



## Berman Capital Management & Research

Ted C. Berman

Michael J. Basso, CFP

3077 W. Jefferson Street

Suite 200

Joliet, IL 60435

815-725-8300

tedberman@afpadvisor.com

www.bermancapitalmanagement.com

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The Frugal Habits of Millionaires

Test Your Knowledge of Financial Basics

Think Outside the Shoe Box When  
Organizing Financial Records

Are you ready to retire?

# Berman Capital Management News *Financial & Investment Insights*

## The Frugal Habits of Millionaires



The word "millionaire" typically conjures up images of a lavish, jet-setting lifestyle, but behind the scenes, that may not always be the case. Like Warren Buffett, who famously still lives in the relatively modest

house in Omaha, Nebraska, that he bought in 1958 for \$31,500, many millionaires (and billionaires) live a modest, if not downright frugal lifestyle--a lifestyle that may have helped them become millionaires in the first place.

We've all heard the saying "It takes money to make money." So how can you find extra dollars to save and invest? If you're looking to improve your financial position, consider putting some of these habits into practice.

### Cultivate a frugal mindset

Many people equate being frugal with being cheap, but that's not really correct. Being frugal means carefully watching your dollars and not spending more than you need to--a trait many millionaires employ. To help cultivate a frugal mindset, get in the habit of asking yourself this question: "With a little extra effort and/or sacrifice on my part, is there any way I can save money here?" Having a frugal mindset can really help when it comes time to playing the role of American consumer, where temptation is everywhere.

### Buy wisely and sparingly

We all need "stuff" now and then; the key is not overdoing it or overpaying for it. Try to buy mostly what you really need, not what you really want. Money you save can then be used to build your savings and investment accounts.

Don't let the price tag of your car, home, or designer suit define your character. For example, a reliable car that safely gets you from Point A to Point B may be completely sufficient for your needs. According to the book *The Millionaire Next Door*, the top car brand among millionaires is Toyota, not Mercedes or BMW. Even Mark Zuckerberg, the billionaire founder of Facebook, has been spotted driving an Acura TSX, an entry-level luxury car whose

base price is about \$30,000. The bottom line? As you move up the net worth ladder, avoid the temptation to elevate your "status" by overspending on luxury goods.

You can be smart about everyday consumer purchases, too. You might be surprised to learn that many millionaires clip coupons, buy in bulk, wait for sales, scour eBay and Craigslist for deals, limit clothing purchases, fly coach, avoid credit cards, and save half their restaurant meal for lunch the next day--habits that can free up cash for the occasional splurge.

### Shun debt

Debt is bad. Well, mostly. At times taking on debt is necessary, for example when buying a home or attending college, because without it, many people won't have saved enough money. But generally speaking, you should be leery of taking on debt for things that cause you to live beyond your means. Remember, every dollar you borrow today is a dollar you'll have to pay back tomorrow, with interest.

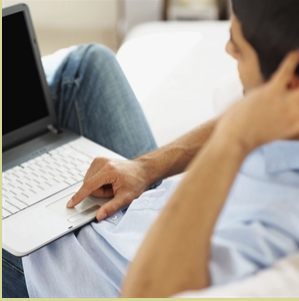
People who turn a modest financial base into wealth often do so by living frugally, saving regularly, investing wisely, and avoiding debt. By contrast, people who end up in a perpetual cycle of debt are often those who spend and borrow excessively to support an unsustainable lifestyle.

### Take action

What do CEOs Tim Cook (Apple), Ursula Burns (Xerox), Robert Iger (Disney), and Indra Nooyi (PepsiCo) have in common? They're all up by 5:00 a.m., hitting the gym, reading, working. As Benjamin Franklin famously quipped: "Early to bed and early to rise makes a man healthy, wealthy, and wise." And indeed, many millionaires and leaders aren't couch potatoes. They don't sit around waiting for things to happen; they make things happen--by getting up early, working hard, looking for opportunities, constantly educating themselves, taking calculated risks, networking, staying active, and generally trying to improve themselves day in and day out. And with the explosion of information online 24/7, learning new things has never been easier.



## Test Your Knowledge of Financial Basics



*A little knowledge can go a long way in pursuing your financial goals. For more information about the topics in this article, or for other personal finance-related questions, speak with a trusted financial professional.*

*All investing involves risk, including the possible loss of principal.*

Working with a trusted financial professional is one of the best ways to help improve your overall financial situation, but it's not the only thing you can do. Educating yourself about personal finance concepts can help you better understand your advisor's recommendations, and result in more productive and potentially more prosperous financial planning discussions. Take this brief quiz to see how well you understand a few of the basics.

