



The Interest Rate Inflection Point And Your Portfolio

Interest rates are on the rise, and that means bond prices are likely to decline. Here's a summary of financial history since WWII demonstrating how long interest rate cycles have lasted in the past and how it could affect you.

moved lower, the prices of bonds climbed. Bonds returned an annual average of 7.86%, for this 36-year period. Which brings us to where we are today.

Interest rates started moving up about two years ago, which means

bond holdings declined in value. The Federal Reserve, which controls short-term rates — the black line — could continue to push rates higher for many years, if history is a

guide. In fact, amid the strengthening economy, the Fed says it expects to ratchet rates higher again and again in 2018.

For investors who, over three decades, have grown accustomed to bonds appreciating at a rate rivaling

Who Is Your Trusted Contact?

We've been with you through the ups and downs of life and the stock market. During that time, we've learned a lot about you - including the questions you tend to ask, your investment approach, and your overall personality. Given that, we are often able to detect any changes in your behavior - especially when it comes to how you make financial decisions. If we notice you're not acting like yourself or you're suddenly unresponsive to our attempts to get in touch, it's important that we have a Trusted Contact (TC) - a family member or friend - to reach out to in case of emergency.

When would we call your TC?

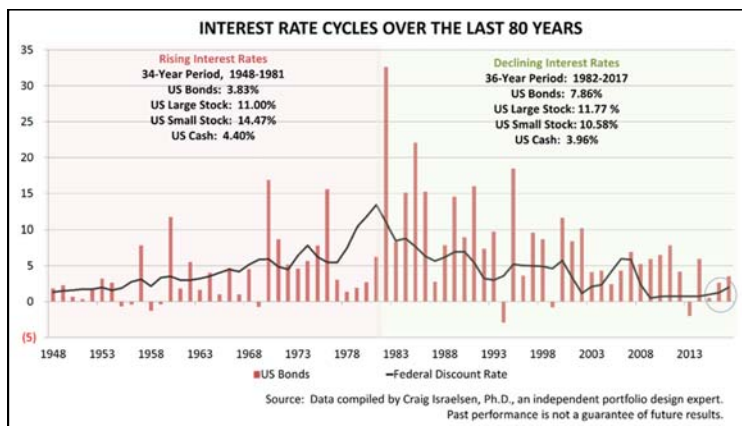
We would only reach out to your TC if we are concerned for your well-being. For example, if after decades of being a conservative investor, you decide to shift your entire portfolio into something highly speculative, or if we feel you are being scammed, we would contact your TC and notify them of what we're seeing.

What would we share with your TC?

Only our concerns. We will not share any account-specific information such as account balances with your TC. If you would like to give someone the ability to receive that information on your behalf, ask us about adding them as Power of Attorney.

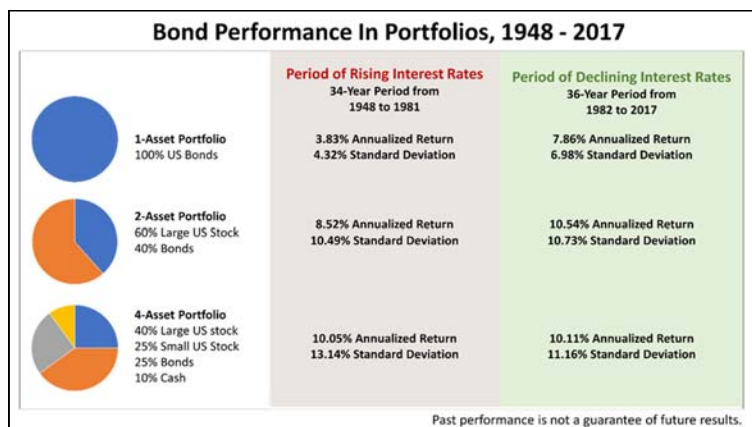
As we meet with you throughout the year, we will be asking for names and contact information of your TCs. If you want to beat us to it, give us a call now and we will update our records.

Kim Scott, CFP®
Senior Financial Advisor



From the end of WWII to 1981, interest rates rose, as is shown in the black line in the chart. Of course, When interest rates rise, bond prices tend to fall because bonds paying less than the new, higher rate are less desirable and their prices adjust downward. Thus, from 1948 to 1981, the average annual return on bonds was just 3.83% annually.

Now look at what happened since the declining rate cycle began in 1982 through the end of 2017. As interest rates



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The Big New Tax Break For Pre-Retired Professionals

Pre-retired dentists, doctors and lawyers as well as other independent professionals may be able save tens of thousands of dollars in income taxes annually during their peak income years under the new federal tax regulations. The new rules are complex. Here are 10 things pre-retired business owners need to know about qualifying for a 20% reduction in qualified business income under Section 199(A) of the new Internal Revenue Code:

1. Sole proprietors, LLCs, S corps, partnerships and other pass-through entities qualify.

2. Real estate and rental business income — including self-rentals — may qualify.

3. Some businesses are specified as ineligible and you may need a professional to determine if you qualify.

4. Service-business owners could get a deduction on 20% of their income, subject to income limitations.

5. A business owner with \$315,000 in taxable income owes tax on only \$252,000 —

saving more than \$12,000 of income tax.

