

FINANCIAL SERVICES

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Factors to Consider

Converting Funds from a Traditional IRA to a Roth IRA

OVERVIEW

Do you qualify to convert funds from a traditional IRA to a Roth IRA? Guessing incorrectly may have serious consequences; the conversion of funds from a traditional IRA to a Roth IRA is considered a taxable distribution, subject to federal income tax and a possible penalty. The fact that you qualify to convert funds from a traditional IRA to a Roth IRA doesn't necessarily mean you should; consider the following factors before making a decision.

Will you pay the tax that results from converting funds with outside (non-IRA) funds?

- Converting traditional IRA funds to a Roth IRA will result in federal income tax due on those funds (to the extent that those funds consist of investment earnings and tax-deductible contributions).
- Paying the tax due with IRA funds reduces the amount that grows tax-free in the Roth IRA.
- IRA funds used to pay the tax may be subject to additional income tax and possibly a penalty.
- Paying the tax due with non-IRA funds allows more dollars to be funneled into the tax-free Roth IRA.

Do you expect to be in the same or in a lower or higher income tax bracket when you eventually take IRA distributions?

- If your tax bracket remains the same and you pay the taxes that result from converting funds with IRA dollars, the conversion may have no tax consequence.
- If you'll be in a lower tax bracket when you take IRA distributions, paying tax now on converted funds at your present (higher) rate may not be very appealing.
- If you'll be in a higher tax bracket when you take distributions, you can convert funds to a Roth IRA now and pay tax at your present (lower) tax rate, and distributions will be tax-free later (assuming you qualify for tax-free withdrawals).

Can you leave your funds in your Roth IRA for at least five years?

- If you withdraw funds after five years from the time you establish any Roth IRA, you may qualify for tax-free and penalty-free withdrawals if you meet one of several other conditions (a qualified withdrawal).
- If you convert a traditional IRA to a Roth IRA, and then make a non-qualified withdrawal within five years, the earnings you withdraw will be subject to income tax, and your entire withdrawal may be subject to a 10 percent penalty unless an exception applies (age 59 1/2, etc.).

Can you leave your funds in your Roth IRA for at least 10 years?

- This time frame becomes more important when you're paying the tax that results from converting funds with IRA funds.
- Generally, converting funds to a Roth IRA makes sense if you plan to leave the funds in the Roth IRA for 10 years or more.
- If you plan to take distributions from the Roth IRA within the next 10 years, make sure converting funds is in your best interest.

Can you live comfortably in retirement without taking IRA distributions?

- You can keep contributing to the Roth IRA after age 70½, as long as you have sufficient earned income.
- Unlike a traditional IRA, you aren't required to take annual minimum distributions from a Roth IRA after age 70½ or at any time during your life.
- Assuming five years have elapsed from the time you established any Roth IRA, your beneficiary receives Roth IRA funds free from federal income tax (but not necessarily from federal estate tax) when you die.

Understanding the Income for Life Model

OVERVIEW

More than ever before, retirees are depending on their investments to generate retirement income. This article explains how the *Income for Life Model™* can help.

What is it?

An investment model designed to provide an inflation-adjusted income for life, the *Income for Life Model™* allocates assets in a manner that places a heavy emphasis on guaranteed streams of income that continue over long periods of time. This is extremely important because Americans are increasingly being forced to rely on their own retirement savings to create the retirement income they will need. With longevity increasing and interest rates low, creating durable streams of retirement income can be challenging. The *Income for Life Model™* provides a sound foundation for creating that income.

How Can it Help Me?

The *Income for Life Model™* helps you achieve a level of psychological comfort over your retirement assets. First, by identifying the amount of assets you have available to dedicate to producing income, the model can help you identify a baseline retirement income for today and in the future. It can then allocate those assets with the goal of producing increasing retirement income adjusted for a reasonable inflation factor.

By placing a heavy emphasis on creating income streams which are guaranteed, this model can help you keep more aggressive assets invested for longer periods of time. This is very important. Too often, people move in and out of investments quickly, suffering sub-par results along the way. These sub-par results are ultimately dangerous to a financially secure retirement.

The Challenge

A “perfect storm” has emerged for today’s retirees, comprised of low interest rates, volatile stock markets and unprecedented longevity. These realities can create stress for retirees as they seek to make their retirement income last as long as they do.

