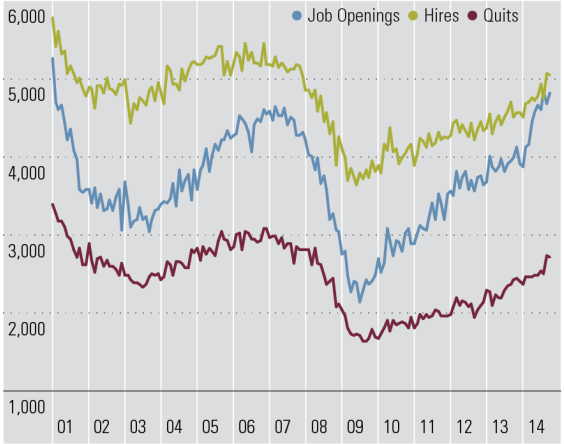
January 2015 | Vol. No. 1 | Investment Updates

One of Yellen's Favorite Metrics 'Jolts' Ahead

The formerly unimportant job openings report has taken on a new significance since U.S. Federal Reserve Board Chair Janet Yellen has included this metric in a list of labor market reports that she is watching closely. And this relatively new report is now sending a message that we really haven't seen before. Job growth isn't much better than it has been in the past three or four years, while the number of openings per person employed is now at its best level since 2001 and way above year-ago levels.

The chart below illustrates how the growth in job openings is outpacing the growth in hires. This means that there are increasingly less workers matched with the jobs that are being posted, and it may soon force employers to increase wages in order to fulfill those unmatched job openings.

Job Openings, Quits, and Hires, Seasonally Adjusted, Thousands of Workers



This article contains certain forward-looking statements which involve known and unknown risks, uncertainties, and other factors that may cause the actual results to differ materially from any future results expressed or implied by those projected statements. Past performance does not guarantee future results.

Source: Bureau of Labor Statistics. Data through November 2014.

Advisor Corner

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2014 Market Performance
01-01-2014 to 12-31-14
DJIA ^DJI Up 7.52%
S&P 500 ^GSPC Up 11.39%
NASDAQ ^IXIC Up 13.40%
Russell 2000 ^RUT Up 3.65%

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

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Could Rising Interest Rates Hurt Your 529? (Part 1)

Bond investors have been worried about a rise in interest rates for years now, pretty much ever since the Fed lowered rates in response to the 2008–09 financial crisis. Any rise in rates hurts the value of existing bonds (on the contrary, a drop in rates helps it), and rates have been hovering near historic lows for quite a while.

For families saving for college, bonds have long been seen as a safe-haven investment—a place to park cash reserved for a specific purpose within a specific time frame and a pretty good bet to increase in value faster than cash while avoiding the volatility of stocks. But what happens when bonds themselves become riskier than they've been in the past? It's a question that many college savers, especially those who will need the money in just a few short years, are asking.

529 Plans and Duration

The majority of the $200 billion invested in 529 college-savings plans is held in so-called age-based portfolios—all-in-one investments made up of stocks, bonds, and other securities allocated based on the age of the beneficiary and, in some cases, the risk tolerance of the account holder. Typically these age-based portfolios are heavily weighted toward stocks when the beneficiary is very young, and they gradually shift assets into bonds and cash as the beneficiary gets closer to college age.

With traditional bond funds, the most commonly used method of gauging interest-rate sensitivity is a statistic called average effective duration. The higher the duration, the more sensitive the fund is to interest-rate movements. It works like this: For each percentage point that rates increase, the fund may be expected to lose in value a percentage equal to its duration in years, minus the fund's yield. For example, if rates increase 1 point, a fund with a duration of 4.5 years and a yield of 2% could be expected to lose 2.5% of its value.

Finding the Numbers for a Specific 529 Plan

Although this rule of thumb may be a convenient way of assessing the interest-rate sensitivity of a single bond fund, most 529 accounts hold multiple stock and bond funds, making it difficult to arrive at a single duration measure for the entire portfolio.

Even though your 529 plan may not provide information on the duration of your portfolio, you might be able to track it down yourself by taking a closer look at the bond funds in the plan.

