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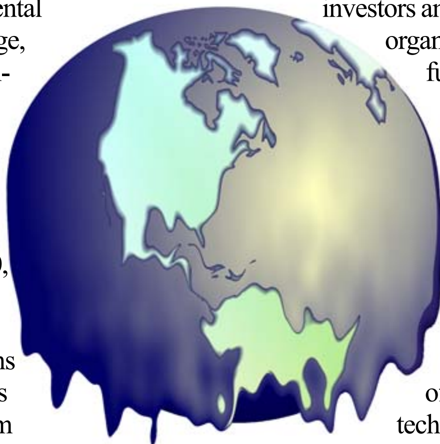
Global Warming, Now A Reality, Impacts Investing

As one debate ends, another begins. If human activity really is changing the climate—and these days, almost everyone agrees it is—investors must next ponder how global warming will affect the economy and particular companies and how best to tap the investment potential of mushrooming control efforts.

The Intergovernmental Panel on Climate Change, an international environmental group, projects that temperatures will rise at least 2.5 degrees and as much as 10.4 degrees Fahrenheit between 1990 and 2100, and investors seem increasingly convinced the financial implications could be severe. "This is becoming a main-stream investment issue," says Dan Bakal, director of electric power programs at Ceres, a Boston research and advocacy group.



Global investors are expected to commit $60 billion to clean energy sources this year, doubling the tally of only two years ago, according to New Energy Finance, a London research firm. Though that's a fraction of the $600 billion energy market, Bakal and other experts expect industries such as wind power, solar energy, and biofuels (ethanol) to grow at a rapid clip for years to come. No one is expecting this to be a dot-com-like bubble. However, clean-energy investing could be a fad, like many of the investment fads spawned during the oil crisis of the 1970s. Nonetheless, global warming is real and fossil fuels are primary contributors.

When gasoline and other fossil fuels burn, they produce large amounts of carbon dioxide and other gases that may trap energy from the sun and push up the earth's temperature, and much of the clean energy focus is on curbing these so-called greenhouse gases. Corporations, private equity firms, and hedge funds are pouring money into clean energy alternatives, while Ceres and other coalitions of investors and environmental organizations press mutual funds to support shareholder resolutions committing companies to control emissions. The California Public Employees Retirement System, one of the nation's largest pension funds, has pledged hundreds of millions to clean technology initiatives, and investment banking firm Goldman Sachs recently announced it will invest $1 billion in alternative energy projects. British billionaire Richard Branson has pledged $3 billion over the next decade to renewable energy initiatives within his company as well as outside investments.

Multinational corporations such as British Petroleum, General Electric, Sharp, and Toyota are among those aggressively pursuing new energy technologies, and that could translate into bigger profits for these companies, says Jeff MacDonagh, a portfolio manager for Domini Social Investments in New York. Toyota, for example, a pioneer in developing hybrid electric vehicles, is now licensing the technology to other companies, while GE Wind has grabbed a 50% share of the U.S.

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Victoria Marrone
Ph.D., MBA, CSA, CFP®
Chief Executive Officer

What Do You Get In A Financial Plan?

Financial plans used to be forbidding, book-length tomes that, not surprisingly, no one read. These days, a plan tends to be more of an outline, spelling out goals and the means for achieving them. But whatever a plan looks like, its purpose is the same. It is the connection between the parts of your financial life. It coordinates short-term needs with long-term goals, and when a change in one part of your life puts other things out of whack, the financial plan restores the balance.

One way to think about a financial plan is by holding up your hand in front of you; your fingers represent retirement, tax, and estate planning, investment management, and insurance. Your financial plan is like the space between your fingers. It's what makes each finger work together with the next one.

Each part of your financial plan can help you get where you want to go, and each can operate separately. You could create a college savings account, for instance, without looking at how that would affect your retirement plan, or use a simple rule of thumb to decide how much life insurance to buy rather than considering what would be needed to replace your income, pay for your children's education, and help your spouse retire comfortably. But it makes sense to use the whole hand, because all of these things are interrelated.

