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The ADVISORY

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Commentary:

That was then...

Before writing this issue of *The Advisory* I re-read the last few issues. My purpose was to ensure that the content is fresh and continues to describe the actions we have taken during the recent quarters. This is to ensure that you, the investor, have a full understanding of the process and thinking that are applied to your portfolio.

I'm fully aware that during the past four years the content and tone of this publication has changed to a more descriptive tone rather than the more philosophical bent of Rusty's prose. Part of this change is normal given the differences in personality and experience but it is primarily due to the volatility of the economic and market conditions we have experienced since mid-2007.

Overall, these last three years have been the most difficult in memory to execute almost any investment strategy whether it is *buy and hold, market timing, opportunistic trading* or even *hedging*. The markets have become interdependent, the politics around the world move the markets like never before, and the combination of markets and politics is extremely volatile.

An example of these dynamics happened in January when the Republican candidate in the Massachusetts Senate race won Ted Kennedy's seat. The market rose only to fall by 6% within the next few days as President Obama announced a new Bank Tax.

Even if one agrees that the banks should pay for the costs of the bailouts, the timing was curious.

By January the sovereign debt situation in Europe had already begun to rile markets around the world as the fear of contagion spread. It continues to move markets even after the massive bailouts offered by the EU & ECB.

The passage of the Healthcare bill here in the U.S. had some market participants breathing a sigh of relief while others moaned.

The same reactions are true for the Financial Reform bill passed by the Senate. It could have been much worse;still it's not welcomed by those it affects the most. By most accounts it does not accomplish the reforms it set out to make and, as a result, will have major unintended consequences. One such consequence surfaced within days of the bill's signing: the Bond rating agencies refused to allow Bond issuers to use their ratings in required documents. The Asset-backed Bond market froze (at least for now).

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Commentary (continued from page 1)

The chart below appeared in our previous issue.
In the interest of continuity, updated comments are inserted. Major factors influencing our investment decisions in 2010:

Money supply - will the Government continue to spend recklessly? ***The short answer is yes. The U.S. annual deficits continue at the 1.3 trillion dollar level with no concrete action taken to reduce that level.***

Inflation - when will it become apparent forcing the Fed to raise interest rates? ***Not yet, and still no signs. Deflation is the current worry.***

National Debt - who will buy all the bonds issued by the U.S. and other developed nations? ***The crisis in Europe has made the U.S. a relatively safe haven again in the Second Quarter but worries continue about the level of US debt issuance.***

Liquidity - the Fed has discussed "how" not "when" it will reduce liquidity. ***Again, no action.***

Economic Recovery - will it be V- or U-shaped depending on interest rate increases? ***Neither to date; very slow growth except some in manufacturing.***

Unemployment - when will it level off and decline? ***Not any time soon. Employers large and small are still not willing to hire. Total jobless rates, including those who have fallen off the rolls, are close to 19%.***

Credit crisis - will banks continue to fail? ***Yes, the rate of failure has slowed but it is still high by normal standards.***

Credit crunch - lack of access to funds continues to put pressure on commercial real estate and REITs as well as consumers. ***Banks still hold record levels of cash. The consumer is actually paying down credit lines and reducing credit exposure.***

Bankruptcies - both personal and small business continue to rise, again caused by the credit crunch, unemployment, etc. ***Same story.***

Health care costs - continue to rise. ***Not as much front page coverage but there are many reports of a steady rise even after passage of the Health Care bill. Polls show most Americans oppose the bill.***

Tax increases - abound on both state and federal levels. ***No Congressional action on extension of the 2001-2003 cuts but there has been some talk of extending the current rates to those earning under $200,000 and limiting the increases on Capital gains and dividends.***

Capital and trade - remain sketchy throughout 2010. ***Very recently nice words were spoken by the Administration about signing the Colombian, South Korean, and Brazilian Trade Pacts, but no action yet.***

Commentary (continued)

Positive Factors

-Interest Rates still low and will probably stay at these levels for some time.

-Inflation below 1%, not showing signs of increasing at present.

-Manufacturing up, employment in this sector is improving slowly.

-BRIC Countries (Brazil, Russia, India and China) continue to grow at sustainable rates. China has taken action to tamp down a real estate bubble.

-Emerging Market countries not suffering from debt overload continue to grow.