6. If you are married filing jointly and have more than \$315,000 of income, the 20% deduction is subject to a phase-out. The phase-out begins at \$157,500 for single filers.

7. If you have more than \$415,000 of income from the service business, the 20% deduction is eliminated (\$207,500 for single filers).

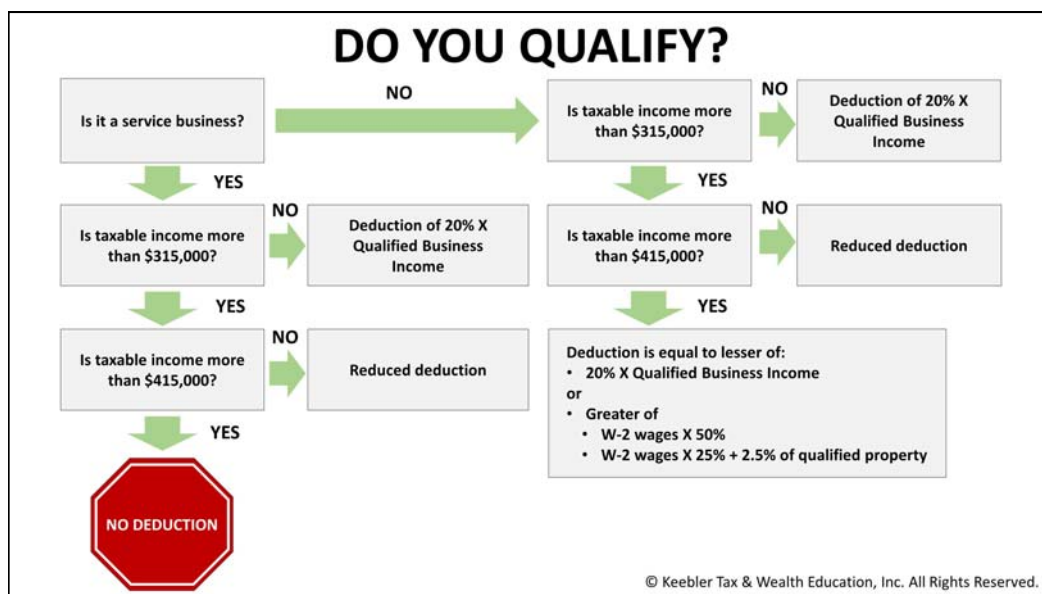
8. To keep your income below these thresholds, consider increasing

contributions to your retirement plan, if eligible.

9. This deduction has been described as “below the below the line” as it is taken from taxable income, after all other applicable deductions, and will appear on the back of the new Form 1040.

10. Architects are specifically excluded from the “Specified Service Business” definition.

We are happy to meet with you and your accountant to discuss this strategy. ●



Sidestepping New Limits On Charitable Donations

If you think you’re no longer allowed to deduct items like charitable donations on your income tax return, think again.

The new tax law doubled the standard deduction, slashing the number of Americans eligible to itemize deductions from 37 million to 16 million.

However, if you are among those who will lose your ability to deduct charitable donations, there is a simple strategy for managing the new limits on charitable giving, and it enables you to

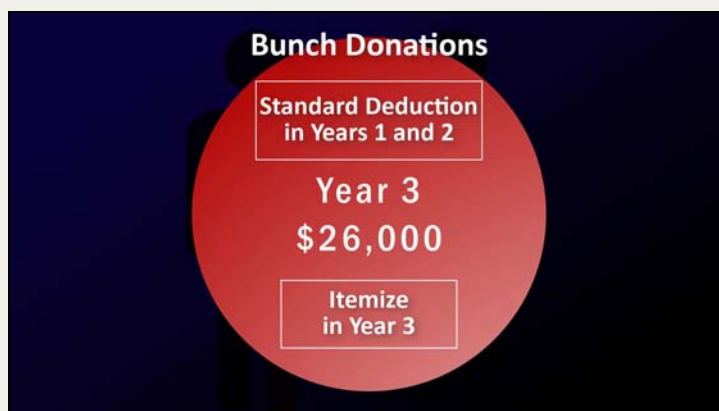
continue doing good while doing well for yourself by reducing your tax bill.

The strategy is simple: bunch a few years of donations into a single tax

year instead of making them annually.

Rather than report charitable donations on your tax return every year, you bunch two or more years of contributions into a single tax year — enough to boost the charitable total above that year’s standard deduction.

Say you’re married and you give \$10,000 in Year 1, \$6,000 in Year 2 and \$10,000 in Year 3. Your \$26,000 total surmounts the \$24,000 eligibility. If you deduct the total donations of \$26,000 in Year 3, you



8 Year-End Tax Planning Strategies

It's the season for year-end tax planning, and savvy taxpayers can still take steps to reduce their liability for this year as it draws to a close. Here are eight prime candidates for income tax savings.

