



JOHNSTON INVESTMENT COUNSEL

TRUSTED FIDUCIARIES & FEE-ONLY ADVISORS

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The Higher Education Opportunity Act



One of the big pieces of legislation that passed in 2008 was the Higher Education Opportunity Act (the Act). Aside from reauthorizing the Higher Education Act of 1965 for another six years, the Act includes many other provisions intended to improve college affordability, access, and accountability. Here are some highlights of this new law.

A new federally run college pricing website

In an effort to make it easier for students and their families to compare the cost of colleges in an apples-to-apples format, the Act directs the Department of Education to create a new website that will list up-to-date cost information on individual colleges, including tuition and fees for the current year, average price of attendance after grant aid, recent price increases, and changes in per-student spending, among other items.

The website will also include calculators that families can use to estimate their expected college costs

Cost considerations

According to a study released by student-loan lender Sallie Mae, 40% of parents and students said they paid no attention to cost when searching for a college.

Source: Sallie Mae, August 2008 study

based on income and family data, as well as the annual and total cost of attending a particular college. The hope is that this information will help students and their families during the college selection process.

A simpler financial aid application

According to remarks by U.S. Secretary of Education Margaret Spellings in a speech at Harvard University in October, 40% of college students—roughly 8 million students—don't apply for federal aid because the process is

too complicated. To address this problem, the Act directs the Department of Education to streamline the federal application, the FAFSA, over the next five years. To support this initiative, Spellings announced a revised form that has only 27 questions (down from 100), and stated that families will now learn how much aid they can expect to receive, as opposed to how much they are expected to contribute under the current system. The new FAFSA should be available for the 2009 application year.

Expanded Pell Grant and work-study

The Act increases the maximum Pell Grant, the federal government's largest financial aid program, from \$5,800 to \$9,000 per academic year. The Act also expands the community service opportunities available under the federal work-study program.

Graduate PLUS loans

The Act creates a six-month grace period for repayment of all graduate student PLUS loans disbursed after July 1, 2008. Under prior law, these borrowers had to begin repaying their loans as soon as they were no longer enrolled on at least a part-time basis.

Other provisions

The Act also includes many other provisions:

- A requirement that textbook publishers sell unbundled versions of textbooks that previously may have been bundled with expensive DVDs and CDs
- A new scholarship program for active duty military personnel and their families
- A requirement that private student loan lenders inform students of their less costly federal borrowing options
- An expansion of student loan forgiveness for individuals who work in certain public service jobs

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Retirement Plan and IRA Limits for 2009

An increasing number of retirement plan and IRA limits are indexed for inflation each year. Some of the key numbers for 2009 are discussed below.

Elective deferrals

If you're lucky enough to be eligible to participate in a 401(k), 403(b), 457(b), or SAR-SEP plan, you can make elective deferrals of up to \$16,500 in 2009, up from \$15,500 in 2008. If you're age 50 or older, you also can make a catch-up contribution of up to \$5,500 to these plans in 2009, up from \$5,000 in 2008.

If your 401(k) or 403(b) plan allows Roth contributions, your total elective contributions, pretax and Roth, can't exceed \$16,500 (\$22,000 with catch-up contributions). You can split your contribution any way you wish. For example, you can make \$9,500 of Roth contributions and \$7,000 of pretax 401(k) contributions. It's up to you.

If you participate in a SIMPLE IRA or SIMPLE 401(k) plan, you can contribute up to \$11,500 in 2009 (up from \$10,500 in 2008). If you're age 50 or older, the maximum catch-up contribution to a SIMPLE IRA or SIMPLE 401(k) plan in 2009 is \$2,500, unchanged from 2008.

IRA limits remain the same for 2009

The amount you can contribute to a traditional or Roth IRA remains at \$5,000 for 2009, and the maximum catch-up contribution for those age 50 or older remains at \$1,000. You can contribute to an IRA in addition to an employer-sponsored retirement plan. But if you (or your spouse) participate in an employer-sponsored plan, your ability to deduct traditional IRA contributions may be limited, depending on your income. Roth contributions are also subject to income limits.



Contribution limits: 2009 tax year* (2008 limits in parentheses)		
Plan type	Annual dollar limit	Catch-up limit
401(k), 403(b), and 457(b)** plans	\$16,500 (\$15,500)	\$5,500 (\$5,000)
SIMPLE plans	\$11,500 (\$10,500)	\$2,500 (\$2,500)
Traditional and Roth IRAs	\$5,000 (\$5,000)	\$1,000 (\$1,000)

*Contributions can't exceed 100% of your pay. If you participate in a 403(b) or 457(b) plan, special rules may allow an even greater catch-up contribution.

