# Quarterly Insight

Wolf Financial Management LLC

*Investment and Retirement Plan Services*

Summer 2010 www.wolffinancial.com 630.545.4700

## The Benefits Of 401(k)s Far Outweigh The Negatives

To paraphrase Mark Twain, the news of the death of the 401(k) plan has been greatly exaggerated. If you halted contributions to your company's retirement plan after the stock market plummeted late in 2008, it may be time to resuscitate your account.

No one could blame you for feeling the heat. The Standard & Poor's 500 stock index declined by a whopping 56% from its peak in October 2007 to its trough in March 2009, resulting in comparable losses for numerous 401(k) plan participants whose portfolios weren't well diversified. About 6% of 401(k) participants had to withdraw funds from retirement accounts in 2008 to meet pressing financial needs, and almost 5% stopped contributing to their 401(k) account altogether. Still, in bad times and good, the benefits of using a 401(k) to save for retirement far outweigh the perceived negatives.

There are risks, of course. The value of your investments will fall from time to time, and the performance of your retirement portfolio depends not only on the investment choices you make but also on market movements beyond your control. There are no guarantees you'll make money or even escape with your principal intact. And, unlike defined-benefit pension plans, 401(k)s aren't insured by the Pension Benefit Guaranty Corporation. Furthermore, while your employer may contribute to your account, you could lose that money if you change jobs or retire before you're "vested." But since employer contributions are essentially free money for your account, that's hardly a negative.

Finally, distributions from your plan during retirement will be taxed at ordinary income rates—and if you take withdrawals early, before age 59½, you'll probably owe a 10% penalty as well.

However, the list of 401(k) pros is much longer than the list of cons.

1. Over long periods of investing for retirement, your account is likely—though not certain—to gain value. Even when markets fall, it can be a blessing if you have a long-term time horizon because your continued regular investments let you accumulate shares at low prices, setting yourself up for big profits when the market rebounds.

2. Your 401(k) offers several investment options, and you're usually the one calling the shots, not your company. Many plans include prepackaged portfolios with broadly diversified investments, and professional advice about investments is often available.

3. Contribution limits are generous. For 2010, you can put as much as $16,500 in your account, or $22,000 if you're age 50 or over. In contrast, the annual limit for IRA contributions is only $5,000 ($6,000 if you're age 50 or over).

4. Contributions to a traditional

*(Continued on page 4)*

## *Despite Concerns, Most Don't Have A Financial Plan*

Even after one of the worst economic downturns in U.S. history, only 17% of Americans have a written and updated financial plan, according to a survey by Certified Financial Planner Board of Standards.

With the value of retirement assets slashed and incomes stalled, it would make sense for people to take steps to rebuild their financial futures. Yet the survey, taken eight months after the economic collapse of October 2008, shows most people don't have a blueprint for getting back on track.

According to the CFP Board survey, a majority of Americans of all incomes and asset levels are worried about managing retirement income, keeping health care insurance, managing debt, and building a retirement fund. Meanwhile, 65% of respondents who employ a financial advisor to help them establish and maintain a financial plan feel they are benefiting from the relationship. Only 46% of those who have a written plan but don't work with an advisor are satisfied.

When it comes to reaching financial goals and life dreams, it doesn't make sense to leave things to chance. A financial plan not only gives you a concrete direction, it helps you stay on course and change direction when necessary.

If you have yet to set up a financial plan, or if your plan is falling short, call our office today so that we can help you chart a solid path to a secure financial future.

# Quiz: The Rules Of Roth IRA Conversions

Roth IRA conversions aren't off limits to six-figure earners anymore. Starting in 2010, you can convert a traditional IRA to a Roth regardless of your income. Previously, such conversions were permitted only in a year in which your adjusted gross income (AGI) didn't exceed $100,000.

Why would you want to convert to a Roth? It's a good idea for many retirement savers. Unlike withdrawals from a traditional IRA, which are taxed as income, "qualified distributions" from a Roth that has been established for at least five years are tax-free. And whereas a traditional IRA forces you to take taxable distributions during retirement, a Roth IRA has no mandatory withdrawals.

