



CAMBIUMSM

November 2009

New Jersey
254 Brick Boulevard
Suite 1
Brick, NJ 08723
Tel 732.262.5323
Fax 732.262.5324

New York
2500 Westchester Avenue
Suite 401
Purchase, NY 10577
Tel 914.825.1025
Fax 914.251.0344

Partners@cambiumonline.com

***"Expect the best. Prepare for the worst. Capitalize on what comes."
- Zig Ziglar***

QUICK AND EASY SELF-QUIZ

For your own enlightenment, answer the following 3½ questions. (If you can't remember what happened in 2007, make a guess.)

- | | | |
|---|------------------------------|-----------------------------|
| 1. Are you currently saving money on a regular basis? | YES <input type="checkbox"/> | NO <input type="checkbox"/> |
| 2. Did you pay income taxes in 2007? | YES <input type="checkbox"/> | NO <input type="checkbox"/> |
| 3a. Was your 2007 adjusted gross income greater than \$66,532? | YES <input type="checkbox"/> | NO <input type="checkbox"/> |
| or... | | |
| 3b. Was your 2007 adjusted gross income greater than \$113,018? | YES <input type="checkbox"/> | NO <input type="checkbox"/> |

If you're reading this publication, it's quite likely you answered "yes" to more than two of the three questions, which means you are a part of a demographic minority in the United States. Whether you know it or not, you have a unique financial standing relative to most of the nation. For an interesting take on what it means to be part of the financial minority, read on. You probably won't get this type of commentary from the teleprompter-reading talking heads in the national media.

THE MINORITY REPORT

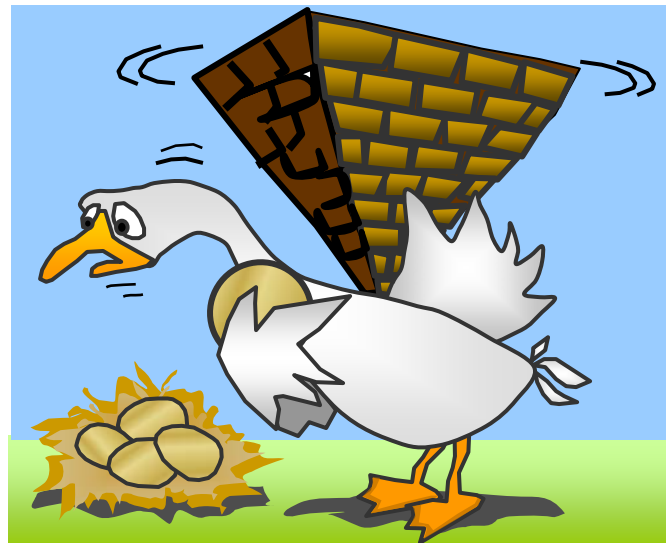
In determining your status as part of the financial minority in the United States, there are two key indicators:

1. Are you paying income taxes?
2. Are you saving money?

In ways you may not have considered, these two financial actions are tightly connected, especially for those in the financial minority. Let's look at the significance of income taxes first.

YOU are one of the "golden geese" supporting the inverted pyramid
(and that might be a good thing).

According to IRS statistics released July 30, 2009, if you reported an Adjusted Gross Income (AGI) on your 2007 federal income tax return of more than \$66,532, your household income is in the top 25% of all American households. If the number was above \$113,018, you made the top 10%.



While defining the term "rich" is always an exercise in *relativity* (the term "rich" is often applied to someone who earns or owns more than you), those whose AGIs are part of the top 10% cumulatively earn 48% of all income in the United States. For the top 25%, their incomes represent 69% of all AGI. Collectively, those at

the top of the AGI scale have a proportionately higher percentage of financial resources.

Even though it's possible that some with high AGIs may not pay income taxes (because of other factors like a large number of dependents, high deductible expenses and/or tax credits), those in the top 25% of AGI in the United States paid more than 86% of all the income taxes collected in 2007, with the top 10% accounting for 71% of all income taxes paid. (Note that these statistics do not include amounts paid as FICA or Medicare taxes; the figures are just the amount assessed by the federal government against your income.)

