ROSEMONT
FINANCIAL GROUP

*Quarterly*Newsletter
Gain Through Confidence

It Certainly Was Five Years For The History Books

Time passes fast, and you might not have noticed the extraordinary financial history we all witnessed in the past five years.

The second quarter of 2014 marked the sixth year — and the sixth quarter — in a row in which stocks climbed higher. It was a bull-market run sure to be talked about for at least a few generations to come.

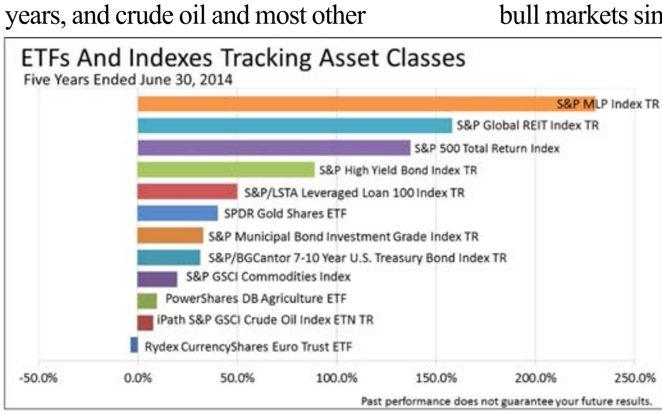
Five years is a good, long stretch. In this case, it was a great, long stretch. The end of the first half of 2014 marked the bull market's fifth anniversary.

It was a five-year about-face from the financial-crisis trough. When stock prices rose from the S&P 500's intraday low of 666 on March 9, 2009, stocks were less than two percentage points shy of tripling!

Looking at the performance of a broad range of asset classes over the five-year period ended June 30, 2014, the dispersion in returns is startling. At the top are Master Limited Partnerships, global REITs and the S&P 500 with gains of +230%, +158% and 137%, respectively. The euro currency has actually declined fractionally in value versus the U.S. dollar over the past five years, and crude oil and most other commodities are approximately flat. The bond total return indexes, both U.S. Treasury and municipals, are a smidge more than +30%, or about +6% per year.

Over the course of the five-year period ended June 30, 2014, investors experienced unprecedented volatility in gold, as it shot from approximately $900 to $1800 before settling lately around $1300. The gold predictions said that QE would ultimately result in massive inflation and debasement of the U.S. dollar. Happily, such predictions have come undone as inflation and bond yields have trended much lower than anybody, including the Federal Reserve, had anticipated.

All this positive news has to make you wonder how much longer the good times can last. Only three out of the 23 bull markets since 1900 lasted six years or longer. However, the S&P 500 index gained 4.7% in the second quarter of 2014, soaring after a brief sell-off in early April on Ukraine-Russian tensions. And, as the end of the third quarter of 2014 approached, the bull run



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Importance Of Summer

Thank you for taking the time to read our 4th-quarter newsletter. All of us at Rosemont enjoyed every minute of the summer, and I am sure like many of you, we felt it was just too short and went by too quickly.

One of the highlights for us this summer was attending the annual conference in Chicago for our broker dealer, Cambridge Investment Research. We really enjoyed the team-building we experienced as a group, as well as putting faces to the names of the many back-office people at Cambridge who help us on a daily basis.

The conference provided extremely valuable information in two major areas. The first was learning about advances in technology, internal systems, staffing, and compliance directly from Cambridge's department heads. Their level of commitment is proof why Cambridge has been voted Independent Broker Dealer of the Year in 6 of the last 8 years. The second was attending lectures given by some of the top leaders in the financial industry. They provided an in-depth look at the coming year in the markets, new product launches and investment updates, technological advancements in trading software and research, and updates on financial planning strategies and techniques.

The entire week was focused solely on advancing Rosemont's ability to improve our clients' experience. Once again, it made us appreciate the importance of independence.

Keeping A 529 Plan Rolling Along

If you were thinking ahead, you may have set up a tax-advantaged Section 529 plan for your first child at an early age. Once your kid is ready for college, you'll reap the rewards of your foresight.

But what happens when your son or daughter graduates? If there's still money in the plan, your tax savings don't have to stop there. If you have other children, you could designate one of them to be next in line as the 529 plan beneficiary, and then choose another and another . . . possibly even extending the plan's benefits to your grandchildren!

Section 529 plans, sponsored and operated by individual states, encourage families to set aside funds for future education expenses of the younger generation. As long as certain requirements are met, the money invested in the plan can grow without any erosion by taxes; and distributions that go to pay qualified college expenses—including tuition, fees, books, supplies, equipment, and room and board for full-time students—are completely tax-free.

There are two main types of plans: prepaid tuition plans and college savings plans. A prepaid tuition plan enables you to lock in rates at an in-state public college, whereas a college savings plan gives you more flexibility—the money can be used at a public or private college of your choice—but doesn't offer guarantees.

Keep in mind that it doesn't matter which state's college savings plan you choose, because no matter where it's set up, you can choose where to spend money from the account. But there could be an advantage to using your home state's plan. More than half of the 50 states offer a state tax deduction or credit for Section 529 plan deposits made by residents.