Of course, there's no such thing as a free lunch. You must pay tax at ordinary income tax rates on the amount you convert from a traditional IRA to a Roth.

How well do you know the rules? Here are 10 questions to test your knowledge.

1. When are contributions to a Roth IRA tax-deductible?
   a) Only when your AGI is less than $100,000
   b) Only when you don't have a traditional IRA
   c) Only when you itemize deductions on your tax return
   d) Never

2. The regular annual contribution limit for a Roth IRA is:
   a) $2,000 c) $6,500
   b) $5,000 d) Unlimited

3. A Roth distribution is not a qualified distribution if it's made:
   a) because of death or disability
   b) after reaching age 59½
   c) to pay first-time homebuyer expenses
   d) to pay higher education expenses

4. When can you contribute to a converted Roth IRA?
   a) Only when you don't have a traditional IRA
   b) Only when your AGI doesn't exceed an annual limit
   c) Only when you're disabled
   d) Never

5. After 2010, contributions to a traditional IRA:
   a) will be subject to the old income limits for Roth contributions
   b) will no longer be subject to mandatory distributions
   c) will be eligible for conversion to a Roth IRA
   d) will be taxable

6. The tax on a Roth conversion in 2010:
   a) must be paid in full in 2010
   b) must be paid in full in 2011
   c) can be divided between 2011 and 2012
   d) can be postponed indefinitely

7. What is the age limit for Roth IRA contributions?
   a) 21 c) 70½
   b) 59½ d) There is none

8. When can you undo a Roth IRA conversion?
   a) Within one year
   b) By your tax return due date
   c) If your AGI is less than $100,000
   d) Never

9. A Roth conversion is valued for tax purposes on:
   a) the date of conversion
   b) your tax return due date
   c) the last day of the prior year
   d) the first day of this year

10. How often are Roth conversions allowed?
    a) Only one per month
    b) Only one per year
    c) Once in a lifetime
    d) Unlimited

Answers: 1-d, 2-b, 3-d, 4-b, 5-c, 6-c, 7-d, 8-b, 9-a, 10-d

# Should Retirees Carry A Mortgage?

Your home mortgage is likely to be the biggest debt you ever take on. And if you've moved or refinanced a few times since your first home loan, you may be years or even decades away from owning your house free and clear. But that begs the question: What about retirement? If you're getting ready to retire or already have stopped working, does it make financial sense to keep making monthly payments? Or should you use some of your savings to retire that debt?

Traditionally, paying off the mortgage was a pre-retirement objective, but the recent trend has been to carry the debt longer. A study by the Center for Retirement Research at Boston College found that in 2007, 41% of households with people in their 60s still had a mortgage, even though more than half owned sufficient assets to repay the loan.

Why would you hold a mortgage in retirement? Depending on your situation, you may value the tax benefits and liquidity. Consider these four critical factors.

**1. Investment returns.** Recently, the average 30-year fixed rate for mortgages has been between 5% and 5½%. You might keep your mortgage if you think you can do better investing the money you would spend to retire it. But retirees who invest heavily in low-risk vehicles such as bank certificates of deposit (CDs) and Treasury securities are likely to come up short. And though stocks and mutual funds may provide higher rates of return, they carry greater risks, and if your portfolio plummets, you could have trouble making mortgage payments.

**2. Tax breaks.** You can generally write off mortgage interest if you itemize deductions. But people who claim the standard deduction—and that's almost two out of every three taxpayers—receive no tax benefit from mortgage interest payments. So if you're not an itemizer, it may make

# Financial Planning Is A Family Affair

Having one spouse handle most family financial matters may feel like an equitable division of labor—with the husband, say, monitoring accounts and making investment decisions while the wife manages other household affairs. But it's an approach that could be damaging in the long run. Divorce or death could plunge the remaining spouse into unfamiliar waters—unable, perhaps, even to find crucial information about life insurance and retirement accounts. And if children have been left out of financial discussions, they may fail to appreciate the family's situation and be ill prepared to take on adult financial responsibilities.

