

# PORTFOLIO WATCH



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Fee **FO** Only

NAPFA-registered Financial Advisor

## Roth IRA Pros and Cons

Roth IRA's have been around since 1997, but they still remain a little confusing to some people, or at least ignorable. This is unfortunate, because for many people, a Roth IRA can play an interesting part of an overall financial plan.

### Roth IRA Differences

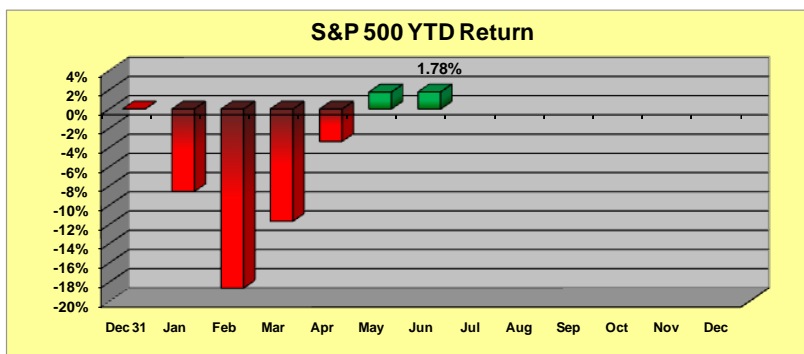
First, let's take a look at what makes a Roth IRA different from a Traditional IRA. When you contribute to a Traditional IRA, you get a tax deduction as long as your Adjusted Gross Income (AGI) is not too high (the deduction phases out if you make too much). This essentially means you don't pay tax on a Traditional IRA contribution, but it also means the government will be watching closely to make sure they get their money eventually. A Roth IRA is very similar, except that you don't get a tax deduction. This means that you've already paid the tax on the money that goes into a Roth IRA. Below is a list of the implications (assumes Married Filing Jointly):

	Traditional IRA	Roth IRA
Contribution Limit	\$5000/yr	\$5000/yr
Add'l contribution if over age 50	\$1000/yr	\$1000/yr
AGI Phaseout Limit (what phases out?)	\$166K - \$176K (deduction)	\$166K - \$176K (contributions)
Limits if active in other plan	Phaseout drops to \$89K-\$109K	None
Req'd Distributions	Age 70 ½ +	None
Penalty for early distribution	10%	10% on gain only
Tax on withdrawal	Treated as income	None

### Why Use a Roth IRA

The simple answer to why you would use a Roth IRA is because you believe that taxes may be higher in the future. If you are in a relatively low tax bracket now or expect a fairly active (and expensive) retirement, this may make sense. However, there is a less obvious but no less important reason. If all of your retirement income is fully taxable, then your expenses will

2006 return: 13.62%    2008 return: -38.49%  
 2007 return: 3.53%



determine which tax bracket you fall into. If you decide, for example, that you would like to show off to your travel club by paying cash for a new RV, this additional one-time expense may bump you into a higher tax bracket for the year. If you don't envision yourself roaming the country in an RV, substitute an unexpected medical bill, an overseas vacation, or any other large expense. Having a "bucket" of tax-free money to tap into for large, non-recurring expenses will allow you to smooth out taxable income, despite occasional spikes in expenses.