**The top 10% of household incomes...
earn 48% of all US income...and pay 71% of
all income taxes.**

**The top 25% of household incomes...
earn 69% of all US income...and pay 86% of
all income taxes.**

To simplify these numbers, look at it like this:

Conversely, those in the bottom 50% of AGI paid less than 3% of all income taxes. In an April 13, 2009 *Wall Street Journal* opinion piece, former presidential advisor Ari Fleischer says Congressional Budget Office statistics show that **40% of Americans pay no income tax at all**. Furthermore, the trend of the past decade, as well as current political sentiment, is for the top income categories to pay even higher percentages of income taxes going forward.

These numbers mean that if you are one of the top 25% or 10% in AGI, you are one of the "golden geese" that is relied on to deliver golden eggs for government use. As Fleischer explains it,

"Picture an upside-down pyramid with its narrow tip at the bottom and its base on top. The only way the pyramid can stand is by spinning fast enough or by having a wide enough tip so it won't fall down. The federal version of this spinning top is the tax code; the government collects its money almost entirely from the people at the narrow tip and then gives it to the people at the wider side. So long as the pyramid spins, the system can work. If it slows down enough, it falls."

At first look, being one of the individuals at the bottom of the inverted pyramid who pays to keep things going for everyone else may seem unfair. But maybe things for the wealthy minority aren't so bad.

The financial minority is larger than you might think

Carl J. Milsted is a theoretical physicist who, according to his weblog* "dabbles in economics and political activism." In a September 11, 2009 article "The Real Secret of the Super Rich", Milsted makes an extensive statistical analysis of the distribution of income in the United States in comparison to standard bell curve results. His conclusion: There are a lot more wealthy people in the United States than should be expected, at least according to models used to make statistical predictions. In Milsted's words, "the rich defy the norm. They are *way* outside the bell curve."

Another way of looking at it is that the United States, in spite of its flaws and critics, still offers more financial opportunity to more people in comparison to other countries and economic systems.

*www.holisticpolitics.org - PaidToBeRich.blogspot.com

The wealth of the minority grows faster – and receives government support

In general, the amount of taxation imposed by various government entities in the United States is high. In particular, the income tax burden on the financial minority is steep. But while it is true that income taxes have risen disproportionately for the top 25%, their incomes have also increased disproportionately as well. For example, the AGIs of the top 1% rose 50 percent from 2001-2007, while the increase was only 29% for the bottom 50 percent. Simply put, the rich got "more rich" than everyone else over that seven-year period.

This quirky occurrence – the rich getting richer even as they are taxed more – is a unique characteristic of a "mixed economy" where governments attempt to manage the national economy, but do not control it entirely. How does this happen? Here's a simplified explanation: Taxes, tariffs and other monetary policies are used to siphon some of the productivity of the wealthy to pay for government programs and services (social welfare, consumer regulation, law and order, national defense, etc.). Once governmental units establish streams of revenue, they don't want them to dry up, because if there is no financial production, there will be no economy to manage. It's the personification of the golden goose fable: If governments want on-going streams of revenue from their citizens, they can't kill the ones who generate them. Since they generate and hold a disproportionate percentage of income and assets, governments need the financial support (or at least compliance) of wealthy individuals.

This dependence on the wealthy minority results in what many economic observers call **corporatism**. According to Steven Malanga (writing in a column for *Real Clear Markets* on April 8, 2009), corporatism is "the notion that elite groups of individuals...committees or public-private boards can guide society and

coordinate the economy from the top down and manage change by evolution, not revolution.” Governments make the rules, but they make them in concert with those who will be most affected by them. And since all governments (at the federal, state and local levels) need money to function, they have a vested interest in maintaining a working relationship with the wealthy minority, despite the occasional populist rhetoric that is broadcast to the other 75% of the population.

On an institutional level, the corporatism mentality explains why some parts of the economy were considered “too big to fail” and received government-sponsored financial assistance, while others were left to wither and die (or go into bankruptcy). On an individual level, it explains why most of the individual tax breaks end up being used by the wealthiest segment of the population. (One example: studies repeatedly show that 401(k) participation increases in proportion to income, partly because wealthier individuals have the ability to save more, but also because the tax advantage is greater for those in higher income tax brackets.)

The idea of governments supporting the wealthy minority may sound like political commentary, but this isn’t a liberal or conservative talking point. Commentators from very disparate ends of the political spectrum say the same thing: The current economic system helps the wealthy – once they get there – and gives them an edge going forward.