Like it or not, most women will one day handle their own finances. According to the Social Security Administration, women live four years longer during retirement than men do, on average, and they comprise almost 60% of Social Security beneficiaries. At age 65, only 43% of women are married, compared with three out of four men. Divorce plays a major role as well. In 2005, the marriage rate was 7.5 per 1,000 people, according to the U.S. Census Bureau, while the divorce rate was 3.6 per 1,000.

It's not that most women are financial novices. According to a recent survey by Oppenheimer Funds, six in 10 wives balance the family checkbook, while more than half pay household bills. The same survey found that 43% considered themselves somewhat or very knowledgeable about investing. Yet that still leaves more than half of women facing a steep learning curve if they're suddenly forced to handle investment responsibilities.

And even when both spouses are around, having one of them take responsibility for a family's finances can be perilous. If family members don't understand their economic situation—how much money comes in each month, what gets spent on fixed expenses as well as discretionary purchases, what the family's short- and long-term saving goals are—it's difficult for them to behave responsibly, and arguments about spending are likely. And if the husband, say, has sole charge of family investments, he may take more risk than if both spouses were responsible for their investments. Taking a flyer on a stock tip is easy when you're sitting alone at your computer; explaining why that sure bet tanked is much harder, as you'll have to do if you and your spouse regularly review account statements.

Failing to bring children into the financial loop could also have unhappy consequences. In many families, money spent on the kids accounts for a large part of the budget, and showering them with extras—from sports camps and music lessons to private school tuition and vacations abroad—may give them unrealistic views about money. Lack of financial grounding at home may be one reason so many kids have problems with credit cards when they head off to college. According to a 2009 study by student lender Sallie Mae, the average student now has four credit cards and debt of more than $3,000. Six in 10 students in the study said they were surprised at how high their account balances had grown, and 40% said they'd charged things knowing they didn't have enough money to pay the bills.

Transparency and a willingness to talk about family finances can go a long way toward minimizing such problems. If family members understand that setting aside a certain amount each month is crucial to pay for the kids' college and the parents' retirement, they may be more inclined to stick to the budget. Having spouses agree on an investment strategy and then reviewing progress and making needed adjustments can also help. Regardless of each spouse's role in the family finances, maintaining an up-to-date list of accounts, insurance policies, and other financial essentials—and making sure everyone in the family knows where to find the list—can be crucial if the financial decision-maker suddenly dies or becomes incapacitated.

Yet as important as it is for families to work together, many don't. According to a recent study of couples by Fidelity Investments, just four in 10 said they collaborated with spouses on decisions about retirement saving and investing, and only 15% thought that if they died, their spouses would be prepared to take over the family finances. If you need help getting on the same page, we may be able to help. ●

sense to pay off the mortgage. Also keep in mind that the tax benefit of itemized deductions will be reduced if your income is high.

**3. Retirement accounts.** It's generally not a good idea to pay off your mortgage if you have to invade your retirement accounts to do it. The money you pull out of a 401(k) plan or an IRA will be reduced by taxes—at ordinary income rates of as high as 35%—plus you'll be hit with an additional 10% penalty if you're under age 59½. And you'll be left with fewer funds to draw upon during retirement.

**4. Refinancing.** One alternative to paying off the mortgage may be to refinance it at a lower interest rate. That can reduce your payments, or you could use the opportunity to pull out equity you've built. But the deep decline in real estate values has underscored the risks of financial strategies built around home loans.

Choosing what to do about your mortgage is a major financial decision. We can help you choose the best approach for your situation. ●

# How You Can Survive A Plane Crash

On Jan. 15, 2009, an airliner crash-landed into the Hudson River and all 155 people aboard survived. Then on Feb. 12, a commuter plane crashed into a house in upstate New York, killing all 49 people on board and one person on the ground.

The January crash was hailed as a miracle, because people assume that virtually all airplane crashes are like the other one, resulting in the death of everyone aboard. Yet statistics show that is very far from true. Not only do most air travelers survive crashes, there are steps you can take to increase your chances of coming out alive.

