



September 2008 Newsletter

Message from John Hayman, Founder & President of Capital Advantage, Inc.

The current financial crisis continues to affect the markets and economy daily. We remain in a defensive mode; one year ago we increased our cash (money market funds) allocation while reducing our equity allocation. Furthermore, within the equity asset class, we reduced exposure to international funds (riskier investments that had a five year run up) and moved to domestic mid/small company funds, which tend to lead the way out of difficult economic times. However, this does not make us completely immune to the ongoing reorganization of the financial markets. The times ahead will continue to be volatile, as the credit crisis and the deflation in the housing market work their way through the system. It is in times like these that we need to remind ourselves that we are long term investors, and that staying the course has always proven itself to be the best strategy.

We want to reassure our clients that both Schwab and Fidelity are very strong financially and manage their money market funds in a very conservative manner. In communicating with our custodians, they have assured us that their first priority in managing these funds has been and will continue to be maintaining the \$1 Net Asset Value. In addition, we have confirmed that neither firms' money market funds own any Lehman securities.

In time, the markets should recover as they always do. If you need to speak with us or come by our office to discuss your individual situation further, please let us know. We appreciate your business and, as always, we are here for you. – *John Hayman*

Press Release:

Capital Advantage, Inc. Promotes Henke to Chief Compliance Officer Business Wire

Lafayette, California --- John Hayman, CFP - Founder and President of Capital Advantage, Inc. - has announced the promotion of Dawnalizabeth Henke to Chief Compliance Officer.

Hayman says, "I am very proud and confident in promoting Dawnalizabeth to this mission critical position within our firm." Dawnalizabeth has over ten years experience within the investment industry and has demonstrated her dedication and attention to detail in ensuring that all business units are in compliance with the regulatory requirements of the United States Securities and Exchange Commission (SEC). Ms. Henke has earned her Master of Science in Financial Analysis & Investment Management, and recently passed the Uniform Investment Adviser Law Examination.

Capital Advantage, Inc. is headquartered in Lafayette, California and specializes in Investment Management and Retirement Planning. The firm has assets under management of approximately \$250 million and over 350 clients, serving as reputable and independent "fee-only" Financial Planners and Investment Advisors in the Lafayette, Moraga & Orinda communities.

Custodian Asset Protection

At times of market volatility, it is understandable that you may have questions about the markets and the custodians at which you hold your assets. At Capital Advantage, Inc., we believe that it is important for investors to expect market volatility and remain focused on investing for the long term. Also, please let us reassure you that Charles Schwab & Co., Inc. ("Schwab") and Fidelity Brokerage Services LLC ("Fidelity"), the firms which custody your assets, remain strong and stable. The following information from our custodians regarding their financial strength may help to address your concerns.

SCHWAB INSTITUTIONAL

An Experienced Custodian: Schwab Institutional pioneered the RIA custodial business over 20 years ago. Both Schwab Institutional, as a division of Charles Schwab & Co., Inc. ("Schwab"), and Schwab have a consistent financial track record. They closely manage their expenses with appropriate adjustments to spending plans.

Customer Asset Protection: Accounts of Charles Schwab & Co., Inc. (including those held by clients of investment advisors with Schwab Institutional), are insured by Securities Investor Protection Corporation (SIPC) for securities and cash in the event of broker-dealer failure. The SIPC provides up to \$500,000 of protection for accounts held in each separate capacity (e.g., joint tenant or sole owner), with a limit of \$100,000 for claims of uninvested cash balances.

Additional Insurance Coverage: Additional brokerage insurance—in addition to SIPC protection—is provided to Charles Schwab & Co., Inc., accounts through underwriters at Lloyd's of London. Schwab's coverage with Lloyd's provides protection of securities and cash up to an aggregate of \$600 million, and is limited to a combined return to any customer from a Trustee, SIPC and Lloyd's of \$150 million, including cash of up to \$1 million. This additional protection becomes available in the event that SIPC limits are exhausted.

FIDELITY INVESTMENTS

An Experienced Custodian

Fidelity has very diversified lines of business, all of which are supported by the strength and stability of its parent company, Fidelity Investments, a strong and growing company that achieved strong operating results in 2007. Revenues of Fidelity's parent company, FMR LLC, were a record \$14.9 billion, 16% higher than 2006 and income before taxes totaled \$2.2 billion, which was also higher than 2006.

