New England Capital Financial Advisors
Independent Objective Advice

New England Capital Times

New England Capital Financial Advisors, LLC
Registered Investment Adviser

July 2015
Volume 34

Special Interest Articles:

"Talk about your plenty, talk about your ills. One man gathers what another man spills."

-St. Stephen,
By the Greatful Dead.

Advising the Grateful Dead

By Christopher W. Beale, CFP®

Hopefully everyone enjoyed the long holiday weekend as we celebrated the 4th of July. 2015 marks not only the 239th anniversary of our nation's independence, but also 80 years since social security became law and 50 years since the Grateful Dead was formed. I was reminded of this milestone as I spent my 4th of July with over 70,000 friends in Chicago watching the Grateful Dead's final shows at Soldier's Field.

I never considered myself a "Deadhead" although I did see the band over half a dozen times in my twenties and early thirties. As my 70,000 plus friends filed into Soldier's Field, I was surprised by the age ranges of the fans. Sure I expected to see 50, 60 and 70 year olds (yes I saw people wearing tie-dyed T-shirts with walkers) as well as 20 somethings with their infants. Imagine 20 and 30 somethings sitting next to me to watch a band whose original members range from age 67 to 75.

Obviously all the band members are all eligible for Social Security (SS) benefits. I don't know if they're taking SS but *what if I was their personal financial advisor*. What would I recommend to them about taking their SS benefits?

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Which is Better: Leasing a Car or Buying a Car?

By Christopher M. Lee, CFP®

The answer is — it depends. It's not possible to simply say that one is always better than the other because the answer depends on the specifics of each individual situation, which I will explain further. First, let's talk about the difference between buying and leasing.

First, leasing is only an option for financing brand new cars, not used cars, although leasing of used luxury cars is available from specialty car dealers in some cities. When you lease, you pay only a portion of a vehicle's total value, which is the part of the value that you "use up" during the time you're driving it.

You have a choice of not making a down payment; you pay sales tax only on your monthly payments (in most states). You may also be required to pay fees and possibly a security deposit that you don't pay when you buy. Lease payments are made up of two parts: a depreciation charge and a finance charge. The depreciation part of each monthly payment compensates the leasing company for the portion of the vehicle's value that is lost during your lease. The finance part (called money factor) is interest on the money the lease company has tied up in the car while you're driving it. In effect, you are borrowing the money that the lease company used to buy the car from the dealer. You repay part of that money in monthly payments, and repay the remainder when you either buy or return the vehicle at lease-end.

At lease-end, you may either return the vehicle, or purchase it for the part of the value that you haven't already paid. The purchase price is stated in your contract at the time you sign. If you decide to return your vehicle, you may be charged a lease-end disposition fee, and for any excessive mileage or wear-and-tear, the details of which are spelled out in your lease contract. Purchasing your vehicle avoids these fees. Since you pay only for a leased car's depreciation (lost value), you have nothing to show for the money you've spent. But, as we'll see in a moment, a car buyer also loses the same value to depreciation.

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Advising the Grateful Dead

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Let's start with some Social Security basics: SS provides primary benefits to workers in the form of retirement benefits and disability benefits. It also provides secondary benefits to dependents and survivors of workers. For the purposes of this article I will only concentrate on retirement benefits.

Of course as the personal financial advisor to the band members, I would have needed to advise both survivors and dependents as several band members, including lead band member Jerry Garcia, died prior to be being eligible for retirement benefits. My knowledge of social security disability benefits would have also helped during Jerry's drug rehabilitation and Phil Lesh's organ transplant surgery.

For your information, to be eligible for disability benefits from social security, you must have worked at least 10 years at a job covered by SS and the disability must be total (not partial) and long term (at least one year).

What about eligibility for SS retirement benefits?

Typically you must work 40 quarters (10 years) at a job covered by SS. Benefits are based on what you paid in – your highest 35 years of indexed earnings – and when you start taking benefits.

Full Retirement Age (FRA) is based upon your year of birth. If you were born 1937 or before, you're FRA is 65. If you were born in 1960 or later, your FRA is 67. There's a sliding scale for those born between 1937 and 1960. Anyone who meets the 40 quarter eligibility test can file for benefits at age 62.

If you're FRA is 66 (you were born between 1943 and 1954), and you start claiming benefits at age 62, you'll receive 75% of what you would have received at age 66. Claiming SS at age 62 will permanently reduce your benefits by 25% of what you would have received had you waited until FRA. In this example, waiting to claim benefits until age 70 would permanently earn you 32% more than claiming at FRA or age 66.

What does the same example look like if you were born in 1960 or later with an FRA of age 67? Claiming benefits at 62, gives you a 30% reduction from claiming at 67. Claiming at 70, gives you a 24% increase over claiming at age 67. There's no financial benefit for waiting to claim past age 70.