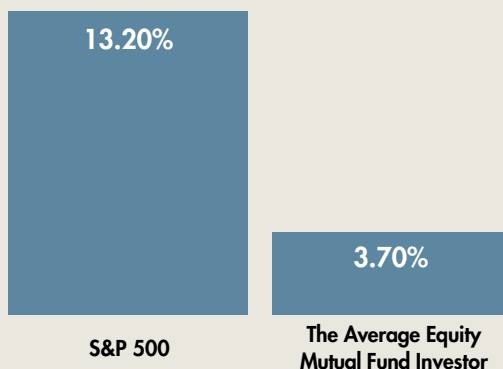
With fewer companies providing traditional pension plans, retirees are being forced to assume the investment risk associated with their retirement assets. Widespread uncertainties about the future of Social Security continue to linger. Increasing budget deficits and financial uncertainty only create additional anxiety for retirees. All of these factors combine in a way that causes retirees to seek investment choices that offer safety but also provide growth opportunities to meet their income needs for both today and tomorrow.

Until now, no asset allocation approach was available that placed sufficient emphasis on the present and future income needs of retirees. The central objective for the *Income for Life Model™* is to provide an inflation-adjusted income for life. In addition, interest rates at levels not seen since the Eisenhower Administration have reduced the current income that can be gained from savings vehicles. Many retirees are thus challenged to find ways to boost levels of current income without taking on undue risk.



The Facts

During the period between 1985-2004, the S&P 500 grew by 13.20%, however, the average equity mutual fund investor earned only 3.70%.¹



Why?

Lack of Strategy

Individuals chased performance and became integral players in momentum driven markets.

Lack of Patience

With the average mutual fund position held for just two years, investors did not give their investment decisions sufficient time to develop.

Emotions

Many investors succumbed to emotionally-based decision making driven first by greed and then followed by fear.

How Assets Are Allocated Using the Income for Life Model

Segment One
Fixed 28%

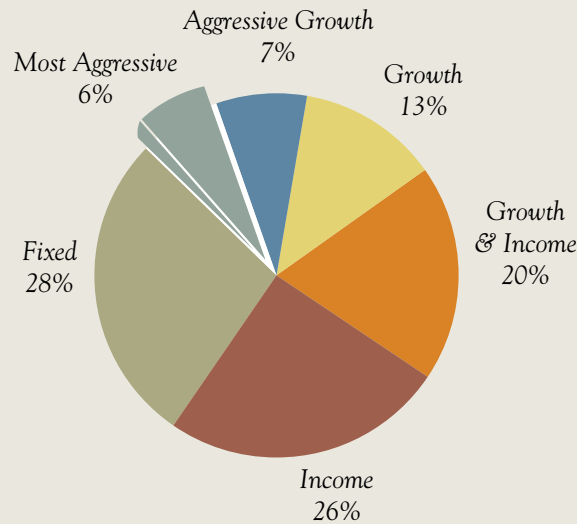
Segment Two
Income 26%

Segment Three
Growth & Income 20%

Segment Four
Growth 13%

Segment Five
Aggressive Growth 7%

Segment Six
Most Aggressive 6%



The Way Assets are Allocated

Your deposit is shown as being allocated to six “segments” that will hold invested assets ranging from very conservative to aggressive. Segment one, the most conservative, receives the largest portion of your deposit – 28%. Successive segments receive 26%, 20%, 13%, 7% and 6% (total, 100%). The segments receiving the smallest amount of money are those which hold progressively more aggressive assets. The more aggressive an investment, the more risk it is subject to. These segments will be held for the longest period of time in order to achieve the best possible chance of excellent investing results.

Initially, a guaranteed income will be provided by a fixed, single premium immediate annuity for a period of 60 months. For each subsequent five-year period, additional segments will be successively converted into fixed, single premium

immediate annuities with payouts of 60 months. Should the projected rates of return be realized in the various segments, sufficient money will be available to purchase these annuities in amounts capable of providing an increasing level of retirement income. Segment six is shown as a hedge against you living beyond 25 years from the date of inception. If that segment meets its projected rate of return, it will hold sufficient assets to continue an income stream. At your death, any remaining assets will pass to your beneficiaries.

To learn more about how the *Income for Life Model*[™] can help you plan for the future, please contact your Eide Bailly financial advisor. ■

CONTACT

- Talk to your local Eide Bailly financial advisor
- Call 866.740.4100 for more information



A Solution for Investing Problems

The Problems

Invest only in Guaranteed Investments:

1. Low rate of return.
2. Insufficient current income.
3. No inflation protection.

Invest in Growth Vehicles:

1. Possibility of negative returns.
2. Drawing income during normal market downturns could put investment principal at risk.

A Solution: Income for Life

A strategic combination of asset allocation and product selection with the following goals:

1. Reduce the impact of emotions.
2. Increase income to bolster purchasing power throughout retirement.
3. Reduce risk.
4. Preserve principal.
5. Realize the best possible chance of achieving substantial investment results by keeping assets invested over long periods of time.

