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Financial Briefs

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Should You Convert to a Roth IRA?

Effective in 2010, all taxpayers, regardless of the amount of their adjusted gross income (AGI) or tax filing status, can convert a traditional individual retirement account (IRA) to a Roth IRA. Amounts converted must be included in income if taxable when withdrawn (i.e., contributions and earnings in deductible IRAs and earnings in nondeductible IRAs), but they are exempt from the 10% early withdrawal penalty.

If you make a conversion in 2010, the taxable amount will be included in income in two installments, half in 2011 and half in 2012, with no tax due in 2010. However, if you prefer, you can elect to pay the tax in 2010, which may make sense if the current lower tax rates are not extended beyond 2010 or you expect much higher income in 2011 or 2012. Taxes on conversions made after 2010 must be paid in the year of conversion.

The question is whether it makes financial sense to pay what could be a large income tax bill now to avoid any future income taxes on your IRA. Several factors need to be considered before answering that question:

What is your income tax bracket now, and what will it be when the funds are distributed? If your tax bracket will be the same at both times, the financial results will be similar. Increasing income tax brackets generally make it advantageous to convert to a Roth IRA, since you are paying the tax bill while income tax rates are lower. Decreasing tax brackets generally favor leaving the balance in the traditional IRA.

How will you pay the income taxes due from the conversion? If you can pay the tax bill from sources outside your IRA, that is a strong factor in favor of conversion. By doing so, you are in essence making an additional contribution to the IRA in the amount of the tax paid. Conversely, paying the tax bill from your IRA account can be a strong factor against converting, since you are withdrawing funds from your IRA and may also have to pay a 10% penalty on that withdrawal.

When will you make withdrawals from your IRA? If you'll make withdrawals within five or 10 years of converting, that may not be enough time for the benefits of tax-free compounding to compensate for the current payment of income taxes. But if you don't need to make withdrawals, your balance in a Roth IRA can grow tax free for a longer time, since you don't have to make required minimum distributions after age 70 1/2.

How will the income from the conversion affect your overall tax situation? That additional income could raise your overall income to a point where you lose some tax credits, deductions, or exemptions in the year of conversion, or increase Medicare premiums.

Will your Social Security

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Advice on Saving for Your Child

Your child has finally finished college and started his/her first full-time job. What is the most important financial advice you can give?

Participate in your 401(k) plan as soon as you are eligible. The quality of your child's retirement will largely be determined by the amount of money he/she saves, and a 401(k) plan is a great place for him/her to start. Before marriage, a new home, or other obligations consume his/her entire paycheck, get him/her into the habit of saving. Because the contributions are deducted before he/she even sees his/her paycheck, it's a great way to get him/her into the habit of saving on a regular basis.

Having trouble convincing him/her this is a good strategy? Perhaps some numbers will make the point. Assume your child starts contributing to his/her 401(k) plan at age 25, contributing $6,000 per year (substantially below the maximum contribution in 2010 of $16,500), with matching employer contributions of $3,000. If he/she earns a hypothetical 8% annually,

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Should You Convert?

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benefits be subject to taxes? In the year of conversion, the income from the conversion may affect your Social Security benefits. However, going forward, distributions from Roth IRAs are excluded from taxable income, while distributions from traditional IRAs may affect your benefits if you have significant amounts of taxable income from other sources.

Are you interested in other estate planning considerations? Paying income taxes currently means that you remove those assets from your taxable estate, thus reducing estate taxes owed at your death. If you plan to leave the IRA balance to your heirs, they receive the Roth IRA proceeds free of income taxes, while income taxes would be due on the traditional IRA. Also, if you don't take withdrawals from the Roth IRA after age 70 1/2, you may end up leaving your heirs with a much larger balance.

After considering all of these factors, you can decide whether converting makes sense for your situation. Keep in mind that you do not have to convert your entire IRA balance at one time. You can convert over a number of years or only convert a portion of your IRA balance. However, be aware that if you have both deductible and nondeductible IRA balances, you cannot just convert the nondeductible balances to reduce your tax liability. You have to assume a pro-rated portion of both the deductible and nondeductible IRA funds are being converted.

Know When to Recharacterize

If you convert and your investments then decline, you end up paying taxes on more than the current market value. However, you can then recharacterize your conversion. For conversions made in 2010, you can recharacterize until October 15, 2011, meaning you can convert back to your original IRA. After the recharacterization, it is as if you did not convert, so you owe no taxes. You can then reconvert at the later of 30 days after the recharacterization or the beginning of the tax year following the first conversion.

You can recharacterize just a portion of the conversion. However, if you have several investments in the IRA, you can't simply choose the ones with the largest losses. In that situation, a pro-rated portion of all the investments in the account will be considered in the recharacterization. You can bypass this rule by setting up separate Roth IRA accounts for each investment. Then, if one declines substantially, you can recharacterize that one Roth IRA account, leaving the other accounts intact.

