

## THE NORTHWEST QUADRANT

Searching for Income from Stock Dividends

Larry Solomon, MBA, CFP®

Not so long ago, many investors bought stocks specifically for the dividends they paid. Dividends can provide an objective measure of a company's health, value and profitability—one that cannot be manipulated. In the "new normal" of near zero interest rates, record high bond prices, and few compelling opportunities in debt markets, stock dividends are back in vogue. If you can buy shares of a blue chip company like General Electric, Kellogg or Waste Management and pick up an immediate yield of more than 3 percent, why wouldn't you?

The S & P 500 has a current dividend yield of 1.8 percent, but almost 70 companies in the S & P 500 are paying more in dividends than the 3.8 percent average yield now being offered in the U.S. bond market, according to a report by Bank of America and Bloomberg. Furthermore, more companies are beating bond yields than at any other time in the last 15 years.

Today, the ten largest dividend paying stocks in the U.S. are AT&T, P&G, Exxon, Chevron, J&J, Verizon, Phillip Morris, Pfizer, GE and Merck. They pay an average dividend yield of 4.0 percent, over 1.0 percent ahead of the yield on standard 10-year treasury bonds. Their average price-earnings ratio, based on 2010 forward earnings, is 11.7 and their earnings are projected to cover their dividend by a 2 to 1 ratio. Investors are increasingly on the hunt for dividends, in part because they see corporate dividends as acting both as a recession safety net and a recovery inflation hedge.

Many investors believe that using a mix of diversified, dividend-paying stocks is a valid way to beat inflation. But dividend-paying stocks aren't risk free, as anyone who investing in Bank of America, Citicorp, or BP for their dividends will tell you. Here are ways to potentially benefit from stock dividends while managing the risks:

1. Understand tax risk. Currently, most dividends are taxed at a maximum rate of 15 percent, the same as long-term capital gains. But those provisions expire on December 31, 2010. After that, dividends would again be taxed like ordinary income -- at rates as high as 39.6 percent if there is no new legislation to protect them. The White House has suggested raising the top rate on dividends and capital gains to 20 percent, but nothing about taxes in this deficit-ridden, mid-term election year is a sure thing. A sharp increase in taxes on dividends would produce a correspondingly sharp drop in the value of dividend-paying stocks.
2. Use professionally-managed strategies. Investors could screen and purchase high-dividend stocks on their own, but we prefer diversified and professionally-managed strategies. There are numerous high-dividend mutual funds, exchange traded funds, and separately managed accounts with strong track records and low expenses. Index-based ETFs generally have the lowest fees, typically around 0.35 percent annually, but this year, at least, the dividend indexes have been underperforming the better active managers.
3. Avoid dividend traps. Yield is a function of income divided by price, so companies with unusually high yields likely have share prices that have collapsed. A yield of 3.8 percent on a solid company is a very good deal, but a yield of 9.0 percent or more probably signifies trouble. Companies that have problems do end up having to cut their dividends. ♦

*Past performance is not indicative of future returns. The above information is intended to be educational only and is not a recommendation to buy or sell any security.*

## Will Bush's Tax Cuts Haunt You or Help You?

Dan Frix, C.P.A.



We've all read about the significant estate taxes that are slated to return and to be applied to the estates of those dying after December 31, 2010. Without Congressional action, the estate tax laws will have a major impact on many. There are also some fairly significant income tax changes scheduled to begin next year. Without action, the "Bush Tax Cuts" and other favorable changes to the Tax Code enacted in 2001 and 2003 will "sunset" effective January 1. Below are a few details you may want to consider.

For Married Individuals Filing Jointly (MFJ), the lowest tax rate of 10% on the first \$16,750 in Taxable Income (TI) will disappear. This income will be taxed at the rate of 15% which will become the lowest tax rate. While the tax rate of 15% on the next \$51,250 of TI will not change, the tax brackets for all TI above \$68,000 will increase as follows:

All Figures Apply to Married Individuals Filing Jointly (MFJ) Based on 2010 Tax Tables				
	2010		2011	
	Rate	Over \$	Rate	Up to \$
Second Tax Bracket	25%	68,000	28%	137,300
Third Tax Bracket	28%	137,300	31%	209,250
Fourth Tax Bracket	33%	209,250	36%	373,650
Top Tax Bracket	35%	373,650	39.60%	----

Roughly speaking, what this means is that a family's income tax obligation will increase a little more than 10% in 2011 – on the same TI as in 2010. For example, if a family's TI in 2010 is \$100,000, they will pay \$1,798 (10.4%) more in income taxes under the new tax rates. A family with TI of \$200,000 will pay \$4,798 (10.8%) more in 2011 and a family with TI of \$300,000 will pay \$7,798 (10.2%) more.