Six Keys to More Successful Investing

OVERVIEW

A successful investor maximizes gain and minimizes loss. Here are six basic principles that may help you invest more successfully.



Though diversification alone cannot guarantee a profit or ensure against the possibility of loss, you can minimize your risk somewhat by diversifying your holdings among various classes of assets, as well as different types of assets within each class.

Long-Term Compounding May Help Your Nest Egg Grow

It's the "rolling snowball" effect. Simply put, compounding pays you earnings on your re-invested earnings. The longer you leave your money at work for you, the more exciting the numbers get. For example, imagine an investment of \$10,000 at an annual rate of return of 8 percent. In 20 years, assuming no withdrawals, your \$10,000 investment would grow to \$46,610. In 25 years, it would grow to \$68,485, a 47 percent gain over the 20-year figure. After 30 years, your account would total \$100,627. (Of course, this is a hypothetical example that does not reflect the performance of any specific investment.)

This simple example also assumes that no taxes are paid along the way, so all money stays invested. That would be the case in a tax-deferred individual retirement account or qualified retirement plan. The compounded earnings of deferred tax dollars are the main reason experts recommend fully funding all tax-advantaged retirement accounts and plans available to you.

While you should review your portfolio on a regular basis, the point is that money left alone in an investment offers the potential of a significant return over time. With time on your side, you don't have to go for investment "home runs" in order to be successful.

Endure Short-Term Pain for Long-Term Gain

Riding out market volatility sounds simple, doesn't it? But what if you've invested \$10,000 in the stock market and the price of the stock drops like a stone one day? On paper, you've lost a bundle, off-setting the value of compounding you're trying to achieve. It's tough to wait it out.

There's no denying it—the financial marketplace can be volatile. Still, it's important to remember two things. First, the longer you stay with a diversified portfolio of investments, the more likely you are to reduce your risk and improve your opportunities for gain. Though past performance doesn't guarantee future results, the long-term direction of the stock market has historically been up. Take your time horizon into account when establishing your investment game plan. For assets you'll use soon, you may not

have the time to wait out the market and should consider investments designed to protect your principal. Conversely, think long-term for goals that are many years away.

Second, during any given period of market or economic turmoil, some asset categories and some individual investments historically have been less volatile than others. Bond price swings, for example, have generally been less dramatic than stock prices. Though diversification alone cannot guarantee a profit or ensure against the possibility of loss, you can minimize your risk somewhat by diversifying your holdings among various classes of assets, as well as different types of assets within each class.

Spread Your Wealth Through Asset Allocation

Asset allocation is the process by which you spread your dollars over several categories of investments, usually referred to as asset classes. These classes include stocks, bonds, cash (and cash alternatives), real estate, precious metals, collectibles and in some cases, insurance products. You'll also see the term "asset classes" used to refer to subcategories, such as aggressive growth stocks, long-term growth stocks, international stocks, government bonds (U.S., state, and local), high-quality corporate bonds, low-quality corporate bonds and tax-free municipal bonds. A basic asset allocation would likely include at least stocks, bonds (or mutual funds of stocks and bonds) and cash or cash alternatives.

There are two main reasons why asset allocation is important. First, the mix of asset classes you own is a large factor—some say the biggest factor by far—in determining your overall investment portfolio performance. In other words, the basic decision about how to divide your money between stocks, bonds and cash is probably more important than your subsequent decisions over exactly which companies to invest in, for example.

Second, by dividing your investment dollars among asset classes that do not respond to the same market forces in the same way at the same time, you can help minimize the effects of market volatility while maximizing your chances of return in the long term. Ideally, if your invest-

ments in one class are performing poorly, assets in another class may be doing better. Any gains in the latter can help offset the losses in the former and help minimize their overall impact on your portfolio.

Consider Liquidity in Your Investment Choices

Liquidity refers to how quickly you can convert an investment into cash without loss of principal (your initial investment). Generally speaking, the sooner you'll need your money, the wiser it is to keep it in investments with comparatively less volatile price movements. You want to avoid a situation, for example, where you need to write a tuition check next week, but the money is tied up in an investment whose price is currently down.

Therefore, your liquidity needs should affect your investment choices. If you'll need the money within the next one to three years, you may want to consider certificates of deposit or a savings account, which are insured by the FDIC, or short-term bonds or a money market account, which are neither insured or guaranteed by the FDIC or any other governmental agency. Your rate of return will likely be lower than that possible with more volatile investments such as stocks, but you'll breathe easier knowing that the principal you invested is relatively safe and quickly available, without concern over market conditions on a given day.