This of course means I would have recommended that Phil Lesh start taking SS five years ago when he turned 70. I would probably recommend that Bob Weir wait three more years until age 70 to increase his monthly benefit by 32%.

If (hopefully) this wasn't the last Grateful Dead tour, or if Bob Weir continues his solo tour between now and when he turns 70, these working years could be some of his best 35 earning years, thereby increasing his monthly SS check. Remember, even though the Grateful Dead was one of the highest grossing touring acts in the entire entertainment business between 1985 and 1995, out earning Bruce Springsteen, Madonna and Michael Jackson, the early years for the band were plagued by weak cash flow and indebtedness.

Certainly a SS lesson to be learned from the band members concerns longevity, which I believe to be one of the biggest risks of retirees. Being productive past what some would consider "retirement age" is becoming more common place. 22% of people who retired in 1980 expected to work in their retirement. In 2013, that number is 47%. Today a 65 year old couple has a 47% chance that one of them will live into their 90s. Life expectancies have increased dramatically in the last 80 years. If we are living longer on average, it is to our advantage to maximize SS benefits by delaying SS benefits.

While I'm not waiting for Phil Lesh, Bob Weir, Bill Kreutzmann or Mickey Hart to call me for advice, I do expect you to take advantage of our expertise at New England Capital. When to claim your SS benefits is only one issue as you maneuver through the complexities of the SS system. The Windfall Elimination Provision, Government Pension Offset, and claiming strategies such as Claim and Suspend, and Restricted Application are too complex for this article but may be the way to maximize YOUR benefits.

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"Don't be a collector of more than you need, got a lot of things growing , but keep watching your seeds."

-One Thing to Try by the Greatful Dead

Which is better: Leasing a Car or Buying a Car?

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When you buy, you pay for the entire value of a vehicle; regardless of how many miles you drive it or how long you keep it. You can pay cash or get an auto finance loan (or a combination of both).

Since you will eventually be building equity in the car, monthly loan payments are usually higher for a loan than for a lease — for the same car. You typically make a down payment of 10%-20%, pay sales tax on the full purchase price, and pay a loan interest rate determined by your loan company, based on your credit score. You make your first payment a month after you sign your contract. Later, you may decide to sell or trade the vehicle for its depreciated resale or trade value.

Now that you know those basics, you then need to answer some basic non-financial questions:

- Which is more important: Driving a new vehicle every two or three years with no major repair risks (Lease) or driving one vehicle for many years and assuming responsibility for all maintenance repairs after the first years (Buy)?
- Which is more important: Lower monthly payments but higher long term cost (Lease) or lower long-term cost but higher initial monthly payments (Buy)?
- Which is more important: Building ownership value and paying off your vehicle (Buy), or building no ownership value, with the benefit of lower monthly payments (Lease)?
- Do you drive no more than an "average" amount of miles in a year (12,000) (Lease) — or is your mileage highly unpredictable? (Buy)
- Do you take good care of your cars and maintain them properly (Lease and/or Buy) — or do you prefer be more lax about such things (Buy)?
- Do you have a stable lifestyle such that you will not want to end your lease early — or is there a high likelihood of wanting out early (Buy)?

"When God way up in heaven, for whatever it was worth, Thought he'd have a big old party, Thought he'd call it Planet Earth."

-One more Saturday Night by the Greatful Dead

Now that we have discussed some non-monetary issues that might affect your buying decision, let's talk about the costs.[1]

Lease Example

If you lease a $20,000 car that will have, say, an estimated resale value of $13,000 after 24 months, you only pay for the $7,000 difference (the depreciation), plus finance charges. This is fundamentally why leasing offers significantly lower monthly payments. You can return the car at lease-end, or buy it for the remaining $13,000 that you haven't already paid.

Buy Example

When you buy with a loan, you pay the entire $20,000 cost, plus finance charges. You own the car at the end of the loan, although its value is less than the $20,000 you initially paid — $7,000 less. All cars suffer the same value depreciation regardless of how they are financed — purchase or lease. You have the option to sell or trade the vehicle, or continue driving it while enjoying no further monthly payments.

If you are looking for a cost comparison when you are shopping for a vehicle, a great tool can be found at https://www.dinkytown.net/java/BuyvsLease.html

Buying versus Leasing a Car

So, buying a car with a loan is essentially like putting money into a declining-value savings account — you never get out as much as you put in. A portion of every payment you make is lost to depreciation and possible finance charges. What you have "to show" for your investment when your loan is paid off is only the part of a vehicle's value that is left over after depreciation and interest. However, if you plan to drive the vehicle for many years to come, its equity value at the end of your loan is of little concern to you.