Roth IRA Contributions

This new conversion provision effectively removes the income limitations for contributions to a Roth IRA. In 2010, Roth IRA contributions can be made by single taxpayers with AGI less than $105,000 (contributions are phased out with AGI between $105,000 and $120,000) and by married couples filing jointly with AGI less than $167,000 (contributions are phased out with AGI between $167,000 and $177,000). It doesn't matter whether you participate in a company-sponsored pension plan. Individuals with incomes over the limits can make contributions to a nondeductible traditional IRA and then immediately convert the balance to a Roth IRA. However, keep in mind that if you have other deductible IRA balances, you will have to assume a pro-rated portion of both the deductible and nondeductible IRA funds are being converted.

Please call if you'd like help deciding whether you should convert to a Roth IRA.

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Keep Saving after Retirement

Just because you're retired doesn't mean you should stop saving. Consider these tips:

- **Develop a strategy.** Most retirees fear that they'll run out of money during retirement. To ease those fears, develop a strategy detailing how much money will be obtained from what sources and how that income will be spent. Make sure your annual withdrawal amount won't cause you to deplete your savings. Review your strategy annually to ensure you stay on course.
- **Consider part-time employment.** Especially if you retire at a relatively young age, you might want to work on at least a part-time basis. Even earning a modest amount can help significantly with retirement expenses. However, if you receive Social Security benefits and are between the ages of 62 and full retirement age, you will lose $1 of benefits for every $2 of earnings above $14,160 in 2010. You might want to keep your income below that threshold or delay Social Security benefits until later in retirement.
- **Contribute to your 401(k) plan or individual retirement plan (IRA).** If you work after retirement, put some of that money into a 401(k) plan or IRA. As long as you have earned income and meet the eligibility requirements, you can contribute to these plans.
- **Try before you buy.** Want to relocate to another city? Before you buy a home in an unfamiliar city, try renting first.
- **Keep debt to a minimum.** Most consumer loans and credit cards charge high interest rates that aren't tax deductible. During retirement, that can put a serious strain on your finances. If you can't pay cash, avoid the purchase.
- **Look for deals.** Take the time to shop wisely, not just at stores, but for all purchases. When was the last time you compared prices for auto or home insurance? Can you find a credit card with lower fees and interest rates? When did you last refinance your mortgage?

Advice on Saving

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he/she could have a balance of $2,331,509 at age 65, before the payment of any taxes. What if he/she waits until age 35 to start contributing? At age 65, the balance could be $1,019,549, still a substantial amount, but $1,311,960 lower than if he/she started at age 25. *(This example is provided for illustrative purposes only and is not intended to project the performance of a specific investment vehicle.)*

What if your child still isn't convinced? Consider reimbursing him/her, as part of your annual gift tax exclusion, for any 401(k) contributions. You can reimburse the entire amount or offer to make a partial reimbursement.

Don't let your child procrastinate because there are too many decisions to be made. Just encourage him/her to start contributing, reassuring him/her that none of the decisions are permanent. He/she can review contribution levels, investment choices, beneficiary designations, and other matters at a later date.

If your child has the option to contribute to a regular 401(k) plan or a Roth 401(k) plan, suggest contributing to the Roth 401(k). Employer matching contributions will still be made to a regular 401(k) plan, but your child's contributions can go to the Roth 401(k). Your child won't get a current tax break for contributions made, but he/she will owe no taxes on the contributions or any earnings when withdrawals are made.

What if your child doesn't have a 401(k) plan at work? Encourage him/her to contribute to an individual retirement account (IRA). Although contributions are limited to $5,000 in 2010 compared to $16,500 for 401(k) plans, IRAs are still a good way to save for retirement.

Clamp Down on Spending

If you're trying to increase savings, remember that savings are directly tied to spending — the less you spend, the more you have to save. Some tips to help you clamp down on your spending include:

- Analyze your spending for a month. Are you surprised by how much you spend on dining out, groceries, entertainment, or clothing? Give serious thought to your purchasing patterns, looking for ways to reduce spending. Clean out your closet and really assess whether you need new clothes. Cut back on how often you dine out or at least go to less-expensive restaurants. Rent a movie instead of going to the theater. Make a list before grocery shopping and don't deviate from it. Look for coupons and sales before shopping.

  You may scoff at these ideas for saving money, thinking you can't possibly add much to your savings. After all, you're just spending a few dollars here and there. But over a long time period, even modest amounts can grow to significant sums.
- Go over major expenditures also. When was the last time you comparison shopped your auto or homeowners insurance? Have you checked mortgage rates lately to see if you should refinance? Have you reviewed strategies to reduce your income taxes? Take a look at all major expenditures, looking for ways to save money.
- Make a spending plan and put it in writing. Budget for all major expenditures and resolve not to purchase items that aren't in your budget.
- Throw out your credit cards (or at least hide them for a while). Most people find it more difficult to spend cash than to charge a purchase. So, for the next couple of months, make sure to only purchase items with cash.
- Don't purchase items over a fairly low dollar amount on your first shopping trip. How often have you purchased something on impulse, only to realize when you got home that you really didn't need it? To control those impulses, compare price and value on your first shopping trip. Then go home, think about whether you really need the item, and purchase it on another trip. Often, you will realize you don't even need to make the purchase.
- Think carefully before making major purchases. Often, upkeep and maintenance can add significantly to your costs. Consider a less-expensive car or a used car. Keep your car for four or five years instead of getting a new one every two or three years.
- Figure out the maximum amount you can afford for a house and then buy one substantially less expensive than that. Not only will you save on your mortgage payment, other costs associated with owning a home will be lower. Living well within your means is one of the best ways to ensure you have money left over for saving.