Now suppose your daughter is finishing college and your son is poised to attend next fall. Assuming some funds are left in the account, you can simply switch the beneficiary designation for the 529 plan to the younger child. Typically, a plan will allow one such change each year. If a younger child will enter college before the older one graduates, you might want to set up a separate account.

Although a plan can continue indefinitely, with your grandchildren eventually becoming beneficiaries, it terminates when the latest beneficiary reaches age 30. Of course, if there's a gap—say, your youngest child turns 30 and you have no grandchildren—you still can set up a new plan for a grandchild in the future.

A final bonus: There's a special gift tax break for 529 plans. Not only are transfers to 529s considered gifts that qualify for the annual gift tax exclusion ($14,000 in 2014), you can make up to five years worth of contributions in one year. And your spouse can do the same. Together, you could transfer up to $140,000 into a child's or grandchild's 529 entirely exempt from gift tax. ●

5 Ways To Cope With The NII Tax

Although the 3.8% tax on "net investment income" (NII) has been around for almost two years, many investors don't understand the rules or the potential consequences. But it's not too late to address potential 2014 tax liability for NII.

If your modified adjusted gross income (MAGI) exceeds $200,000 for single filers or $250,000 for joint filers, you may have to pay the 3.8% tax. It applies to the lesser of your investment income that qualifies as NII or the amount by which your MAGI exceeds those thresholds. For example, if you're a joint filer with MAGI of $300,000 and you have $25,000 in NII, you'll pay the 3.8% tax on the $25,000 (because it's less than the $50,000 by which your income exceeds $250,000) and you'll owe $950.

NII includes investment interest, capital gains, and dividends, among other items. And while it excludes distributions from IRAs and employer-sponsored retirement plans, that money will increase your MAGI and thus could affect your NII tax liability.

So what can you do? Here are five tax-aware investments that renowned tax expert Robert Keebler recommends:

1. Municipal bonds. Not only is interest income from munis exempt from federal income tax—and in some cases from state income tax—it also doesn't increase your NII. So allocating more of your portfolio to munis could reduce your tax bill.

2. Tax-deferred annuities. With an annuity, you pay premiums to a financial institution, which agrees to pay you income for a specified term or for your lifetime. By delaying when you'll receive taxable income, an annuity could help you leapfrog high-income years during which you're more likely to owe the 3.8% tax.

3. Life insurance. There are a lot of good non-tax reasons to consider buying permanent life insurance,

Locked Out Of A Roth? Open The Back Door

Not everyone can contribute to a Roth IRA because IRS rules disallow such contributions if your income exceeds a threshold amount. Of course, you still can put money into a traditional IRA and later convert that account to a Roth IRA, but that requires paying income tax on the amount you convert, and federal tax rates on ordinary income now reach as high as 39.6%. You also might owe state income tax and you could be subject to the "net investment income" surtax. Converting a large amount all at once may not be worth the cost.

But there's another possibility. If you're denied entrance to a Roth, you could try to sneak in through the back door. This involves a two-step process that's perfectly legitimate, but you have to observe all of the technicalities related to Roth conversions.

Here's how it works:

For starters, you can contribute up to $5,500 a year to a traditional IRA, or $6,500 if you're age 50 or over. Such contributions may be wholly or partially tax deductible, depending on your modified adjusted gross income (MAGI) and whether you (or your spouse, if you're married) actively participate in an employer retirement plan. For instance, your IRA contribution for 2014 won't be deductible if you're married, you're covered by a retirement plan at work, and your joint MAGI is more than $116,000. If you don't participate in an employer plan but your spouse does, you can't deduct your contribution if your joint MAGI exceeds $191,000.

When you withdraw money from a traditional IRA, the part that represents deductible contributions and earnings is taxable at ordinary income rates. Any portion representing nondeductible contributions is exempt from tax.

In contrast, contributions to a Roth IRA are never deductible, but "qualified" distributions—such as those made after you reach age 59½, made on account of death or disability, or that are used to pay for first-time homebuyer expenses (up to a lifetime limit of $10,000)—are 100% tax-free if you've had the Roth for at least five years. And even earlier distributions may be wholly or partially tax-free based on the IRS "ordering rules." Those rules treat distributions as coming first from nontaxable contribution amounts before any taxable amounts occur.

So what's blocking the front door? Contributions to a Roth IRA must be reduced if your MAGI exceeds a certain threshold. For 2014, the phaseout occurs between $114,000 and $129,000 of MAGI for single filers and $181,000 and $191,000 for joint filers. Once you exceed the upper limits of the phaseout range, you can't make any contributions to a Roth.

But fear not. You can sidestep this obstacle with a fast two-step move. (1) Set up a traditional IRA and make nondeductible contributions to it. (2) Convert the traditional IRA to a Roth IRA soon after. The funds you convert will be made up largely of your nondeductible contributions, so you won't owe any tax on that portion. Only the small portion, if any, that represents taxable investment earnings will be subject to tax. With this method, it's as if you were contributing to a Roth IRA, and if you repeat the technique over several years, you should be able to build up a sizable nest egg in your Roth.