Most long-term capital gains are currently taxed at a maximum rate of 15%. This rate will rise to 20% starting January, 2011. Similarly, qualified dividends currently are taxed at the same 15% maximum tax rate. Starting next year, these dividends are scheduled to revert back to ordinary income and, therefore, could be taxed at a rate as high as 39.6%, depending upon your TI.

The effect of both of the following provisions is to raise the taxes that higher-income taxpayers will pay. By lowering the amount of personal exemptions and itemized deductions that these taxpayers can legitimately claim, the TI is increased.

This brief summary highlights some the changes that we thought would be of interest to you. If you would like to discuss your

	2010	2011
Personal Exemptions	No reduction to the personal exemptions for certain high-income taxpayers.	Deduction will be reduced by 2% for each \$2,500 or fraction that taxpayer's Adjusted Gross Income (AGI) exceeds \$250,200.*
Itemized Deductions	No reduction to deductions a high-income taxpayer can claim.	Some deductions will once again be reduced once the taxpayer's AGI exceeds \$166,800.*

\* MFJ based on the 2009 tax tables for these provisions.

personal tax situation, please do not hesitate to call us. ♦



## MANAGING PARTNER

Weston D. Burnett, J.D., LL.M., CFP®

We expect both the Madoff case and the Financial Overhaul bill to have a substantial effect on the Financial Services industry. It is as yet unclear if any of those actually affect our clients but mostly we think it will increase oversight and expenses related to investing. For many years, the new account form from our broker dealer for our securities clients had been two pages long. As a result of the enacted laws and regulations, the broker dealer recently redid the form making it six pages in length.

On July 21, 2010, the SEC voted to propose measures intended to improve the regulation of mutual fund distribution fees (12b-1 fees) and to provide better disclosure to investors. The SEC's proposal is designed to:

- ♦ Protect investors by limiting fund sales charges;
- ♦ Improve transparency of fees for investors;
- ♦ Encourage retail price competition; and
- ♦ Revise fund director oversight duties.

According to SEC Chairman, Mary Schapiro, "Despite paying billions of dollars, many investors do not understand what 12b-1 fees are, and it's likely that some don't even know that these fees are being deducted from their funds or who they are ultimately compensating. Our proposals would replace rule 12b-1 with new rules designed to enhance clarity, fairness and competition when investors buy mutual funds."

In other firm news, Kathryn Duffy, our law clerk joined Cohen & Burnett as an associate and is awaiting the results of the bar exam she took in July. We bid farewell to our paralegal, Janis Ellsworth, who moved on from the firm in August.

On the family side, Edward and Alka's three-day wedding was August 6 - 8. It included both Hindu and Christian ceremonies with the latter being celebrated by a retired Navy chaplain who is an Episcopal minister that baptized and confirmed all our children. Edward and Alka honeymooned in Croatia and have set up residence in Washington, D.C., where they both work, Edward for Booz Allen and Alka for Milbank Tweed Hadley McCloy, LLP International Law Firm. That wonderful event combined with our daughter, Jennifer's, wedding in May to J.D. Beard made for a summer of joy. My mother made it to the first wedding, but not the second one, which she watched on Skype.

I showed my stamp exhibit at the American Philatelic Society Circle of Champions in mid-August where I won an award for Research. On October 9, I expect to complete my fourth Sea Gull Century race with Mark and my two sons, and will hike the Grand Canyon later in October. ♦

Fall 2010

## Mortgage Lending: Opportunities Abound

By Eric Mullis  
Senior Loan Officer/Branch Manager  
Intercoastal Mortgage Company



I am sure most of you have heard or read that obtaining a mortgage loan in 2010 is one of the most difficult under takings someone could ever endure. Nothing, in my opinion, is further from the truth. What has changed and is being interpreted as making mortgage lending difficult is that the media has focused on what the last few years brought us, which was lax lending policies and loans where basically the only item required for approval was a credit report.

Today, mortgage lending has reverted back to the way it was when I started in the industry 20 years ago.

You need good credit which by today's standards is a credit score over 640. You must have a job and/or documentable incomes (i.e. pay stubs, W-2's, tax returns). You must have a down payment, closing costs, and reserve funds. The proportion of your gross monthly income and minimum monthly payments for your revolving and installment debt, plus the mortgage payment cannot exceed 45 percent of your gross monthly income. These are just sound lending practices.