Unless you have all of your 529 assets in a single bond fund, you might have to do some calculations to figure out how to weight the various duration measures. For example, if your 529 portfolio is made up of 60% equities and 40% bonds, but the bond portion is half intermediate-term bonds with a duration of 5 years and half short-term bonds with a duration of 1 year, then the bond portion of your portfolio has an average duration of 3 years.

On average, an age-based portfolio for a 15-year-old beneficiary holds about 55% of assets in bonds, according to Morningstar data, and by the time most beneficiaries are ready to enroll in college at age 18, that weighting reaches 60%. At the same time, the average allocation to cash increases even more, from about 15% at age 15 to about 30% at age 18.

Options for 529 Plan Holders

Once you have some idea of how vulnerable your 529 assets are to a rise in rates, you then can decide what, if anything, to do next. If stocks dominate your account, leaving just a small allocation to bonds, you may have little to worry about in terms of interest-rate risk. But if bonds make up the bulk of your account and you find the average duration of the portfolio makes you nervous in case rates do rise sharply, you may be contemplating some major changes.

Could Rising Interest Rates Hurt Your 529? (Part 2)

But before you do anything, consider the following for some perspective. Let's go back in time to May 2013, when interest-rate concerns also were running high because of fears that the Fed would soon begin tapering its bond-buying stimulus program. Rates climbed throughout the summer, and for the year the Barclays Aggregate Bond Index, a proxy for the U.S. investment-grade bond market, lost 2% of its value. By comparison, funds in the Age 13–18 Low Equity category actually gained 1.62% (the category includes conservatively invested age-based portfolios designed for 529 beneficiaries between the ages of 13 and 18 and currently averages a 66% allocation to bonds and a 10% allocation to stocks, according to Morningstar data). Not great, but hardly the disaster some had feared amid a rising-rate environment.

Interest rates have actually been declining in 2014, meaning that you may have been better off holding intermediate- and long-term bonds than stocks. Of course, rates could very well go up in the coming year, and 529 account holders with heavy allocations to bonds could see losses. But the larger point is that interest rates don't move in a straight line, and predicting their near-term direction (and thus their effect on bond prices) can be just as difficult as predicting that of stocks.

However, if you still wish to reduce the interest-rate risk of your 529 holdings, there are steps you can take. One would be to move the bond portion of your portfolio to a short-term bond option, if your plan offers one (short-term bonds are more immune to interest-rate movements than longer-term bonds), or perhaps to cash. If you've been using an age-based portfolio, this might require you to move assets out of it and create your own customized allocation using the plan's pure-stock-fund and pure-cash-fund offerings. But that might be the only way you can completely remove bonds from the equation.

Keep Calm and Carry On

Although there's no imminent reason to worry about a rise in interest rates wreaking havoc on the bond portion of your 529 portfolio, investors with heavy allocations to bonds still would be well-served in taking a peek under the hood just to see what's there in terms of interest-rate sensitivity. If what you find makes you uncomfortable, consider the aforementioned actions of reconfiguring your portfolio. If not, at least now you know what to expect if and when rates do rise.

529 plans are tax-deferred college savings vehicles. Any unqualified distribution of earnings will be subject to ordinary income tax and subject to a 10% federal penalty tax. Tax law is ever-changing and can be quite complex. It is highly recommended that you consult with a financial or tax professional with any tax-related questions or concerns. An investor should consider the investment objectives, risks, and charges and expenses associated with municipal fund securities before investing. More information about municipal fund securities is available in the issuer's official statement, and the official statement should be read carefully before investing.

Indexes are unmanaged and not available for direct investment. Past performance does not guarantee future results. Investments in securities are subject to investment risk, including possible loss of principal. Prices of securities may fluctuate from time to time and may even become valueless.

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Fall/Winter 2014
Advertisement Newsletter Containing Important Estate Planning Information

Estate Plan focus

OUR MISSION: To guide our clients through various legal challenges with compassion, sensitivity, and professionalism.