Will the IRS object? It doesn't have a legal leg to stand on, but you're more likely to avoid a confrontation if you wait at least a month or two between when you set up the traditional IRA with nondeductible contributions and when you make the conversion.

But there might be another impediment. When you convert to a Roth, you can't simply designate that the money is coming from one particular IRA. Any distribution from a traditional IRA will be treated as if it came—on a "pro-rata" basis—from all of the IRAs in your name. That might trigger a large tax bill on a conversion if you recently rolled over a lump sum from a 401(k) or other company plan.

One possible solution is to use a "roll-in" instead of a rollover prior to the conversion. With this approach, you first transfer traditional IRA funds that are comprised of taxable amounts (investment earnings and any deductible contributions) to your 401(k), assuming your plan allows such transfers. Once you're ready to enter the back-door Roth, you will have reduced the taxable amount to the small earnings from your nondeductible IRA.

Obviously, you'll need to move carefully between company plans and both types of IRAs. We can help steer you in the right direction. ●

which can help your beneficiaries with cash to pay taxes and other debts. But those proceeds also can be exempt from federal income and estate taxes, and putting money into a life insurance policy rather than into other investments could help you avoid the NII tax.

4. Rental real estate. If you invest in real estate, you can reap tax benefits such as a generous depreciation allowance, although the deductibility of your losses may be restricted by "passive activity" rules. But even if you show a modest positive income, the depreciation deduction can help reduce your NII liability.

5. Oil and gas deals. The rules on deducting losses from oil and gas drilling partnerships are stricter now than they used to be, but deals that are structured properly still can yield tax benefits.

With the NII tax as with other kinds of taxes, it's important to consider the investment aspects of possible tax-cutting moves. But the right year-end planning could help limit your exposure to the 3.8% tax. ●

Social Security: Taxes In And Out

It seems like the IRS has you coming and going on Social Security. While you are working for a living, you must pay taxes into the system to provide benefits for current retirees. Then, when you finally retire, you're entitled to receive retirement benefits but they might be subject to tax as well.

Don't confuse the two taxes. The Social Security tax you pay as an employee is a payroll tax that applies to wages, commissions, and other compensation as part of the FICA tax. An employee's combined FICA rate for Social Security and Medicare in 2014 is 7.65% on the first $117,000 of compensation and 1.45% (Medicare only) above that. But the tax that may apply to Social Security benefits you get in retirement is a federal income tax that is reported along with other items on Form 1040. It's more complicated than the payroll tax.

Here's how it works: You're liable for tax on Social Security benefits if your provisional income (PI) exceeds certain thresholds in the tax law. For this purpose, PI is the total of (1) your adjusted gross income (AGI), (2) your tax-exempt interest income (for example, from municipal bonds), and (3) one-half of the Social Security benefits you received. For example, if the combined AGI of you and your spouse is $100,000 and you collect $5,000 in municipal bond income and $20,000 in Social Security benefits, your PI is $125,000 ($100,000 + $5,000 + $20,000).

There are actually two thresholds for computing the tax on Social Security benefits.

Threshold 1: For a PI between $32,000 and $44,000 ($25,000 and $34,000 for single filers), you're taxed on the lesser of one-half of your benefits or 50% of the amount by which PI exceeds $32,000 ($25,000 for single filers).

Threshold 2. For a PI greater than $44,000 ($34,000 for single filers), you're taxed on 85% of the amount by which PI exceeds $44,000 ($34,000 for single filers) plus the lesser of the amount determined under the first tier or $6,000 ($4,500 for single filers). Silver lining: You'll never owe tax on more than 85% of your total benefits.

These two thresholds aren't indexed annually for inflation. If your PI exceeds a relatively low level of $32,000 ($25,000 for single filers), you'll owe the tax year in and year out. And you'll get hit with the higher tax rate every year that your PI exceeds just $44,000 ($34,000 for single filers).

What can you do about it? You might lower your PI by harvesting capital losses to offset capital gains or deferring taxable income to the following year. But remember that the income from tax-free municipal bonds counts against you in the calculation of PI. Consider all the relevant factors, including the potential tax implications for Social Security benefits, in your investment decisions. ●

It Was Five Years

(Continued from page 1)

was chugging along, with the S&P 500 up a very respectable 8.8% with just 10 calendar days left in September.

As the third quarter neared an end, it had been well over three years since the stock market had last experienced a 10% correction. As usual, more and more of the talking heads on TV began predicting a drop in stock prices.

However, economic data suggested continued strength in the months and quarters ahead. The Conference Board's index of Leading Economic Indicators improved sharply in July, suggesting the economy was gaining traction. Growth should continue at a strong pace for the remainder of the year, according to the Conference Board data released August 21, 2014. Historically, the LEI has turned down definitively before a recession.

Indices are unmanaged and not available for direct investment. Investing in small companies involves greater risks than those associated with investing in more established companies, such as business risk, significant stock price fluctuations and illiquidity. Foreign securities have additional risks, including exchange rate changes, political and economic upheaval and the potential lack of strict financial and accounting controls and standards. Emerging markets involve still more risk. Fluctuations in the price of gold and precious metals often dramatically affect the profitability of the companies in the gold and precious metals sector. ●