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The Cost of Taking a Cash Distribution

Deciding what to do with your 401(k) balance when you leave a job does not have to be difficult. It is something that almost everyone will have to do at some point. The best approach is to look at the various options, understand the differences, and figure out how your decision will impact your ability to save for retirement. In general, here are the options available: 1. Keep your savings in your previous employer's 401(k) plan (typically allowed if you have a balance of $5,000 or more), 2. Transfer your savings to your new employer's 401(k) plan, 3. Transfer your savings to a Rollover IRA, or 4. Take a cash distribution.

Let's look at a hypothetical example of an individual with $20,000 in a 401(k) who has left his or her job. This person now has to choose between the options above. Let's assume a hypothetical 8% annual return over a 20-year period. If the money was kept in a 401(k) plan or rolled into an IRA, it would have grown to $93,219 over 20 years. Alternatively, you could spend the $20,000 or put it into a taxable account, but these options do not provide the benefits of tax deferral. Furthermore, the tax consequences and early withdrawal penalties involved with the cash distribution would greatly reduce the actual amount of cash received. While cashing out from your retirement plan when you leave a job may seem like an attractive option, even the smallest withdrawal may have more sizeable financial consequences than you realize.

Withdrawals from tax-deferred accounts will be taxed at then-current rates. Early withdrawals may be subject to surrender fees, and withdrawals made prior to age 59½ may be subject to a 10% IRS penalty tax. Past performance is no guarantee of future results. You should consult your tax advisor as to the tax consequences of a particular investment.

Advisor Corner

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2012 Market Performance
01-01-12 to 6-30-12
DJIA ^DJI Up 5.42%
S&P 500 ^GSPC Up 8.31%
NASDAQ ^IXIC Up 12.66%
Russell 2000 ^ RUT Up 7.77%
* Index performance is gross of fees
Source: http://finance.yahoo.com

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How to Cope with Financial Anxiety

No one likes uncertainty. We want to maintain at least the illusion of control. But that's almost impossible to do today, given the volatility of the stock market and employers' belt-tightening. Even the steadiest hand is shaking just a little. It is imperative to avoid letting your emotions get in the way of making smart investment decisions. In times of doubt, it might be in your best interest to follow these steps for re-examining your current financial strategy.

Reassess Your Risk Tolerance: Today's investor is living those "hypothetical" questions that appear on risk-tolerance questionnaires. If you haven't checked your risk tolerance (the degree of uncertainty that you can handle in your investment portfolio) in more than a year, you're most likely due—especially if you're uncomfortable right now. Maybe you've taken on more risk than is prudent. If so, it might be in your best interest to change your asset mix. If you find that you're taking on the appropriate amount of risk for your goals, just sit tight.

If You Have to Do Something, Review Your Expenses: When dealing with uncertainty, some people feel compelled to act. Instead of trying to time the market (which even the professionals can't do with any consistency), focus on things you can control with certainty: expenses. Identify where you can tighten your belt. Try to identify unneeded or underused services. After such cuts, you'll have some extra cash to invest each month. Expenses also matter in investment accounts. Do you know what you're paying in expense ratios, 12b-1 fees, front- or back-end loads? Burn up some of your nervous energy by making sure those expenses aren't eating up what little positive returns you might have.

Create a Shopping List of Investments: Research stocks or funds that would complement your portfolio, then see where they are currently trading. This could be a great opportunity to pick up some of your favorite picks at rock-bottom prices. However, make sure they are trading at historical lows because of investor overreaction and not because they are no longer financially sound.

Win the Psychological Battle: Don't let the financial media scare you into making poor investment decisions. Times of great uncertainty are usually bad times to be making major decisions. What is healthy is knowing how the human mind works and factoring that into your investment decision-making process. Researchers and academics in the field of behavioral finance attempt to better understand and explain how emotions and perceptions influence investors and their decisions. If you are interested in learning more, there are plenty of publications devoted to this relatively new field.

Consider all of the complex financial decisions faced by investors today. Without experience in different market environments or knowledge of market history, how might investors make such decisions? Potentially through their perceptions or based on their emotions. Thus, it is imperative that investors understand and combat the myriad of illusions to which they might be prone.