So what does this mean for you? Do your homework upfront. Consult with a mortgage lender before you decide to sell, buy, or refinance a home so that your specific financial situation can be analyzed; this way you will have the proper information before you make decisions.

Consult with your financial advisor and tax expert so you know what benefits and possible detriments there are to your specific situation.

Here are examples of what is available in today's mortgage environment:

In the Washington, D.C. metropolitan area, you can buy a home with as little as a 3.50 percent down payment for a maximum loan amount of \$729,750 by utilizing funding by the Federal Housing Administration (FHA). This type of financing is available to everyone.

So, say you want to refinance but have less than 20 percent equity. We can still utilize a combination loan where the first loan is capped at 80 percent of your home's value and a second trust for another 10 percent in order to avoid the need for mortgage insurance. With less than 10 percent equity, we can utilize FHA for refinancing.

The most compelling reason to buy or refinance a home now is that interest rates are the **LOWEST** since Fannie Mae and Freddie Mac have been keeping records. Most 30-year fixed mortgages are between 4.00 - 4.75 percent. After you take into account the tax advantage of the mortgage interest and real estate tax deductions, you are looking at effectively borrowing money in the 3.00 percent range, if not lower.

You will more than likely never see rates this low in your lifetime so, now is the best time to buy, sell, or refinance a home.

**Eric Mullis is Branch Manager for Intercoastal Mortgage Companies (ICMTG) McLean, Virginia branch. ICMTG is an independently owned Direct Mortgage Lender with processing, underwriting, and closing all handled locally. Eric has 20 years of mortgage lending experience and has closed over 1 billion dollars in residential loans. You can reach Eric at 703-890-1802, or via email at: [ericm@icmtg.com](mailto:ericm@icmtg.com).**

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# Wall Street Reform

## A Ripple in the Tides of Change

I. Mark Cohen, J.D., LL.M., & CFP® and Andrew Vanderhoof, J.D., LL.M.



The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act") was signed into law on July 21, 2010. As lengthy as the bill itself is, we have boiled down some of the high points here for your information.

The goal of the legislation is "to promote the financial stability of the United States by improving accountability and transparency in the financial system, to end 'too big to fail,' to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices, and for other purposes."

The Act establishes three new agencies: (1) the Financial Stability Oversight Council; (2) the Office of Financial Research; and (3) the Bureau of Consumer Financial Protection.

The independent Bureau of Consumer Financial Protection has strong and autonomous rulemaking authority and the ability to enforce those rules both for large banks and non-banking entities, like payday lenders and mortgage finance companies. In addition, it requires electronic trading and centralized clearing of standardized over-the-counter derivatives contracts, as well as more robust collateral and margin requirements. It gives regulators the explicit authority to break up megabanks that pose a "grave threat" to financial stability, and includes a provision to give regulators enhanced tools and powers to pursue financial fraud.

The bill also establishes minimum leverage and risk-based capital requirements for bank holding companies and systemically risky non-bank institutions that are at least as stringent as those that apply to insured depository institutions. It will also ensure that the capital base of megabanks is not adulterated with debt that masquerades as equity capital. Among the many changes, several have an immediate impact on our practice and clients. When a security is offered to the public for purchase, it usually must be registered with the SEC. "Reg D" contains an

exception for securities that are private and only offered to "accredited investors," which are investors who meet one of several standards relating to income or net worth. The net worth standard prior to the Act was \$1 million, including the value of the residence. That has now been raised to \$1 million *excluding* the value of the house. The other standards have remained the same.

The Act also disqualifies certain "bad boy" issuers from relying on a Reg D exemption if they have been previously convicted of certain crimes or subject to certain legal and other proceedings stemming from activities in the securities, banking, insurance or credit union industries. This means that a person convicted of crimes in one of these industries can no longer go to a related industry to continue committing such crimes.

The Act revises the powers and structure of the SEC, credit rating organizations, and the relationships between customers and broker-dealers or investment advisers. To prevent regulatory capture within the SEC and increase the influence of investors, the Act creates an Office of the Investor Advocate, an Investor Advisory Committee composed of 12-22 members and an ombudsman appointed by the Office of the Investor Advocate. The SEC is also specifically authorized to issue "point-of-sale disclosure" regulations when retail investors purchase investment products or services. These disclosures would include concise information on costs, risks, and conflicts of interest.

