Tarheel Advisors Newsletter

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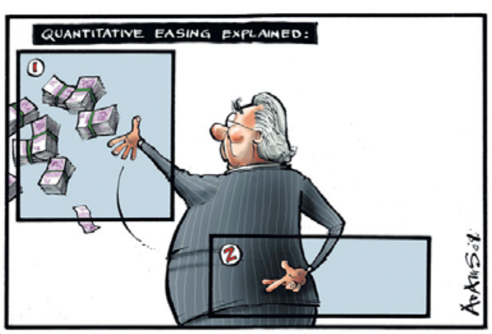
Market Déjà Vu

It's now officially Springtime and we've witnessed the global equity markets start off 2012 with a roar. The numbers are in and the first quarter is the best performance-wise in 14 years. With the S&P 500 and Nasdaq indices jumping double digits thus far in 2012, it's almost like the meltdown last Summer is a distant memory. The headlines no longer dwell on the debt ceiling debate at home or the sovereign debt crisis abroad. So, what has changed?

At the very least, investor perception has certainly tilted to a more positive slant. Part of this is likely due to healthier employment data as well as continued operational improvement for most domestic corporations. The other main factor in recent bullish sentiment definitely comes from the somewhat orderly restructuring (read default) of Greek debt. The Market was able to shrug off the major haircut for bond holders and firmly kick that can down the road as the short-term contagion fears eased in the other troubled countries. The last major contributor to the surprise Market outperformance this year is the European Central Bank (ECB). Like the Federal Reserve has done here in the US over the last several years, the ECB has embarked on its own version of Quantitative Easing. The so-called Long Term Refinancing Operations (LTRO) is designed to stabilize the Euro, forestall any further credit crunch, and shore up troubled European Bank balance sheets with billions of dollars worth of easy money. Sound familiar? That's because we've seen this movie before.

OK. Maybe not this movie exactly, but it's definitely a remake of a Hollywood classic — same storyline, just different actors.



The good news is this time around we have the script and we know how this movie ends. Unfortunately, in the short-term this probably means the global equity markets are in for a hiccup. Just this time last year the US Market was overheating on the bullish sentiment from QE2 and everything looked on track before a Summer swoon. In 2011, the catalyst was the US debt ceiling debacle and the ensuing credit rating downgrade, but the underlying cause is the temporary nature of the stimulus effect associated with Quantitative Easing. Noted portfolio manager and PHD in Economics, John Hussmann, describes QE as having "no durable economic benefit" and a policy that "does little but to repeatedly lay fresh wallpaper over the rotting edifice that is the global banking system." Not exactly the review from critics that Mr. Bernanke was hoping for.

What scenes are in the movie trailer for the rest of 2012? My best guess is we will once again remember that Europe has not solved their structural debt imbalances; but, instead of Greece, we will be hearing much more about Portugal and Spain. Couple that with the waning enthusiasm for the LTRO and money managers taking some early year profits off the table, and you've got a formula for a pullback. On the positive side, the latter part of the year promises to bring an end to a lot of uncertainty related to the Presidential election and expiring tax provisions. Historically, markets respond favorably to a clearer vision of the future, whatever that entails.

Either way, we think that investors would be prudent to watch the preview before paying the full admission price to this movie. Remember, sequels and re-makes are almost always never as good as the original. Putting your portfolio's success in the hands of desperate politicians, debt-laden nations, and spend-thrift Central Bankers is not the way to earn two thumbs up.

-Walter Hinson, CFP®

2012 Market Update

S&P 500	**+12.6%**
DOW	**+8.8%**
NASDAQ	**+18.7%**
MSCI World	**+8.7%**
BONDS	**+.30%**
GOLD	**+6.7%**

Mortgage Rates

15-Year	**3.5%**
30-Year	**4.25%**
5/1 ARM	**3.25%**

Did You Know?

Due to the normal tax day falling on a weekend and an obscure federal holiday the following day, the deadline to file your tax return is Tuesday, April 17th.

For those considering a last minute IRA or Roth IRA contribution, the maximum amount for tax year 2011 is $5,000, plus an additional $1,000 for individuals over age 50.

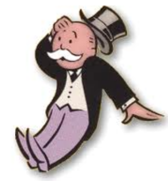
O Canada! — As of March, the Canadian government passed a law raising the retirement age from 65 to 67 in a bid to balance the budget. This change, however, is not scheduled to take effect until 2023.

IRA Bankruptcy Protections

Bankruptcy, Do Not Pass Go, Do Not Collect $200. Few people ever plan on filing bankruptcy, but bad investments, bad luck, or just plain bad decision making can make it a possibility for anyone. Nearly 1.5 million people filed in 2011 alone.