Top 10 Estate Planning Mistakes

Even the best laid estate plan intentions can go awry. Signing wills, trusts and powers of attorney alone do not put your "affairs in order." Following are some of the more popular mistakes people make in their estate plans:

10. Treating all beneficiaries the same even when your beneficiaries have special needs or circumstances.
9. Transferring significant money to adult children during your lifetime without specifying whether you are making a gift, an advancement of inheritance, or a loan to be repaid even if the balance owed exceeds the debtor/beneficiary's share of the estate.
8. Not authorizing a co-signer on a safe deposit box so that it can be opened upon your death.
7. Neglecting to ensure that your named fiduciaries (executors, successor trustees, guardians and agents for all powers of attorney) are able and willing to act.
6. Storing an original will somewhere that is either inaccessible (see #8) or difficult to locate.
5. Failing to provide trustees, executors and beneficiaries the necessary tools (such as passwords) to find and ultimately take control of your assets.
4. Withholding important information from your attorney regarding family dynamics and finances.
3. Owning joint tenancy accounts inconsistent with your overall estate plan.
2. Making do-it-yourself changes to your estate plan documents without the help of competent legal counsel.
1. If you have a trust, not funding it.

If you, or anyone you know, could benefit from learning more about these issues, please feel free to contact our office.

To help us keep your contact information updated, please e-mail us your current address and phone numbers to Clerk@ericmatlin.com or call us at 847-770-6600.

ARE TAX PROVISIONS IN YOUR TRUSTS CURRENT?

Due to changes in federal estate tax laws enacted by the American axpayer Relief Act ("ATRA"), of which went into effect in 2013, many earlier trusts for married couples that include shelter provisions for each other should be examined to ensure that tax goals are met. In 2015, the threshold for federal estate taxes is $5.43 million and $4 million for Illinois.

You may be affected by this aspect of the ATRA in Illinois if you and your spouse have trusts that, upon the first death, leave assets to the survivor with restrictions. Shelter trust provisions that were appropriate at the time the trusts were signed may no longer be necessary and can be counter-productive, resulting in increased capital gain taxes and forcing the surviving spouse to do significant bookkeeping.

If your combined net worth is currently less than $8,000,000 and is unlikely to grow beyond than that, you may be in this category. Absent non-estate tax reasons (such as a blended family, where the ultimate beneficiaries of the spouses may be different), the rational for the shelter provisions of your trusts may be out of step with current needs.

On a different note, due to the discrepancy in the thresholds of federal estate tax and Illinois estate tax, if you are Illinois residents and the estate of the first spouse-to-die might exceed $4,000,000, we may advise a change to your shelter trusts to defer or avoid an Illinois estate tax upon the first death.

We offer a no-cost consultation to determine whether or not a change to your trusts is advisable.

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Ryan S. Smith

Our newest associate attorney is Ryan Smith, a 2011 University of Pittsburgh School of Law graduate. Ryan spent the first three years of his career with a law firm in Pittsburgh, Pennsylvania. Having relocated to the Chicagoland area, he focuses his practice on estate planning estate administration and litigation, probate, and family law. We welcome Ryan to the Matlin team!

Illinois Law Bit

755 ILCS 5/6-1 expounds upon the duties of anyone in possession of a dead person's last will. Among the highlights:

- Duty to file with the clerk of the circuit court within 30 days of decedent's death.
- Prohibition on willfully altering, secreting or destroying a will except at the testator's direction. Willfully altering, secreting or destroying a will is a class 3 felony (potential 2-5 year prison term).

The criminal element of this statute is intended to apply to people who act intentionally, rather than the unknowing person who stumbles upon a will or was in possession of it, but never realized that he or she should have filed it a long time ago. If you discover that you are in possession of a deceased person's last will who died months or even decades ago, please give us a call.

Clients, Can You Answer These Important Questions?

- Are your assets properly structured so as to avoid probate and/or accomplish your planning goals?
- Do you know where your original documents are? Except in rare circumstances, Matlin & Associates, P.C. does not retain original documents.
- Do key people have access to your original documents in case they are needed?
- Do you keep your electronic passwords in a location that can be accessed by your financial fiduciaries when needed?
- Have you updated your documents in recent years?

Happy Thanksgiving!

Everyone here at Matlin & Associates wishes you and your loved ones good health and much happiness this Thanksgiving.

