

Retirement Weekly

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When the need passes on To keep, cash in, or donate life insurance, that is the question

It's a pickle. Many seniors own life-insurance policies purchased years ago when they first bought a house or had children. Now that the house is paid off, and the kids are out on their own, the value of maintaining the policies becomes a ponderous question. Should they keep them in force, cash them in, donate them to charity or what?

There is no one-size fits all answer to that question. "People have to remember what insurance is for," says Michael Snowden, professor of financial planning and insurance at the Denver-based College for Financial Planning. "It's a means to provide money when it's needed."

Edward Graves, professor of insurance at the American College and co-author of McGill's Life Insurance, concurs: "Insurance provides cash upon death. If you don't have the need, you should consider terminating the contract or exchanging it for another contract."

The hard part is figuring out whether you still have the need for the coverage. And that requires what those in the life-insurance business call a "capital needs analysis." It's not unlike the process seniors should have gone through when they first purchased their life insurance decades ago.

It's the process of analyzing sources of funds and financial needs such as living expenses for the surviving spouse, children,



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Debt remains the same

Older American families had the same level of debt and debt payments in 2001 as they did in 1992, says a new Employee Benefit Research Institute (EBRI) report.

But the composition of debt is changing and an increasing number of Americans are putting their retirement security at risk by loading up on housing debt, says EBRI President Dallas Salisbury. The study found that 57 percent of debt payments now go toward housing debt. What's more, the study showed that the 5 percent to 10 percent of the near elderly and very elderly have debt payments greater than 40 percent of income. The report can be found at <http://www.ebri.org>. **RW**

Biding life insurance policies farewell

(Continued from page 1)

grandchildren, disabled dependents; bequests; debts, including a mortgage; and final expenses. In cases where seniors have a shortfall, as is often the case, Snowden says keeping the policy in force makes sense.

In fact, seniors often learn they need even more life insurance than they have. That's especially true for those with a business or estate, inclusive of their retirement account, a home that has appreciated greatly over the years, and other assets that create a federal or state tax liability.

The cost of insurance for seniors can be equal to the value of the death benefit. If the insurance is not cost-prohibitive, however, Snowden says seniors ought to purchase the policy from a company rated A or A+ by A.M.

Best, that is licensed to do business in New York, Texas and Florida, the states with the toughest life insurance sales regulations, and not on the National Association of Insurance Commissioner's Watch List. Best case they simply upgrade the existing policy with the existing provider.

Seniors who determine they need more life insurance, to pay for a business succession plan or other unmet needs, should consider a term policy rather than a permanent or whole life policy if the need is less than 20 years, Graves says. In addition, he said consumers should not purchase a variable life-insurance policy if they can't pay the premium on an annual basis.

Graves says seniors who need life insurance, but find the premium onerous should consider converting the policy into a fully paid-up one. Doing so will reduce the death benefit, but it will also eliminate the monthly expense.

Meanwhile, anyone who doesn't need the life insurance and doesn't have unmet needs for income has several options.

- **Bequests:** Seniors intending to leave money to charity should consider changing the policy's named beneficiary to that of the charity. "This is a painless way to provide a gift at death," Snowden says. Another option: naming a trust that would provide income to the senior's children, grandchildren or loved ones.
- **Exchanges:** Seniors might be able to exchange their old policy for a newer one that provides a larger benefit or for an annuity that provides immediate income or tax-deferred growth. Graves suggests that seniors who don't need the insurance but do need monthly income could cash in their policy, borrow against the cash value in their policy, or use what's called a viatical settlement (albeit from a reputable company). That's when seniors, usually those who are very elderly or seriously ill, sell their life insurance policy for a lump-sum cash payment. Calculating the after-tax returns of each option will help seniors determine the best choice, Graves says. **RW**

Resources

- **National Association of Insurance Commissioners**
<http://www.caionline.org>
- **National Association of Insurance and Financial Advisors**
by Ellen Hirsch de Haan, Esq.
- **A.M. Best**
<http://www.aarp.org/life/homedesign/Articles/a2004-03-23-caps.html>

Tips of the Week

IRS denies 60-day rollover waiver request

Investors who take distributions from their IRA to cover living expenses or special purchases take heed. You better put the money back within 60 days or else expect to pay taxes and, for those under age 59½, a penalty on the distribution.

