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Get a Tax-Smart Plan for In-Retirement Withdrawals

The following sequence may make sense for retirees to preserve the tax-saving benefits of tax-sheltered investments for as long as possible.

1) For retirees over age 70 1/2, the first stop for withdrawals are those accounts that carry required minimum distributions, or RMDs, such as Traditional IRAs and company retirement plans such as 401(k)s (to avoid paying penalties).

2) For retirees who are not required to take RMDs or have taken their RMDs and still need cash, turning to taxable assets may be an option. A good start may be selling assets with the highest cost basis first and then moving on to those assets where cost basis is lower (and the tax hit higher). Relative to tax-deferred or tax-free assets, these assets have the highest costs associated with them. However, taxable assets could also be valuable to tap in later retirement years because retirees will pay taxes on withdrawals at their capital gains rate, which is generally lower than the ordinary income tax rate.

3) Finally, after taking RMDs or tapping taxable assets, retirees still in need of cash may want to further tap company retirement-plan accounts and IRAs (Roth IRA assets last.)

401(k) and IRA plans are long-term retirement-savings vehicles. Withdrawal of pretax contributions and/or earnings will be subject to ordinary income tax and, if taken prior to age 59 1/2, may be subject to a 10% federal tax penalty. Direct contributions to a Roth IRA are not tax-deductible but may be withdrawn free of tax at any time. Earnings may be withdrawn tax and penalty free after a 5 year holding period if the age of 59 1/2 (or other qualifying condition) is met. Otherwise, a 10% federal tax penalty may apply. Please consult with a financial or tax professional for advice specific to your situation.

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Mitchell McLeod Pugh & Williams, Inc. - Return of Volatility

The fourth quarter has arrived along with renewed market volatility. The final three months of the year are typically a busy period for investors and their advisers - portfolios are being reviewed, year end results are being evaluated and tactical changes are being considered. And as unwelcome as short-term volatility may be, it should never be a reason to alter one's long term strategy. Equity markets have been delivering large losses or gains on a daily basis. The reasons for this volatility are myriad. But what has actually changed since the market highs of September? The European slowdown, weakness in China and Fed policy have all been discussed at length in recent months. Clearly, the fear of Ebola's spread and increasing tensions in the Middle East are additional areas of concern. But none of this has changed our long term view, and we believe it may even lead to investment opportunities as we approach year end.

Monthly Market Commentary

The U.S. market returned 8.3% so far this year (as of the end of the third quarter). The U.S economy appears to be holding its own despite setbacks in the rest of the world.

Employment: Private sector employment growth has been stuck in an exceptionally narrow range of 2.0%–2.2% year-over-year growth since 2011. As suggested by a falling unemployment rate (5.9%), recovery-low initial unemployment claims, and wage growth in select categories, Morningstar economists believe the economy may face spot labor shortages in 2015. That could mean that pay rates in some industries will need to go up. That could also pressure corporate earnings in the year ahead, along with rising interest rates and an increase in the trade-weighted dollar that has now appreciated by close to 12%. 2015 could be the first year when it might be better to be an employee than an employer.

Consumption and Income: For most of 2014, income growth has been excellent while consumption growth has been volatile and much slower. Between December and August real wages are up 3.1%, real disposable income is up 2.8%, and consumption a meager 1.4%. The premise and reason for optimism, at this point, is that incomes don't grow faster than consumption for long in the United States. As inflation backs down again and the job market continues to improve, consumers are likely to increase spending in the back part of 2014, which in turn should help push overall third-quarter GDP growth.

Trade: The trade deficit shrank from $40.3 billion in July to $40.1 billion in August. The inflation-adjusted deficits for July and August are running considerably lower than the slightly inflated numbers of the second quarter. Net trade took 0.4% off of GDP growth in the second quarter and is likely to add 0.2% in the third quarter, providing potential for a meaningful swing. Unfortunately, trade may hurt the U.S. economy in the fourth quarter because of a stronger dollar.

Quarter-End Insights: 2014 was to have benefited from a huge swing in the government category as well as a continued big rebound in housing and a strengthening world economy. That didn't happen. Housing slowed because of affordability and credit tightness. Government did get a little better, but not nearly as much as hoped, as last year's budget agreement weighed on spending. In fact, as fiscal 2014 draws to a close, federal government spending looks to be lucky to grow at 1%, before adjusting for inflation.

Furthermore, world growth has been a big disappointment. After just one year of mediocre growth, Europe didn't show any growth at all in the second quarter. China, too, has been a disappointment, with both exports and real estate turning in poor results. China's currency has been weaker, also, which has helped exports to the U.S. and hurt imports. The bright side to this surprising world weakness has been more liberal central banks, falling inflation rates, and lower interest rates.

