



# Axial Financial Group

Centered on You.

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Dear Clients:

It's hard to believe we are already through the first quarter of 2010. By the time you receive this newsletter we will have pushed our clocks ahead for Daylight Saving Time and seen the first day of Spring.

With Spring comes tax time. Hopefully your paperwork is organized and you have been in touch with your accountant or tax preparer. Remember, you still have time until the tax filing deadline to contribute to your IRA, Roth IRA or other select retirement vehicles for 2009.

Lastly, the growth of our firm is greatly a result of the referrals we receive from all of our clients. If you know of anyone who may benefit from our services, we would be pleased to meet with them.

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## Key Economic Indicators and What They Mean

Late last year, members of the Federal Reserve Board's Open Markets Committee (FOMC) outlined some of the indicators they're watching to help determine when the economy might be stable enough to handle higher interest rates. Here's a primer on some of those indicators and why they're important.



*Gross Domestic Product (GDP)* indicates whether the economy is growing, shrinking, or stagnant. It represents the value of all goods and services produced in the United States, minus the value of all imports. This is the broadest measure of economic health.

Inflation represents increases in the cost of goods and services. The *Consumer Price Index (CPI)* represents increased costs for everyday expenditures such as housing, transportation, food, energy, and clothing. In addition to serving as an inflation gauge, CPI affects any payments tied to the cost of living, such as Social Security benefits.

A related measure, so-called core CPI, excludes food and energy prices because they can vary dramatically from month to month. Core CPI is closely watched by the Fed in determining whether and when to raise or lower its target interest rate, which in turn affects bond prices and other interest rates.

Still another inflation yardstick is the *Producer Price Index (PPI)*, which reflects prices at the wholesale level. If prices are rising for items used to manufacture a product, manufacturers and wholesalers may pass increased costs on to retailers and/or consumers. As a result, increases in the PPI can be an indicator of potential future inflation at the consumer level.

*Unemployment and payroll statistics* may seem similar, but they indicate slightly different things. The unemployment percentage usually

quoted in news headlines is based on a Bureau of Labor Statistics (BLS) survey of households. However, it doesn't include people who are working part-time involuntarily, or so-called "discouraged workers" who haven't been able to find a job and have given up looking. The BLS payroll figure uses corporate job records to show whether employers are creating or shedding jobs.

The unemployment rate is traditionally considered a lagging economic indicator, because an increase in jobs typically shows up only after other economic indicators, such as business inventories and unused manufacturing capacity, have begun to show signs of health. However, some economists argue that because the economy has relied heavily for many years on consumer spending, unemployment may now be more of a leading indicator than in the past.

*Personal incomes* as measured by the Commerce Department reflect not only paychecks but corporate and government benefits, pension checks, rental income, dividends, and interest payments; the data can give hints about future spending. *Personal consumption expenditures (PCE)* data show actual consumer spending on goods and services. As with core CPI, the Fed relies on PCE when setting its target interest rate.

*Industrial production* figures indicate whether factories are producing as much as they're capable of. When resource utilization is low, it suggests that factories are unlikely to experience near-term inventory shortages that could spark inflation. Somewhat related are *durable goods orders*, an indicator of inventory level and business investment in equipment. Also of interest are housing starts, new building permits (which hint at future construction), and new and existing home sales and prices.

These are only some of the data points to watch as guideposts in the months ahead.



## 529 College Savings Plans vs. Roth IRAs



According to an article in *The Wall Street Journal* ("More Parents Are Becoming 529 Dropouts," November 11, 2009), after the 2008/09 market collapse, some investors--and financial advisors--have reduced their reliance on 529 plans. Some of this pullback can be attributed in part to a broader retreat from the stock market as a whole. But another part can be attributed to parents who have opted to trade the tax benefits of 529 plans for college savings vehicles that don't have a "must-be-used-for-college" restriction. And as parents seek to save for their own retirement too, one such vehicle is a Roth IRA. So, just how does a favorite of the college savings world, a 529 college savings plan, stack up to a favorite of the retirement savings world, a Roth IRA, as an education-funding vehicle?

### Tax benefits

Both 529 college savings plans and Roth IRAs offer federal tax-free earnings if certain conditions are met (and most states follow this tax treatment), but only 529 plans offer the possibility of a state tax deduction too.