Investments, taxes, insurance, your estate—it all comes together in one plan

Suppose, for example, that you struck it rich during the 1990s' bull market. Maybe you used some of your gains to pay off your mortgage, and that freed up more of your earnings to put into your retirement plan. But your income taxes went up because you lost your mortgage interest deduction, and your expanding net worth meant that estate taxes could also become a problem.

To create a financial plan, an advisor first must probe the details of your financial situation. What are your objectives? How do you feel about risk? If stock investments plummet, will you stay the course or sell out? How old are your children, and where do they want to go to college? What kind of pension or 401(k) plan do you have at work? Are you hoping to leave an inheritance for your children, or are you willing to exhaust your savings in retirement? And so on.

Once your needs are understood, a plan is put together that connects the dots. Your investment plan takes into account your risk tolerance and is designed to fund your current and long-range goals. Those objectives, in turn, are based on what it will cost for college, the income you'll need in retirement, the amount you want to leave to your children. The plan stipulates how much insurance will be required to protect your family if you die prematurely, and whether insurance should be part of your estate plan.

But no financial plan is a once-and-done document. It's part of an ongoing process of checking progress, making adjustments, and getting back on track when life derails your best-laid plans. If you have another child, receive an inheritance, lose your job, or get divorced, a good financial plan, like a helping hand, should be able to pull things back together again. ●

Tax Law Now Allows Those Inheriting Retirement Plan Assets

Most 401(k)s and other employer-sponsored retirement plans are bequeathed to spouses, and with good reason. Until a recent change in rules, only a spouse could inherit a retirement plan other than an IRA and avoid immediate taxes. Now, although the process must be handled carefully, any beneficiary should be able to receive a retirement plan and enjoy the same tax-postponing benefits that a husband or wife always could.

Under the old rules, if your husband got the money, fine; he could roll over the windfall into his own IRA and make withdrawals over the course of his expected lifespan. Though each year's required distribution would add to his taxable income, the rest of the account would continue to compound, and there might be a sizable balance left at his death.

But your daughter? Most employer plans require an account to be emptied within five years of an employee's death. She would have had to take the money and, not being allowed to move it into an IRA, would have been stuck paying income tax immediately—and likely would have lost a third or more of her inheritance to taxes in the process.

The new rules are much kinder to non-spouse beneficiaries. Now, should you choose to leave your 401(k) to a child, a same-sex partner, or anyone else, that person may roll over the inherited plan to an IRA. But the law is prickly about the process. To make a successful rollover, your heir must:

- Open an inherited IRA to take the money. A spouse who inherits a 401(k) can merge the account with her own IRA, but others must set up a new account specifically created to receive funds transferred from the deceased's retirement plan.
- Be sure to title the new account correctly. For instance, Dad IRA (Deceased) FBO Daughter.
- Make sure the money goes directly from the company plan to the

Five Financial Ideas For Grandparents

Spoiling your grandchildren with extravagant gifts may be fun, but you're not really doing them—or yourself—any favors. Instead, it may be wise to look for ways that help grandchildren but that also make financial sense for all of you.

Your long experience handling money matters is one invaluable gift you can pass along. Sharing your savvy not only helps grandkids develop healthy financial habits but also to understand family and cultural values. So tell them about your first job, how you started a business, and financial goofs you've made, such as spending too much or getting suckered into bad investments. "There's a big legacy gap," says Nathan Dungan, author of *Prodigal Sons and Material Girls: How Not to Be Your Child's ATM*. "Grandparents aren't having these conversations with the grandkids."

But don't leave your own children out of the loop. Make sure your advice and giving strategies don't conflict with their plans or guidance for your grandchildren. Here are several ways you might help:

Leverage your gifts. A grandparent can now give as much as $12,000 a year tax-free to each child and grandchild. If you have a large family and make such gifts for several years, you could substantially reduce your taxable estate. But rather than simply putting cash in the grandchildren's pockets, consider creative alternatives. For example, you might open a custodial savings account for a grandson and match what he saves. Or you could establish a brokerage account and use your contributions to help your granddaughter learn about investing. But stick to broad mutual funds rather than individual stocks. Choosing the wrong stock could lead to deep losses and discourage your would-be Warren Buffett.

