how much money dealers get from the carmaker when they make a sale.

**2. Prepare to cross swords.** Salespeople have a host of tactics to boost the car's price—and their commission. They will try, for example, to focus your attention on the monthly payment; to keep it low, they may push you to extend the loan term or to lease instead of buy.

Insist on negotiating the price of the vehicle, whether you're buying or leasing. If the salesperson asks about your trade-in, steer the conversation back to the new car. Lumping the purchase and the trade-in together means the dealership can give you a lower trade-in value and still look as if it's giving you a good deal.

**3. Stand your ground.** If the price is at or near invoice, the dealership is making a profit. Don't waver on your

price if the salesperson leaves the room to "get approval from my manager" only to return and say, "We can't do it." Bottom line: Walking away is the best tool in your arsenal. There are nearly identical cars at other dealers.

**4. Or skip the showroom show-down.** Once you've taken a test-drive and decided exactly what you want, go home. Contact the Internet managers at several dealers and ask for bids. Let them know you're shopping around, and get firm offers via e-mail. If you're a repeat buyer, ask for the "loyalty discount." If you're new to the brand, ask for the "conquest discount." Then take your old car to several dealers and CarMax and sell it to the highest bidder.

**5. Let a pro do it.** A car-buying service lets you skip the haggling and the stress. Free services, such as those from TrueCar.com and

Edmunds.com, offer prices from participating dealers that are guaranteed but may not be the lowest possible. CarBargains, the buying service of the nonprofit Consumers' Checkbook ([www.carbargains.org](http://www.carbargains.org)), charges \$200 to hire its professional negotiators to shop for your car at a minimum of five local dealers. Leasing? Check out LeaseWise ([www.leasewise.org](http://www.leasewise.org)); for \$350, you will get at least five bids.

**6. One more hurdle: F&I.** The finance-and-insurance office is where dealers make a chunk of their profit, so keep your wits about you (and prepare to be there for a while). Come with loan preapproval from your bank or credit union; unless there's a special interest rate from the manufacturer, the bank's financing may be better. Resist pitches for paint sealant, fabric protection and extended warranties; they aren't worth the money. Review the contract to make sure extras you didn't approve weren't added. Fees for shipping and regional advertising are standard, but document fees are suspect. Never pay a floor-plan fee (the cost to hold inventory at a dealership) or a vehicle-preparation fee for cleaning the car, removing plastic and checking fluids. ■





# 3 SIMPLE STEPS

## Earn More on Your Savings

### STEP 1

If you've been a loyal customer of a bank or credit union, see whether your institution will give you a higher interest rate on a savings or money market deposit account. Some banks, for example, offer higher rates on savings accounts if you have a checking account with them, too.

### STEP 2

Compare what your bank offers with high-yielding accounts you find at [www.depositaccounts.com](http://www.depositaccounts.com) and [www.bankrate.com](http://www.bankrate.com). Both tools show nationally available accounts that have the best interest rates, and you can enter your state or zip code to see the accounts from local institutions as well.

### STEP 3

Before you commit to an account, compare fees, such as monthly or annual charges, withdrawal penalties and inactivity fees. Also, check for minimum deposit or balance requirements, as well as any limit on how much of your deposit earns interest. Make sure your account is protected by the Federal Deposit Insurance Corp. or the National Credit Union Share Insurance Fund.

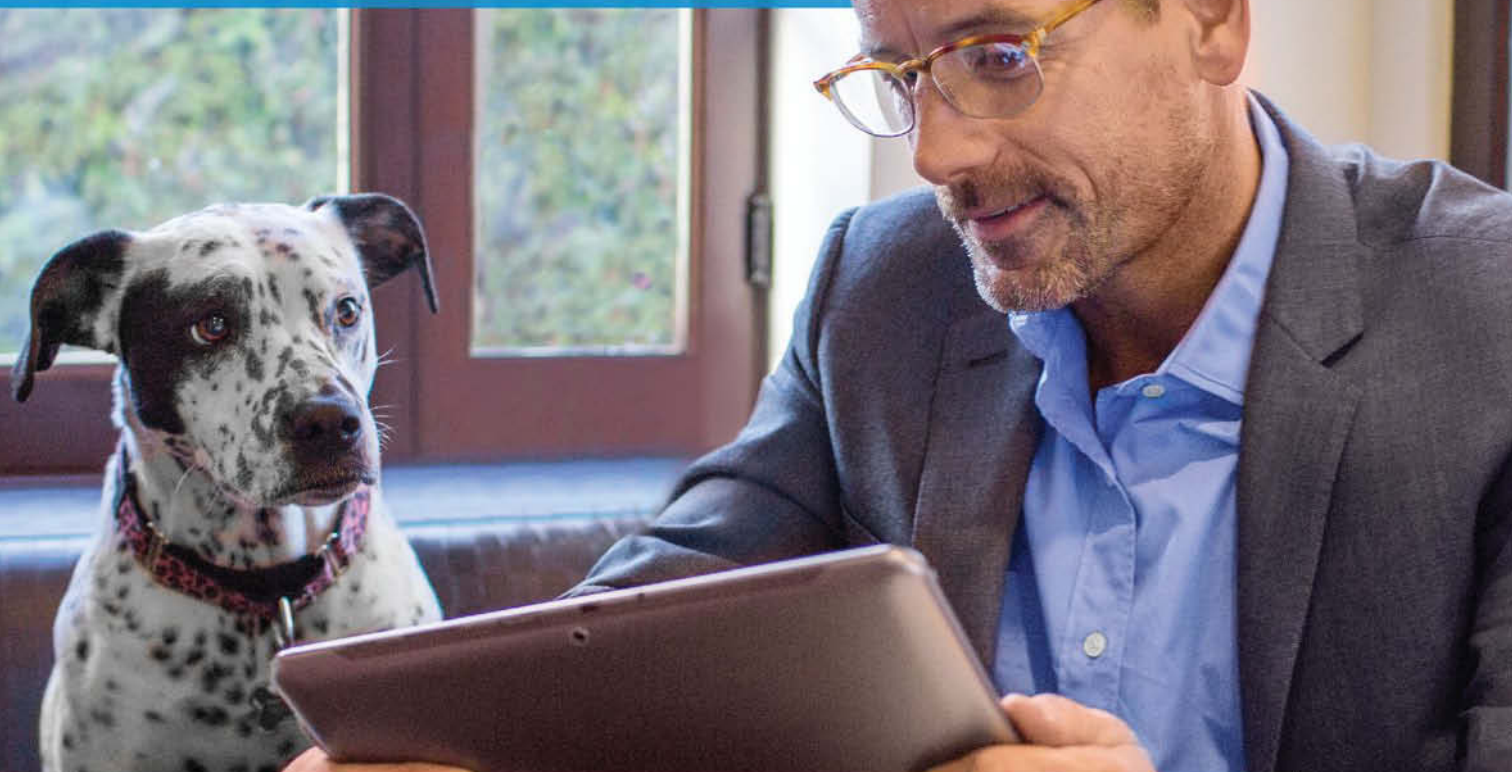
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