### What If You're Not Eligible For a Roth IRA

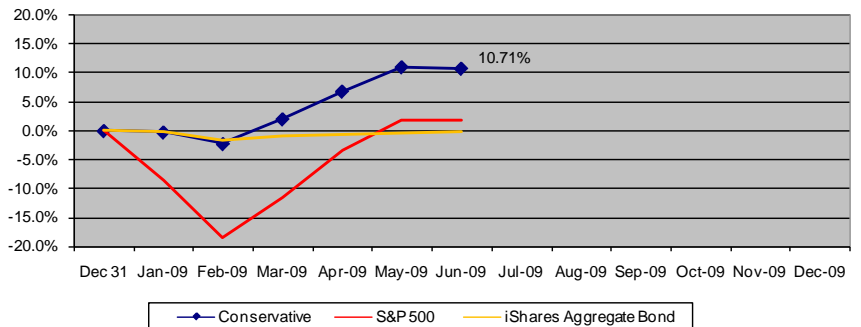
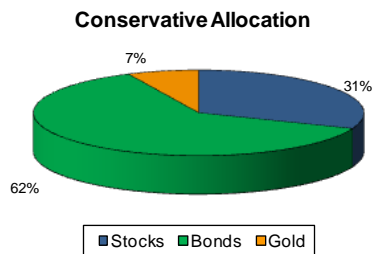
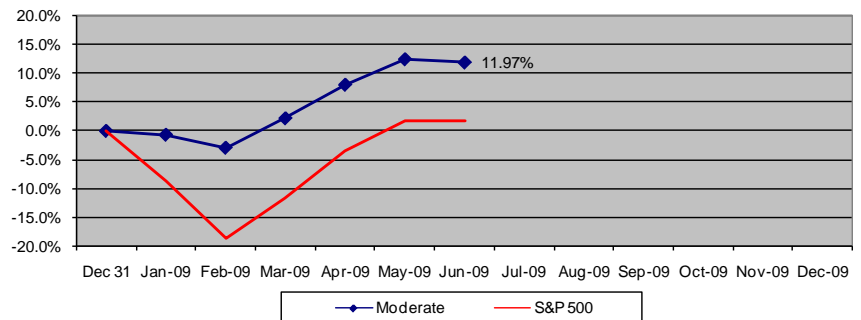
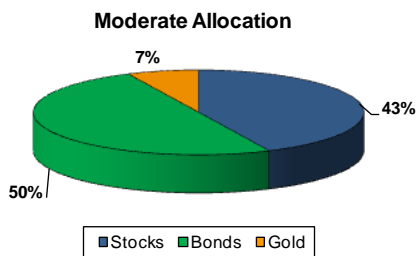
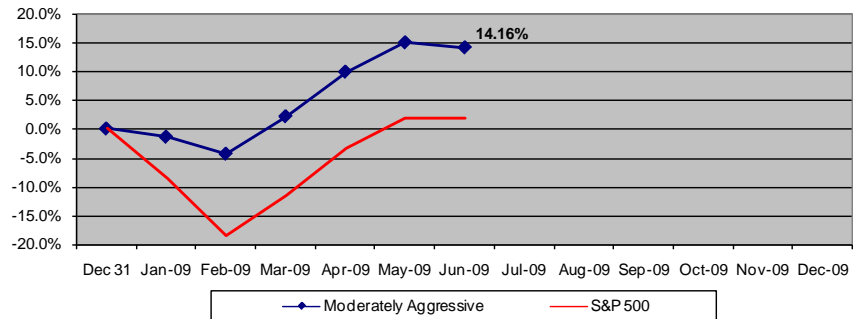
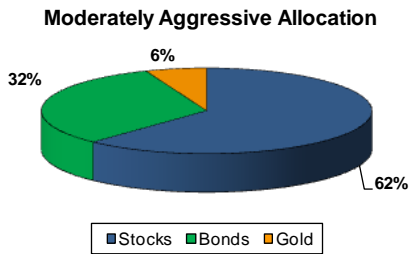
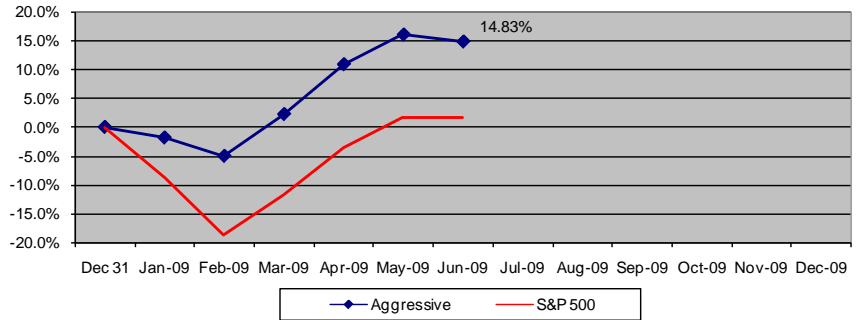
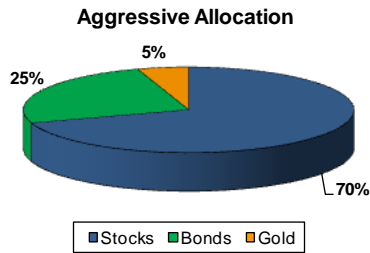
Not being eligible for a Roth IRA means you make too much, which is not completely a bad thing. Some companies (Intel is one) are now offering Roth 401(k) plans, which can be rolled into a Roth IRA at retirement. If you can afford the loss of tax deduction now, building a tax-free income source may make sense. Another option is to use tax-efficient investments in a taxable account. Although this won't be tax-free, the lower long-term capital gains tax can be used in a similar way.