Take care of college. Setting up a state-sponsored 529 college savings plan for your grandchild brings benefits for both of you. Start early and kick in the annual gift-tax-free maximum, and your grandson or granddaughter should be in fine shape when tuition comes due. Money in 529 plans grow tax free and withdrawals for qualified college expenses aren't taxed, either. And, if you want to accelerate giving, you can make five years' gifts—a maximum of $60,000—all at once. Moreover, because you control the plan, you don't have to worry about a spendthrift scion squandering the money. And, if you didn't get around to starting a 529? Consider sending a tuition check directly to your grandchild's college. It won't count against your $12,000 annual gift-tax exemption.

Put a roof over their heads. First-time homebuyers often earn enough to qualify for a mortgage but lack cash for a down payment and closing costs. Your gift could make up the shortfall. But there are other options, too. You could make a low-interest or interest-free loan, though that may raise complicated tax issues. Or, if qualifying for a home loan is a problem for your grandchildren, you could co-sign a mortgage. Some financial companies offer programs allowing grandparents to pledge securities as collateral for a grandchild's mortgage, so you can lend a helping hand without the expense and taxes of liquidating personal holdings.

Guide with your gifts. One alternative to direct giving is to fund one or more type of trusts, which can be customized to fit many financial and personal situations. An incentive trust, for example, could be instructed to distribute funds to your grandchildren in installments, at specified points in their lives, and may tie payouts to your grandchild's accomplishments—reaching a certain income level, for example, or getting a college or graduate degree. But tread carefully, warns Dungan. "You need to help a grandchild develop healthy financial habits before trust distributions start," he says. And be careful about the kinds of hurdles you set up. "You want your grandchildren to be connected to their life passions, not yours, so don't strive for too much control," he suggests.

Encourage philanthropy. There are several options for helping your grandchildren learn the value of charitable giving, and many of these vehicles also offer estate tax advantages. For example, you could transfer assets from your estate into your own family foundation, though to be effective, a family foundation needs an initial commitment of as much as $1 million. Your grandkids could get involved by helping screen grant applications or serving on the foundation's board. A less expensive alternative is a donor-advised fund, which also lets grandparents and grandchildren confer about what charities to support. "This is like having your own foundation to support causes you believe in, but without the hassles and paperwork that go along with operating one," Dungan says. ●

To Retain Tax Deferral Much Longer

heir's new IRA. If your beneficiary touches the money, he or she will be immediately taxed.

Keep in mind that it doesn't matter when the account owner dies as long as the beneficiary postpones the rollover until 2007. So if the account owner died in 2006, an heir can benefit from the new rules as long as the rollover is made in 2007.

If you've ever changed jobs, you may already have transferred retirement funds from your former employer to an IRA. Until the rules changed, that was the only way to ensure favorable tax treatment for a nonspousal heir. And even now, a rollover is often advisable. IRAs tend to offer a wider range of investment options than you get in a typical 401(k), and it's easier to monitor investments in a single account.

There is at least one advantage to keeping money in a 401(k), however. If you retire, you may begin taking distributions from an employer plan at age 55 without incurring the 10% early withdrawal penalty you would owe for withdrawing assets from an IRA before age 59½. Under the new rules, you can have the penalty-free early access of a 401(k) while also accommodating nonspousal heirs. ●

What To Do When Identity Thieves Strike

Maybe you notice an unfamiliar transaction on your credit card statement. Or perhaps you're rejected for a loan for no apparent reason. Whatever tips you off, if you think you may be a victim of identity theft, act immediately to limit further damage to your financial resources and reputation. Set up a plan of action and keep a record of everything you do. Here are several essential steps.

