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THE FINANCIAL FORMULA

Giving You The Financial Information You Need

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Welcome to the 2nd edition of The Financial Formula! It was quite a volatile week for the markets. If you have any questions, please let me know - thank you!

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As gold continues to escalate in value, investors may wonder if they should add the precious metal to their portfolio. But is the run-up the result of a bubble that's about to burst?

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A rollover IRA can provide investors with the broadest range of investment choices and the greatest flexibility for distribution planning.

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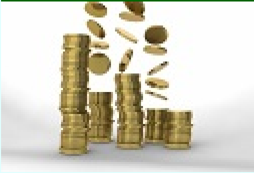
Four Risks to Your Retirement Future

It may be helpful to look at various types of risk from the vantage point of how they affect retirees at different life stages. Here are four key risks to consider.

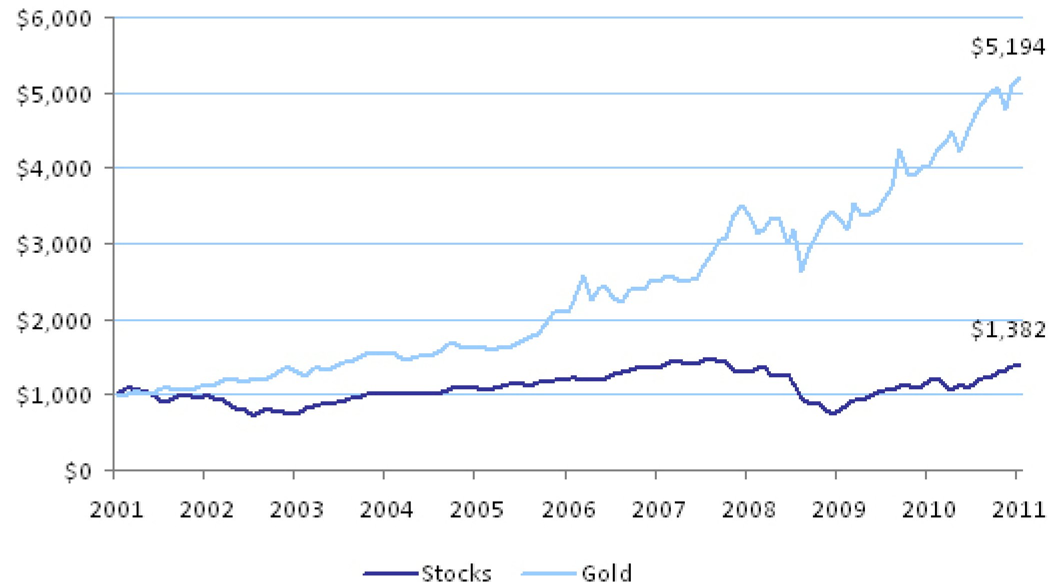


Gold: Still Shining Brightly

As investors watch a series of potentially calamitous world events -- questions about nuclear safety in Japan, U.S. government gridlock, and sovereign debt woes in various corners of the globe -- the price of gold continues to set new highs.

The closing price of gold bullion on the London fix increased 29% between March 31, 2010, and March 31, 2011.[1] In April, gold vaulted to over $1,500 an ounce, its highest price in more than 30 years.

The Value of $1,000 Invested in Gold and Stocks



Sources: Standard & Poor's; World Gold Council. Stocks are represented by the S&P 500 index and gold is represented by the monthly change in price of gold as determined by the London 4 p.m. fix. Data from January 1, 2001, to March 31, 2011.

When any asset surges in value to this extent, it's natural for observers to question whether a bubble is underway. A number of elements have contributed to gold's upward momentum.

- Hedge opportunities: Investors perceive gold as an inflation hedge and given that inflation has been much lower than the historical norm for several years, it is likely to increase.[2] Factors that could contribute to higher inflation include sizeable federal deficits and rising prices for oil, which push up costs for consumers and businesses.
- Increased demand: Demand remains strong on a variety of fronts. Annual demand for jewelry, driven by growth in China and India, increased 17% during 2010.[3] Gold used in technology increased 12% between 2009 and 2010, largely because of growth in the electronics industry.
- Decreased supply: Conversely, the supply of gold is not riding the same growth path. During 2010, central banks became net buyers of gold for the first time in 21 years, which removed a significant source of supply. Global mine production has been stagnant for more than a decade.[4] When demand outstrips supply, prices usually rise.