### Questions

**1. How much should you set aside in liquid, low-risk savings in case of emergencies?**

- a. One to three months' worth of expenses
- b. Three to six months' worth of expenses
- c. Six to twelve months' worth of expenses
- d. It depends

**2. Diversification can eliminate risk from your portfolio.**

- a. True
- b. False

**3. Which of the following is a key benefit of a 401(k) plan?**

- a. You can withdraw money at any time for needs such as the purchase of a new car.
- b. The plan allows you to avoid paying taxes on a portion of your compensation.
- c. You may be eligible for an employer match, which is like earning a guaranteed return on your investment dollars.
- d. None of the above

**4. All of the money you have in a bank account is protected and guaranteed.**

- a. True
- b. False

**5. Which of the following is typically the best way to pursue your long-term goals?**

- a. Investing as conservatively as possible to minimize the chance of loss
- b. Investing equal amounts in stocks, bonds, and cash investments
- c. Investing 100% of your money in stocks
- d. Not enough information to decide

### Answers

**1. d.** Conventional wisdom often recommends setting aside three to six months' worth of living expenses in a liquid savings vehicle, such as a bank savings account or money market mutual fund. However, the answer really depends on your own individual situation. If your (and your

spouse's) job is fairly secure and you have other assets, you may need as little as three months' worth of expenses in emergency savings. On the other hand, if you're a business owner in a volatile industry, you may need as much as a year's worth or more to carry you through uncertain periods.

**2. b.** Diversification is a smart investment strategy that helps you manage risk by spreading your investment dollars among different types of securities and asset classes, but it cannot eliminate risk entirely. You still run the risk of losing money.

**3. c.** Many employer-sponsored 401(k) plans offer a matching program, which is like earning a guaranteed return on your investment dollars. If your plan offers a match, you should try to contribute at least enough to take full advantage of it. (Note that some matching programs impose a vesting schedule, which means you will earn the right to the matching contributions over a period of time.)

Because 401(k) plans are designed to help you save for retirement, the federal government imposes rules about withdrawals for other purposes, including the possibility of paying a penalty tax for nonqualified withdrawals. You may be able to borrow money from your 401(k) if your plan allows, but this is generally recommended as a last resort in a financial emergency. Finally, traditional 401(k) plans do not help you avoid paying taxes on your income entirely, but they can help you defer taxes on your contribution dollars and investment earnings until retirement, when you might be in a lower tax bracket. With Roth 401(k)s, you pay taxes on your contribution dollars before investing, but qualified withdrawals will be free from federal, and in many cases, state taxes.

**4. b.** Deposits in banks covered by the Federal Deposit Insurance Corporation are protected up to \$250,000 per depositor, per bank. This means that if a bank should fail, the federal government will protect depositors against losses in their accounts up to that limit. The FDIC does not protect against losses in stocks, bonds, mutual funds, life insurance policies, annuities, or municipal securities, even if those vehicles were purchased at an insured bank. It also does not protect items held in safe-deposit boxes or investments in Treasury bills.

**5. d.** To adequately pursue your long-term goals, it's best to speak with a financial professional before choosing a strategy. He or she will take into consideration your goals, your risk tolerance, and your time horizon, among other factors, to put together a well-diversified strategy that's appropriate for your needs.





*If you have questions about how long to keep copies of your federal tax returns and related records, see IRS Publication 17, Your Federal Income Tax. And because states may have different rules, check with your state's tax authority to find out how long to keep state tax returns and records.*

## Think Outside the Shoe Box When Organizing Financial Records

If you've ever had trouble finding an important financial document, you know why it's necessary to keep your financial records organized. Less clutter means less stress, and though you'll need to commit a bit of time up front to organize your files, you can save time and money over the long term when you can find what you need when you need it.

### What records do you need to keep?

If you keep paperwork because you "might need it someday," your files are likely overflowing with nonessential documents. One key to organizing your financial records is to ask yourself "Why do I need to keep this?" Documents that you should retain are likely to be those that are related to tax returns, legal contracts, insurance claims, and proof of identity. On the other hand, documents that you can easily duplicate elsewhere are good candidates for the shredder. For example, if you bank online and can view or print copies of your monthly statements and cleared checks, you may not need paper copies of the same information.

### How long should you keep them?

A good rule of thumb is to keep financial records only as long as necessary. For example, you may want to keep ATM receipts only temporarily, until you've reconciled them with your bank statement. If a document provides legal support and/or is hard to replace, you'll want to keep it for a longer period or even indefinitely.

#### Records that you may want to keep for a year or less include:

- Bank or credit union statements
- Credit card statements
- Utility bills
- Annual insurance policies

#### Records that you may want to keep for more than a year include:

- Tax returns and supporting documentation
- Mortgage contracts and supporting documents
- Receipts for home improvements
- Property appraisals
- Annual retirement and investment statements
- Receipts for major purchases

#### Records that you may want to keep indefinitely include:

- Birth, death, and marriage certificates
- Adoption papers
- Citizenship papers

- Military discharge papers
- Social Security card

Of course, this list is not all-inclusive and these are just broad guidelines; you may have a good reason for keeping some records for a shorter or longer period of time.