- File a police report, and get a copy as proof of a crime against you. If your local police department is reluctant to make the report, try the state police or the state attorney general's office.
- Contact the fraud department at any of the three major credit reporting agencies—Equifax (800-525-6285); Experian (888-397-3742); or TransUnion (800-680-7289) and ask to have a fraud alert on your file. That agency will notify the other two, and you'll receive free credit reports you can review for signs of fraudulent activity. An initial alert, active for at least 90 days, goes on when you suspect you may be a victim—if your wallet has been stolen, for instance. Once you provide proof a crime has been committed, the agency may activate an extended fraud alert that remains on your account for up to seven years. A fraud alert lets creditors know to contact you before making changes to existing accounts or opening new ones in your name. Keep in mind that if you place a fraud alert on your account, you may be required to approve big changes or call your credit card company to okay individual transactions.
- Close any accounts you believe may have been tampered with or opened fraudulently. Make sure to document the accounts and keep a record of fraudulent charges. Just a phone call will get some credit card companies to initiate charge dispute investigations on your behalf, while others may require you to fill out a fraud dispute form. The company may also request a copy of a police report and for you to fill out an affidavit about the crime. In most cases, Visa and MasterCard limit your losses to $50 no matter when the fraud occurred.
- Contact all financial institutions where you have accounts and review your statements for fraudulent activity. If you suspect your bank account has been tampered with, you have 60 days from the date your statement is sent to you to make a written report to the bank. But the more vigilant you are, and the more quickly you take action, the smaller your losses are likely to be. A loss reported within two days of the fraud could limit your liability to $50. Letting the bank know after two days but before 60 days could leave you liable for at least $500 of what the thief has taken. After 60 days, you may have to bear the burden of the entire loss.
- Be sure to let the Federal Trade Commission (FTC) know when you suspect you've been victimized. Call 877-ID-THEFT. The agency maintains an identity theft database that is used by federal law enforcement agencies. ●

Impact Of Global Warming

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market for wind turbines.

Retail and homebuilding companies are embracing efficiency measures, from switching to energy-saving florescent lighting to installing solar panels, MacDonagh says. Insurance companies, meanwhile, stung by losses from Hurricane Katrina and other catastrophes that could be linked to global warming, have begun factoring climate risk into their business models, according to MacDonagh. He also sees opportunities for utilities and natural resource extraction companies. These range from traditional producers of oil, natural gas, and coal to new clean energy technologies such as coal gasification and carbon sequestration.

Venture capital dollars are also flooding in. The three biggest technology initial public offerings in 2005 were for solar companies, and Ron Pernick, a founder of Clean Edge, a consulting firm in San Francisco, dubbed 2006 "the year of biofuel." Last July, two biofuel IPOs, Aventine Renewable Energy Holdings and VeraSun Energy, brought in more than $800 million, and the global market for biofuels, created from a wide range of animal and vegetable sources, hit $15.7 billion in 2005, up 15% from the previous year, says Pernick. The markets for wind and solar technologies reached $11.8 billion and $11.2 billion, respectively, in 2005, up 47% and 55% from previous year totals.

Investing in alternative energy, however, can be perilous, says Pernick, with some small, promising companies unable to keep pace with demand. The solar industry, for example, has suffered from a lack of silicon for solar electric cells. Biofuels, whose prices rise and fall along with volatile world markets for oil and other fuels, also face obstacles, particularly in getting products to consumers. And the rising cost of steel and unpredictable government subsidies could slow the growth of wind turbines.

With so many competing new technologies, it can be tough to decide what's worth supporting, says Maurice Schoenwald, a portfolio manager who specializes in environmental innovation. "Some things deserve investment, but many aren't going anywhere," Schoenwald says. Hydrogen fuel cells, for example, remain mostly in a research and testing phase and may not be widely adopted any time soon, while Schoenwald remains bullish on ocean and tidal energy. "If those can be harnessed, they could supply the world," he says. ●

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