-The European Union has not collapsed over the fiscal crises in Greece, Spain, Portugal, Ireland and Italy.

-Congressional Gridlock may be at hand as the Republicans seem poised to take back at least the House. (Markets like gridlock.)

Negative Factors

-Developed countries' economies are growing very slowly.

-Double-dip Recession is still feared and expiration of tax cuts in 2011 could stifle any recovery.

-The U.S. economy remains extremely over-indebted. In the First Quarter total debt to GDP ratio was 357%, 100 points higher than in 1998.

-Capacity underutilization, enormous supply of vacant homes, labor demand weak, wages stagnant.

-Continued stress over the ability of Europe and its banks to work their way through the Sovereign Debt Crisis without more serious damage.

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Roth IRA:Convert...or not convert?

2010 is a big year for Roth IRAs. This year the IRS has lifted the income limits and anyone, at any income level, may convert his/her traditional IRA to a Roth IRA.We all know that a Roth IRA has no required minimum withdrawals determined by age and all withdrawals are tax-free but even those benefits might not be attractive enough to override the downside:

1. *Not enough time to make a difference* – **If you are retired or close to retirement and plan to start taking withdrawals soon, there will be no benefit since the new Roth has not had time to profit from tax-free growth. (Age 58 and under have the most to gain.)**

2. *Tax consequences* – **Any money moved out of a traditional IRA is subject to both state and federal income tax. The catch is that tax money must come from another source and not be taken from the IRA. For example, if your IRA holds $10,000 then you potentially must have $3500 in another account to pay the taxes after you convert/ transfer the $10,000 to a Roth IRA. (You do have the option of a partial conversion spreading the tax bill over several years.)**

3. *Higher tax bracket* – **Depending on the size of the conversion, you could bump yourself into a higher tax bracket. The traditional IRA is actually liquidated, declared as taxable income and then converted. That amount is added to your income tax return as taxable income for the year. It could push you into the next level of taxes potentially increasing your tax bill, reducing eligibility for financial aid or causing you to pay taxes on Social Security.**

4. *Future tax brackets* - **With all the talk of higher income taxes in the next few years, many people may want to beat the increase by converting their traditional IRA now. But more than likely, retirement income will put them into a much lower bracket once they stop receiving regular paychecks.**

5. *Limited income sources* – **If you have no pension and will depend primarily upon your tax-deferred sources for retirement income, you will not give the converted money enough time to benefit from years of tax-free growth after paying the resulting taxes. Here is where a partial conversion makes sense using only that amount of money you have designated for future years' income, say 15-20 years out.**

If you are considering converting your traditional IRA to a Roth IRA, ask us for an evaluation beforehand. It may save you time and money.

Estate Planning: Part III
Irrevocable Trust

Continuing our review of estate planning tools, we will now describe and assess the Irrevocable Trust. Remember that a trust is a form of ownership of your assets. The trust is managed and controlled by your trustees under your designated terms within the proper IRS/legal framework.

By transferring your assets to the irrevocable trust you no longer own them; thereby protecting them from lawsuits and creditors and removing them from your taxable estate. *But* once formed and funded (assets transferred), the "irrevocable" trust *cannot* be dissolved nor can the terms be altered nor beneficiaries changed. As an estate planning tool some use this trust to comply with the "nursing home spend-down" provisions for Medicare.

There are serious obligations placed on the Trustee as the fiduciary of your trust that includes duties and liabilities to prevent the abuse or avoid fraud. In addition to acting in a prudent manner, the trustee must act only in the best interests of the beneficiaries of the trust.

All income, dividends, and interest are credited to the trust and the trust files its own tax return.

Benefits

There are several benefits of executing an Irrevocable Trust...

1. Avoids probate by eliminating the onerous process of proving the will, and deterring the heirs.
2. Protects assets from creditors and lawsuits.
3. Eliminates estate taxes since the owner owns no assets.
4. Provides a channel for charitable gifts.
5. Aids in qualifying for a Medicare nursing home.
6. Provides peace of mind knowing your financial house is in order should you become incapacitated or pass on.

Drawbacks

...And there are some drawbacks:

1. Loss of ownership and control of assets. You relinquish ownership!
2. Generates its own tax basis, which can be higher and cost more to administer.
3. An Irrevocable Trust is taxed at 35%.
4. Files its own tax return.
5. Is costly to set up and administer.

