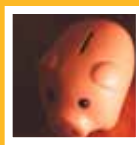




**Commentary**  
Market performance continues to improve during Q2.  
**PAGE 1**



**Roth IRA**  
Now may be the perfect time to make the switch.  
**PAGE 2**



**Principles of Wealth**  
Discipline and savings are the basis of wealth.  
**PAGE 3**



**Tax Corner**  
Changes headed our way.  
**PAGE 3**

Summer 2009



**WATERFORD ADVISORS**  
An SEC Registered Investment Advisor

# Quarterly Newsletter

## INVESTMENT COMMENTARY—SECOND QUARTER 2009



*Gregory L. Kozerski, CPA, CFP®, AIFA®  
President, Waterford Advisors LLC*

Stocks tacked small gains in June on to big gains in April and May, and closed the second quarter with their biggest three-month gain in more than 10 years. The large-cap Vanguard 500 Index Fund gained 16% for the quarter, and is now up 3.2% for the first half of 2009. The small-cap iShares Russell 2000

surged by almost 21% in the second quarter, but still trails year-to-date with a gain of 2.7%. Growth and value performed similarly in the second quarter, but for the first half of the year, growth is significantly ahead thanks to a much stronger (less bad) first quarter. The Vanguard Total International Stock Index soared 27.3%, bringing its year-to-date gain to 10.7%. Despite a 2.3% loss in June, Vanguard Emerging Market Stock Index did even better in the second quarter, gaining 34.2%, which is also its six-month return. High-yield bonds (based on the Merrill Lynch U.S. High Yield benchmark) padded their already big

*“Each of our model portfolios outperformed in the second quarter.”*

year-to-date returns with a 3% gain in June. So far in 2009 the asset class is up 29%. The extreme volatility we’ve noted in REITs is exemplified by the performance of Vanguard REIT Index; it lost 3.3% in June, finishing the second quarter with a 30% gain, but is down almost 12% year-to-date. The Vanguard Total Bond Market Index Fund, a proxy for high-quality, intermediate-term bonds, gained 1.8% over the second quarter, and is up 2.1% for the year through June. Each of our model portfolios outperformed in the second quarter. This is a result of both our tactical positions (mainly high-yield bonds) and of value added by our active managers, who in aggregate have significantly beaten their benchmarks.

### BETTER DAYS BUT STILL ANXIOUS

Since our last quarterly commentary the market environment has improved. The stock markets have experienced a powerful rebound. The economy has also showed signs of bottoming, as economic activity continues to worsen but at a decreasing rate. What is not good is that the global economy continues to be extremely fragile as the consequences of massive wealth destruction and the unwinding of too much private-sector debt continue

to play out. Last quarter we wrote about uncertainty. There is always uncertainty in the markets but we believe the range of potential economic and investment outcomes is particularly wide now.

As we have mentioned in the past, our approach to dealing with uncertainty is:  
*(continued on page 4)*

### JUNE BENCHMARK RETURNS (PRELIMINARY)

Large-Cap Benchmarks	June	2Q	YTD
Vanguard 500 Index	0.2%	16.0%	3.2%
Russell 1000 iShares	0.2%	16.4%	4.3%
Russell 1000 Growth iShares	1.1%	16.2%	11.4%
Russell 1000 Value iShares	-0.7%	16.7%	-2.8%
Mid-Cap Benchmarks			
Russell Midcap iShares	0.3%	20.7%	9.9%
Russell Midcap Growth iShares	0.5%	20.6%	16.5%
Russell Midcap Value iShares	0.2%	20.9%	3.2%
Small-Cap Benchmarks			
Russell 2000 iShares	1.5%	20.7%	2.7%
Russell 2000 Growth iShares	3.3%	23.3%	11.3%
Russell 2000 Value iShares	-0.3%	18.0%	-5.2%
Other Benchmarks			
Vanguard Total Int'l Stock Index	-1.3%	27.3%	10.7%
Vanguard Emerging Market Stock Index	-2.3%	34.2%	34.2%
Vanguard REIT Index	-3.3%	30.0%	-11.7%
Vanguard Total Bond Market Index	0.5%	1.8%	2.1%
Merrill U.S. High-Yield Cash Pay	3.0%	22.5%	29.0%
Barclays 7 Yr. Muni Bond Index	-0.9%	0.7%	3.0%
Citigroup World Govt. Bond Index	0.1%	3.5%	-1.5%
JPMorgan ELMI +	1.1%	10.2%	5.8%
DJ-UBSCI (Commodity Futures)	-1.9%	11.7%	4.6%

## IS IT TIME TO SWITCH TO A ROTH IRA?

**Have you wondered whether you'd benefit from converting your traditional IRA into a Roth IRA? If the answer is yes, there are a couple of reasons you might want to consider making the change sooner rather than later.**

### TWO WINDOWS OF OPPORTUNITY



Right now, you're only able to convert a traditional IRA to a Roth if your adjusted gross income is less than \$100,000.