Lately, there was some fear that in the long term, U.S. GDP growth could slip well under 2%. That is as overblown as the expected return to 3%-plus growth was just a few short years ago. First and foremost, residential spending has yet to return to its normal level (5% of GDP), despite population growth and five years of economic recovery. Exports to the rest of the world will also help keep the U.S. growth story afloat. Airliners are likely to be in strong demand throughout the world over the next 10 years. With long production and design cycles, competition for the U.S. airliners will prove minimal. Growing agricultural demand and growing oil-related exports should also keep the U.S. ahead of the developed world growth rates. Demographics, however, including lower population growth rates and an unfavorable shift to older, lower-spending consumers, may keep a lid on long-term economic growth.

Concerned About Longevity? Three Mistakes to Avoid

Longevity is often cheered as an achievement, but the downside of living well beyond one's average life expectancy is that it can strain (or worse, completely deplete) an individual's financial resources. The first step in addressing longevity risk is to evaluate just how great the odds are that either you or your spouse will have a much longer-than-average life span. Health considerations, family longevity history, employment choices, and income level may all be factors. If you've assessed these considerations and are concerned about longevity risk--or if you've determined that you'd simply rather be safe than sorry--here are three key mistakes to avoid.

Mistake 1: Holding a Too-Conservative Portfolio. When investors think about reducing risk in their portfolios, they often set their sights on curtailing short-term volatility—the risk that their portfolios will lose 10% or even 20% in a given year. But a too-conservative portfolio (one that emphasizes cash and bonds at the expense of stocks) can actually enhance shortfall risk while keeping a lid on short-term volatility. But, right now, interest rates have much more room to move up than they do down, which may reduce the opportunity for bond-price appreciation during the next decade. With such low returns, retirees with too-safe portfolios may not even outearn the inflation rate over time.

Mistake 2: Not Delaying Social Security Filing.* Because it provides an inflation-adjusted income stream for the rest of your life, Social Security is designed to provide you with at least some money coming in the door even if your investment portfolio runs low (or out) during your later years. If you file early (you're eligible to do so as early as age 62), you permanently reduce your annual benefit from the program.

Delayed filing, on the other hand, has the opposite effect, amping up the value of your hedge. Not only will your benefits last as long as you do, but they'll be higher, perhaps even substantially so, as well. Those who delay filing until age 70 may receive an annual benefit that's more than 30% higher than what they would have received had they filed at full retirement age (currently 66) and more than 50% higher than their benefit had they filed at age 62.

Mistake 3: Not Adjusting Withdrawal-Rate Assumptions. Just as savings rates are the main determinant of success during the accumulation years (much more than investment selection, in fact), spending rate is one of the central determinants of retirement plans' viability.

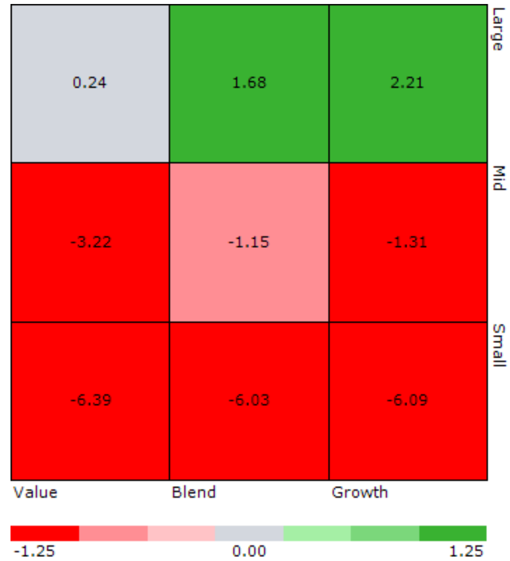
The 4% rule, which indicates that you can withdraw 4% of your total portfolio balance in year 1 of retirement, then annually inflation-adjust that dollar amount to determine each subsequent year's portfolio payout, is a decent starting point in the sustainable withdrawal-rate discussion. But it's important to tweak your withdrawal rate based on your own situation. If you have a sparkling health record and it looks likely that you'll be retired longer than the 30-year withdrawal period that underpins the 4% rule, you may be better off starting a bit lower.

In a similar vein, it's important to not set and forget your retirement-plan variables, such as your spending rate and your asset allocation, because retirement progresses and new information becomes available about your health and potential longevity, market valuations, and so forth.

This is for informational purposes only and should not be construed as legal, tax, or financial planning advice. Please consult a legal, tax, and/or financial professional for advice specific to your individual circumstances. Asset allocation and diversification are methods used to help manage risk. They do not ensure a profit or protect against a loss. Returns and principal invested in securities are not guaranteed, and stocks have been more volatile than bonds.

*Source: Social Security Administration.

Quarterly Market Barometer



3 Month, ending September 30, 2014. The U.S. Market returned 0.21% (YTD 7.33%).

The Morningstar Market Barometer provides a visualization of the performance of various stock market indexes. The color scale (red for losses and green for gains) allows you to assess which areas of the market performed strongly and which areas showed weakness for the time period analyzed. The nine-square grid represents stocks classified by size (vertical axis) and style (horizontal axis). There are three investment styles for each size category: small, mid and large. Two of the three style categories are “value” and “growth” while the central column represents the core style (neither value nor growth characteristics dominate). Large-caps account for the top 70% of the capitalization; mid-caps represent the next 20%; and small-caps represent the balance.

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