Finding Unclaimed Funds

There are 117 million accounts of unclaimed property. These are inactive accounts in which a company has not been able to reach the person(s) due the funds. These unclaimed funds range from bank accounts, stocks, and uncashed dividends to payroll checks, trust distributions, and refunds.

To search for unclaimed funds go to the National Association of Unclaimed Property Administrators (NAUPA) website at www.unclaimed.org. When you click on states you've lived in, you will be brought to each state's uncaimed fund division. If you get results, claim your property as per the state's instructions.

Any unclaimed retirement benefits? First, contact all old employers. Then try the National Registry of Unclaimed Retirement Benefits (NRURB) at www.unclaimedretirementbenefits.com.

Please let us know of any success!

How to Contribute to your Grandchild's College Savings

With costs soaring and an inflation rate of double the normal inflation rate, many parents are finding it harder and harder to fund college education costs. Parents scrimp, save, and hope that the completed financial aid forms and co-signed student loan applications will be approved. With the understanding of their financial situation, some students are forced to compromise where they attend. As a grandparent, what can you do to lessen the financial burden on your children and grandchildren and help your grandchild attend college? Here are some ideas:

- **Talk to your children about the importance of having college savings for *their* children. Ask if an account has already been established and inquire as to the regularity of contributions. If an account has not been opened, ask them to talk to a financial advisor here at Income & Asset Advisory or to call their state's 529 plans.**
- **Open a 529 plan for your grandchild yourself. 529 Plans are flexible secondary education savings vehicles. You can be the owner of the account and have your grandchild be the beneficiary. You can own multiple 529 accounts. They can be opened through any state. Some state's offer a tax benefit for contributions. If you have multiple accounts for multiple grandchildren and one child does not need the savings, it can be used for another grandchild.**
- **Set up automatic monthly contributions to the account. (minimum contributions are between $25 and $50).**
- **Make an accelerated gift contribution of up to $65,000 if single and $130,000 if married in one tax year. Talk to your accountant or Income & Asset Advisory for details; there can be estate tax benefits.**
- **For birthdays, holidays and special occasions give a small gift (like a book) to your grandchild and make a contribution to their college savings account. Encourage other family members and friends to do the same. When the child gets older talk to them about why you contribute to a college account for them, how important it is to save and how proud you will be when they attend college.**
- **Join *UPromise* (upromise.com) and *Baby Mint* (babymint.com). These organizations have agreements with thousands of retailers to contribute part of your purchase (1-25%) towards a college savings account. There are many ways to accrue savings: online shopping, dining out and at the grocery store. You can register your grocery, debit and credit cards that link to your account; thus receiving contributions from participating companies.**

If you are interested, please give us a call to discuss college savings options. Also, consider having your children give us a call - we would be happy to help them create a college savings strategy.

Market Activity

	Prices			Percent Changes	
Market Indicator	**6/30/2009**	**3/31/2010**	**6/30/2010**	**Last Year**	**Last Qtr**
1 Ounce of Gold ***(London PM Fixing)***	942.00	1096.50	1254.00	16.4%	14.4%
Technology Oriented Stocks ***(NASDAQ Index)***	1838.22	2395.13	2223.48	30.3%	-7.2%
Small Company Stocks ***(Russell 2000 Index)***	513.22	678.97	645.11	32.3%	-5.0%
International, Global Stocks ***(EAFE Index)***	1305.82	1572.26	1382.04	20.4%	-12.1%
Large Company Stocks ***(S&P 500 Index)***	918.90	1166.59	1253.31	27.0%	7.4%
Higher Yielding Stocks ***(DJ Utilities Index)***	355.79	376.36	366.21	5.8%	-2.7%
High Yield Bonds ***(M.L. High Yield Index)***	803.05	1023.78	1026.90	27.5%	0.3%
Tax Free Municipal Bonds ***(Bond Buyer Index)***	105 10/32	113 30/32	115 1/32	8.2%	1.0%
Long Term US Gov't Bonds ***(Lehman Index)***	1815.44	1737.92	1892.58	-4.3%	8.9%
Inflation ***(Consumer Price Index)***	215.70	216.00	216.00	0.1%	0.0%

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