Trading on Behalf of Clients: The decline of the mortgage market and other credit markets in recent months has led to losses in certain types of fixed income securities and has contributed to the difficulties faced by some financial firms. In contrast to these firms, Fidelity does not have an investment banking business or pursue its own trading strategies, such as taking a large position or maintaining large inventories of particular fixed income securities; rather, it executes trades at the direction of retail and institutional brokerage clients. Similarly, Fidelity's fund operations trade on behalf of the company's mutual funds.

Customer Asset Protection: Fidelity Brokerage Services LLC is a member of the Securities Investor Protection Corporation (SIPC). Brokerage accounts maintained with Fidelity are protected by SIPC, which protects brokerage accounts of each customer up to \$500,000 in securities, including a limit of \$100,000 on claims for cash awaiting reinvestment. Money market funds held in a brokerage account are considered securities.

Additional Insurance Coverage: In addition to SIPC protection, Fidelity provides additional coverage for its customers, which offers asset protection for total net equity (cash and securities) in an account. This supplemental coverage, called "excess SIPC coverage", is not subject to a dollar limitation for any one account or for the firm. For more information about Fidelity's excess SIPC coverage, visit www.capcoexcess.com.

Open Enrollment: Should You Take Advantage of Your Health Savings Account Option?

By the Financial Planning Association

Fall is approaching, which means for many workers that open enrollment is coming. Open enrollment is a specified time period during which companies let their employees sign up for various health and retirement savings benefits as well as smaller benefit options that may be unique to a company.

One of those options might be a health savings account, also known as an HSA. Health savings accounts were created as part of the Medicare Modernization Act of 2003. Anyone under age 65 who buys a *qualified* high-deductible health plan (HDHP) can open an HSA. However, you can still own an HSA and be covered under other types of insurance policies that cover liability, dental, vision and long-term care needs.

Why are companies offering these plans? Because a high-deductible health plan option allows the company to save money while giving their employees a shot at lower or stable monthly individual and family premiums. And it's important to know that in 2007, the contribution rules on these plans changed. Previously, the maximum contribution was calculated as the lesser of the deductible of the high-deductible health plan or a specific indexed amount. Now, the limit is the maximum annual contribution alone.

What's the big advantage to choosing one? Contributions are made to HSAs on a pretax basis where they are allowed to grow tax-deferred and spent out on a tax-free basis for medical expenses. HSA contributions could be made through a company's cafeteria plan if allowed by the company's cafeteria plan document, and can potentially save FICA/Medicare taxes on the contribution along with federal and state taxes. Yet there are some critical things to know before you make the switch:

Understand your 2008 HSA limits: The following cover the maximum contributions you can place in an HSA and the minimum and maximum out-of-pocket amounts for an HDHP insurance plan:

- Maximum HSA contribution: \$2900 for individual, \$5800 for families
- Minimum HDHP deductible: \$1100 self-only coverage, \$2200 family coverage
- Annual out-of-pocket maximum: \$5600 self-only coverage, \$11200 family coverage
- If you are 55 or older and your HDHP is in effect, you are eligible to deposit catch-up contributions, and in 2008, the additional amount is \$900.

Know the difference between an HSA and a medical flexible spending account (FSA): One important difference is that HSAs allow balances to be rolled over from year-to-year, growing on a tax-free basis as long as they're used for medical expenses. On the other hand, Medical FSAs require that the money you contribute each year to be spent by year-end (or a brief grace period if provided by the plan) or you lose it. In some cases, such as when you incur medical expenses early in a year, you can be reimbursed by your FSA without fully funding it – so FSAs might be a bit more flexible in this regard.

Know whether you can have both: In some situations, you may be able to have both an HSA and an FSA. If your FSA provides for limited reimbursement for items not covered by your health insurance plan (such as dental, vision or wellness care), you can use an HSA for items covered by your plan and your FSA for medical expenses that are not.

Know penalties for non-medical withdrawals: You'll get hit with a 10% penalty, plus any withdrawals will be taxed at ordinary income tax rates. After age 65, you're free to use the funds for any purpose without penalty, but non-medical withdrawals are still taxable.

You may use an IRA to fund an HSA on a one-time basis: The rules let individuals roll over money from an IRA once so people can use the money tax-free for medical expenses, but the amount of the rollover is limited to the HSA maximum contribution for the year minus any contributions already made.