The IRS last week issued a Private Letter Ruling denying a taxpayer's request to have the 60-day rollover requirement waived on an IRA distribution. The taxpayer, who was unemployed for part of 2001 and 2002, tapped his IRA to cover personal expenses and tuition, says Steve Leimberg's Employee Benefit and Retirement Planning newsletter. And after landing a job, the taxpayer tried to return the distributed amounts to the IRA, albeit after the 60-day tax-free rollover period. In his waiver request, the taxpayer claimed that IRS' failure to waive the requirement would be against equity or good conscience.

The IRS' response? Sorry Charlie. "The IRS has granted waivers in more than 30 cases where there has been legitimate reasons," says Barry Picker, author of "The Guide to Retirement Distribution Planning." "But in this case, the taxpayer intentionally took out what was in effect a tax-free loan and messed up. Investors should now be on notice that if they take out a loan from their IRA, the IRS will not bail you out. The risk to put the money back within 60 days is on you." Picker says many Americans likely withdrew funds from their IRAs over the last four years to cover living expenses, but most likely paid the tax and/or penalty or replenished their IRA within the 60-rollover period. The IRS has granted waivers in cases where taxpayers used mental illness and substance abuse, Alzheimer's disease, blizzards, and financial firm gaffes as the waiver-request reasons.

For his part, Ed Slott, author of "The Retirement Savings Time Bomb and How to Defuse It" says the lesson to be learned from the IRS' ruling is this:

- Use direct transfers (trustee-to-trustee transfers) when moving retirement funds from one plan or IRA to another. A rollover, Slott says, is where you withdraw funds from your IRA and redeposit them to another IRA or plan. With a direct transfer, the IRA funds are never withdrawn and redeposited. They go directly from one financial institution to another. Many problems raised in previous IRS rulings on 60-day waiver requests could have been avoided if taxpayers had used a trustee-to-trustee transfer. Slott says you can only use the 60-day rule once per 12 months.
- IRA owners should not try to use the 60-day rule to borrow from their IRA. If you cannot return the funds within 60 days, which is often the case, you will owe income tax on the full distribution, plus a 10 percent early withdrawal penalty if you were under 59½ when you withdrew from your IRA. **RW**

Website of the week

An Equal Employment Opportunity Commission (EEOC) ruling could cost 12 million retirees their health plans, AARP claims. The American Benefits Council (ABC) has meanwhile lauded the ruling, saying it will stabilize the retiree health benefit system. Learn more about ABC's view at <http://www.americanbenefitscouncil.org>. **RW**



Tips of the Week

Medco to pay millions for drug switching

Seniors who buy prescription drugs from Medco Health Solutions can expect greater cost disclosure and transparency following last week's \$29.3 million settlement between the nation's largest pharmacy-benefits manager (PBM) and federal and state authorities. Under the terms, Medco will start telling patients, doctors and employers about the billions in annual rebates it receives from drug makers for pushing their products.

The Justice Department accused Medco in a lawsuit last year of getting \$430 million from Merck, its former parent, to switch patients using Lipitor to costlier drugs such as Merck's Zocor. The settlement prohibits Medco from switching drugs when the cost of doing so would be higher than the cost of the prescribed drug.

Medco says the cash portion of the settlement will be used to provide drug cards providing free generic prescriptions for low-income and elderly Americans or prescription medicines for state-affiliated healthcare clinics; and a maximum \$25 per patient reimbursement to patients from the 20 states involved in the settlement whose doctors had approved a mid-stream change in cholesterol-lowering drugs.

"People were completely in the dark," says Bill Trombetta, a Saint Joseph's University professor and author of "Customer-Driven Marketing Strategies." "People won't be able to rest easy, but at least they will now know the cost of their drugs."

PBMs such as Medco manage about 1.8 billion prescriptions per year. The companies use managed-care techniques to administer drug benefits for HMOs and PPOs, large employers and government agencies. In 1999, PBMs managed more than 70 percent of prescriptions filled at retail pharmacies.

Meanwhile, a separate study released this week says two-thirds of health plans are protecting patients by auditing their PBMs to verify cost-effectiveness. But consumer advocates say they should stay on guard for drug switching that results in higher costs. Medicare Rights Center's Deane Beebe says participants should advise consumer organizations and consumer protection agencies whenever there is a formulary switch that impacts them negatively. "There will be bait-and-switch temptations galore."

