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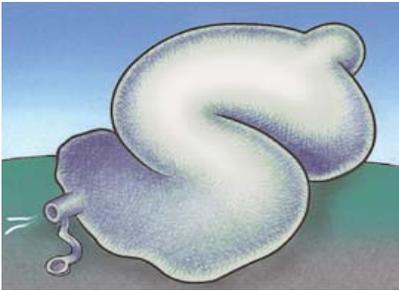
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Five ways to fight deflation fears



Which way will the economic winds blow in 2011 and beyond? Although no one knows for sure, the Wall Street Journal recently reported a growing concern among economists over potential deflation. This

contrasts with other opinions voiced during the past few years that have focused on fears of inflation.

In simple terms, deflation is a decline in the value of assets and consumer prices. It may result from a drop in demand during a recessionary period. However, there are several ways you might protect yourself from the trend. Here are five practical suggestions:

1. Bring down debt. In a deflationary economy, dollars are worth more in the future, due to falling prices. Therefore, paying off loans becomes more expensive. For example, in a deflationary economy, an automobile costing \$25,000 today might be priced at \$22,000 the following year, but your loan amounts remain the same. As a result, you might try to lessen your burden through astute consolidation of credit card debt or other means.

2. Save for a “rainy day.” It often is suggested that you should maintain savings to cover three to six months’ worth

of living expenses in case of emergencies, such as a sudden job loss or an unexpected medical condition. With higher unemployment rates, you might extend that target out six to nine months’ worth of expenses. If deflation occurs, you will be in a better position to benefit.

3. Take control of your financial situation. Getting a grip on personal finances can help ease fears arising in turbulent economic times. If you don’t already have one, draw up a budget. Try saving for specific financial goals by arranging automated transfers from your main bank account to another account. Earmark the savings for specific goals like a college fund for your children, a retirement nest egg, or a well-deserved vacation.

4. Make yourself “indispensable” at work. Deflation usually takes its toll on the job market. If your employer needs to make cuts, you will want to be the last in line. Don’t just do the bare minimum required of you: Go the extra yard. Also, remain poised for other opportunities. Should your job be eliminated, you will want to explore your options quickly. Take advantage of networking and social media contacts.

5. Prepare to cash in on bargains. A deflationary economy may create unique buying opportunities. For instance, some first-time homebuyers are already finding homes selling at much lower prices than sellers were asking a year

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Five ways to fight deflation fears

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ago. Similarly, if you want to build up an investment portfolio, you might benefit by acquiring stocks of solid companies at low prices. Of course, there are no absolute guarantees, and investors must be aware of all the inherent risks.

These are sound fundamental strategies to follow whether deflation occurs or not. Coordinate your efforts with the help of a trusted financial advisor.



Climbing up a bond ladder

Bonds are often added to a portfolio for greater stability. However, while they are historically not as volatile as stocks, bonds can still be affected by rising and falling interest rates.

Basic premise: If interest rates rise before a bond's maturity date, you will be saddled with a below-market rate for the term of the bond. In that case, you could sell the bond at a loss or hope to invest the principal at a higher rate when the bond matures.

On the other hand, if you hold a bond until its maturity date, the reverse occurs if interest rates fall: Investors will pay more for an existing bond that hasn't reached its maturity. The longer the maturity of a bond, the faster the price of the bond rises or falls in relation to changing interest rates.

There is a relatively simple way you might protect yourself against interest rate fluctuations while managing the cash flow from bond investments. It's called a "bond ladder."



How it works: Instead of buying, say, one \$100,000 ten-year bond, you buy ten \$10,000 bonds with varying maturities, beginning with one year and going up to ten years. As a result, you own bonds maturing every year for the next ten years. This provides a laddered portfolio of short-term, midterm and long-term bonds.

If interest rates go up, you will have a bond maturing sooner that can be reinvested at a higher interest rate. You can reinvest the maturing one-year bond at ten years to keep the ladder going. If interest rates drop, only a small portion of your portfolio - the maturing one-year bond - must be reinvested at the low rate.

Watch your step; Using a bond ladder is like most other investment strategies. You need to move cautiously and only after you have investigated all your options. Here are a few basic suggestions to follow in the process:

1. Find out when the bonds can be called, if at all. The rules may differ depending on the type of bonds you have acquired. **Key point:** Know all the details before you invest. As a rule of thumb, you may want to concentrate on bonds that cannot be called.

2. Only invest in high-quality bonds. Be careful about using certain corporate and municipal bonds to build your ladder. **Reason:** Changes in the credit status of the entity that issues the bonds could mean that you won't receive your interest or principal on time. Even worse, the issuer may default.

3. A bond ladder doesn't have to follow the ten-year example used above. For example, you might use a five-year ladder. The longer the ladder, the higher the yield and the greater the risk.

