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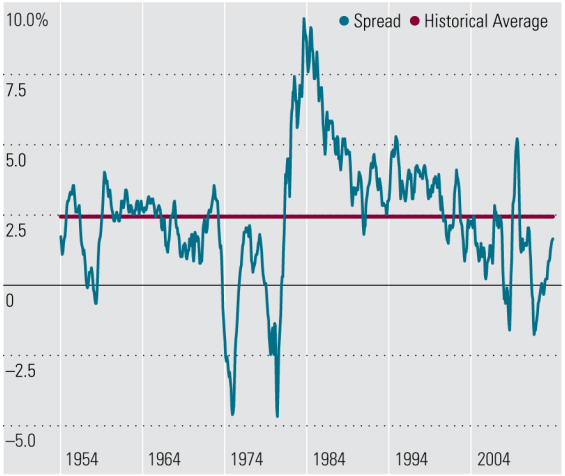
Fed Policy, Inflation, and Interest-Rate Risk

With interest rates still relatively low, the question today is by how much they are likely to rise. Historically, the 10-year Treasury bond has yielded, on average, about 2.5% over the inflation rate. With inflation at 1.5%, the 10-year Treasury bond typically would yield about 4.0%. In an attempt to support economic and job growth, the Federal Reserve has been purchasing long-term Treasury and mortgage-backed bonds to artificially keep interest rates low. As long as the Fed kept this asset purchase program up, 10-year Treasury yields remained relatively low. However, the Fed has begun tapering, and interest rates are likely to rise significantly in the near future. Both investors and advisors should be aware of the implications of rising interest rates.

Spread of 10-Year Treasury Over Inflation



Treasury bonds are guaranteed by the full faith and credit of the U.S. government as to the timely payment of principal and interest.

Source: 10-year Treasury yield data from the Federal Reserve. Inflation is represented by the Consumer Price Index, three-month rolling average, and data from the Federal Reserve. The time period displayed in the chart is January 1954 to December 2013.

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Advisor Corner

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2014 Market Performance
01-01-2013 to 2-28-14
DJIA ^DJI Down (-1.54)
S&P 500 ^GSPC Up 0.60%
NASDAQ ^IXIC Up 3.15%
Russell 2000 ^RUT Up 1.67%

What will 2014 bring? ... First down Jan since 2009

* Index performance does NOT include any fees (Gross of fees)
Source: http//finance.yahoo.com

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Five Estate-Planning Tasks That You Shouldn't Put Off

Keeping tabs on the estate-planning rules during the past few years has been a little like watching Olympic-level table tennis: The action moves quickly, and it's difficult to keep up. However, no matter how laws and rules change, there are a few basic tasks that are actually pretty evergreen and that everyone should execute. Five such estate-planning to-dos are outlined below.

1) Update Beneficiary Designations. Even people who have never set foot in an attorney's office may have laid the groundwork for an estate plan if they filled out beneficiary designation forms for their financial accounts. Those designations, in fact, trump other estate-planning documents when it comes to distributing assets, so it's worthwhile to periodically review them to make sure they're up-to-date with your current situation—if you've gotten married or divorced, for example. (How would your spouse feel if you inadvertently left your 401(k) account to your brother?) People who have drafted estate-planning documents such as wills should ask their attorneys to help them review beneficiary designations to ensure that they sync up with other estate-planning documents.

2) Designate Legal Guardians. Parents of young children should designate legal guardians who will look after their children if the parents should die or otherwise be unable to care for their minor children. It is important to focus the discussion on actual child-rearing abilities and willingness to do the job. What is not helpful is to get hung up on hurting anyone's feelings or bypassing friends or family members who might expect to be guardians but aren't the best choice. Most importantly, a guardian should be willing and able (emotionally and financially) to take care of your children if the need arises, so an essential step is to discuss the responsibilities with the potential guardian beforehand.

3) Create a Living Will and Last Will and Testament. A living will tells your health-care providers and your loved ones how you would like to be cared for if you should become terminally ill and unable to express your wishes yourself. It is called a "medical directive" in some states. This document details your views toward life-support equipment. Not to be confused with a living will, a last will and testament details how you'd like your assets and possessions distributed after your death.

4) Draft Powers of Attorney. A basic estate plan should also address what would happen to your affairs if you are still living but incapacitated. A power of attorney is a document that specifies who will handle your affairs if you are unable to do so. You'll need to draft two separate documents: one that names your power of attorney for health-care decisions and another for financial matters (often called a durable power of attorney). The person you entrust with your power of attorney for health care will, ideally, live in close geographic proximity to you. The person you name on your durable power of attorney form should be detail-oriented and comfortable with financial matters.