More information about PBMs can be found at the following Web sites: Medicare Rights Center (<http://www.medicarights.org>); Pharmaceutical Care Management Association (<http://www.pcmanet.org>); AARP (http://research.aarp.org/health/2000_20_rx.html); and PBMWatch (<http://www.pbmwatch.org>). **RW**



And the survey says...

Most Americans don't have the right plan for a financially secure retirement, a Golden Retirement Resources survey says. The right plan, which the company says doesn't exist, would combine savings and income-distribution in one product. **RW**

Tips of the Week

New site to help investors find advisers

Paladin Investor Resources launched a Web site this week aimed at helping investors find, select, monitor and replace financial advisers. It's an independent service that "receives no compensation from advisers or companies, accepts no outside advertising, sells no financial products, services, or advice, and has no conflicts of interest," Paladin's Jack Waymire says.

The site, <http://www.paladininvestors.com>, is reportedly the first to offer advisor-monitoring services to investors. The service, which costs \$52 per year, provides tools to walk investors through selecting competent, trustworthy advisers; a performance-monitoring service; summaries of investment schemes and scams; and access to the Paladin Learning Center.

Waymire, author of "Who's Watching Your Money? The 17 Paladin Principles for Selecting a Financial Advisor," produced the site. Is it worth the money? Before you plunk down \$52 per year, we offer a sampling of Waymire's 17 principles so that you can judge for yourself. You cannot control the volatility of the securities markets, but you can control the quality of your adviser. Make sure you select advisers for their qualifications and not their personalities. Use an objective, rational process for selecting an adviser that is not affected by emotions or sales skills. Require all-important adviser information to be in writing. Permit no exceptions to your due diligence process. Require full disclosure about all potential conflicts of interest. Verify integrity by reviewing the adviser's compliance record. Verify competence by evaluating education and experience. Make sure you are the adviser's only source of compensation. Make sure quarterly performance reports are a mandatory service. Don't ignore red flags. Minimize the personal relationship with your adviser. And always interview multiple advisers so you have a choice.

New and noteworthy

Medicare's Web site (<http://medicare.gov>) this week unveiled a comparison-shopping tool that lets seniors check drug prices in their area to help in picking a discount card. **RW**

And the survey says...

More than half (52 percent) of 125 companies polled are considering changes or already have made changes to their pension plans, says a new Deloitte survey. As a result, the burden for funding their own retirement is increasingly shifting to individuals, Brian Augustian, a Deloitte principal, says.

Among those that have changed their plans, the single most common shift was freezing their pension plan and moving to a defined contribution plan. Two-thirds of companies that made plan changes cited cost savings as the primary driver, with 63 percent also seeking to reduce cost volatility. The survey can be found at <http://www.deloitte.com/us>. **RW**

The Income Investor

Absolute-return strategy gains favor

One of the nation's leading wealth-management firms plans to invest a portion of its clients' money in the only U.S. mutual fund that tracks the performance of hedge fund managers.

Coral Gables, Fla.-based Evensky Brown & Katz said it will invest 10 percent of its \$400 million in fully discretionary funds in the Rydex SPhinX Fund, which tracks the Standard and Poor's Hedge Fund index and is designed to provide absolute returns.

The S&P Hedge Fund index (S&P HFI) represents the major hedge fund strategies and has become the talk of the investment world lately. It's outpaced the better-known S&P

500 index by a wide margin over the past three years. And now more advisers are seeking ways to match the performance of the S&P HFI, which has 40 parts divided into three sub-indices: S&P Arbitrage, S&P Event-Driven and S&P Directional/Tactical.

Further sub-indices represent nine investing strategies, including Equity Market Neutral, Fixed-Income Arbitrage, Convertible Arbitrage, Merger Arbitrage, Distressed, Special Situations, Equity Long/Short, Managed Futures and Macro. The strategies are equally weighted, S&P says. More information about the S&P HFI and other S&P hedge fund indices can be found at <http://www.hedgefundindex.standardandpoors.com>.

At present, the only publicly traded fund available that tracks the S&P HFI is the Rydex SPhinX fund (Symbol: .SPGH). Launched last June, this hedge fund of funds requires investors to have a net worth of at least \$1 million, annual income in excess of \$200,000, and an account managed by an investment advisor registered under the Securities and Exchange Commission's Advisers Act.