Note: If you're considering a mutual fund, consider its investment objectives, risks, charges and expenses, all of which are outlined in the prospectus, available from the fund. Consider the information carefully before investing.

Dollar Cost Averaging: Investing Consistently and Often

Dollar cost averaging is a method of accumulating shares of stock or a mutual fund by purchasing a fixed dollar amount of these securities at regularly scheduled intervals over an extended time. When the price is high, your fixed-dollar investment buys less; when prices are low, the same dollar investment will buy more shares. A regular, fixed-dollar investment should result in a lower average price per share than you would get buying a fixed number of shares at each investment interval.

Remember, just as with any investment strategy, dollar cost averaging can't guarantee you a profit or protect you against a loss if the market is declining. To maximize the potential effects of dollar cost averaging, you should also assess your ability to keep investing even when the market is down.

An alternative to dollar cost averaging would be trying to "time the market," in an effort to predict how the price of the shares will fluctuate in the months ahead so you can make your full investment at the absolute lowest point. However, market timing is generally unprofitable guesswork. The discipline of regular investing is a much more manageable strategy, and it has the added benefit of automating the process.

Six Keys to Investing—continued on page 6



Your liquidity needs should affect your investment choices. If you'll need the money within the next one to three years, you may want to consider certificates of deposit or a savings account, which are insured by the FDIC, or short-term bonds or a money market account, which are neither insured or guaranteed by the FDIC or any other governmental agency.

The image shows a collage of financial information. On the left, there are three dice. In the center, a large 'STOCK EXCHANGE' board is visible, featuring a 'MOST ACTIVE' section with columns for Name, Val (Bil), Last, and Chg. To the right, there are several columns of stock data with columns for Name, High, Low, Cls, and Chg. The data includes various stock tickers and their corresponding prices and changes.

Six Keys to Investing—from page 5

Buy and Hold, Don't Buy and Forget

Unless you plan to rely on luck, your portfolio's long-term success will depend on periodically reviewing it. Maybe your uncle's hot stock tip has frozen over. Maybe economic conditions have changed the prospects for a particular investment, or an entire asset class.

Even if nothing bad at all happens, your various investments will likely appreciate at different rates, which will alter your asset allocation without. For example, if you initially decided on an 80 percent to 20 percent mix of stocks to bonds, you might find that after several years the total value of your portfolio has become divided 88 percent to 12 percent (conversely, if stocks haven't done well, you might have a 70-30 ratio of stocks to bonds). You need to review your

portfolio periodically to see if you need to return to your original allocation. To rebalance your portfolio, you would buy more of the asset class that's lower than desired, possibly using some of the proceeds of the asset class that is now larger than you intended.

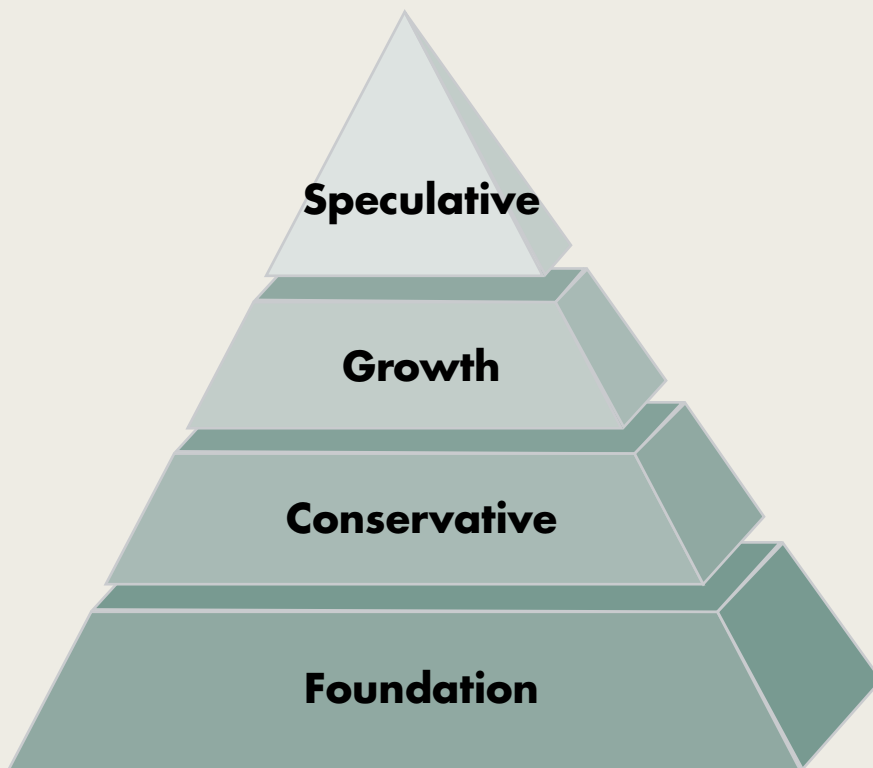
Another reason for periodic portfolio review: your circumstances change over time, and your asset allocation will need to reflect those changes. For example, as you get closer to retirement, you might decide to increase your allocation to less volatile investments, or those that can provide a steady stream of income. ■

