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Will You See Higher Tax Rates in 2011?



The year was 2001. The top marginal federal income tax bracket was 39.6%, and the tax rate that applied to most long-term capital gains

was 20%. Then came the Economic Growth and Tax Relief Reconciliation Act of 2001, followed two years later by the Jobs and Growth Tax Relief Reconciliation Act of 2003. By mid-2003, the top marginal tax rate was 35%, and the 20% capital gains rate had dropped to 15%. But this tax relief was designed to be temporary--the provisions that established lower rates were crafted to self-expire after a period of time. And now, in 2010, we're only months away from seeing those provisions expire.

Federal income tax brackets

Right now, there are six marginal income tax brackets: 10%, 15%, 25%, 28%, 33%, and 35%. For 2010, these brackets apply to married couples filing joint federal income tax returns in the following manner:

| 2010 Marginal Income Tax Brackets | |
|-----------------------------------|-------------------|
| Married Filing Jointly | |
| Taxable Income | Marginal Tax Rate |
| Not over \$16,750 | 10% |
| Over \$16,750 to \$68,000 | 15% |
| Over \$68,000 to \$137,300 | 25% |
| Over \$137,300 to \$209,250 | 28% |
| Over \$209,250 to \$373,650 | 33% |
| Over \$373,650 | 35% |

As it stands now, these marginal tax brackets will expire at the end of 2010. There would be no 10% bracket for 2011, and the remaining bracket rates would return to their original 2001 levels: 15%, 28%, 31%, 36%, and 39.6%.

Long-term capital gain tax rates

For 2010, if you sell shares of stock that you've held for more than a year, any gain is long-term capital gain, generally taxed at a maximum rate

of 15%. If you're in the 10% or the 15% marginal income tax bracket, however, you'll pay no federal tax on the long-term gain (a 0% tax rate applies). That means if you're a married couple filing a joint federal income tax return, and your taxable income is \$68,000 or less, you'd pay no federal tax on the gain.

However, these rates are also scheduled to expire at the end of 2010. Absent new legislation, in 2011, a 20% rate will generally apply to long-term capital gains. Individuals in the 15% tax bracket (remember, there won't be a 10% bracket in 2011) will pay the tax at a rate of 10%. Special rules (and slightly lower rates) will apply for qualifying property held for five years or more.

Finally, while qualifying dividends are taxed in 2010 using the same capital gain tax rates described above (i.e., 15% and 0%), in 2011 they'll be taxed as ordinary income.

Will Congress take action?

In the proposed 2011 budget submitted to Congress in February, President Obama asked for a permanent extension of the current 10%, 15%, and 25% marginal income tax brackets, and an expansion of the current 28% tax bracket. The current 33% and 35% brackets would be allowed to expire, resulting in the top two marginal rates for 2011 returning to 36% and 39.6%. The expanded 28% bracket would be calculated in a way that would allow individuals earning less than \$200,000 (less the standard deduction amount and one exemption) and married couples filing jointly earning less than \$250,000 (less the standard deduction and two personal exemptions) to escape taxation at the top rates.

The President also proposed making the current tax rates that apply to long-term capital gain (i.e., the 0% and 15% rates) permanent, but adding a new 20% rate for those in the newly reestablished 36% and 39.6% brackets.

Will Congress act, or will it simply let current rates expire? There's plenty of time before 2011, so stay tuned ...

Hope you enjoy our mid-year newsletter. I look forward to visiting with you soon. Have a great summer.

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Returning to Work After You've Retired



According to the U.S. Department of Labor, 29% of Americans age 65 to 69 are currently employed.

No matter how much you've looked forward to retirement, you might find yourself missing the social interaction and financial benefits you enjoyed when you were employed. Perhaps getting a full- or part-time job will enable you to rely less on your retirement savings, leaving more to potentially grow for the future. Or maybe you're looking forward to pursuing your dream of owning a business. Whether working during retirement is a choice--or a necessity--make sure you understand the financial implications.

Finding the right work opportunity

Many people spend 20 years or more in retirement, so it's important to do something you love. If you don't quite know what that is, or you aren't ready to commit to a permanent position, you might try working in a contract job, or signing up with a temporary employment agency that will allow you to work when, and where, you wish. Some agencies even offer health and retirement benefits. If it's been a while since you searched for work, get in touch with a local career counselor to get tips on preparing a job application or resume, and to learn more about the jobs available in your community.

To help you determine your salary requirements and how many hours you'll work, spend some time reviewing your retirement plan, focusing on your retirement income needs. Then limit your job search to businesses that offer the right combination of pay, benefits, and working environment.

