

## Fund Differences

Most people believe a fund is a fund or an index is an index. This is totally understandable, but very far from the truth. The newest fund on the block is the ETF or exchange traded fund. These relatively newly created investment tools are designed to trade like stocks, they trade during the day, and investors call this trading intraday. The growth in these products has been explosive to say the least. In 2006 there were 374 ETFs, today we have 834 as of December 31<sup>st</sup>, 2009. The pure number of options has caused a lot of misunderstanding as well, because the options are seemingly endless.

These tools may seem to be alike in that they track the same market basket, index, have exposure to the same area, etc. but the chassis they're built on can be very different so a clear understanding of them is critical. All of the like portfolios are constructed of similar securities, but the methodology of coming up with the names varies widely. Not only the methodology but the use of leverage or inversions is also prolific in the industry today too. Let's look at some examples of funds that sound similar and the average person would think to be virtual twins, and why they're actually so different.

Financial funds are available widely but they all do it a little differently. Revenue shares financial sector fund uses financial stocks weighted by company revenue instead of market capitalization. Power shares dynamic financial sector picks stocks by looking at trailing stock performance as well as other criteria. Direxion Financial bull tracks the Russell 1000 financial services index at triple the performance with the use of options contracts

*Continued on page 2, Fund Differences*

### INSIDE THIS ISSUE

- 2 The Guarantee Fallacy; Fund Differences
- 3 Noteworthy News; International Exuberance
- 4 \$ Quiz; Ideal vs. Reality
- 5 Inspirational Quotes; Easter Egg Hunt

## Education Changes

When you're saving for the education of a child close to your heart, there is a plethora of options to fund the objective. 529 plans are all the rage today and for good reason, once the money is in the account it grows tax deferred and is ultimately tax free if used for qualifying higher education expenses. The 529 isn't limited by income or other Government gimmicks, anyone can put money into the plan, and a lot of money. Most 529 plans allow people to put in around \$300,000.00 per beneficiary. A downside to 529's is that if the loot isn't used for education, taking it out will cause income tax and a 10% penalty on the earnings in the account. Another downside is that they're state sponsored, which causes a lot of games because not all states offer good plans, but some states do offer tax incentives only if their plan is used. All of the plans only offer mutual funds as options, as they haven't yet matured to the point where you can use a brokerage account to fund them. They also only allow you to change your investments within the plan once a year. This happens because the state is sharing in the revenue of the account, so they have incentive to keep you in their states plan. 529 plans can only be used for post secondary education so no private high schools here.

Another great funding option is the UTMA (Uniform Trust to Minors) or UGMA (Uniform Gift to Minors) accounts. These accounts are legally owned by the minor, but an adult is trustee until the youth reaches the age of maturity in your state. These plans are much more flexible, but offer different tax advantages. These plans offer a tax free ride on the first \$950.00 in interest income, the next \$950.00 is taxed at the child's tax bracket (typically zero) and the rest of the income is taxed at the parents top marginal bracket. These plans can be used for anything, college, high school, daycare, braces, whatever comes up, but it must be for the benefit of the child. These plans can be in a brokerage account and you can invest in anything, they're not limited to a vanilla list of mutual funds based on a political and corporate deal with some state treasurer. It'll be interesting to see if as time unfolds the 529 plans continue to be state sponsored or if they just become account types that are free from the minutia of more rules and law.

*Continued on page 3, Education Changes*

## **Fund Differences.** *Continued from page 1*

on top the stocks themselves. Direxion financial bear will track the same Russell 1000 Financial Services index, but will perform at triple the inverse of what the index actually makes. There are four funds that appear to be twins, or last siblings or cousins, but are really almost different species altogether.

Not only are the names and structure different, so are the actual results. Here is how each fund fared during the past 12 months as of April 9<sup>th</sup> 2010.

Direxion Financial Bull	144.5%
Direxion Financial Bear	- 88.44%
Revenue Shares Financial	69.36%
Power shares Dynamic Financial	22.42%

Clearly this data shows big time differences in results from a pool of funds that appear to be very similar on the surface and in name. This is how similarly sounding funds can be structured very differently within, now let's look at how they can be structured very similarly. We'll switch gears to traditional index funds, both open ended and ETF's to see the similarities. Here is the annualized 5 year performance for some very similar funds.