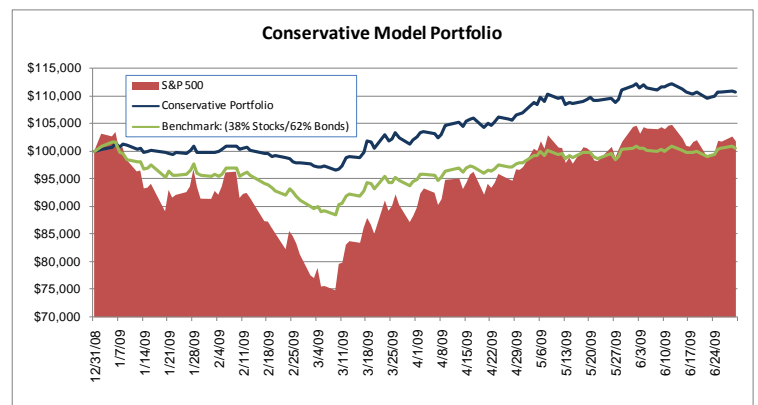
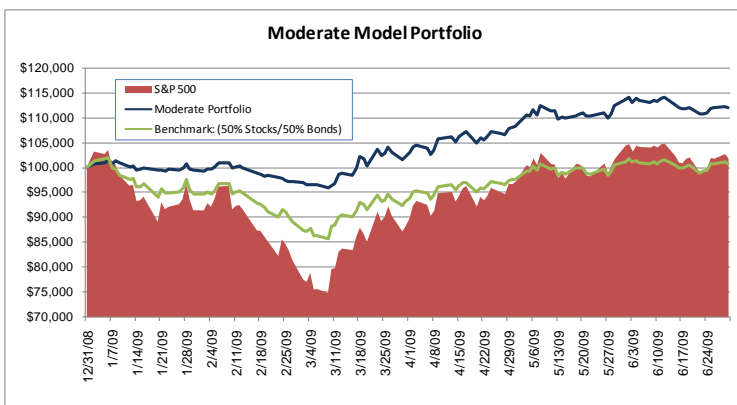
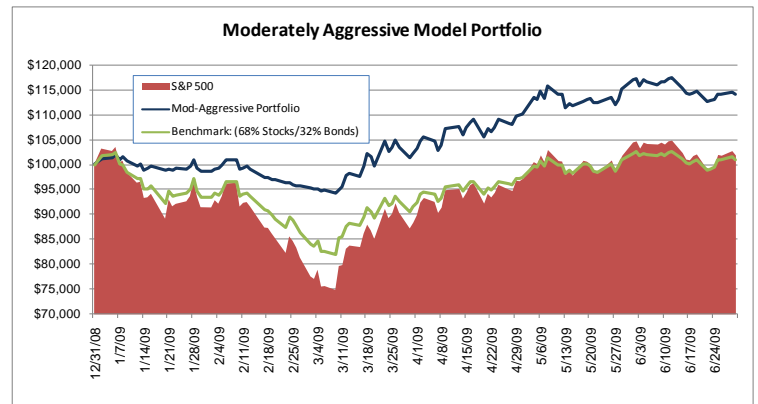
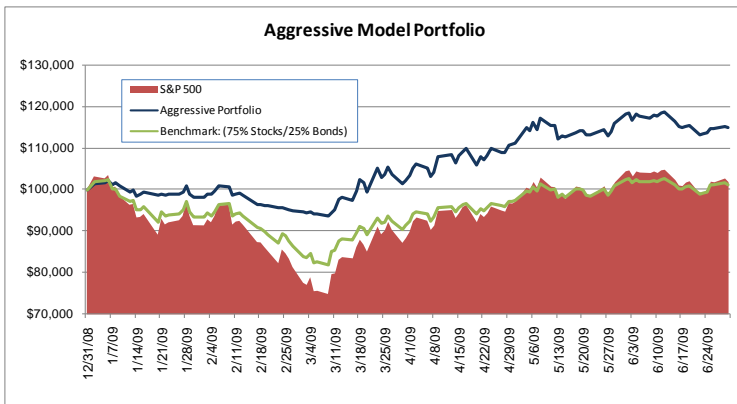
### Veripax Common Cents Blog