Eric, Julie, Johannah, Mary, Ryan, Kathryn, Lee, Ashley, Sara, and Melissa

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Avoid These Mistakes With Your IRA, Part 1

Funding an IRA may seem like a simple financial task: Pick your provider, send in your money, and choose your investments. Done.

But a look at Internal Revenue Service Publication 590, which details the ins and outs of IRAs, suggests there's more to it. There are two key IRA types (Traditional or Roth), as well as two subtypes of Traditional IRAs (deductible and nondeductible), not to mention byzantine rules regarding rollovers, conversions, and recharacterizations. And what about when you begin taking IRA withdrawals in retirement? More kooky rules there, too.

There are a few obvious IRA mistakes, such as pulling money out of a Traditional IRA before age 59 1/2, but here are some IRA pitfalls that might be less familiar.

Mistake 1: Not taking full advantage of the tax benefits. One of the key benefits of any type of IRA, whether Roth or Traditional, is the ability to avoid taxes as the money grows. Investors who hold stocks and bonds in a taxable account are likely to receive taxable income and capital gains distributions from their holdings each year. Investors who hold the assets in an IRA, by contrast, have the potential to be taxed at a lower rate, or not at all, on those payouts, assuming they don't take the money out prior to age 59 1/2. That represents an opportunity to stash high-income-producing securities, such as dividend-paying stocks, for example, within the IRA wrapper, while saving more tax-efficient assets, such as broad market equity index funds, in taxable accounts.

Mistake 2: Being dogmatic about asset location. The key consideration here is when investors expect to need the money. For young accumulators, IRAs may be stock-heavy, and there may be no reason to add income producers into the mix. Meanwhile, for a 35-year-old holding bonds to fund a remodeling project, for example, it may make more sense to hold them in a taxable account, without any strictures to withdraw the money before retirement. The same reasoning applies to retirees who would like to pull some money for living expenses from their taxable accounts. It doesn't make sense to have all of the bonds residing in an IRA; bonds' relative liquidity might be helpful in taxable accounts, too. Finally, it's worth noting that it's often desirable to tap Roth assets toward the back end of retirement—if at all—because their tax-saving features are generally the greatest and should be stretched out for as long as possible.

Mistake 3: Not giving due care to IRA beneficiaries. The importance of beneficiary designations (they actually trump other bequests laid out in estate plans) is an under-discussed topic. As with any type of beneficiary designation, it's important to keep your IRA beneficiary designations up to date as your life situation changes—marriages, divorces, parents passing away, and so forth. Most people will name their spouses as their IRA beneficiaries; when the account owners die, their spouses can generally roll the assets into their own IRAs.

Mistake 4: Triggering a tax bill on a Roth IRA withdrawal. One of the key benefits of funding a Roth IRA is the ability to take tax- and penalty-free withdrawals in retirement. The Roth may also be a great vehicle for accumulators who worry about tying their assets up for a long time, as it's possible, under certain conditions, to withdraw contributions at any time and for any reason without triggering taxes or a penalty. Things get more complicated, however, when it comes to withdrawing investment earnings, or if your money got into the Roth because you converted it from a Traditional IRA or 401(k).

Mistake 5: Triggering a tax bill on a rollover. When it comes to the financial tasks that might crop up on your to-do list during your investment career, an IRA ranks as easy on the degree-of-difficulty scale. But it's still possible to goof up a rollover.

Avoid These Mistakes With Your IRA, Part 2

One of the key rules to bear in mind when rolling over money from a former employer's 401(k) into an IRA is the 60-day rule—that is, you have 60 days to complete the rollover. If you don't complete the rollover within that 60-day window and you're younger than 59 1/2, the amount will be treated as an early distribution and be subject to taxes and a 10% penalty. That's why it's a good idea to have your providers deal with one another on the rollover. That way, you never put your hands on the money, and the financial-services providers know the need to complete the rollover in a timely fashion.