Working for yourself

Once you retire, you may finally be ready to turn your ideas and talents into a business. Mature entrepreneurs often have the time and experience necessary to become successful business owners. However, make sure you have enough capital to start up and run your business--it may take longer than you think for your business to become profitable. And don't jeopardize your retirement security by relying on your credit cards, life savings, and home equity to finance your business.

Will working affect your Social Security benefits?

If you're receiving Social Security retirement benefits and you're younger than your full retirement age (65 to 67), your benefits will be reduced if you earn more than a certain amount. In 2010, \$1 in benefits will be withheld

for every \$2 you earn over the annual earnings limit of \$14,160. A higher earnings limit applies in the year you reach full retirement age. If you earn more than this limit (\$37,680 in 2010), \$1 in benefits will be withheld for every \$3 you earn over that amount, until the month you reach full retirement age--then you'll get your full benefit every month thereafter, no matter how much you earn. (But note that even if your benefits are withheld, that reduction isn't permanent. Your benefit will be increased at full retirement age to account for the amount withheld because of your earlier earnings.)

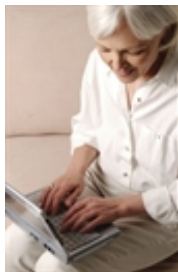
Not all income reduces your Social Security benefit. In general, Social Security only takes into account wages you've earned as an employee, net earnings from self-employment, and other types of work-related income, such as bonuses, commissions, and fees. Pensions, annuities, IRA payments, and investment income won't reduce your benefit.

Also, keep in mind that working may enable you to put off receiving your Social Security benefit until a later date. In general, the later you begin receiving benefit payments, the greater your benefit will be. Whether delaying the start of Social Security benefits is the right decision for you depends on your personal circumstances.

What about income taxes? In general, your Social Security benefit won't be subject to income tax if that's the only income you receive during the year. But if you work during retirement (or you receive any other taxable income, or tax-exempt interest), a portion of your benefit may become taxable. IRS Publication 915 has a worksheet that can help you determine if any part of your Social Security benefit is subject to income tax.

Will working affect your pension?

Unless you plan to return to work with your former employer, your pension benefit won't be affected--you can work, receive a salary from your new employer, and also receive your pension benefit from your former employer. However, if you are considering taking another job--even part-time--with your former employer, check with your plan administrator. Some plans require that your pension benefit be suspended if you retire and then return to work for the same employer.



Avoiding Probate: Is It Worth It?

When you die, your estate goes through a process that manages, settles, and distributes your property according to the terms of your will. This process is governed by state law and is called probate. Probate proceedings fall under the jurisdiction of the probate court (also called the Surrogate's, Orphans', or Chancery court) of the state in which you are domiciled at the time of your death. This court oversees probate of your personal property and any real estate that is located in that state. If you own property located in a state other than the state in which you are domiciled at the time of your death, a separate "ancillary" probate proceeding may need to be initiated in the other state.

Note: "Domicile" is a legal term meaning the state where you intend to make your permanent home. It does not refer to a summer home or a temporary residence.

Items that are subject to probate are known as probate assets. Probate assets generally consist of any property that you own individually at the time of your death that passes to your beneficiaries according to the terms of your will. Nonprobate assets include all property that passes outside of your will. Examples of nonprobate assets include property that is owned jointly with right of survivorship (e.g., a jointly held bank account) and property that is owned as tenants-by-the-entirety (i.e., real property owned jointly by a husband and wife). Another example is property that passes to designated beneficiaries by operation of law, such as proceeds of life insurance and retirement benefits.

Why avoid probate?

Most wills have to be probated. The rules vary from state to state, but in some states, smaller estates are exempt from probate, or they may qualify for an expedited process.

Probate can be slow. Depending on where your executor probates your estate and the size of your probate estate, the probate process can take as little as three months or as long as three years. Three years can be a long time to wait for needed income. It can take even longer if the estate is a complicated one or if any of the heirs are contesting the will.

Probate can be costly. Probate costs usually include court costs (filing fees, etc.), publication costs for legal notices, attorney's fees, executor's fees, bond premiums, and appraisal fees. Court costs and attorney's fees can vary

from state to state. Typically, the larger the estate, the greater the probate costs. However, if a smaller estate has complex issues associated with its administration or with distribution of its assets (e.g., if the decedent owned property in several states), probate can be quite costly.

Probate is a public process. Wills and any other documents submitted for probate become part of the public record, something to consider if you or your family members have privacy concerns.

Why choose to go through probate?

For most estates, there's usually little reason to avoid probate. The actual time and costs involved are often modest, and it just doesn't make sense to plan around it. And, there are actually a couple of benefits from probate. Because the court supervises the process, you have some assurance that your wishes will be abided by, and, if a family squabble should arise, the court can help settle the matter. Further, probate offers some protection against creditors. As part of the probate process, creditors are notified to make their claims against the estate in a timely manner. If they do not, it becomes much more difficult for them to make their claims later on.