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Advising the Greatful Dead
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SS has become an integral part of most people's retirement picture. For my fellow Baby Boomers, let us help you coordinate SS with the rest of your retirement plan. For my Millennials and GenX friends, I tell you SS will be there for you. According to the 2014 Report from the Social Security Trustees, SS has a $2.8 Trillion surplus and can pay promised benefits through 2033. After that it will provide 77% of scheduled benefits if Congress doesn't act. The SS system can be fixed but: 1) benefits must be reduced; 2) taxes into the system must increase; or 3) a combination of 1 & 2. Conceptually it is an easy problem to solve. It's the implementation that's difficult. But as the Trustees say in their report "Lawmakers should address the financial challenges facing Social Security and Medicare as soon as possible. Taking action sooner rather than later will leave more options and more time available to phase in changes so that the public has adequate time to prepare."

"Reach out your hand if your cup be empty. If your cup is full may it be again."

-Ripple by the Greatful Dead

Our goal at New England Capital is to help you financially prepare and plan for this long strange trip called life.

Fare Thee Well!

References:
Social Security; Boston College Center for retirement Research; AARP; J P Morgan

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Leasing, then, is similar to buying but without the equity "savings account." You pay for what you use (the depreciation and finance costs) and you don't put anything extra each month into "savings." It's true that you'll own nothing at the end of a lease; you'll have nothing "to show" for the money you've put into it. But … what you don't own is the same part of the car's original value — the depreciated part — that a buyer too doesn't own at the end of his loan. Again, a car's value depreciates the same amount whether it is leased or purchased. That money is gone forever, lease or buy. This is why we are not keen on using "investible assets" to buy a car outright. You are using potentially appreciating assets to buy a depreciating asset. You may be better off taking out a loan, which in today's market should be less than 3% interest rate (if you have qualifying credit score).

When leasing, it's often easy to overlook the fact that vehicle price is important and should be negotiated just as it should if you were buying. In fact dealers sometimes state, or imply, that price is not important or that price cannot be negotiated in a lease. **Not true**, it's just the opposite. Price is the most important factor — in either a lease or a purchase — for creating a low monthly payment.

On the surface, leasing can be more appealing than buying. Your monthly lease payments are typically much lower. Then, after enjoying the most trouble-free two or three years of the vehicle's life, you bring it back to the dealership and either lease another new one or simply walk away. There are other advantages to leasing [2]:

- There's often no down payment required when leasing, or only a low one.
- You can drive a higher-priced, better-equipped vehicle (newer technology) than you might otherwise be able to afford to buy.
- You're always driving a late-model vehicle that's usually covered by the manufacturer's warranty.
- It may offer an attractive tax deduction for someone using the car for business. An accountant is the best resource for more information on this subject.

Which is Better: Leasing a Car or Buying a Car?

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As attractive as a lease appears, however, there are a number of disadvantages:

- Leasing typically costs you more than an equivalent loan, in part because of higher finance charges.
- Once you're in the leasing habit, monthly payments go on forever. In contrast, the longer you keep a vehicle after a loan is paid off, the more value you get out of it.
- You have a limited number of miles in your lease contract, typically 12,000 to 15,000 miles a year. If you drive more than that, you'll have to pay an excess mileage penalty of 10 cents to as much as 25 cents for every additional mile. On the other hand, if you drive too little, you don't get credit for the unused miles.
- You must maintain the vehicle in good condition, or you'll have to pay excess wear-and-tear charges when you turn it in. So, if your kids are apt to turn the interior into a finger-painting studio or your car's a magnet for parking lot dents and dings, be prepared to pay extra.
- If you need to get out of a lease before it expires, you may be stuck with thousands of dollars in early-termination fees and penalties—all due at once. This could equal the amount it would cost had you stuck with the lease for its entire term.
- You aren't allowed to customize your vehicle in any permanent way.
- Arranging a lease can be a confusing, complicated process that can easily leave you paying more than you should.

It's important to consider these pros and cons very carefully, crunching the numbers for a particular vehicle both ways to see how they compare (using the above reference link).

One of the biggest expenses of buying a new car is depreciation. When you think of your other major purchases, which may be a house or even your investments you are expecting some form of appreciation. New cars, which include leased cars, have a lot of depreciation the second you drive it off the lot. With that being said used cars can offer more value for the dollar as someone else has already paid for that depreciation. Obviously buying used versus buying new comes with a whole set of pros and cons. But nonetheless, from a financial standpoint, the most beneficial decision may be to purchase a used car, as you may miss out on paying all of that depreciation – but it may come with more cost down the road with vehicle maintenance.

Happy car shopping!

Sources:

[1] http://www.leaseguide.com/
[2] http://www.consumerreports.org/cro/2012/12/pros-and-cons-of-leasing/index.htm

"Fare thee well now, let your life proceed by its own design. Nothing to fall now, let the words be yours, I'm done with mine.

-Cassidy by the Greatful Dead.