CONTACT

- Talk to your local Eide Bailly financial advisor
- Call 866.740.4100 for more information

Building an Investment Portfolio

When planning an investment strategy, it is important to have a strong foundation and a well-balanced portfolio.



Increase Risk = Increase Potential Reward

Speculative

Art
Coins
Precious Metals
Options
Penny Stocks
Commodities
Venture Capital

Growth

Stock and Stock Mutual Funds
(Blue Chip and Growth)
Investment Real Estate

Conservative

Balanced Funds
High Grade Corporate and
Municipal Bonds
U.S. Government Notes and Bonds

Foundation

Insured Certificates of Deposit
Traditional Savings Accounts
Treasury Bills

Decrease Risk = Decrease Potential Reward

*Factors to Consider—from page 1***Does your traditional IRA consist of any non-deductible (after-tax) contributions?**

- You've already paid federal income tax on any nondeductible contributions to your traditional IRA, so these dollars are not subject to federal income tax when you convert funds to a Roth IRA.
- After you convert funds, future investment earnings on your Roth IRA will accrue tax-free.

When you die, will federal estate tax be due?

- When you die, the value of your IRA (traditional or Roth) will be included in your taxable estate to determine if federal estate tax is due.
- When you convert funds from a traditional IRA to a Roth IRA, you pay federal income tax on your IRA funds now rather than later.
- The money you use to pay the tax now effectively removes those dollars from your taxable estate, potentially reducing your federal estate tax liability after your death.

Will you apply for financial aid in the next few years?

- When you convert funds from a traditional IRA to a Roth IRA, you pay federal income tax on your IRA funds now rather than later.
- The money you use to pay the tax now effectively removes those dollars from the assets to be considered in determining your child's eligibility for financial aid.

Are you currently receiving Social Security benefits?

- The portion of your Social Security benefits that is taxable in any year depends on your income and tax filing status for that year.
- Excluding any nondeductible contributions, funds that you convert to a Roth IRA are treated as taxable income to you for that year.
- If more of your Social Security benefits will be taxed as a result of converting funds to a Roth IRA, factor in the additional tax cost to you.
- Balance this cost against the fact that distributions from Roth IRAs, in addition to being tax-free, are not currently counted in determining the taxable portion of your Social Security benefits.

Does your state follow the federal income tax treatment of Roth IRAs?

- If your state does not follow the federal income tax treatment of Roth IRAs, you must factor in the way that your state tax treatment will affect your situation.

Does your state provide Roth IRAs with protection from creditors equal to that provided to traditional IRAs?

- Up to \$1,095,000 (and in some cases more) of your total IRA assets, Roth and traditional, are protected under federal law in the event you declare bankruptcy. State law may provide additional creditor protection, but the protection given to funds in Roth IRAs may be less than that given to funds in traditional IRAs.
- If you have a significant percentage of your assets in IRAs and you are at risk of being sued by creditors, you should consider your state's degree of creditor protection for each type of IRA.

*To qualify to convert funds from a traditional IRA to a Roth IRA, your modified adjusted gross income (MAGI) for the year must be less than or equal to \$100,000 if you are a single taxpayer. If you are married and file a joint return, the \$100,000 refers to the combined MAGI of you and your spouse. (Note: The \$100,000 limitation is repealed after 2009.)

If you participate in a 401(k) or 403(b) plan at work, you may be able to make Roth contributions to the plan. (Check with your plan administrator—401(k) and 403(b) plans aren't required to offer this option.) Qualified distributions of Roth contributions and related earnings are income tax free (and penalty free) at the federal level. This may be a factor in your decision of whether to convert funds from a traditional IRA to a Roth IRA. However, be sure to discuss your situation with a professional advisor before making any decisions. ■

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Helping You Stay Focused

Recent events in the financial world have raised a lot of questions in the minds of investors—should I buy ... sell ... or hold? When emotions take control of your financial decisions, you may not make the right choices. Our financial planning team is here to help you stay focused on your needs and make financially-sound decisions.



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