Vanguard S&P 500 Index	0.45%
Fidelity Spartan 500 Index	0.93%
Power shares 500 Index ETF	0.93%
T. Rowe Price Equity Index 500	0.66%

The common thread in all of these products is that they control trillions of investor dollars. It is the fund companies' responsibility to vote the shares they own in the best interests of the shareholders, which isn't happening. The huge money paid to company CEO's and other executives is something that must be approved by shareholders, and big shareholders have a big say in what goes on in corporate boardrooms. What is happening in the past few decades is that the people running the funds are just as guilty of making so much more than what they're worth they're not willing to make any noise about the ridiculous compensation practices at many of the big businesses in the world.

Realize there is a big difference in pay between people running a \$100 Billion dollar firm and a \$1 Billion dollar firm. A pay package of a few million dollars for a corporate executive is great pay and a great person deserves it. A pay package of \$100 million for a corporate executive of a larger company is downright ludicrous and nobody deserves it. If you wonder how your funds have been voting your shares, you can check on the SEC website under the N-PX form section where each fund must disclose their votes.

## **The Guarantee Fallacy**

The insurance industry never misses a trick. I'm not a big insurance fan, but believe you must insure the big things that are life altering and truly irreplaceable. It's prudent to insure your life, your income, your health care, your home and any other highly valuable possessions. Many things can be added on as a rider to your home policy such as jewelry, collections, etc. It's also important to have great personal and professional liability insurance in our lawsuit crazed society to protect yourself against a judgment that likely will be life altering.

It's not the best idea to insure every little thing. When at the store buying anything from appliances to cars to electronics they're happy to sell you disability insurance on anything you own or can buy. It may come under the term warranty or service contract or whatever, at the end of the day it's disability insurance on whatever it is you're buying. For services this makes sense but for products it's not the best deal for the consumer. I tend to look for the most reliable brands and products and buy them. If you follow this advice and keep the products forever, the insurance typically isn't needed.

After the market meltdown of 1999 and again in 2008 and the investor terror that has followed, the industry is capitalizing on the fear with a new breed of insurance products. These new products are supposedly "guaranteed" and will provide you with returns that are typically not guaranteed at all. The annuities and CD's today are all touted as the next best thing in the world, offering the guarantees of a fixed investment with the return potential of anything out there. This is a fallacy and as the old saying goes, if it sounds too good to be true, it likely is.

Here is how most of these Variable Annuities with guarantee products work. They offer you a guaranteed income stream, stated in an interest rate, such as 5%, 6% or 7%. They're guaranteeing that as long as you only take out a little bit of your money each year, you'll never get less out of the investment than you put into it. This is a very different thing than actually guaranteeing you 5%, 6% or 7% on your money. The guarantee is complicated, this is why the prospectus for the contract is 300 pages thick and although it implies your money is guaranteed to grow at the guaranteed rate at a minimum, and hopefully a lot more like stocks will, it's typically a fallacy. There are a few contracts out there that provide those guarantees, but most of them are unavailable now after 2008 when the insurance industry realized they grossly under reserved for the contracts that were previously issued. This very scare is what brought the Hartford down to its knees.

# Noteworthy News! ! !

- Congratulations to Gregg Golembeski on his new job! ☺
- Congratulations to Anthony Sgaglione on his new job! ☺

## International Exuberance

The traditional thought that investing overseas was a great diversifying idea has lost its power. Historically when the U.S. markets were strong the foreign markets may have been weak, and vice versa. This non correlated relationship made diversifying into the various markets a great idea as it smoothed out portfolio returns. That's the whole concept of diversification in the first place, not to put all of your eggs in one basket.

The reason for this not being so powerful of a tool anymore is that the world is truly one marketplace. We in the U.S. are no longer isolated from Europe, Asia or any other market. We're all interdependent in the world so get used to the fact that many markets will move in sync from now on. This isn't a bad thing and there is no way we can change it, it's just something we need to identify and accept as we move forward and make our investment decisions. Let's take a quick look at some companies from around the globe, headquartered all over, and see what percentage of their revenue comes from domestic markets vs. outside of the home country.