However, in 2010, this limit is scheduled to be lifted, and the Roth IRA option will be available to almost anyone with earned income.

### WHAT CAN A ROTH IRA DO FOR YOU?

Even though the idea of getting a tax break today by investing in a traditional IRA may be attractive, it's what you have at the time of withdrawal that really matters—and that's why the Roth approach is worth considering.

By converting to a Roth IRA in 2010, you'll spread any taxable income created by the conversion evenly across 2011 and 2012, unless you choose to recognize the income in 2010. Keep in mind that when you convert, all pre-tax contributions and earnings will be subject to taxation at ordinary income tax rates.

The primary reason to convert to a Roth IRA is if you expect tax rates to go up or think you'll be in a higher tax bracket when

you retire. That said, if you convert to a Roth in the near future, the tax liability associated with the conversion may be lower than in previous years. Why? Because the value of your portfolio has most likely declined along with the financial markets in recent months.

### BENEFITS OF A ROTH IRA

What's all the fuss about? Well, there are definitely some significant benefits to investing for retirement in a Roth IRA.

With a traditional IRA, your investment contributions are generally tax-deductible, depending on your income and whether you participate in an employer-sponsored retirement plan such as a 401(k). You won't pay taxes on any earnings while your money remains invested, but your withdrawals will be subject to taxes in retirement.

However, with a Roth IRA, you're investing after-tax dollars—that is, money that's already been taxed. And you won't owe any additional taxes when you take withdrawals in retirement, as long as you've had the Roth for at least five years.

Many investors prefer to hedge their bets on future tax rates by investing in both tradi-

tional and Roth IRAs. This approach is often referred to as "tax diversification," and it may be worth considering—especially if you're uncertain about your future tax liability.

### WHAT ELSE DO YOU NEED TO KNOW?

As with any investment decision, you should be aware of both the pros and cons before converting to a Roth IRA or making any other changes to your portfolio. If you're still unsure, here are some additional items to consider:

- If the conversion could push you into a higher tax bracket, you could do a partial conversion and keep some of the money in your traditional IRA.
- If you think you will be in a higher tax bracket later or that significant tax hikes could be on the horizon, you may want to consider converting to a Roth IRA and being subject to today's lower tax rates.
- With a traditional IRA, you need to begin taking required minimum distributions (RMDs) beginning at age 70½. If you convert to a Roth IRA, you're no longer subject to RMDs.
- How are you going to pay the taxes you'd owe on the conversion? Generally setting aside some of the conversion to pay the tax is not a good idea, so you would want to have other assets to pay the tax when it comes due.

### KUDOS TO WATERFORD COLLEAGUES



**Christina M. Sporer**, a Financial Planner with Waterford Advisors LLC, has achieved the designation of Certified Financial Planner (CFP®) by successfully passing the national exam and completing two years of related work experience. A 2007 graduate from SUNY Alfred College of Technology, Christina excelled in her studies of financial planning, earning an overall 3.80 GPA. Christina continues to become an experienced CFP® by adding to her credentials in insurance, tax preparation and Social Security Planning.

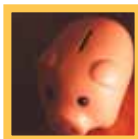
**Elaine M. Lechanski**, the Office Manager for Waterford Advisors LLC, has achieved the designation of Registered Paraplanner (RP®) by successfully passing the national exam and completing the necessary related work experience.



These accomplishments demonstrate Waterford's commitment to continually improve our people and to enhance our knowledge and the services we deliver to our clients.

## THE PRINCIPLES OF WEALTH ARE BUILT ON DISCIPLINE AND SAVINGS

Imagine a world without credit cards. Imagine paying cash for a new car or a home mortgage that's limited to three times your annual income.



This may sound like the economy of an underdeveloped country, but all it really means is a world where people buy and live within their means.

If you are a standard-issue baby boomer, your parents lived in such a world. Just ask them.

Our current economic problems reflect shifts in the values and attitudes about credit among both consumers and institutions. Individuals from this generation of golden opportunity have learned not to question the cost of a major purchase. Instead, they are thinking only about how they pay for it. The consumer's thinking, just like corporate America's, has tilted toward cash management and debt service. We would like to remind you that the principles of wealth are built on discipline and savings.

### DISCIPLINE

We forget that the credit and capital markets were created to purchase capital assets that hopefully would generate and appreciate in value. A value shift occurred when credit was extended to support a lifestyle, or when the debt-to-income ratio became an acceptable measure for lenders to judge whether something would be repaid. Basic accounting calls for assets to offset liabilities. In the old world, loans were made to the most creditworthy people, whose assets were expected to appreciate against a defined liability. In the new

world, it's often difficult to assess the liability of lending against assets or income subject to sudden change. Financial institutions require discipline to distinguish between the old world and the new realities we face today.

### SAVINGS

The United States has one of the lowest savings rates among industrialized nations. Wealth accumulation requires the discipline to forgo something today that may provide immediate gratification in favor of saving for a more secure or financially sound tomorrow. The notion that collective consumption will be supported by future income is fundamentally unsound. A strong savings component can help us weather financial storms, both as individuals and as a country.

