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Back to basics: how to diversify

How can you protect yourself against the inherent volatility of the equities markets in this uncertain economy? No matter what anybody says, even the so-called "experts," there is no 100% foolproof method. But proponents of diversification often rely heavily on this fundamental investment principle to help minimize risk.

In a nutshell, diversification is the process of including different kinds of investments - such as stocks, bonds and cash alternatives - in your portfolio. It also means that you should maintain a mix of investments in different sectors or industries. For example, you might view investments in international stocks as a way to offset domestic stock risks, realizing that such investments raise special risks. The basic concept is to try to reduce overall risk, as opposed to "placing all of your eggs in one basket."

Caveat: Even if you rely on fundamental investment principles such as diversification, you are not protected against the potential for an overall loss in your portfolio. There are no absolute guarantees, and you must recognize the inherent risks involved with your investments.



The concept of diversification is often combined with an asset allocation strategy that divides up your portfolio based on your needs and objectives, as well as your personal tolerance for risk. You can rely on experienced financial professionals to help you develop the general parameters.

As part of the diversification process, you should determine

- your investment goals
- the time horizon for reaching these goals.
- the amount you can currently afford to invest
- the amount you can afford to invest in the future
- the amount you need to generate to reach your goals
- the level of risk you are willing to assume in pursuit of your goals

Of course, everyone's situation is different. The exact methodology you might use to diversify your portfolio should be tailored to your particular circumstances. For example, a single 25-year-old embarking on a new career or a 30-year-old newlywed starting a family will likely opt for an investment mix different from a married 50-year-old professional with a couple

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Back to basics: how to diversify

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of children in college or a 60-year-old with retirement looming. Furthermore if you are already retired, protecting principal will take on added significance, as opposed to trying to grow your investments.

It is also important to monitor your investments to avoid having the asset allocation stray off course. If this occurs, you may want to adjust the current allocation or re-think the stated percentages. In addition, your situation may be affected

by life-changing events such as getting married, or divorced, having a child, switching jobs or careers, starting your own business or retiring. Although these events tend to occur at “busy” times of your life, don’t ignore their impact.

Reminder: You don’t have to go it alone. Rely on a trusted financial professional to provide guidance in developing a strategy.

Don’t hesitate to designate

It is important to take time to figure out the beneficiaries of retirement plans, life insurance policies and other assets. Here are seven suggestions to consider.

1. Do not leave the beneficiary lines blank. If you don’t name specific beneficiaries of your accounts, or if you name your estate as the beneficiary, your heirs will likely end up in probate court. This can be both time consuming and costly. If assets go to your estate, they are subject to the reach of creditors. A better option is to choose individual beneficiaries and list them on the forms.

2. Use trusts for beneficiaries who are minors. In some states, minors face restrictions until they turn age 18 or 21. If you designate a minor as a beneficiary, a court will appoint a guardian to manage the funds until the child reaches the age of majority. Alternatively, you might establish a trust to handle the funds and name the trust as the beneficiary. Thus you maintain control now and provide asset protection for minors when you are gone.

3. Understand the key rules. Other than your spouse, beneficiary designations on retirement accounts and insurance contracts will override your will. If you want someone besides your spouse to inherit assets, your spouse must sign a written waiver. Without the waiver, a non-spouse beneficiary designation will be invalid upon your death.

4. Inform your beneficiaries. Do not keep your designations a secret. Let your beneficiaries know where to find important documents and contact information for your professional advisors. On the other end, make sure your advisors have the vital contact information for those sources.

5. Double-check names and numbers. Make sure names are spelled correctly and that figures are accurate. This is particularly important when listing Social Security numbers, telephone numbers and addresses.



6. Use percentages instead of dollar amounts. For example, suppose you have an IRA worth \$100,000, and you designate a niece as beneficiary of \$75,000 of that amount. If the IRA drops in value to \$75,000 or below at your death, your niece gets the entire amount - any remaining beneficiaries receive zero. Perhaps a better way to meet your objectives is to give your niece 75% of the overall account value; that provides protection if the value increases or decreases.

7. Name contingent beneficiaries. If your primary beneficiary has died and you have not named a replacement, the assets will go to your contingent or (“secondary”) beneficiaries. Without a contingent beneficiary, the assets are transferred to your estate (*see point #1*). Avoid potential problems by indicating contingent beneficiaries as appropriate.

Finally, don’t stuff all the paperwork in a desk or drawer somewhere and forget about it. Review your beneficiary designations periodically to ensure that they remain up-to-date. When warranted, have documents revised to reflect your latest intentions.

Estate planning: peeking through the clouds



It seems like estate planning has been “under a cloud”. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 - the

short - brought some clarity to the situation. But the estate-tax provisions in the new law are scheduled to expire after 2012.

Nevertheless, you can incorporate the latest changes into your estate plan while trying to remain flexible.

To help you plan, here’s a brief overview of the current landscape in estate planning.

Taking shelter: Under the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), the estate-tax exemption for an individual gradually increased from \$1 million to \$3.5 million for decedents dying in 2009. At the same time, the top estate-tax rate decreased from 55% to 45%. EGTRRA also “decoupled” the estate- and gift-tax systems and retained a lifetime gift-tax exemption of \$1 million.