One item that is commonly misunderstood by those in financial hardship is the protections given to IRAs and other qualified investment accounts. Keep in mind bankruptcy law can vary from state to state, but generally speaking retirement plans covered by ERISA such as a 401k or company pension are fully protected when it comes to a bankruptcy petition. Additionally, thanks to the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) there are extended protections for a debtor's IRA or Roth as well. The original law exempted up to $1,000,000 in contributory IRA or Roth value which has since been indexed for inflation up to $1.17 million. This means up to $1.17 million in an IRA can typically not be touched if you file bankruptcy.

Financial advisors are usually quick to recommend investors rollover their 401k/403b/etc. and consolidate them with an existing IRA. While this is usually a time and paperwork saving best practice, one should think twice if total qualified assets are near the $1 million threshold. If one rolls over a 401k account into a rollover IRA it retains the unlimited bankruptcy protection afforded by ERISA. However, if funds are commingled with a contributory IRA they are more likely to be limited to the $1million protection afforded by BAPCPA. So, if you're a business owner, or in a profession at high risk for lawsuits, make sure you're not unknowingly giving up a valuable form of asset protection.



If you've inherited an IRA the answers aren't as clear cut yet. Different states and courts have ruled both ways as to whether or not an inherited IRA is covered by BAPCPA. Until further court precedent is set, one would be wise to hire an excellent bankruptcy attorney before trying to protect an inherited IRA in court.

Given these protections, what should one do when encumbered with unserviceable debt loads? The most common thing debtors do is to start taking early IRA distributions or 401k hardship withdrawals and loans. Unfortunately, by doing so the funds will become subject to creditors during bankruptcy. If you are on the path to certain bankruptcy, qualified accounts should not be tapped prior to filing due to their preferential treatment.

The tough question arises when one is near retirement and having to decide which is more important, tapping retirement funds to pay large sums of debt, or taking the hit to one's credit report and filing for bankruptcy. Many times it is far more advantageous to take the hit to one's credit report than to deplete qualified accounts that are supposed to be providing income over the next several decades.

So in short, if you have significant debt problems try to resist the temptation to spend or borrow against retirement savings. If you're on the path to bankruptcy, it could be the difference between having over a $1million at the end of the day or nothing.

-Ryan Glover, CFP®

Five Mistakes to Avoid if You Have Minor Children

Admittedly if you have minor kids, you are going to make plenty of mistakes. But, by covering some basic estate planning issues once you have children you can avoid the following common problems:

1. **Naming a minor as a direct beneficiary on retirement assets, life insurance or a TOD account.** Do not name a minor as a direct beneficiary…ever! Minor beneficiaries create unneeded administrative problems and usually require the creation of a court ordered guardianship. The added expense often takes a substantial toll on the financial resources intended for the beneficiary.

2. **Not having a Will and assuming that a surviving spouse will inherit the entire estate.** It is true that if a husband and wife own property jointly or have life insurance and retirement that passes by beneficiary designation, then those assets will almost always pass to the spouse even if there is no Will. However, some assets can only be transferred under a Will or by default under the North Carolina intestacy laws. If one spouse has a substantial amount of liquid assets or real estate in his or her individual name and there is no Will, the intestacy laws dictate that some of those assets must be divided between the children and the spouse.

3. **Not having a Will and failing to name a personal guardian for the children.** When a couple has their first child the choice of guardian is typically the most important decision in their estate planning. If something happens to both of them who will become the child's surrogate parent and where will they live? This is a personal and often a very difficult decision, but it is something that deserves attention. Ultimately the courts will decide the choice of guardian, but they rely heavily on the nomination of the parents provided in the Will.

4. **Not having enough life insurance to provide for surviving spouse and children's education.** Even though most families now have two wage earners, this doesn't obviate the need for a decent amount of life insurance to cover the risk that one spouse may die unexpectedly. In that case a surviving spouse is left with the substantial task of raising kids and being the primary source of financial support for the family. Most families also want to ensure that there are enough funds for college education for the children. When all the costs of child care and college education are added up many families simply don't have enough life insurance in place to foot the bill.

5. **Assuming that there are no estate tax concerns if you are just starting to build your net worth.** Most young families start out with a zero net worth and they don't think of themselves as wealthy enough to be concerned about estate tax. However, many of these families have avoided the mistake in number 4 above and have substantial life insurance in place. Remember life insurance is usually counted as part of your estate for estate tax purposes. When the life insurance proceeds are added to other assets many young families are bumped into a net worth that does have estate tax exposure and they need basic tax planning in their documents.

The best advice I can give is simply to begin the process. Talk to your advisors about these issues once you have children.

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