### ACTION PLAN

The following actionable concepts will help you reinforce discipline and savings:

1. Adopt a new consumer attitude. Credit is for emergencies. Everything else should be paid for within 30 days.
2. Lower your personal monthly expenses. This will lower drag on your income from earnings and investments. Personal budgeting can quickly expose items that may be discretionary, problematic or disproportionate in relation to income.
3. Use dollar cost averaging for systematic savings.

## FACT : The Lifetime Value of Social Security

A person who starts out receiving the maximum monthly benefit in 2009 will receive a total of \$302,000 if they live 10 years, \$715,000 if they live 20 years and more than \$1.2 million if they live 30 years, assuming benefits are increased by 2.8% annual cost of living adjustments.



## TAX CORNER

The president's budget outline is very clear on this point—tax hikes are on the way. Not immediately, in light

of the current economic downturn, but in 2011 when the administration figures the economy will have recovered.

The targets of most of these tax increases will be high incomers and businesses. The proposed budget reinstates the 36% and 39.6% income tax brackets for married filers making over \$250,000 and for singles that make more than \$200,000, beginning in 2011. The proposal essentially substitutes the 36% and 39.6% tax rates for the current 33% and 35% tax brackets. Lower tax brackets would not be affected. Taxes will also increase for capital gains and qualified dividends. The current 15% maximum rate would rise to 20% (a 33% increase) for all filers who are above the 28% income tax bracket starting in 2011. The current phase-outs of personal exemptions and itemized deductions set to lapse after 2009 would be reinstated beginning in 2011, but only for taxpayers who in the highest tax brackets.

One piece of good news is that estate tax reform will likely pass in 2009. The proposal is for 2010 and beyond. Congress will likely maintain the current \$3.5 million exemption amount and the top tax rate of 45%. Also, to simplify estate planning, any unused exemption amount will pass to a surviving spouse and will not be lost as it is under the current law.

### INCOME TAX BRACKETS FOR 2009

#### Married, filing jointly:

\$0 - \$16,700	10%
\$16,701 - \$67,900	15%
\$67,901 - \$137,050	25%
\$137,051 - \$208,850	28%
\$208,851 - \$372,950	33%
Over \$372,951	35%

#### Single:

\$0 - \$8,350	10%
\$8,351 - \$33,950	15%
\$33,951 - \$82,250	25%
\$82,251 - \$171,550	28%
\$171,551 - \$372,950	33%
Over \$372,951	35%

- Be intellectually honest about what we can and can't know and about our circle of competence.
- Focus our efforts on scenario analysis that encompasses a spectrum of market and economic environments so that we can understand the possibilities and assess how different investment asset classes might fare in each. This also helps us to assess the magnitude of the risk presented by investments we own or are considering. As we discussed in detail last quarter, this is of critical importance to our decision-making
- Challenge our own thinking about how our analysis could be wrong.
- Make tactical asset allocation decisions with a five-year horizon so that we give adequate time for the economic and investment fundamentals to play out in asset class returns.

#### **OUR CURRENT PORTFOLIO POSITIONING IS BIASED TOWARD CONSERVATIVE**

Overall we continue to be conservatively postured relative to our benchmarks. Our equity exposure is a bit below that of our benchmark, though several factors offset some of that risk reduction. Our high-yield bond exposure (which is funded largely from the reduction in equities) has some equity-like risk, though we expect much less than a pure equity play. Because we use opportunistic bond managers, our fixed-income exposure may see more short-term volatility than the overall bond market, but we are willing to make this trade-off because we believe our holdings offer much better long-term value. We also think it is very likely that non-government investment-grade bonds would hold up much better in a down market than they did last year because the government has made it clear it will not allow a financial system collapse. At the overall portfolio level, we believe this all nets out to a below-benchmark risk exposure.

#### **POTENTIAL RETURNS ARE BETTER THAN THEY APPEAR**

We believe we can earn returns better than just what the market gives us through additional opportunities we expect to see at the tactical level, and because our managers continue to enjoy an environment that offers good individual stock- and bond-picking opportunities. Our research efforts will continue to focus on identifying these asset class opportunities and staying on top of our managers as we seek to earn the best returns possible given the risks we see.

*If you wish to be removed from our mailing list or if you have friends, family, or colleagues you think would benefit from our newsletter, please email us at [eml@waterfordadv.com](mailto:eml@waterfordadv.com) or send a fax to 716-580-3913.*

*As always, we welcome your comments or questions, and we invite you to share our newsletters with friends and acquaintances. Have a wonderful summer!*



An SEC Registered Investment Advisor • Certified Financial Planner™

Visit us online at [www.waterfordadv.com](http://www.waterfordadv.com)

Phone: 716-580-3906 • Toll-free: 877-512-4924

6225 Sheridan Drive, Suite 214  
Williamsville, NY 14221