What's more, the investor's adviser must also act as a fiduciary when buying shares in the fund, the company says. And if that wasn't enough to scare off most investors, this fund requires a minimum investment of \$25,000 plus its fees are 1.95 percent per year, quite a bit more than the average stock mutual fund. Plus, the fund has limited liquidity; it allows only quarterly redemptions. And it's risky. The entire amount of your investment could be lost, the fund company says.

That said, the fund — although not designed for income investors — could provide useful diversification to those who have well-balanced portfolios. It rose 3.45 percent from its inception through 2003. The S&P HFI gained 4.68 percent in the same period. Learn more at <http://www.rydexfunds.com/campaigns/sphinxoverview.cfm>. **RW**

S&P Hedge fund index performance vs. S&P 500			
Index/ Ticker	Q1 '04 (%)	3 Years (%)	5 Years (%)
S&P Hedge Fund index/ SPHG	1.89	24.88	64.66
S&P 500 Stock index/ SPX	1.29	(9.17)	(9.05)

Source: Standard and Poor's



Ask Mike

More on IRA distributions

Editor's Note: Last week I discussed inherited IRAs and some of the options available to spouse and non-spouse beneficiaries. This week we will focus in more detail on the options available to a spouse who inherits a traditional IRA.

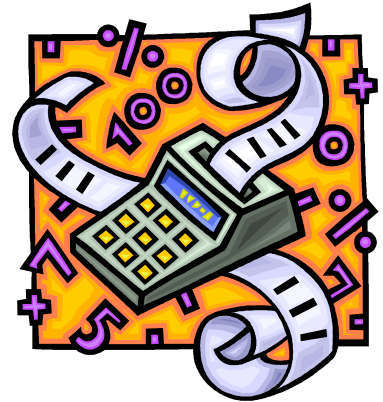
For the sake of clarity, I will use the terms "spousal IRA" when referring to a traditional IRA that a spouse chooses to treat as her own. I will use the term "inherited IRA" to define a traditional IRA that a spouse does not choose to treat as her own.

A good reason to refrain from immediately withdrawing assets from a decedent's IRA is the ability to stretch out the benefits of the IRA's funds. As we mentioned last week, a surviving spouse who is the sole beneficiary can elect to treat an IRA as her own. This is generally called a "Spousal IRA." This is particularly advantageous for a spouse who is considerably younger than the decedent. A surviving spouse that elects to treat an IRA as her own must take any distributions that the decedent was required to take in the year of death. In the years that follow, she gets a so-called "fresh start." The amount and timing of her distributions can be based on her age, not that of the older decedent. Her distributions could be calculated based on the Table III Uniform Life, which provides for smaller required minimum distribution amounts than the Single Life Expectancy Table.

If you are older than your spouse and your spouse dies before the required beginning date for taking distributions, the strategy may be a bit different. For example, a spouse, age 73, who inherits an IRA from a 61-year-old decedent may not want to treat the IRA as her own because that means commencement of distributions. The spouse may want to remain the beneficiary of the inherited IRA. The amount of the distributions would be based on her age using the Single Life Expectancy Table. The timing of the distributions, however, will be based on the younger decedent's age at the time of his death. Therefore, the spouse can wait until December 31 of the year in which the younger decedent would have turned 70 ½ before taking any distributions.

In the example above, if the decedent instead had passed away at age 72, then the surviving spouse would have to start taking distributions by December 31 of the year following the decedent's death.

Beneficiaries who are not spouses do not have the ability to roll over an inherited IRA nor can they defer the timing of the distributions. Next week we will examine in detail their options. **RW**



Michael S. Finer, a certified public accountant, a certified financial planner®, and a chartered life underwriter, is president of Salem, Mass.-based Major League Investments Inc. Robert Powell is a minority shareholder in the firm. Email "Ask Mike" questions to rpowell@marketwatch.com.

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Robert J. Powell III is President of Unison Associates, LLC, a Salem, Mass.-based financial education, communication, and consulting firm. Powell, who has more than 20 years of experience in the financial services industry, is also co-author of *Decoding Wall Street* and Executive Producer of PBS' *More Than Money*. Previously, Powell served as editor-in-chief of DALBAR's Mutual Fund Market News and columnist for the *Boston Herald*.

Powell owns no shares of any investment mentioned in this week's issue. He currently provides consulting services to the Financial Planning Association and Major League Investments, in which he also holds a minority interest.

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