Learn to clamp down on your spending, and your savings should increase. Please call if you'd like help in this area.

Business Data

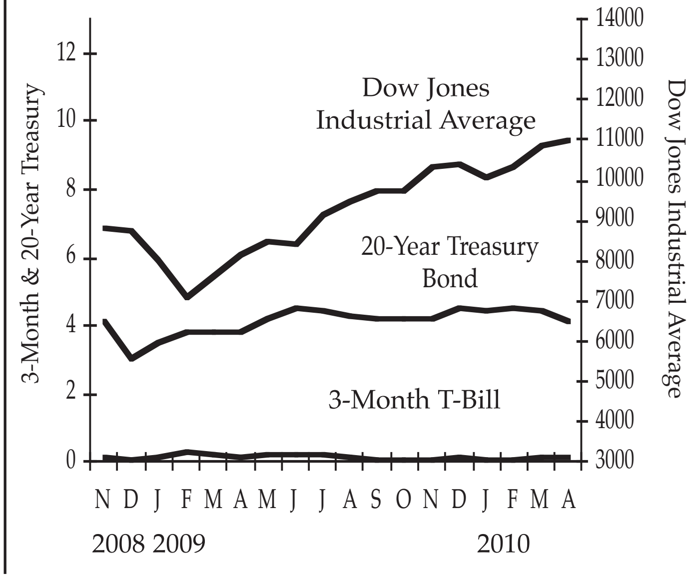
Indicator	Month-end Feb-10	Mar-10	Apr-10	Dec-09	Apr-09
Prime rate	3.25	3.25	3.25	3.25	3.25
3-month T-bill yield	0.10	0.15	0.15	0.11	0.14
10-year T-note yield	3.74	3.68	3.81	3.76	2.87
20-year T-bond yield	4.56	4.43	4.50	4.53	3.80
Dow Jones Corp.	4.22	4.33	4.11	4.43	6.52
GDP (adj. annual rate)#	+2.20	+5.60	+3.20	+2.20	-6.40

Indicator	Month-end Feb-10	Mar-10	Apr-10	% Change YTD	12 Mon.
Dow Jones Industrials	10325.26	10856.63	11008.61	5.6%	34.8%
Standard & Poor's 500	1104.49	1169.43	1186.69	6.4%	36.0%
Nasdaq Composite	2238.26	2397.96	2461.19	8.5%	43.3%
Gold	1108.25	1115.50	1179.25	7.2%	33.5%
Unemployment rate@	9.70	9.70	9.70	-3.0%	14.1%
Consumer price index@	216.70	216.70	217.60	0.6%	2.3%
Index of leading ind.@	107.50	108.10	109.60	4.5%	11.8%

— 3rd, 4th, 1st quarter @ — Jan, Feb, Mar Sources: *Barron's, Wall Street Journal*
Past performance is not a guarantee of future results.

18-Month Summary of Dow Jones Industrial Average, 3-Month T-Bill & 20-Year Treasury Bond Yield

November 2008 to April 2010



News and Announcements

Get Your 401(k) Plan on Track

To make sure you have sufficient funds for retirement, you need to get your 401(k) plan on track. To do so, consider these tips:

- **Increase your contribution rate.** With investment values down and future stock market returns uncertain, you need to boost your savings to help increase the value of your 401(k) plan. Strive for total contributions from you and your employer of approximately 10% to 15% of your salary. At a minimum, make sure you're contributing enough to take advantage of all employer-matching contributions.
- **Rebalance your investments.** You can't select your investments once and then just ignore your plan. Review your allocation annually to make sure it is close to your original allocation. If not, adjust your holdings to get your allocation back in line. Selling investments within your 401(k) plan does not generate tax liabilities, so you can make these changes without tax ramifications. Use this annual review to make sure you are still satisfied with your investment choices and your allocation is still appropriate for your situation.
- **Don't raid your 401(k) balance.** Your 401(k) plan should only be used for your retirement. Don't even think about borrowing from the plan for any other purpose. You don't want to get in the habit of using those funds for anything other than retirement. Similarly, if you change jobs, don't withdraw money from your 401(k) plan. Keep the money with your old employer or roll it over to your new 401(k) plan or an individual retirement account.
- **Seek guidance.** It is important to manage your 401(k) plan carefully to help maximize your future retirement income. If you're concerned about the long-term impact of the recent market fluctuations, call for a review of your 401(k) plan.

Rebalancing, asset allocation, and diversification do not assure a profit or protect against loss in declining financial markets.

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Anyone who would like a copy of our privacy policy or our ADV Part II, give us a call at 330.668.6991.

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