If you are involved in an aviation accident, you have a 95.7% chance of survival, according to the National Transportation Safety Board. In accidents from 1983 to 2000, a total of 51,207 passengers survived out of 53,487 passengers involved. Even among the most serious crashes, the survival rate was 76.6%, excluding those in which no one had a chance to survive.

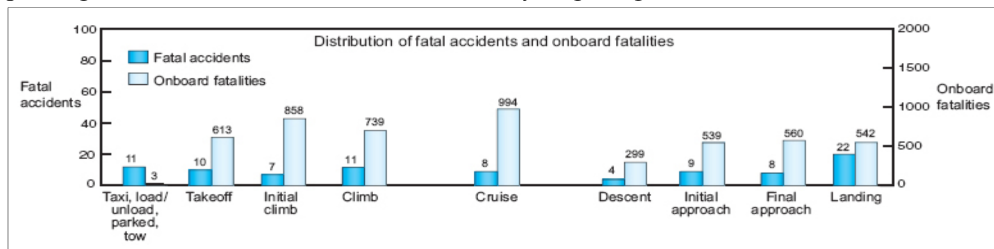
"In a crash, many people believe there's nothing you can do to save yourself," writes Ben Sherwood, author of the best-selling *The Survivors Club: The Secrets and Science that Could Save Your Life.* "In truth, however, your life is in your hands. Some experts believe that as many as 30% of the deaths in airplane accidents could have been prevented if people knew what to do and took action."

Sherwood, who attended the plane crash survival course at the Federal Aviation Administration's training center in Oklahoma City, offers the following advice on how to survive a plane crash:

- Be calm. The odds you will die on any single flight are one in 60 million.
- Choose a seat on the aisle within five rows of an exit row. After looking at seating plans and interviewing 2,000 passengers involved in 100 crashes, a British safety expert concluded that this significantly increases your chances of making it out of an airplane that catches fire.
- Listen to the pre-flight safety briefing and develop a plan in the event of an emergency—and have a back-up plan, too. Know how many rows are between your seat and the nearest exit row, and the next closest. That could help you feel your way in case of smoke or darkness.
- During the first three minutes and the last eight minutes of your flight, focus on your emergency plan. About 80% of accidents occur during those times.

Still not convinced? Consider these additional tips, from howstuffworks.com, on how to increase your survival odds:

- Avoid alcohol because it slows your reflexes.
- Wear long pants, long sleeves, and closed-toed shoes to protect your body from flying objects and the elements. ●




## The Benefits Of 401(k)s

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401(k) may be made as pre-tax salary deferrals, which reduce your taxable income and the amount you owe the IRS. Nor are you taxed on investment earnings until you withdraw funds from your account.

5. Employers often match a portion of employee contributions with company-paid contributions based on a percentage of your salary. And once you meet the 401(k)'s vesting requirements, that money is yours to keep.

6. The impact of long-term, tax-deferred compounding can magnify annual contributions into a sizeable nest egg. For example, if you put $20,000 in your account each year and average a 7% return, your account will be worth about $1.3 million after 25 years.

7. When you retire or change jobs, you can roll over the assets in your 401(k) tax-free to an IRA or the qualified plan of your new employer. That preserves the tax advantages of your retirement plan. For some, it will also make sense to roll over the assets to a Roth IRA.

8. Because you pay into Social Security only until you reach a specified income ceiling—$106,800 in 2010—once you've crossed that threshold, you could use payroll savings to increase your 401(k) contribution without reducing your paycheck.

9. Because your company's 401(k) plan is protected by the Employee Retirement Income Security Act (ERISA), it cannot be garnished by creditors or assigned to others (except in domestic court cases involving a divorce decree or a child support order).

A 401(k) plan continues to be one of the easiest ways to save for retirement, and its advantages far outstrip its drawbacks. If you bailed out during the financial crisis, you may have already missed substantial gains during the market recovery. But getting back in now and sticking with your financial plan going forward could help you resume building for a comfortable life after work. ●

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