In addition, some states require that your will be probated before the beneficiaries under your will can exercise certain rights. Among the rights that may otherwise be limited are the right of your surviving spouse to waive his or her share under the will and elect a statutory share instead, the right of your surviving spouse to use your residence during his or her remaining life, the right of your surviving spouse to set aside certain property, and the right of your surviving spouse to a family allowance.

How to avoid probate

An estate plan can be designed to limit the assets that pass through probate or to avoid probate altogether. The major ways property is passed outside of probate are by owning property jointly with rights of survivorship; by ensuring that beneficiary designation forms are completed for those types of assets that allow them, such as IRAs, retirement plans, and life insurance; by putting property in a trust; and by making lifetime gifts.

See your financial professional or attorney for more information.

Why avoid probate?

- *It can be slow; getting needed assets into the hands of your heirs may be delayed*
- *It can be costly, especially if an estate is large or complex, or ancillary probate is needed*
- *It is public; documents that you wish to remain private can be accessed by the public*



How to avoid probate

- *Own assets jointly with rights of survivorship*
- *Own assets that pass by beneficiary designation, such as life insurance and retirement plans*
- *Use a trust*
- *Gift assets during your lifetime*



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Ask the Experts



How have stocks performed after a recession?

Mark Twain said it best: "History doesn't repeat itself; at best it sometimes rhymes." Past performance is no guarantee of future results, and history can be

an uncertain guide in terms of what might happen with stocks this time around as the economy begins to stagger out of a recession.

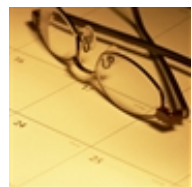
That said, it's fascinating to look at how various subsegments of the stock market have behaved relative to one another. Particularly interesting is the comparison between the performance of small-cap stocks and that of large caps after each of the last six recessions. In each case, small caps led the way out of those downturns. During the 12 months after the recession came to an end, as declared by the National Bureau of Economic Research (NBER), small caps beat large caps every time.

The average difference over the six recovery periods was 14.5%. In some cases, the difference was dramatic; in others, small caps were barely ahead. Here are the percentages by which small caps beat the S&P 500*:

- December 1970-November 1971: 1.3%
- April 1975-March 1976: 23.2%
- August 1980-July 1981: 28.4%
- December 1982-November 1983: 14.4%
- April 1991-March 1992: 14.8%
- December 2002-November 2003: 5.2%

Will history rhyme this time? It's hard to say. Many economists feel the current recession ended sometime in summer 2009. Small-cap stocks have certainly done well since then, but some experts feel large caps are best equipped to navigate a credit crisis. However, until the NBER retroactively declares an official end to this recession, there's no way to know for sure. And don't forget that small caps historically have involved greater risk from market fluctuation, so a double-dip downturn could hit them hardest.

*Percentages calculated based on data from Ibbotson SBBI *Market Results for Stocks, Bonds, Bills, and Inflation* for small company stocks and the S&P 500 Composite Index.



How long does it take a bear market to end?

A bear market, typically defined as an overall stock market decline of at least 20% over an extended period, historically has lasted an average of a little

over a year.* On average, bull markets tend to last almost twice as long as bear markets, but sometimes the differences can be even more dramatic. For example, the bear market that began in January of 2002 lasted almost nine months; it was followed by a five-year bull market from October 2002 to October 2007.

The shortest bear market on record lasted only about six weeks, from mid-July 1998 to the end of August. The longest? October 1939 through April 1942 (almost 30 months), beating out April 1930 to June 1932 (just over two years).

However, defining bear markets and subsequent recoveries from them isn't as straightforward as it might seem. For one thing, a long-term bear market can be interrupted by one or more shorter-term bull markets (or vice versa). For example, was the period between March 2000 and October 2002 a single

30-month bear market with a roughly 3-month "bear market rally" from September 2001 to the beginning of 2002, as some market technicians argue? Or was it two independent bear markets--one from March 2000 to September 2001 and a second from January 2002 to October 2002--that were separated by the shortest bull market since the Depression summer of 1932?

By definition, you only know you're in either a bear or bull market in retrospect, once the market has moved consistently in one direction or another. And the past isn't necessarily a good predictor of what will happen in the future. Since investing is about the future rather than the past, it may make sense to focus more on factors such as asset allocation than on the timing of a recovery you can't control.

*All time frames based on data from the *Stock Trader's Almanac 2010* on the Standard & Poor's 500, a market-cap weighted index composed of the common stocks of 500 leading companies in leading industries of the U.S. economy.