5) Name an Executor. Your executor will gather all of your assets after you're gone and make sure they are distributed in accordance with your will. Ideally, your executor will be someone who's comfortable with numbers and good with details, and will also be able to find the time to work on your estate. It's common to name family members as executors, but in more complicated situations it might be preferable to use a professional, such as a bank trust officer, to serve as your executor. It's a good idea to tell your executor that you've named him or her, and also provide details on how to obtain access to important documents, such as your will and a master directory detailing all of your accounts.

This information is for informational purposes only and should not be considered as legal or financial planning advice. Please consult a legal and/or financial professional for advice specific to your individual circumstances.

Tips for Preparing Your Taxes

It's that time of year again. While many people cannot say they enjoy preparing their income-tax returns, you'll like it even less if you make mistakes and pay more tax, penalties, and interest than you need to. Here are some things to watch out for as you prepare this year's return or ready your tax documents for your accountant.

Qualified Dividends versus Nonqualified Dividends: Nothing can be more frustrating than receiving a corrected 1099 from your brokerage company. The 1099 is used to report various types of income other than wages, salaries, and tips. If you receive one after you had already filed your taxes, you might have to amend your return.

The problem is that mutual fund companies are required to submit tax information by the end of January, and in some cases they might not have the correct breakdown of qualified and nonqualified dividends by then. Because the tax treatment of qualified dividends might result in you paying less income tax, a revised 1099 might be to your advantage (although in many cases, only by a small amount). So it might pay to wait a bit before filing your tax return if you expect to receive a 1099.

Capital Gains and Losses: When you sell an investment for less than you paid for it, you realize a capital loss. The bright side is that capital losses can help you save on taxes. You can use capital losses to offset capital gains in your portfolio. You'll need to know if your gains and losses are short term or long term. If you held an investment a year or less, it will be a short-term gain or loss. If you held an investment longer than a year, it will be a long-term gain or loss.

In 2014, short-term capital gains are taxed at ordinary income-tax rates from 10% to 39.6%. Long-term capital gains, meanwhile, are taxed at lower, preferential tax rates from 0% to 20%.

Municipal Bond Income: If you own municipal bonds, interest income you receive is exempt from federal income tax. That income may or may not be exempt from state income tax. If the bonds are issued in your state of residence, you usually won't have to pay state and local taxes on the interest. You can find out for sure by contacting your state or the brokerage company at which you hold your securities.

Does that mean all money you receive from municipal bonds isn't subject to taxes? Not necessarily. If you own a municipal-bond fund that paid out capital gains, that money is taxable on your federal and most state returns. In addition, if you own municipals that are classified as "private-activity" bonds, you may be subject to the Alternative Minimum Tax. You may want to consult an accountant about this type of bond. To see if you have both interest income as well as capital gains distributions, check the 1099 forms you received.

Exclude Interest from U.S. Government Securities: Don't forget to exclude the interest from government securities on your state income tax return. You can exclude all income from "direct" government securities (for example, Treasuries). Some states also allow you to exclude income from "indirect" securities (for example, agency bonds like GNMA and FNMA securities). To know for sure, contact your state or the brokerage firm at which you hold your bonds.

Some mutual fund companies can be very good about sending information on the percentage of your funds that are invested in government securities. But there have also been situations where the fund company will only provide this information if you ask.

If you didn't obtain this type of breakdown when you received your 1099 statements, visit your fund company's website to find the information, or call the fund's customer-service line.

Simple Steps for Late Savers

The sooner you start putting aside money for retirement, the more you might have once that highly anticipated day arrives. Saving for college tuition, purchasing a new home, unforeseen medical expenses, or life's other necessities, surprises, or even enjoyments can cause investors to postpone saving. Starting the retirement planning process late in one's life can be daunting, but it is by no means impossible.

Crunch the Numbers: The first step to getting back on track is to put together a budget—this will force you to focus on your financial situation and can serve as a road map to success. Once you have outlined all of your expenses, simply subtract the total from your net income. The result will give you a clear indication of how much you can potentially save, and also help you identify areas in which you may be spending too much.

Cut Any Unnecessary Expenses: There are essential expenses that cannot be eliminated: food, electricity, etc. However, most people can identify some areas, like entertainment, that are not vital to one's existence and can be cut back on. The more areas that you can trim will lead to more money that can be earmarked for retirement.

Take Advantage of Catch-up Contributions: Catch-up contribution limits allow investors age 50 and above to increase their contribution. For example, they can make an extra contribution of $5,500 to their 401(k) in 2014, equating to a maximum contribution of $23,000. IRA catch-ups are $1,000 in 2014, leading to a maximum contribution of $6,500.

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