For those who haven't checked it out yet, I have started a blog at [veripax.wordpress.com](http://veripax.wordpress.com) (there's also a link on my website). The blog deals with various investment topics and current news events, and is geared toward those who are interested in what's going on in the investing world but would like to cut through the candy coating and misinformation that I see in a lot of other commentaries. I try to post something new a couple of times per week, and you can sign up for email updates by visiting the blog website.

# Model Portfolio Performance

The following allocation models and Year-To-Date performance graphs represent the preferred investments in Veripax Financial Management's target portfolios. Investment allocation for each model is determined based on time horizon and risk tolerance. In most cases, individual client portfolios will contain slightly different investments and allocation mixes based on individual financial goals, investment priorities, and tax considerations. The Model Portfolios invest primarily in Exchange Traded Funds and no-load bond funds.





**Benchmarks:** The Benchmark for each of the above graphs utilizes the Russell 1000 Index for stocks and Total Bond Market Index for bonds. The ratio of stocks and bonds in each Benchmark matches the ratio of the associated VFM model portfolio.

**Portfolio Construction:** Each Model Portfolio consists of up to 8 stock sectors, 7 bond sectors and gold. Buy/Sell decisions are based on VFM's proprietary algorithm and are consistent across all portfolios. Each Model Portfolio and the associated Benchmark are rebalanced quarterly.

## Portfolio Comments

The market is in a sideways pattern, which allowed the S&P 500 to stay in positive territory for two months in a row. The last quarter was the 2<sup>nd</sup> quarterly increase in a row, which hasn't happened in over a year and a half. Investors seem to be pulled between signs that the economy is a little less bad than it has been, meaning there could be an end in sight, and continued unemployment increases, which means if the end is in sight it's still a long way off.

The model portfolios maintained their lead over the benchmarks, which means they all pretty much moved sideways as well. Four sectors (Financials, Real Estate, Energy, Basic Materials) dropped more than 8% and triggered sells. Each of these sectors except for Energy made a small recovery immediately after the sells, but I expect the recovery was due to portfolio managers doing end-of-quarter "window dressing". These four sectors are now in cash awaiting buy points.

Utilities, Technology, Healthcare and Corporate Bonds were the only sectors to make gains last month, and the portfolios remain invested in each of these. The Gold Miners ETF was the biggest loser at 14.36%. Although this ETF is not tracked in the model portfolios, it is sometimes used in actual client portfolios. Fortunately, client portfolio holdings were switched from Gold Miners to Gold before the miners dropped.

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