The Act provides a number of additional protections for whistleblowers, including a provision that rewards them monetarily for alerting authorities to fraud in the stock and commodities industries. The Act also strengthens anti-retaliatory measures for workers who reveal fraud to commodities agencies and/or the SEC and who give information to the new Bureau of Consumer Financial Protection. ♦

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*A compass rose is a figure displaying the orientation of the cardinal directions, north, south, east and west on a map or nautical chart. We found it fitting to name our newsletter after this recognizable symbol of navigation and direction.*  
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# THE COMPASS ROSE

COHEN & BURNETT, P.C. NAVIGATOR WEALTH MANAGEMENT, LLC

ESTATE AND FINANCIAL PLANNING UPDATE

Fall 2010

Volume 10



## FOUNDING PARTNER

I. Mark Cohen, J.D., LL.M., CFP®

Fall is back and the leaves will be changing soon. My family and I had a wonderful time in Yosemite in July. If you remember from the last newsletter, our plan was to spend some time in Curry Village and then Michael and I were going to backpack from the valley to Devil's Postpile (Mammoth Mountain). Well, we did almost all of it. Unfortunately on the last two days on the trail to Devil's Postpile, we encountered 100 percent snow and it was more work than either of us wanted to do. So we cut our backpacking trip short and decided to enjoy some time in San Francisco instead. I took over 450 pictures and am still sorting through them.

In August we attended Edward Burnett's spectacular wedding in New Jersey, then spent the better part of a week in Cape Cod kayaking, relaxing and sightseeing. From there we went to Boston to my niece's wedding, and then made it home after ten days.

Back to work! Almost every day it seems that I am being asked what will happen to the estate tax laws in 2011. I will go on record here to share my opinion: I think that Congress will not act on any estate tax legislation now that we are into election season, and given the likelihood of more Republicans being elected, there will be no way to reach consensus on such a bill for a long time. Besides, it is much easier to raise taxes by doing nothing than acting to cut taxes. Thus, we will likely revert to the old laws as if the Bush-era estate-tax cuts never happened. That would mean a Unified Credit of \$1 million per person and a 55 percent tax on the excess.

If you haven't given it a second thought, I suggest you do so and review your estate documents and give me a call if you have any concerns. ♦

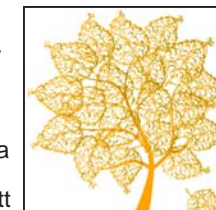
## Lessons to My Children Captures Media Attention and Parents' Hearts

*Lessons to My Children* was met with great interest by reporters, book reviewers, bloggers, and major consumer magazine editors alike, when Navigator Wealth Management issued the first press release on August 5, 2010. Among the publications that thought *Lessons* has a lot to offer, *Worth* magazine will feature a blurb about the book in their October/November issue and *The Dallas Morning News* interviewed Wes Burnett for a personal finance article entitled: "Before College, Share Life Lessons," where he was asked to comment about the value of teaching a college-bound student about budgeting. He said, "I'm a strong believer in them having some money in play themselves, so it isn't all Mom and Dad or somebody else paying for it. That's a bad habit to build. They rob the child of the lessons of learning how to do it themselves."

During the September 15 Digital Book Launch party, which was hosted exclusively on the Internet, Mark and Wes revealed the book's promo videos, a webinar on the book's basics, a live interview on Blog Talk Radio, and a Twitter party where consumers and reporters got to ask questions of the authors.

Consumers have also proactively expressed their satisfaction with *Lessons*. One parent eloquently commented: "[*Lessons*] promises to become an important tool for children and even others who need help with money management. I shall mention it to my friends..., many of whom struggle with their kids in trying to inculcate good values with regard to spending, saving and budgeting."

Learn more at [www.LessonsToMyChildren.com](http://www.LessonsToMyChildren.com). Fans of the book are following on Facebook (<http://www.facebook.com/pages/To-My-Children/114636771892505>), and Twitter (<http://www.Twitter.com/ToMyChildren>), where people can register for Weekly Wealth Lessons. Sign up today! ♦



## The Top Twenty Mistakes of Affluent Investors (First in a Series)

Join us to learn five of the biggest missteps smart people make over and over again with their own investments... are you making the same ones?

Please join us for an eye-opening discussion with **Mark Cohen**, Founder of Navigator Wealth Management, LLC.

**Wednesday, October 6, 6:30pm** for an hors d'oeuvres reception; or **Thursday, October 7, 8:30am** for breakfast at the **Tower Club, 8000 Towers Crescent Drive, Suite 1700, Vienna, VA**

Contact Nicci Yang for more details or to RSVP: (703) 847-0965; [rsvp@cohenandburnett.com](mailto:rsvp@cohenandburnett.com).