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MENTOR
CAPITAL

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Mentor Monthly Missive

In this issue:

Uncle Sam wants YOU – To save for retirement

By giving incentives to taxpayers who put money aside for retirement, the federal government is engaging in a bit of social engineering and acting in its own best interests: People who prepare financially for retirement are less likely to be a burden. That's good public policy.

So U.S. tax laws provide an abundant array of tax breaks for individuals and businesses to bolster wage-earners' retirement. Because retirement planning is high on most of our clients' lists of planning issues, we are fully familiar with the options. Here is a brief rundown:

For individuals:

- Traditional IRA – Contributions are tax-deductible but may be limited if the taxpayer is covered by a qualified retirement plan. Withdrawals of contributions and gains are taxed at the taxpayer's highest marginal bracket. Penalties apply for most pre-age 59 ½ withdrawals. Withdrawals must begin by April 1 of year following the year in which account holder turns 70 ½ years old.
- Roth IRA – Contributions are not tax-deductible but may be limited if the taxpayer's income is too high. Withdrawals of contributions are tax-free at any time. There is no requirement that withdrawals begin by any age.
- Non-deductible IRA – Appropriate when tax-deductibility of contributions is limited. Ordinary income taxes apply to earnings when distributed; no tax applies to distribution of basis. Maximum contribution for all IRAs is $5,000 per year ($6,000 for those 50 and older).
- Non-qualified savings – Many advantages exist for saving outside of any qualified retirement account. Although current tax breaks are not available, no penalties apply for withdrawal. Having a source of non-qualified assets to draw on in retirement can create a scenario with maximum flexibility.

For employers:

- SEP-IRA – For self-employed individuals. An IRA with higher contribution limits: 20% of net self-employment income after the self-employment tax deduction, up to a maximum of $49,000. No administrative costs. Contributions subject to Social Security and Medicare taxes, but not income taxes.
- SIMPLE IRA – For small (less than 100 employees) businesses. Requires employer contributions; employees may contribute up to $11,500 per year ($14,000 for those 50 or older). Few if any administrative costs. Contributions subject to Social Security and Medicare taxes, but not income taxes.
- 401(k) – Employees contribute from wages, and employer can contribute from profits. Testing and compliance with federal law tend to result in high administrative costs. Employee deferrals limited to $16,500 ($22,000 if 50 or older). Employee contributions subject to Social Security and Medicare taxes, but not income taxes.
- Profit-sharing – Company makes contributions. No employee contributions allowed. Employees may be excluded based on age or service. Contributions are not taxed for Social Security or Medicare.
- Defined-benefit pension – May be funded by employer contributions or both employee and employer

contributions. Benefit is typically a monthly payment beginning at retirement and lasting for the life of the retiree. Currently the least popular retirement plan option because it is the least flexible.

Dozens of factors, such as tax bracket, personal cash flow and goals other than retirement must be considered before choosing any retirement-saving option. Call one of our advisers if you'd like to discuss.

Markets review – February 28, 2011

This new monthly feature of the Mentor Missive will attempt to provide insight into what happened in the financial markets during the previous month.

Although it hit an oil slick in late February, the Dow Jones Industrial Average ended February up 334.41, or 2.8%, a continuation of the stock market's advance that began in March 2009. After hitting a high of 12,391.25 on Feb. 18, rising oil futures put a damper on the fun, driving the average down below 12,060 before it recovered to close out the month at 12,226.34

Measured by the Dow Industrial Average, on Feb. 28 domestic stocks were up 86.75% from their March 9, 2009, low. The Russell 2000 small-stock index got about as close as it could to doubling during the period, up 99.84%.

The winning domestic stock index for the first two months of 2011 was the S&P Midcap 400, up 6.5%. That benchmark also has been the sweet spot for the 52-week period ending Feb. 28, up 28.7%. By comparison, the 30 industrials were up 17.5% and the Russell 2000 small-cap index was up 28.1% for the 52 weeks.

The bond market ended February little changed from Jan. 31, although there was some volatility in between. The yield on the 10-year Treasury rose 0.89% to close February at 3.41%. (Bond prices move inversely to yields.) For the 30-year Treasury, the yield actually declined to 4.49% from the Jan. 31 close of 4.57%, narrowing the spread between the 10- and 30-year and emphasizing the market's belief that increased inflation is in the cards.

We are continuing to recommend stock allocations of between 60% and 85% for aggressive investors with long time horizons. Our model portfolios of low-expense, passively managed exchange-traded funds continue to perform as expected based on our asset-allocation models.

Readers often ask us: Is now the time to buy oil companies? Gold? Our response is always: If you are invested properly in stocks, you already own oil and gold. The index funds in your portfolio include appropriate holdings of oil companies and mining stocks. After a run-up like we've seen in oil and metals, it's not the time to be increasing exposure. Buy low and sell high, remember?

To discuss, call or email.