Options for Investors

Whether you should take a shine to gold depends on your assessment of existing conditions, your current level of diversification, and your tolerance for the risks presented by gold. When making your decision, consider the following:

- Over the long term, the correlation between gold and U.S. stocks has been negative, meaning that when stocks have gone down in value, gold has gone up.[5] Performance in the short term may differ, but gold potentially could act as an effective diversifier for a portfolio weighted to stocks.
- Gold also can present considerable volatility. When examining all 1-year, 3-year, and 10-year periods between 1977 and 2010, the volatility of gold was higher than that of stocks.[6] Because of gold's potential volatility, consider allocating only a small percentage of your portfolio to this asset.
- If you are interested in adding gold to your investment portfolio, you may have several options: bullion, such as jewelry or coins purchased through a dealer; stocks or bonds issued by companies in gold-related industries; mutual funds; or exchange-traded funds.[7] Keep in mind that all options may be influenced by trends in the stock market.

Note, too, that commodities are highly speculative investments and therefore should not represent a significant portion of an individual's portfolio.

[1]Source: Standard & Poor's. Gold is represented by the closing price on the London fix. Data represents price only and is not annualized.

[2]Source: Bureau of Labor Statistics. Inflation is measured by the Consumer Price Index.

[3]Source: World Gold Council, "Gold Demand Trends Full Year 2010," February 2011.

[4]Source: Standard & Poor's, "Is Gold Overvalued?", April 5, 2011.

[5]Source: Standard & Poor's. Stocks are represented by the S&P 500; gold by the closing price on the London fix. Returns are for all 10-year periods between 1977 and 2010. You cannot invest directly in an index. Past performance does not guarantee future results.

[6]Source: Standard & Poor's. Volatility is measured by standard deviation.

[7]Investing involves risk, including loss of principal.

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Rollover IRAs Offer a Wide Range of Benefits

As compared with employer-sponsored retirement accounts, a rollover IRA can provide you with the broadest range of investment choices and the greatest flexibility for distribution planning. Also, a rollover IRA can typically be operated with fewer restrictions. This brief overview highlights some of the key benefits of a rollover IRA compared with an employer-sponsored plan.

IRA assets can generally be divided among multiple beneficiaries in an estate plan.

- **More control:** As the IRA account owner, you make the key decisions that affect management and administrative costs, overall level of service, investment direction, and asset allocation. You can develop the precise mixture of investments that best reflects your own personal risk tolerance, investment philosophy, and financial goals. You can create IRAs that access the investment expertise of any available fund complex, and can hire and fire your investment managers by buying or selling their funds. You also control account administration through your choice of IRA custodians.
- **More flexibility:** IRAs can be more useful in estate planning than employer-sponsored plans. IRA assets can generally be divided among multiple beneficiaries in an estate plan. Each of those beneficiaries can make use of planning structures such as the Stretch IRA concept to maintain tax-advantaged investment management during their lifetimes. Beneficiary distributions from employer-sponsored plans, in contrast, are generally taken in lump sums as cash payments. Also, except in states with explicit community property laws, IRA account holders have sole control over their beneficiary designations.

Efficient Rollovers Require Careful Planning

One common goal of planning for a lump-sum distribution is averting unnecessary tax withholding. Under federal tax rules, any lump-sum distribution that is not transferred directly from one retirement account to another is subject to a special withholding of 20%. This withholding will apply as long as the employer's check is made out to you -- even if you plan to place equivalent cash in an IRA immediately. To avert the withholding, you must first create your rollover IRA, and then request that your employer transfer your assets directly to the custodian of that IRA.

Keep in mind that the 20% withholding is not your ultimate tax liability. If you spend the lump-sum distribution rather than reinvest it in another tax-qualified retirement account, you'll have to declare the full value of the lump sum as income and pay the full tax at filing time. In addition, the IRS generally imposes a 10% penalty tax on withdrawals taken before age 59 1/2.

Also, if you plan to roll over the entire sum, but have the check made out to you rather than your new IRA custodian, your employer will be required to withhold the 20%. In that event, you can get the 20% refunded if you complete the rollover within 60 days. You must deposit the full amount of your distribution in your new IRA, making up the withheld 20% out of other resources. When you file your tax return for the year, you can then include a request for refund of the lump-sum withholding.

If you have after-tax contributions in your employer plan, you may opt to withdraw them without penalty when you roll over your assets. However, if you wish to leave those funds in your retirement account in order to continue tax deferral, you can include them in your rollover. When you begin regular distributions from your IRA, a prorated portion will be deemed nontaxable to reimburse you for the after-tax contributions.

Potential Downsides of IRA Rollovers

While there are many advantages to consolidated IRA rollovers, there are some potential drawbacks to keep in mind. Assets greater than $1 million in an IRA may be taken to satisfy your debts in certain personal bankruptcy scenarios. Assets in an employer-sponsored plan cannot be readily taken in many circumstances. Also, you must begin taking distributions from an IRA by April 1 of the year after you reach 70 1/2 whether or not you continue working, but employer-sponsored plans do not require distributions if you continue working past that age.

Remember, the laws governing retirement assets and taxation are complex. In addition, there are many exceptions and limitations that may apply to your situation. Therefore, you should obtain qualified professional advice before taking any action.