A September 21, 2009. *Huffington Post* article by Dean Baker, Co-Director of the Center for Economic and Policy Research makes this comment:

“It is now pretty much official policy that financial giants...will not be allowed to fail. If their bad investment decisions again bring them to the edge of bankruptcy, the federal government will again rush to the rescue, handing out whatever cash and loans are needed to keep the banks afloat.

“This status gives these banks a clear edge in credit markets against their smaller competitors. If everyone knows that the government can be counted on to come to the rescue of these banks, then there is less risk in lending them money. Therefore, they pay lower interest rates than if they had to borrow in a free market.”

This perspective can be applied at an individual level. Individuals with money get the tax breaks – because they *have the money to take advantage of them*. Taxable income from capital gains receives favorable tax treatment compared to income from wages. Mortgage interest deductions are for homebuyers, not renters. Just like Baker’s “financial giants,” individuals in the wealthy minority “have a

clear edge in credit markets against their smaller competitors” – i.e., they can actually borrow money, and at better rates. And just like wealthy institutions, government-sponsored “bailouts” are always a possibility.

You may not have thought of it this way, but an example of tax law adjusting to support/bail out the wealthy minority is the Roth IRA. As it became apparent that many wealthy individuals might actually pay more income tax when they withdrew funds from their IRAs and 401(k)s than the tax deduction they received for the deposit, the Roth IRA was established. Roth IRAs offer no tax deduction for the deposit, but incur no taxes on either gains or withdrawals. Besides establishing a new type of retirement account, new tax law also made it possible to convert a 401(k) or IRA to a Roth IRA, as long as you paid the tax on the old accounts before reconfiguring them. When the stock market tumbled, many people with IRAs and 401(k)s realized now might be a good time to pay the tax and make the change. As a special concession for Roth conversions executed in 2010, the IRS will allow for the tax payment to be spread over two years, instead of paid in the year the transaction is completed. A rather benevolent gesture by government, wouldn’t you say?

The necessity of the wealthy minority to save

If the only things you’re doing as a member of the financial minority are earning a big income and paying taxes, you’re really not in the game. In order to take advantage of your minority status, it is imperative to accumulate assets. You must save – not only for your own financial well-being, but for the preservation of the whole inverted-pyramid/golden-goose system.

Remember, in order for governments to collect revenues, there must be people producing revenue. Someone must be making a profit. And while governments may be good at assessing taxes on profits, governments aren’t intended to make a profit, and don’t know how to make a profit.

Making a profit requires a forward-thinking, future-oriented mindset. People save because they understand that it’s not only what is happening today that matters, but what could happen tomorrow.

People who save provide the foundation for a functioning economy.

Some of this saving reflects a prudent view of the future; that a job may not last forever, and things might have to be replaced. But saving is also the seed money for future productivity. Saving provides the capital that moves innovative ideas into practical use. Eventually some of those innovations will become new engines of progress, improving existing markets and opening new ones.

Whether it stems from an attitude of caution or ambition, people who save provide the foundation for a functioning economy.

This emphasis on saving and accumulating assets may read like an “Economics for Fifth-Graders” discussion, but a quick once-over of the facts reveals most Americans don’t understand the importance of saving, or the consequences of not saving. Which is why the economic playing field is skewed to favor the wealthy minority.

How to accumulate assets as part of the wealthy minority

People acting on behalf of government (legislators, political analysts, economic advisors, etc.) may know that saving is a critical component in maintaining a solid economy. Often, they will enact legislation to encourage saving, such as IRAs or 401(k)s, but the governmental perspective on saving and asset accumulation is prone to be short-sighted or incomplete.

Consider that the major purpose of IRAs or 401(k)s is to provide retirement income. That’s a worthwhile savings goal, but there are plenty of other reasons to save. When Bill Gates was 25, what would have been the value of saving in a 401(k) for retirement in 40 years as opposed to investing some of his savings directly in his business? In real life, especially when one is interested in making a profit, the need for capital is fluid, constantly changing. Most government-sponsored asset accumulation programs don’t offer much flexibility.

This leads to another counter-intuitive conclusion: The best way for the wealthy minority to save or accumulate assets is often outside of government programs – so that you can take full advantage of government programs at a later date.