For 529 plans, earnings are tax free at the federal level if the distribution is used to pay the beneficiary's qualified education expenses--a broad term that includes tuition, fees, room and board, books, and computers--at any accredited college in the United States or abroad. If the distribution is used for any other purpose, earnings are subject to income tax and a 10% federal penalty tax.

For Roth IRAs, earnings are tax free at the federal level if the distribution is "qualified." A distribution is qualified if a five-year holding period requirement is met and one of the following conditions is met: (1) you are at least age 59½; or the distribution is made (2) due to a qualifying disability; (3) to pay certain first-time homebuyer expenses; or (4) by your beneficiary after your death.

If you are younger than age 59½ and you have a taxable distribution, you will also pay a premature distribution tax (also called an early withdrawal penalty) equal to 10% of the earnings portion of the distribution. But there are exceptions to this penalty, and one is if the money withdrawn is used to pay your child's qualified higher education expenses.

Bottom line: if you withdraw money before age 59½ to pay your child's college expenses, you'll generally owe income tax on the earnings, but not an early withdrawal penalty. However, you

may not end up owing income tax on the earnings, because Roth IRA distributions generally aren't taxed as earnings until the principal has been fully withdrawn. (By contrast, a distribution from a 529 plan is considered part principal and part earnings.)

### Financial aid

There is an important difference here. Under federal financial aid rules, 529 plans are counted as a parent asset (if the parent is the account owner), and 5.6% of all parent assets are deemed available for college costs. By contrast, the federal aid methodology doesn't count retirement assets in determining aid eligibility. So a Roth IRA won't impact the amount of federal aid your child may be eligible for. However, although Uncle Sam doesn't count retirement assets, colleges typically do when awarding their own institutional aid.

### Investment choices

Roth IRAs have the edge here--you can choose from a wide range of investments to fund your Roth IRA, and you can buy and sell investments whenever you like. But with a 529 plan, you are limited to the investment options offered by the plan. If you're unhappy with the investment performance of the options you've chosen, most plans let you change the investment options for your future contributions at any time, but for existing contributions, you can only change investment options once per year (twice per year in 2009 only). In 2008 and 2009, this restriction proved costly for many 529 account owners: having reached their limit on investment changes for the year, they were unable to make further changes in response to deteriorating market conditions.

### Lump-sum contributions and eligibility

If you have a lump sum to contribute, 529 plans allow individuals to gift up to \$65,000 in 2010 (\$130,000 for married couples) and avoid gift tax if certain conditions are met. By contrast, Roth IRAs have a contribution limit in 2010 of \$5,000 (\$6,000 for individuals age 50 or older). And your ability to contribute to a Roth IRA depends on your income level. But anyone can contribute to a 529 plan--there are no restrictions based on income.

### Bottom line

Whether a Roth IRA or a 529 college savings plan is best for your college savings depends on your personal circumstances and the factors discussed here.

### Note on 529 plans

*Investors should consider the investment objectives, risks, charges, and expenses associated with 529 plans before investing. More information about 529 plans is available in each issuer's official statement, which should be read carefully before investing. Also, before investing, consider whether your state offers a 529 plan that provides residents with favorable state tax benefits.*

## Special Needs Trusts

A special needs trust (SNT), sometimes referred to as a supplemental needs trust, is a trust that is established to benefit a disabled person, or a person who has special needs, while still allowing such persons to qualify for and receive governmental health-care benefits.

### Background

Some government programs aimed at assisting the disabled, such as Medicaid and Supplemental Social Security Income (SSI), are needs based. That means that if the disabled individual has access to more than a specified level of resources (generally \$2,000), he or she will not be eligible to receive such benefits. In 1993, Congress officially approved the use of SNTs to maximize the use of all available resources, both private and governmental, to provide more fully for the needs of the disabled.

For persons of limited means, government programs may constitute the primary, if not the only, source of funding for their current and future needs. However, government assistance is also available to families who have resources available to meet their loved one's basic needs. These families may be fortunate enough to be able to use their personal resources to provide for non-basic needs as well. With an SNT, the disabled person is able to first tap into any government benefits to which he or she is entitled, and then can spend personal resources as a secondary source for additional support and comfort.

### Types of SNTs

There are three types of SNTs: a self-settled or first-party SNT, a pooled SNT, and a third-party SNT.