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Strategies for Smart Retirement Planning

Whether retirement is just around the corner or 30 to 40 years away, regularly setting money aside -- particularly in a tax-deferred vehicle such as a 401(k) or tax-exempt account like a Roth IRA -- can often be the smartest move you can make.

A study conducted by the Employee Benefit Research Institute estimated that the average American worker will face a retirement savings shortfall of more than $47,000.[1] How can you avoid a similar fate?

Some factors that influence your retirement savings results, such as the types of investments available to you through your plan and the performance of the financial markets, can't always be controlled. But there are some factors you can influence that can help keep your portfolio on track.

Step 1: Stay invested.

It's not easy to see your account value decrease after a decline in the stock market, particularly after a steep, sudden drop of 10% or more. But one of the dangers of cashing out is missing a potential market rebound. Trying to "time" the market is a strategy even the most-seasoned financial professionals have difficulty mastering. It can also lead investors into the trap of "chasing gains"; that is, moving your money from one investment that's lagging into another one that's currently achieving better performance.

Step 2: Regularly monitor your investment mix.

One of the benefits of a diversified portfolio is balance. If one type of investment is experiencing losses, another type may be earning gains. Over time, these gains and losses may cause your asset allocation to skew away from your target mix.[2] Or your tolerance for risk may evolve over time. Lifestyle changes can also necessitate a readjustment to your allocation. That's why it's important to monitor your mix and make adjustments when necessary.

Step 3: Increase your savings rate.

Perhaps the most important way to help fund your future is to sock away as much as possible. Finding the extra money to invest can be tough -- you've got plenty of expenses to worry about today without the added anxiety of worrying about tomorrow. But every dollar you can spare can make a difference. Whether retirement is just around the corner or 30 to 40 years away, regularly setting money aside -- particularly in a tax-deferred vehicle such as a 401(k) or tax-exempt account like a Roth IRA -- can often be the smartest move you can make.

2011 Retirement Plan Account Limits	
Maximum contribution limit for 401(k), 403(b), and 457 plan participants	$16,500
Maximum additional "catch-up" contributions for 401(k), 403(b), and 457 plan participants age 50 and older	$5,500
Maximum traditional IRA contribution	$5,000
Maximum additional "catch-up" contributions for traditional IRA account holders age 50 and older	$1,000
Maximum contribution limit for SIMPLE retirement accounts	$11,500
Maximum contribution limit for Roth IRAs[3]	$5,000

[1]Source: Employee Benefit Research Institute, EBRI Notes, October 2010.

[2]Diversification and asset allocation do not ensure a profit or protect against a loss in a declining market.

[3]Roth IRA contributions may be made only by single taxpayers with modified adjusted gross incomes (MAGIs) of less than $122,000 and married joint filers with MAGIs of under $179,000. Phase-out limits for partial contributions also apply. If your MAGI is close to or over these limits, talk to your financial or tax professional before contributing to a Roth IRA.

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Four Risks to Your Retirement Future

Because younger retirees typically are planning for a time horizon of 20 years or more, it is important that their portfolios include a source of growth that is likely to exceed inflation over the long term.

As Americans live longer, the task of managing money after retirement gets more complex. A retiree in his or her mid-60s typically has a different risk profile than an individual approaching 90. It may be helpful to look at various types of risk from the vantage point of how they affect retirees at different life stages. Here are four key risks to consider.

1. Investment Risk -- Balancing risk and return takes on a different meaning for individuals as they age. A negative rate of return during the early years of retirement could leave an individual with a significantly smaller nest egg when compared with negative returns later in the retirement life cycle. Your financial advisor can help you craft an investment mix with the goal of smoothing out returns over the long term and increasing the chances that your assets will last throughout your lifetime.

2. Longevity Risk -- Withdrawing too much from a portfolio during the early years of retirement may heighten the chance of depleting your assets during your later years. For this reason, many financial advisors recommend limiting annual withdrawals to 5% or less of a portfolio's value, adjusted for inflation, to make assets last as long as possible.

3. Inflation Risk -- Because younger retirees typically are planning for a time horizon of 20 years or more, it is important that their portfolios include a source of growth that is likely to exceed inflation over the long term. To complement this potential growth, many retirees rely on more conservative investments that may generate income and help to balance risk and potential return.

4. Health Care Risk -- It is not unusual for medical costs to increase as retirees age, and it may be prudent to plan for these costs before the need is immediate. Preretirees and younger retirees may want to explore options for medical insurance that supplements Medicare, as well as long-term care insurance, to reduce the possibility of dipping into personal assets to finance illness- or accident-related expenses. Also, remember that those who retire before age 65 need to find an alternate source of medical insurance prior to becoming eligible for Medicare.

Reviewing these and other challenges associated with retirement planning with your financial advisor may increase your confidence that you have considered all scenarios. While it may not be possible to prepare for every situation, planning ahead may help you cope with financial issues that come your way.

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