Company Name & Home Country	% of revenue from outside
Nestle (Switzerland)	87%
Vodafone (U.K.)	87%
Nokia (Finland)	84%
CEMEX (Mexico)	82%
Honda (Japan)	82%
Roche (Switzerland)	80%
Acer (Taiwan)	77%
Coca Cola (U.S.)	72%
Siemens (Germany)	72%
ExxonMobil (U.S.)	68%
Proctor & Gamble (U.S.)	61%
Sony (Japan)	61%
Hewlett Packard (U.S.)	59%
Lenovo (China)	47%
Samsung (S. Korea)	47%

# Education Changes *Continued from page 1*

Another popular funding tool is the Coverdell Education Savings Account, also commonly known as the Education IRA. There are a lot of changes set to expire on these accounts by year end so be wary of how you put these tools to work for you. As of today, mid April 2010 you can use the Coverdell account to pay for K-12 education expenses, but that nice tool is about to go away unless Congress acts to extend the benefit. We've used these plans extensively in the past for just this reason, it's one of the best tools that one can use to fund pre college educational expenses and it appears that it's going away. Right now these plans are quite limiting because you can only put in \$2,000.00 annually to them, which doesn't buy too much of an education today. It'll buy the books and take care of a good chunk of a community college, and more people should be doing that rather than going into deep debt to fund a four year education at a premium priced institution. The recession has moved many people in that direction, and I'm a big believer in going to a community college and transferring to a state school as it is the best bang for your educational buck. The new rule starting next year will limit contributions to these accounts to \$500.00 annually. At that point they'll lose a lot of their popularity as that drastically limits their usefulness.

These plans are a lot like 529's, but with much lower contribution amounts and no state tax deductions for deposits. The tax deferred nature of growth and tax free withdrawals for qualifying expenses match the 529 plans exactly. Investment options are more advanced in Coverdell accounts than in 529 plans. You can invest in almost anything in these accounts except life insurance. There are age restrictions in a Coverdell account that do not exist in 529 plans. If the beneficiary reaches age 30 the Coverdell account distributes the money to him/her and it is taxed, unless used for qualifying higher education expenses. Apparently after 30 there is no more ability to learn, we're too old and all washed up! Investors in these plans can switch investments whenever they want, unlike the once a year choice available in 529 plans.

Some of the heat on the Coverdell accounts today is because opponents believe these accounts push private schools over public ones in that they allow the money to be used for K-12 education. That isn't true as the owner can use the money for any qualifying school, private or public. There are public and private options for college too, are they going to get rid of 529's too? If the rules change for year end it makes sense to roll your Coverdell accounts to 529 plans and enjoy all the benefits without having to get hit with the changes. This may be by design, perhaps this is how the government wants to consolidate the number of education savings tools available to people. ☺

## Money Quiz

This month's challenge is to tell me how much annual earnings for S&P 500 companies are up, in a percentage, this year from a year ago. Last month's quiz wasn't won. The government takes on average, 442 days to process a disability claim. Ouch! ☹️ The winner will enjoy lunch/dinner on us at Chili's. ☺️ 04052010: 06

### S

y that all need content they'll , they're going e hear about it ens the media are less about bout it. Does l that much to warped sense away anytime else's who is

y. Here is a .tomobiles on faction/quality to be haunted ily going to be i too to add to congress have rrogate auto melted down, nal crosshairs? the gas pedals :he end of the The fact that stopped the rey value their should have ne and energy he media can ture. ☺️ ☺️ ☺️

Knowing the difference in these two perspectives is critical in our world today, especially as we move forward with record financial issues. The most recent glaring example of a complete disconnect between reality and ideals is what is going on in the political circles. There is the economic reality of our world, where just about everyone on the planet has adjusted spending. In the past few years, as income has gone down, most have learned to live on less, excluding government. Government continues to carry on its path and spend more, stimulate more, make more laws, create more minutia and compliance work, etc. even though revenue is down. They just keep borrowing more; it's like a gambler with an unlimited credit card. We need all of these things but we need them in moderation and they cannot come at the expense of the overall good. We're reaching a tipping point where there is so much minutia, so much irresponsibility at the top, that it becomes so counterproductive it could really inhibit our ability to grow, innovate, and move on as we always have.

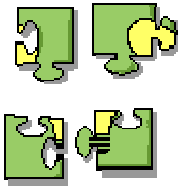
California leads the charge in clean energy, green living, high environmental standards, etc. but the economic disaster it has created cannot be ignored. They are just beginning to see the reality of a global warming law they have where they want business to get 33% of their energy from renewable resources. That's a great goal, but to get there it's really expensive and there will be lots of layoffs and price increases from businesses to do it.

They're banking on technologies that are not mature and some that don't even exist yet to satisfy laws. It's great that they're thinking ahead, but come on let's get real here.