#### *Self-settled or first-party SNT*

A self-settled or first-party SNT is created for the sole benefit of a disabled person who is under age 65. The trust must be established by the disabled person's parent, grandparent, guardian, or by the court, but it cannot be created by the disabled person. However, the disabled person can fund the trust. For example, the disabled person could fund the trust with money that has been inherited or received in settlement of a lawsuit, or as a result of a divorce.

As previously stated, in order to qualify for Medicaid or SSI, the person who is enrolling must have a limited amount of income and

resources. Generally, Medicaid and SSI will look back 36 or 60 months to see if assets have been transferred to someone else in order to qualify for benefits, and if so, a penalty is imposed. The penalty will be that the person who is enrolling won't be able to receive benefits for a certain amount of time. Transferring assets to an SNT, however, does not trigger these look-back provisions.

The other benefit of this SNT, of course, is that assets in the trust will not be countable as resources for eligibility purposes.

One disadvantage, however, is that upon the disabled individual's death, any money or assets remaining in the trust must be used to reimburse the government for Medicaid benefits extended to the individual during his/her lifetime.

#### *Pooled SNT*

A pooled SNT is a trust that is managed by a nonprofit organization. Funds are pooled for investment purposes, but separate subaccounts are maintained for each disabled beneficiary. A pooled SNT works in the same way as a self-settled or first-party SNT. However, with a pooled SNT, the disabled individual can create the account for himself or herself.

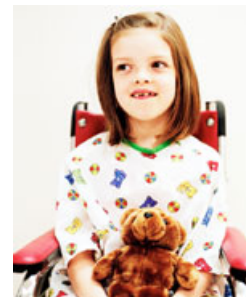
Further, any funds remaining in the account upon the individual's death can be used to pay back Medicaid, or they can remain in the pooled SNT to help others in the pool, depending on state law.

#### *Third-party SNT*

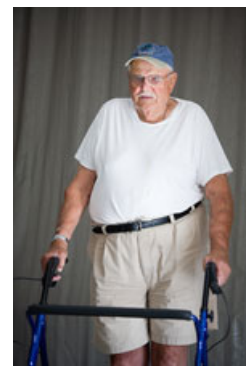
A third-party SNT is a trust created by a disabled person's parent or other third party, but this type of SNT has no payback requirement. The person establishing the trust must not have a duty to support the disabled child, so the child must be age 21 or older, depending on your state's laws. There is no requirement that the disabled person be under the age of 65. However, transfers to a third-party SNT may or may not trigger the Medicaid or SSI penalty period. Again, it depends on your state's laws.

### Conclusion

An SNT requires careful drafting and administration to avoid disqualification for government benefits. Be sure to consult a specialist.



***"In 1993, Congress officially approved the use of SNTs to maximize the use of all available resources, both private and governmental, to provide more fully for the needs of the disabled."***

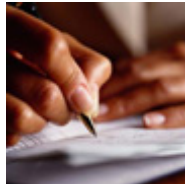




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## Ask the Experts



### What is the premature distribution tax?

Taxable distributions you receive from an IRA, 403(b), 401(k), or qualified employer plan before age 59½ are generally referred to as premature distributions, or early withdrawals.

To discourage early withdrawals, they're subject to a 10% federal penalty tax (and possibly a state penalty tax) in addition to any federal and state income taxes. This 10% penalty tax is commonly referred to as the premature distribution tax. Not all distributions before age 59½ are subject to this penalty, however.

Here are the most important exceptions:

- Distributions due to a qualifying disability
- Distributions to your beneficiary after your death
- Distributions up to the amount of your tax-deductible medical expenses
- Distributions made pursuant to a qualified domestic relations order (QDRO)

- Qualified reservist distributions
- Distributions from an IRA (but not an employer plan) to pay first-time homebuyer expenses (up to \$10,000 lifetime)
- Distributions from an IRA (but not an employer plan) to pay qualified higher education expenses
- Distributions from an employer plan (but not an IRA) after separation from service at 55 or older
- Certain distributions from an IRA (but not an employer plan) while you're unemployed up to the amount you paid for health insurance premiums
- Amounts levied by the IRS
- Distributions that qualify as a series of substantially equal periodic payments (SEPPs)

If you must take a distribution from your IRA or employer plan before age 59½, be sure to determine if one of these exceptions applies to you.