When the markets are doing well, people tend to think the trend will continue indefinitely. During the recent crisis when the market was struggling, we witnessed overreaction: Investors were running away from the stock market. However, if you think U.S. companies are still fundamentally strong and will profit in the next five to 10 years, then you should still have a stake in the stock market. Just make sure you set your asset allocation policy first, and then stay the course with an appropriate mix of stocks, bonds, and cash. Investing is a long-term proposition—don't let your emotions overpower your sense of reason.

Stocks are not guaranteed and have been more volatile than bonds. Past performance is no guarantee of future results. Diversification does not eliminate the risk of experiencing investment losses.

Three-Step Checklist for Turbulent Markets

When the stock market experiences extreme volatility, an investor's best bet is to focus his/her energy on factors that can be controlled. Unfortunately, many investors panic-sell and lose their money. When the market rebounds, many investors are left wondering if it's the right time to get back in.

Your best bet during turbulent markets is an investment of time. You want to invest in time to see where you stand now, and, if you determine changes are in order, thoroughly research your options. Here is a three-step checklist to manage your investments during turbulent markets.

Step 1: Check adequacy of cash reserves.

The best way to manage your portfolio during volatile markets is to make sure you have adequate cash on hand to cover your near-term needs. This way, your long-term stock investments can ride out the market ups and downs, but you can take comfort in knowing that they won't affect your ability to fund short-term cash needs.

Step 2: Check your long-term positioning.

Once you've done the liquidity check, the next step is to check the asset allocation of your long-term assets. Market sell-offs can be alarming for retirees and people getting close to retirement simply because they typically have more money invested, compared with their younger counterparts. Checking your long-term positioning helps you put things into perspective so that you can make sound investment decisions for your future.

Step 3: Initiate defensive hedges with care.

During turbulent markets, investors may initiate defensive strategies like selling out of stocks and buying into the so-called "safe" investments like gold. Gold and treasuries can serve as a legitimate defensive role in a portfolio; however, these investments may have already enjoyed a sizable run-up. If you're moving into either, do so with caution, and only after you've checked your existing exposure to those asset classes.

Treasuries are guaranteed by the full faith and credit of the U.S. government as to the timely payment of principal and interest. Debt securities are subject to credit/default risk and interest-rate risk (they have varying levels of sensitivity to changes in interest rates). In general, the price of a debt security tends to fall when interest rates rise and rise when interest rates fall. Securities with longer maturities and mortgage securities can be more sensitive to interest rate changes.

Gold/commodity investments will be subject to the risks of investing in physical commodities, including regulatory, economic and political developments, weather events, natural disasters, and market disruptions. Exposure to the commodities markets may subject the investment to greater volatility than investments in more traditional securities, such as stocks and bonds.

Wealth by Numbers

America has long been known as the land of opportunity and the promise of a better life to people from all over the world. Recently, however, many Americans feel robbed of opportunities and better lives by the top 1% of their own. This growing income inequality has led to problems and civil unrest, as demonstrated by the "Occupy Wall Street" movement.

The table presents household income distribution data from the U.S. Census Bureau. Given that the poverty threshold for a two-member household is around $14,000, it appears that approximately 13.7% of Americans are poor. At the other end of the income spectrum, 3.9% are rich, with household incomes higher than $200,000.

Household Income Distribution in 2010

Under $5,000	3.5%
$5,000 to $9,999	4.3%
$10,000 to $14,999	5.9%
$15,000 to $19,999	6.1%
$20,000 to $29,999	11.5%
$30,000 to $39,999	10.2%
$40,000 to $49,999	8.9%
$50,000 to $74,999	17.7%
$75,000 to $99,999	11.4%
$100,000 to $149,999	12.1%
$150,000 to $199,999	4.5%
$200,000 and over	3.9%

Source: U.S. Census Bureau, Current Population Survey, 2011 Annual Social and Economic Supplement. Poverty threshold also from the U.S. Census Bureau.

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