### Where should you keep them?

Where you should keep your records and documents depends on how easily you want to be able to access them, how long you plan to keep them, and how many records you have. A simple set of labeled folders in a file cabinet works fine for many people, but electronic storage is another option if space is tight.

For example, one easy way to cut down on clutter and still keep everything you need is to store some of your files on your computer. You can save copies of online documents or purchase a scanner that you can use to convert your documents to electronic form. But make sure you keep backup copies on a portable storage drive or hard drive, and make sure that your files are secure.

Another option to consider is cloud storage. Despite its lofty name, cloud storage is simply an online backup service that allows you to upload and store your files over the Internet, giving you easy access to information without the clutter. Information you upload is encrypted for security. If you're interested, look for a company with a reliable reputation that offers automatic backup and good technical support, at a reasonable subscription cost.

### Staying organized

Keeping your financial records in order can be even more challenging than organizing them in the first place. One easy way to prevent paperwork from piling up is to remember the phrase "out with the old, in with the new." For example, when you get this year's auto policy, discard last year's. When you get an annual investment statement, discard the monthly or quarterly statements you've been keeping. It's a good idea to do a sweep of your files at least once a year to keep your filing system on track (doing this at the same time each year may be helpful).

But don't just throw your financial paperwork in the trash. To protect sensitive information, invest in a good quality shredder that will destroy any document that contains account numbers, Social Security numbers, or other personal information.

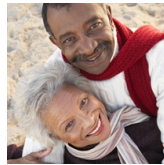
Whatever system you choose, keep it simple. You'll be much more likely to keep your records organized if your system is easy to follow.



**Berman Capital Management & Research**

Ted C. Berman  
 Michael J. Basso, CFP  
 3077 W. Jefferson Street  
 Suite 200  
 Joliet, IL 60435  
 815-725-8300  
 tedberman@afpadvisor.com  
 www.bermancapitalmanagement.com

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**Are you ready to retire?**

Here are some questions to ask yourself when deciding whether or not you are ready to retire.

**Is your nest egg adequate?**

It's obvious, but the earlier you retire, the less time you'll have to save, and the more years you'll be living off of your retirement savings. The average American can expect to live past age 78. (Source: CDC, "Deaths: Preliminary Data for 2011") With future medical breakthroughs likely, it's not unreasonable to assume that life expectancy will continue to increase. Is your nest egg large enough to fund 20 or more years of retirement?

**When will you begin receiving Social Security benefits?**

You can begin receiving Social Security retirement benefits as early as age 62. However, your benefit may be 25% to 30% less than if you waited until full retirement age (66 to 67, depending on the year you were born).

**How will retirement affect your IRAs and employer retirement plans?**

The longer you delay retirement, the longer you can build up tax-deferred funds in your

IRAs--remember that you need compensation to contribute to an IRA. You'll also have a longer period of time to contribute to employer sponsored plans like 401(k)s--and to receive any employer match or other contributions. (If you retire early, you may forfeit any employer contributions in which you're not yet fully vested.)

**Will you need health insurance?**

Keep in mind that Medicare generally doesn't start until you're 65. Does your employer provide post-retirement medical benefits? Are you eligible for the coverage if you retire early? If not, you may have to look into COBRA or a private individual policy--which could be an expensive proposition.

**Is phasing into retirement right for you?**

Retirement need not be an all-or-nothing affair. If you're not quite ready, financially or psychologically, for full retirement, consider downshifting from full-time to part-time employment. This will allow you to retain a source of income and remain active and productive.



**How much can I contribute to my IRA in 2014?**

The amount you can contribute to your traditional or Roth IRA remains \$5,500 for 2014, \$6,500 if you're 50 or older. You can contribute to an IRA in addition to an employer-sponsored retirement plan like a 401(k). But if you (or your spouse) participate in an employer-sponsored plan, the amount of traditional IRA contributions you can deduct may be reduced or eliminated (phased out), depending on your modified adjusted gross income (MAGI). Your ability to make annual Roth contributions may also be phased out, depending on your MAGI. These income limits (phaseout ranges) have increased for 2014:

Income phaseout range for deductibility of traditional IRA contributions in 2014	
1. Covered by an employer-sponsored plan and filing as:	
Single/Head of household	\$60,000 - \$70,000
Married filing jointly	\$96,000 - \$116,000
Married filing separately	\$0 - \$10,000
2. Not covered by an employer-sponsored retirement plan, but filing joint return with a spouse who is covered by a plan	
	\$181,000 - \$191,000

Income phaseout range for ability to fund a Roth IRA in 2014	
Single/Head of household	\$114,000 - \$129,000
Married filing jointly	\$181,000 - \$191,000
Married filing separately	\$0 - \$10,000