Mistake 6: Letting your brokerage or fund company call the shots on your RMDs. Investors who are age 70 1/2 know that that's the year in which they must begin taking required minimum distributions from their Traditional IRAs and 401(k)s. Those RMDs are taxable. But RMD season also gives you the opportunity to make lemonade by being strategic about the investments from which you pull the distributions. Did your stock holdings shoot up in 2013? If so, it may be an ideal time to trim those holdings to restore your asset allocation back to your targets. As long as you take the right amount of RMDs from all accounts of a given type (you can't mix and match RMDs from your 401(k) and IRA, for example), you'll be on the up and up with the IRS. By contrast, if you leave it to your brokerage fund company to decide where to pull the money from, it may not be to your advantage. They may pull the money in accordance with their default rules, often proportionally from each holding.

Mistake 7: Not appealing a penalty on missed RMDs. Fail to take the RMD, and you'll be on the hook not just for the taxes, but also a 50% penalty (excise tax) on the amount that you should have taken and did not. That said, there may be legitimate reasons that you (or a loved one) missed the RMD. Perhaps you were ill, for example, or perhaps your parent is in the early stages of dementia and you haven't yet implemented a system to help with financial matters. The first step is to take the required distribution as soon as possible. Then fill out IRS form 5329, requesting a waiver of the 50% excise tax on missed distributions and providing the reason. Assuming the IRS finds that the missed RMD owes "to reasonable error and you are taking reasonable steps to remedy the shortfall," you should be able to get that penalty waived.

Mistake 8: Spending RMDs you don't need. In addition to the taxes due on RMDs, many retirees grouse about the distributions because they're taking them over their desired distribution rates. Shortly after they commence, RMDs quickly escalate well above the distribution rates that much research deems prudent and up into the range of 6% or 7%. Of course, as retirees age, they can arguably take more from their portfolios than they could earlier in their retirement years because their life spans are shorter. Additionally, your IRA may not be your only retirement resource; you can forgo distributions from other account types so that your RMDs don't take you over your planned spending rate. But if the RMD requirements are going to take you over your planned distribution rate, you can reinvest the money back into your retirement accounts—either a taxable account or a Roth IRA.

401(k) plans are long-term retirement savings vehicles. Withdrawal of pre-tax contributions and/or earnings will be subject to ordinary income tax and, if taken prior to age 59 1/2, may be subject to a 10% federal tax penalty. Funds in a traditional IRA grow tax-deferred and are taxed at ordinary income tax rates when withdrawn. Contributions to a Roth IRA are not tax-deductible, but funds grow tax-free, and can be withdrawn tax free if assets are held for five years. A 10% federal tax penalty may apply for withdrawals prior to age 59 1/2. This is for informational purposes only and should not be considered tax or financial planning advice. Please consult a tax and/or financial professional for advice specific to your individual circumstances.

Retirement Distribution Pitfalls: Not Reinvesting RMDs You Don't Need

Accumulation is a key facet of reaching your retirement goals. However, we tend to see far less about portfolio drawdown, or decumulation—the logistics of managing a portfolio from which you're simultaneously extracting living expenses during retirement. This can be even more complicated than accumulating assets.

Pitfall: One of the big mistakes of retirement distribution can be not reinvesting RMDs you don't need. Retirees may experience a situation where the amount they must withdraw from 401(k)s and IRAs for required minimum distributions can take them over their desired distribution threshold. The RMD rules require that people initially withdraw less than 4% of assets at age 70 1/2, but distributions can quickly step up into the 5%, 6%, and 7% range.

Workaround: What people might not realize is that there's nothing saying they have to spend their RMDs; they can reinvest in a taxable account if they'd like that money to stay invested in the market. This can be a wise strategy for retirees who are concerned with legacy planning or long-term care needs down the line. It's possible to build a taxable account that has many of the tax-saving features of a tax-deferred account.

401(k) plans and IRAs are long-term retirement savings vehicles. Withdrawal of pre-tax contributions and/or earnings will be subject to ordinary income tax and, if taken prior to age 59 1/2, may be subject to a 10% federal tax penalty. Funds in a traditional IRA grow tax-deferred and are taxed at ordinary income tax rates when withdrawn. This is for informational purposes only and should not be considered tax or financial planning advice. Please consult with a financial or tax professional for advice specific to your situation.

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