Another train wreck in the works is the ownership of local and state government by local unions. Historically municipal and state employment offered stability of job, great benefits and low pay. Today it offers stability of employment, great benefits and great pay. All three are simply unsustainable moving forward so something is going to give. It would be best if union bosses just stepped up and did the right thing, not holding out and letting a town or state gut every service known to man just so the employer (the town or state as it may be) can continue to satisfy its contractual obligations. Just because something is contractual it doesn't make it right. Nobody could have predicted what health costs have exploded to be. Someone should have been on the watch when pay scales escalated and surpassed the private sector, benefits should have been cut back then. The most painless compromise would be to freeze pensions where they are today, move to 401(k) or 403(b) type plans only moving forward, and getting Health Savings accounts as the only medical benefit option. Some states and towns are pushing for this now, it's just a matter of time that things end up here, and it's the only way to make the system viable over the long run. ☺️

# Inspirational Quotes

- The mediocre teacher tells. The good teacher explains. The superior teacher states. The great teacher inspires. -William Arthur Ward
- Everyone is trying to accomplish something big, not realizing that life is made up of little things. -Frank A. Clark
- Patience with others is love, patience with self is hope, patience with God is faith. -Abel Bestavros
- Motivation is what gets you started, habit is what keeps you going. -author unknown
- Patience and perseverance have a magical affect before which difficulties disappear and obstacles vanish. -John Quincy Adams



**We can piece the puzzle together and make your money work for you. ☺**

## Corner

children, one better than the other kids who they're meant to feel the pain. Pain can come in many ways, to the pain of failure, to the pain of being insulated from pain, to the pain of not being able to feel the pain and work through it of life and we're all going to feel the true colors show up when a challenge. Does the child come to mommy and daddy for help, or do they come to a person. My kids usually don't let them work through it, even when the acting ensue. It makes them work through it. Maybe we should bail them out more! ☺ ☺ ☺

### Connecticut Directory (860) 673 1942

Mike = [mike@fiscalwisdom.com](mailto:mike@fiscalwisdom.com),  
Nancy = [nancy@fiscalwisdom.com](mailto:nancy@fiscalwisdom.com),  
Betsy = [betsy@fiscalwisdom.com](mailto:betsy@fiscalwisdom.com),  
Andrea = [andrea@fiscalwisdom.com](mailto:andrea@fiscalwisdom.com),  
Michele = [michele@fiscalwisdom.com](mailto:michele@fiscalwisdom.com),  
Maureen = [maureen@fiscalwisdom.com](mailto:maureen@fiscalwisdom.com),

### New York Directory (315) 682 0348

Teresa = [teresa@fiscalwisdom.com](mailto:teresa@fiscalwisdom.com),  
Mark = [mark@fiscalwisdom.com](mailto:mark@fiscalwisdom.com),  
Jackie = [jackie@fiscalwisdom.com](mailto:jackie@fiscalwisdom.com),  
Tom = [tom@fiscalwisdom.com](mailto:tom@fiscalwisdom.com),  
Josh = [josh@fiscalwisdom.com](mailto:josh@fiscalwisdom.com),

who they are and they will help them and having their best

le \_\_\_\_\_

member FINRA/SIPC. Investment Research, Inc.

Visit us online = [www.fiscalwisdom.com](http://www.fiscalwisdom.com)



Connecticut Offices (860) 673 – 1942  
CT Toll Free (800) 438 – 4513  
New York Office (315) 348 - 0348  
NY Toll Free (888) 693 - 8390



Place  
Financial Advisors

Please think of us whenever you or someone you care for needs the following:

ersification  
on qualified  
es

t Advice  
cession

egies  
utions  
ment  
otiations  
;

urly or annual retainer  
it management  
risk analysis  
Planning  
s – IRA, 401(k), etc.  
Guaranteed or variable  
Techniques  
stance  
Protection Strategies  
es & Strategies  
ion strategies  
Plan Rollovers  
& charitable planning  
d foundation planning

## Mike Chadwick’s Money Matters

15 New Britain Avenue  
Unionville, CT 06085  
(860) 673 1942

Torrington, CT  
Manlius, NY

## Chadwick Financial Advisors Place Financial Advisors



CERTIFIED FINANCIAL PLANNER™



The certification marks above are owned by Certified Financial Planner Board of Standards Inc. and are awarded to individuals who successfully complete CFP Board’s initial and ongoing certification requirements.