4. The ladder doesn't need to have a rung for every year. For instance, you could choose bonds that mature in two- or three-year increments. But adding more rungs increases the diversification.

Reminder: Seek professional guidance with respect to your investment decisions.



Questions?

Please contact us.
We would be glad to
serve you in any way
that we can.

Can you undo a Roth conversion?

With all the buzz about Roth IRA conversions in 2010, you may have taken the plunge. But now you want to “undo” the conversion. Is it possible? Yes. This technique is called the Roth IRA recharacterization.



The deadline for recharacterizing a Roth is your tax return due date plus extensions. So you effectively have until October 17, 2011, to recharacterize a 2010 conversion.

Background: When you convert a traditional IRA to a Roth IRA, you are taxed on the amount transferred. But qualified distributions (e.g., distributions after age 59 1/2) from a Roth in existence at least five years are completely tax-free.

Plus, unlike a traditional IRA, you don't have to take required distributions after age 70 1/2.

Prior to 2010, you could not convert a traditional IRA to a Roth in a year in which your modified adjusted gross income (MAGI) exceeded \$100,000. But this rule no longer applies. Also, for a conversion occurring in 2010, you can split the taxable income evenly over 2011 and 2012.

However, if you converted to a Roth in 2010, you may find that paying the tax bill dilutes much of the tax benefit of the conversion. Or maybe you didn't count on state income tax liability. Perhaps you did not consider the possibility of rising tax rates. Finally, if the value of the assets has declined since the conversion date, you could face a higher tax bill than you expected.

If it suits your needs, you can convert a recharacterized Roth back into a Roth before the later date of:

- the beginning of the tax year following the tax year of the conversion
- the end of the 30-day period beginning the day of the reconversion (regardless of whether the reconversion falls in the year of the conversion or the following year)

For example, if you converted a traditional IRA to a Roth on December 15, 2010, and recharacterized it on January 1, 2011, you cannot reconvert before January 14, 2011.

Finally, be aware that you don't have to recharacterize the entire amount. You can undo part of the conversion and keep the rest in the Roth.

Catch a Break for FSAs

Do you still have money in your flexible spending account (FSA) from 2010? You will be able to use the funds for qualified expenses - such as health care or dependent care expenses - if you act soon.

Generally, FSA amounts are forfeited if they are not exhausted by the end of the year. This is often called the “use-it-or-lose-it” rule. However, if your employer permits it, you can take advantage of a special 2 1/2-month grace period. Thus, you have until March 15, 2011, to spend 2010 allocations to an FSA.

Check with your employer to see whether you are eligible for this break.



Social Security: Fact or fiction?

As you work your way toward retirement, you may be relying on Social Security benefits to help sustain a comfortable lifestyle. But there are numerous misconceptions about the Social Security system. Here are the “facts” dispelling some common “fictions” about Social Security.

Fiction: The Social Security program has never been cut.

Fact: Not exactly. In 1977 Congress effectively made a cut when it adjusted the formula for paying Social Security benefits. Further modifications in the system occurred in 1980, 1984, 1989 and 1990. And in 1993, Congress increased the maximum amount of Social Security retirement benefits subject to income tax from 50% to 85% of the benefits received

Fiction: You have a legal right to collect Social Security benefits when you retire.

Fact: Unlike participants in funded private pension plans, Social Security participants have no property right in their benefits. If it chooses, Congress is free to amend the rules regarding payouts and eligibility to meet changing economic needs. In fact, some commentators believe that changes are inevitable.

Fiction: If you retire at age 65, you will get the full amount of Social Security retirement benefits that you are entitled to.

Fact: This is true only if you were born before 1938. Otherwise, you must work past age 65 in order to get full benefits. The “magic age” for individuals born between 1943 and 1954 - the majority of the “Baby Boomers” - is 66 years old. It is 67 years old for someone born in 1960 or later.

Fiction: The total amount of benefits you receive is based solely on your contributions to the system.

Fact: There is a connection between your contributions to the system and the benefits you ultimately receive. But two other important factors affecting the size of benefits are often overlooked: the age when you retire and apply for benefits, and how long you live.

Fiction: When you retire, you don't need as much money to live on as you did before.

Fact: Perhaps that was true at one time. But there's no historical precedent in this country for so many 65- to 75-year-olds having living parents. The National Center for Health Statistics (NCHS) says that the number of people 75 and older has doubled from 3% to 6% since 1950. By 2060,



NCHS estimates that one out of eight Americans will be 75 or older. About 22.4 million households already provide care to a family member 50 or older, according to the American Association for Retired Persons (AARP). The “sandwich generation” of new retirees may face unusual economic burdens in the coming years.

This article points out the importance of generating income from investments, qualified retirement plans and other sources to help pick up the slack in retirement. It is unlikely you will be able to maintain your current lifestyle on Social Security benefits alone.

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