Then EGTRRA repealed the estate tax, but only for decedents dying in 2010. The estate tax was scheduled to be reinstated in 2011, with a \$1 million estate-tax exemption and a top 55% estate-tax rate. Also, for decedents dying in 2010, EGTRRA imposed “carryover basis” rules for heirs inheriting assets instead of allowing a step-up in basis in value on the date of death.

Caveat: A spousal beneficiary could benefit from up to \$4.3 million in exemptions (\$1.3 million for non-spousal beneficiaries and \$3 million from a spouse).

Change in the weather: For 2011 and 2012 only, the 2010 Tax Relief Act overrides the EGTRRA estate-tax provisions and creates an estate-tax exemption of \$5 million with a top estate-tax rate of 35%. The government recently announced the inflation-indexed exemption for 2012 is \$5.12 million.

The new law also reinstates the “step-up in basis” rules that existed prior to 2010. Furthermore, it reunifies the estate- and gift-tax systems with a \$5 million lifetime gift-tax exemption (\$5.12 million for 2012).

The new law allows for “portability” of the estate-tax exemption for married couples. If a deceased spouse’s estate doesn’t exhaust the entire exemption, the balance is available to the estate of the surviving spouse. Thus, heirs may more easily benefit from the maximum \$10 million in exemptions, but only if both spouses die before 2013.

In the wake of the new law changes, lifetime gift-giving to reduce the size of a taxable estate remains a viable option for affluent individuals. For 2012, you can give each family member up to \$13,000 without any gift-tax consequences - \$26,000 for joint gifts by a married couple.

For instance, a couple could give five relatives a total of \$130,000 (five \$26,000 gifts tax-free this year). This annual gift-tax exclusion is separate and apart from the lifetime gift-tax exemption.

Finally, other changes, including coordinated changes in the generation-skipping tax for transfers by grandparents, may affect estate planning. It is recommended that you review any wills and other estate-planning documents with the assistance of your professional advisors.

It is expected that estate planning will be a key consideration in the national elections this year. Significant new developments will be reported as soon as possible.

Tap three sources for retirement income

Where is the income you need to sustain you through retirement going to come from? If you are like most people, there are three primary sources.

1. Social Security benefits. Generally, the size of your retirement benefit is based on your earnings throughout your working years and the age when you retire. For instance, if you were born in 1950 and retire in 2012 at the age of 62, you will receive only 75% of the full amount of retirement benefits available to you at age 66. (For those

born after 1937, the age for full benefits gradually increases from age 65 to age 67.)

You can obtain more details about your personal status from the Social Security Administration (SSA). The SSA will tell you what you will receive in Social Security benefits when you retire. Similarly, if you are married you can obtain an estimate of your spouse’s benefits.

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Tap three sources of retirement income

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Note: If you work during retirement, you may lose some of your Social Security benefits if you are younger than normal retirement age, based on the “earnings test.” For those attaining normal retirement age after 2012, the annual threshold in 2012 is \$14,640. You forfeit \$1 for every \$2 over this limit. For those attaining normal retirement age in 2012, the annual threshold is \$38,880. You forfeit \$1 for every \$3 over this limit.

2. Qualified retirement plans.

One of the best ways to save for retirement is through a qualified retirement plan. Usually, the contributions’ accumulated earnings are tax-deferred until the money is withdrawn. In addition, you can take advantage of favorable tax provisions for some distributions. These plans come in many different shapes and sizes. The list includes popular 401(k) plans, pension and profit-sharing plans, and plans targeted to small businesses such as SIMPLEs (Savings Incentive Match Plans for Employees) and SEPs (Simplified Employee Pensions).

Be aware that the exact rules and contribution limits vary from plan to plan. Obtain expert advice with respect to your situation.



3. Individual savings and investments. Assuming Social Security and retirement benefits aren’t enough - and there’s a good chance they won’t be - the balance of your retirement income may have to be supplied by savings and investments. **For example:** You may be able to feather a retirement nest egg by investing in stocks and bonds, mutual funds, money market funds, annuities, real estate or other investment vehicles.

Don’t overlook amounts you have stashed away in bank accounts and U.S. Savings Bonds. In addition, you may continue to receive income from existing business interests.

You also may be able to tap into the cash value of a life insurance policy (with certain limitations).

Finally, if you sell your principal residence when you retire, you may benefit from a special tax exclusion. If certain requirements are met, the first \$250,000 of profit may be excluded from federal income tax (\$500,000 for a married couple).

Best advice: Don’t put off saving for the future. The longer you wait, the harder it will be to secure a comfortable retirement.

Seeking Comfort in Retirement



How comfortable are you about your level of retirement savings? If you are like most Baby Boomers - including the 77 million-plus Americans born between 1946 and 1964 - the answer is, “not very”

According to a new survey conducted by Associated Press-LifeGoesStrong.com, only 11% of respondents said they are firmly convinced they will be able to live in comfort. In contrast, 55% indicated that they were either somewhat or very certain they could retire with financial security. Worst of all, 44% expressed little or no faith that they will have enough money to live on comfortably when their careers end.

Demonstrating the problem still further, one in four Baby Boomers who are still working said they do not expect to ever retire.

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