**\$5,500 catch-up applies only to governmental 457(b) plans.

Some other key numbers for 2009

For 2009, the maximum amount of compensation your employer can take into account when calculating SEP and qualified plan contributions and benefits is \$245,000 (up from \$230,000 in 2008).

The maximum annual benefit you can receive from a defined benefit pension plan is limited to \$195,000 in 2009 (up from \$185,000 in 2008).

And the maximum amount that can be allocated to your account in a defined contribution plan (for example, a 401(k) plan or profit sharing plan) in 2009 is \$49,000 (up from \$46,000 in 2008), plus age-50 catch-up contributions. (This includes both your contributions and your employer's contributions. Special rules apply if your employer sponsors more than one retirement plan.)

Income phaseout range for determining deductibility of traditional IRA contributions in 2009	
1. Covered by an employer plan	
Single/Head of household	\$55,000 - \$65,000 (\$53,000 - \$63,000 in 2008)
Married filing jointly	\$89,000 - \$109,000 (\$85,000 - \$105,000 in 2008)
Married filing separately	\$0 - \$10,000 (same for 2008)
2. Not covered by an employer plan, but filing joint return with a spouse who is covered	
	\$166,000 - \$176,000 (\$159,000 - \$169,000 in 2008)
Income phaseout range for determining ability to fund Roth IRA in 2009	
Single/Head of household	\$105,000 - \$120,000 (\$101,000 - \$116,000 in 2008)
Married filing jointly	\$166,000 - \$176,000 (\$159,000 - \$169,000 in 2008)
Married filing separately	\$0 - \$10,000 (same in 2008)

The ABCs of 1031 Like-Kind Exchanges

A like-kind exchange, sometimes called a 1031 exchange after the section of the Internal Revenue Code that governs these transactions, is the exchange of one business or investment property for another. Provided the property you receive is of a "like kind" to the property you transfer, and all other requirements are met, no gain or loss is recognized on the income deferred as a result of the exchange. This has made like-kind exchanges a popular technique for investors looking to defer the payment of taxes on capital gains. When it comes to like-kind exchanges, though, even the most straightforward transaction is complicated.

Simultaneous swaps

If there is a "basic" like-kind exchange, it takes the form of a simultaneous exchange. You transfer business or investment property to another party in return for similar property. For example, let's say you own a piece of land that has a basis of \$200,000 (your cost) and a fair market value of \$400,000. If you were to sell the property, you would recognize \$200,000 in gain. Instead of selling the land, however, you exchange it for a rental property owned by another individual. If all the conditions of IRC Section 1031 are met, you do not recognize any gain as a result of the exchange (recognition of any gain is deferred until you sell the rental property). If you receive cash in addition to the rental property, gain is recognized to the extent of the cash received.

Deferred exchanges

With a deferred exchange, you give up your original property before receiving the replacement property. During the time that you're looking for a replacement property, you can't touch the proceeds from your original property (taking control of cash or proceeds before the entire like-kind exchange is complete can disqualify the transaction). For this reason, deferred like-kind exchanges generally involve executing a written exchange agreement with a qualified intermediary or other exchange facilitator, such as a bank, trust company, or attorney, that you pay to handle the transaction. The intermediary, who may assist you in locating a replacement property, is responsible for keeping the proceeds from your original property separate in an escrow account until the exchange is complete.

In a deferred exchange, you have 45 days from the date that you relinquish your original

property to identify, in writing, potential replacement properties. You must then receive the replacement property and close the exchange within 180 days from the date you relinquish your original property, or by the due date of your tax return (including extensions) for the tax year in which you relinquished your original property, whichever is earlier.

Tenancy-in-common (TIC) exchanges

With a TIC exchange, you exchange real property, and as replacement property, you receive a partial ownership interest (you're a co-owner, specifically a tenant-in-common) in commercial real estate. For example, you might exchange a piece of land with a fair market value of \$400,000 for a 10% TIC ownership interest in a \$4 million commercial property. TIC interest offerings include partial ownership interests in manufacturing facilities, office buildings, and malls.

These exchanges are extremely complicated. In fact, for a TIC interest to even qualify as potential replacement property in a like-kind exchange, there are extensive conditions that must be met. Most TIC interests are sold as securities, and are not available to the general public. TIC interests are generally available only to individuals who qualify as "accredited" investors (basically, those with a net worth greater than \$1 million, or income of at least \$200,000--\$300,000 for a married couple--for the prior two years). TIC offerings are non-conventional investments, and while they might provide ownership opportunity in a larger property than you might otherwise be able to afford, they are not suitable for all investors. In addition to the significant fees and lack of liquidity generally associated with TIC exchanges, you'll typically have little or no day-to-day control over the TIC property.