Go back to the Roth IRA conversion example. The sticking point for making the transition from an IRA to a Roth IRA is paying the tax. In order to take full advantage of the potential long-term tax savings and avoid an early-withdrawal penalty, you want to pay the conversion *cost* from “outside funds,” i.e., from a non-qualified savings or brokerage account.

Along the same line of thought, since many qualified plans now have “catch-up” contribution clauses (another “adjustment” that benefits the wealthy minority), it might be to your long-term advantage to focus early accumulation efforts in places that offer more liquidity, knowing that gains could be poured over into an IRA,

If you’re paying income taxes but not accumulating assets, it’s time to reassess your financial behavior.

401(k), etc. at a later date.

The Pragmatic Idealist

There are compelling social and philosophical issues regarding the widening wealth gap in the United States between the top 25% and everyone else. In his article mentioned above, Ari Fleischer concludes America would be a better country if everyone paid taxes. Milsted, the theoretical physicist who dabbles in economics, is a staunch free-market supporter who says “I want to narrow the wealth gap by creating *more* millionaires. I want a society where it is *easier* to get rich, but harder to stay rich. And in the process we can dispense with many of those pesky government programs.” Those are both interesting perspectives.

But this is not a discussion of the social or ethical ramifications of the gap between the wealthy minority and everyone else. It’s simply a practical assessment of which approaches work best in light of the current state of affairs. As it stands, most people’s economic lives would be better off if they were earning enough to both pay income taxes and save.

If you’re paying income taxes but not accumulating assets, it’s time to reassess your financial behavior. Because for those who earn enough to pay taxes but never acquire the saving habit, the long-term prognosis is they eventually become part of the financial majority.

If you are already saving, it might be time to address the other issue: What percentage of your asset accumulation program is placed into “outside” (outside of government control) sources?

These concepts relating to your position as part of the financial minority may be a bit counter-intuitive, but relatively simple. However, the applications of these ideas can be complex (don’t try a Roth IRA conversion on your own). **The practical answer: consult with your financial professionals!**



Life Insurance Policyholders Conclude: We Don’t Want The Risk

“There are worse things in life than death. Have you ever spent an evening with an insurance salesman?” – Woody Allen

For most people, discussing the working parts of a life insurance policy probably isn’t captivating after-dinner conversation. But a recent report concerning the current state of the life insurance industry in the United States reveals some basic information that even Woody Allen might find worthwhile.

The Recession Hits Life Insurance Companies Too...

While life insurance companies remain some of the most solid financial institutions in the world, sales of life insurance have been affected by the downturn in the economy. According to an August 31, 2009 report released by the Life Insurance Research and Marketing Association (LIMRA), annualized premiums are down 23% for the first six months of 2009, the greatest six-month decline since the second half of 1942.

Considering the declines in employment, housing and the stock market, it's not surprising that the recession would affect life insurers as well. People may want life insurance, may want to keep the life insurance they already have, but some just don't have the money to pay premiums. But the surprise is that certain types of life insurance have experienced great decline in sales while others did not.

The LIMRA report divided life insurance into four broad categories: Term, Whole Life, Universal Life and Variable Life. Here is the year-over-year change in sales for each type:

Term	- 03%
Whole Life	- 04%
Universal Life	- 29%
Variable Life	- 72%

In light of the broad-based recession, a decrease of 3% or 4% (for term and whole life) doesn't seem too bad. And in fact, the LIMRA report noted that 40% of the companies in the evaluation were reporting increased sales compared to the first six months of the previous year.

But the numbers for universal and variable life are a different story. And the story is about what can happen when the assumptions for life insurance don't match reality.

The Nuts and Bolts: Who assumes the risk? (This is the part Woody Allen won't read)

A life insurance policy is comprised of three elements: the cost of insurance, the operating expense of the company, and the investment return generated from the collected premiums.

Term and Whole Life policies are designed to provide a high degree of contractual certainty in regard to these three variables.

With level term, the premiums are established for the period of the term, and typically guaranteed not to change. There are no cash values. If the insured dies during the term, a benefit is paid.

For Whole Life, a level premium delivers both a guaranteed lifetime cash value accumulation and a death benefit. If the insurance company's performance exceeds the contractual guarantees, this surplus/profit is

Here's a quick quiz on a financial concept.
Do you know the answer?