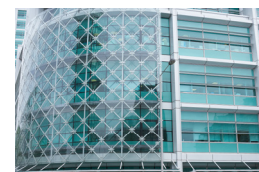
Final thoughts

It can't be overemphasized: like-kind exchanges are complicated, and there's simply no way to cover all the rules here. So, before you even consider a like-kind exchange, you should familiarize yourself with the details, including all tax aspects of an exchange. Note as well that special rules apply to exchanges between related parties.

A like-kind exchange can be a powerful strategy for investors and business owners, so it's worth understanding. But, if you're interested, make sure that you contact a qualified professional who can help you navigate the intricate rules that apply.

Like-kind property is property of the same nature, character, or class. Quality or grade does not matter. Most real estate will be like-kind to other real estate. For example, real property that is improved with a residential rental house is like-kind to vacant land. One exception for real estate is that property within the United States is not like-kind to property outside of the United States. Also, improvements that are conveyed without land are not of like kind to land.

**IRS Fact Sheet
FS-2008-18**



The like-kind exchange rules do not apply to:

- *Stock in trade or other property held primarily for sale*
- *Stocks, bonds, or notes*
- *Other securities or evidences of indebtedness or interest*
- *Interest in a partnership*
- *Certificates of trust or beneficial interests*
- *"Choses in action" (rights to recover money or property in a court proceeding)*



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Ask the Experts



Is my brokerage account protected?

Most brokerage accounts are protected by the Securities Investor Protection Corporation (SIPC). Unlike the Federal Deposit Insurance Corporation (FDIC), which protects bank deposit accounts, the SIPC is not a government agency. Though created by Congress, it is a nonprofit corporation funded by its membership of broker-dealers registered with the Securities and Exchange Commission (SEC).

The SIPC helps return customer property, including securities and cash in brokerage accounts, should a broker-dealer or clearing firm experience bankruptcy, insolvency, or unauthorized trading in a customer's account. Should a SIPC member become insolvent, SIPC would ask a court to appoint a trustee to oversee transfer of customer securities to another firm, or act as the trustee itself.

SEC regulations also apply

The SEC also has provisions that can help protect investor assets. For example, the SEC

requires brokerage and clearing firms to segregate money and securities in customer accounts from their own proprietary assets and funds. This helps protect customers from being harmed by a firm's own trading activity. Also, firms are required to maintain a certain level of capital reserves to enable the firm to return customers' securities and cash in case of a financial failure. Finally, the SEC specifies that customer claims take precedence over other claims on a firm's assets.

What if a firm is liquidated instead of sold?

Securities registered in a customer's name (as opposed to being held in "street name," the most common method today) are returned to customers first. Assets held in street name make up what's known as the "fund of customer property." That fund is divided on a pro rata basis; assets are shared in proportion to the size of claims. Only if securities are still missing after the pro rata distribution would SIPC coverage be applied to make up the difference, up to the statutory coverage limit.

How much coverage does SIPC provide?

SIPC covers a maximum of \$500,000 per "separate customer," including up to \$100,000 in cash, at a given institution. As with banks, total coverage can be higher for multiple accounts at one firm. As long as accounts are held by what the SIPC considers "separate customers," each account qualifies for separate coverage. For example, a married couple could have two individual accounts with \$500,000 of coverage each, plus a joint account that would bring their aggregated potential coverage for that firm to \$1.5 million.

Categories of separate customers include:

- Individual accounts held by someone in his or her own name, or by an agent for another individual
- Accounts held jointly by two individuals with equal authority over the account
- Accounts held by executors, administrators, and guardians in the name of a decedent, an estate, or someone else (for example, a guardian for an UGMA account)
- Accounts held by a corporation, partnership, or unincorporated association

- Accounts held on behalf of a valid trust created by a written instrument (trust accounts are considered separately from those of an individual trustee)

Each of your retirement accounts at a given firm also generally is eligible for up to an additional \$500,000 SIPC coverage (including as much as \$100,000 in cash) if securities are lost or stolen.

In general, SIPC covers notes, stocks, bonds, mutual funds, and other shares in investment companies. It does not cover investments that are not registered with the SEC, such as certain investment contracts, unregistered limited partnerships, fixed annuity contracts, currency, gold, silver, commodity futures contracts, or commodities options. Remember also that SIPC does not protect against market risk or price fluctuations in securities.

Additional information and a brochure titled "How SIPC Protects You" is available at www.sipc.org.