Remembering 9/11

When the stock market closed in September 10, 2001 the Dow Jones Industrial Average (DJIA) stood at 9,605.51. The next day, the terrorist attacks on the World Trade Center occurred.

Question: Eight years later, on September 11, 2009, was the closing price of the DJIA...

- a. higher?
- b. lower?
- c. the same?

passed on to policyholders in the form of non-guaranteed dividends. Paying the base premium always assures the policyholder that the guaranteed benefits will remain in place.

In both Term and Whole Life policies the only requirement of the policyholder is that the premium be paid. All other financial responsibilities are shouldered by the insurance company.

By design, Universal and Variable Life are contracts that offer a lesser spectrum of guarantees, potentially lower out-of-pocket costs and/or greater investment return opportunities to the policy owner, and more risk to the policyowner.

Universal life gives policyholders the option of flexible premiums, some of which may be much less compared to whole life. Because the owner isn't *required* to pay as much premium on a regular basis, cash value accumulation will also be less certain. And instead of dividends reflecting "over-performance" based on guaranteed assumptions (as in a whole life policy), the interest rate credited in a Universal policy may be designed to bolster or extend the initial costs of the contract. In this way, a policy guaranteed to last until age 65 may also *project* to remain in-force for the rest of one's life.

Essentially, the Universal Life policy owner assumes responsibility for some of the future costs of insurance. If at some point the dividends aren't sufficient to pay the costs of insurance, the policyholder will either have to increase premium payments, decrease benefits or surrender the policy.

In a Variable Life policy, the policyholder is given the option of investing cash values in the stock market, usually through participation in the underlying investment funds within the policy. The cash values placed in these investments are not guaranteed; they will fluctuate in value according to the performance of the

underlying funds. With Variable Life, the policy owner assumes responsibility for the performance of the underlying investments.

What Happened?

When Universal Life first reached the marketplace in the 1970s and 1980s, it was not uncommon for policy illustrations to project a dividend rate of 10-12% or higher. Over the next two decades, when these historically high dividend projections did not come to pass, many policy owners faced the unwelcome prospect of higher premiums or diminished benefits. What was once projected to perform like a stripped-down “leaner” version of a whole life policy now became an expiring term policy unless the premiums were increased. Similarly, Variable life policies suffered when the underlying investments did not perform as anticipated.

If the purpose of insurance is to manage risk, universal and variable life policies obviously place more of the risk management responsibility in the hands of the policy owner. And as best-selling financial author Garrett Gunderson is fond of saying, “self-insurance is really no insurance.” Considering the events of the past two years, it’s logical that individuals would be more risk-averse and less likely to gamble on any financial decision – including their life insurance program.

During three decades of explosive economic growth, financial risk management sort of got lost in the euphoria. But as recent events indicate, there are no shortcuts. There are legitimate uses for Universal and Variable Life insurance, but the plain vanilla versions of life insurance – Term and Whole Life – provide a strong level of risk management for most people.

Do you have Universal or Variable Life Insurance policies? If so, now might be a good time to find out how much "risk" is in your contract.

“The path of least resistance is the path of the loser.”

- H.G. Wells

“If you are not willing to do some homework, plan on getting screwed sooner or later.”

- Errol F. Moody, Professor and Expert Witness for life insurance

FINANCIAL LITERACY QUESTION

Here's a quick quiz on a fundamental financial issue. Do you know the answer?

Remembering 9/11

Answer: **c. the same.** On Friday, September 11, 2009, the Dow closed at 9,605.41.

Material discussed is meant for general illustration and/or informational purposes only and it is not to be construed as tax, legal or investment advice. Although the information has been gathered from sources believed reliable, please note that individual situations can vary, therefore the information should be relied upon when coordinated with individual professional advice.

Cambium Group, LLC

New Jersey
254 Brick Boulevard
Suite 1
Brick, NJ 08723
Tel 732.262.5323
Fax 732.262.5324

New York
2500 Westchester Avenue
Suite 401
Purchase, NY 10577
Tel 914.825.1025
Fax 914.251.0344

www.cambiumonline.com

Cambium Group, LLC is an agency of The Guardian Life Insurance Company of America (Guardian), New York, NY.
Cambium Group, LLC is not an affiliate or subsidiary of Guardian