1. Harvesting capital gains. Year-end tax planning typically focuses on “harvesting” capital losses by selling stocks or other securities. Losses realized on those sales may offset capital gains and other income.

But your situation may call for a different strategy. If you harvest long-term capital gains, you'll generally pay a maximum tax rate of only 15%, compared with much higher tax rates on ordinary income. (If you're in the top tax bracket for ordinary income, the maximum long-term capital gain rate is 20%.)

2. Putting more in your retirement plan. Virtually everyone can benefit from a boost to retirement plan accounts. Typically, you might participate in a 401(k) or another plan at work and supplement it with savings in IRAs.

The tax law allows generous contributions to grow on a tax-deferred basis. For 2018, you can contribute up to \$18,500 to a 401(k) or \$24,500 if you're age 50 or older. The limit for IRAs is \$5,500 or \$6,500 if you're reached 50. Contributing more to your accounts at year-end may reduce your tax bill while increasing your savings.

3. Adding to education savings plans. Tax laws also offer incentives to set

aside money for your children's college education. There are numerous options, but the Section 529 plan often gives you the biggest benefit.

These plans are offered by states and some educational institutions. You can normally sock away hundreds of thousands of dollars in an account for a future student. There are no taxes on earnings within the account and most withdrawals for college costs are also not taxed. Some states offer tax deductions for contributions.

4. Take Advantage of Your Gift Tax Exclusion. In 2018, you and your spouse can each gift up to \$15,000 per recipient without triggering a gift tax return. In other words, if a married couple has two grandchildren, they are able to gift each child \$30,000 (for a total of \$60,000) without dipping into their lifetime gift tax exemption.

Although the lifetime gift-tax exemption is currently \$11,180,000 per person (\$22,360,000 per married couple), the lifetime exemption often is a topic of discussion when tax reform occurs. If gifting plays a significant role in your financial plan, it may make sense to take advantage of your annual exclusion. Plus, you have the added benefit of being able to see your loved ones enjoy your gift versus waiting for them to inherit your assets once you're gone.

5. Investing with tax-efficiency. When you invest, it's always important to focus on the fundamentals of potential investments. But don't forget to factor taxes into the equation. The income from municipal bonds, for example, is

normally not taxed at the federal level and may not be subject to state taxes either.

6. Managing your retirement accounts. If you're already contributing to IRAs, you're ahead of the game. But you might do even better converting funds in a traditional IRA to a Roth IRA.

Although you'll be taxed now on the amount you convert, future distributions from a Roth will likely be exempt from tax. In contrast, traditional IRA distributions are taxed at ordinary income rates. To cushion the tax blow of a conversion, you might do it over several years to keep your income from moving into the highest tax brackets.

7. Making the most of net unrealized appreciation. Do you know the secret of “net unrealized appreciation” (NUA)? If you receive a retirement plan payout in company stock, you'll be taxed on the stock's initial cost rather than its current value. That means that any appreciation in value is completely tax-exempt. When you later sell that stock, any gain from the sale will be taxed at the lower rates for capital gains.

8. Giving more to charity. The full amount of monetary donations to charity made during the year can be tax-deductible, and you can still deduct donations you charge online as late as December 31.

In some cases, giving appreciated property in lieu of cash can be particularly advantageous. If you've held stocks or other property for more than a year, you can deduct its current fair market value, getting a deduction for appreciation that otherwise would have been taxed as a capital gain. Other sophisticated techniques, such as the use of charitable remainder trusts (CRTs), may also provide tax benefits while also helping the philanthropic causes you select. Feel free to reach out to your advisor to discuss implementing some of these year-end strategies. ●



can take the standard deduction in Years 1 and 2 and itemize in Year 3.

Instead of giving in dribs and drabs, you will need to plan your giving strategy, but this will allow you to give as much as you used to before the limits

without losing the tax benefits.

And if you can plan to make the larger donations in a year when you expect higher income, bunching charitable donations can be even more effective in lowering your tax bill.

We'll be

speaking with clients about this in the months ahead because this tactic does take some planning in advance.

If you have any questions about your personal situation, please do not hesitate to give us a call. ●

Key Facts On Deducting Medical Expenses

Medical expenses can run up your expenses a lot. For that reason, the new tax law gives people a break by sweetening the long-time tax deduction for health care, at least for a couple of years.

Before the Tax Cuts and Jobs Act (TCJA), you could deduct medical expenses that exceeded 10% of your adjusted gross income (AGI). For the tax years of 2017 and 2018, the TCJA lowered the threshold to 7.5%. AGI is taxable income minus all deductions, IRA contributions and student loan interest. Of course, the medical tax break is available only to people who itemize.

The trouble is the more generous deduction expires after 2018, when the threshold rises back to 10%. Groups like AARP are lobbying in Washington to get the 7.5% level extended or made permanent, and that could factor into your timing and decisions about medical expenses in the months ahead.

Say your AGI is \$45,000 and you rack up \$5,475 in medical costs. You multiply \$45,000 by 0.075 (7.5

percent) to get your deduction threshold of \$3,375. Only medical expenses above \$3,375 would be deductible. Result: your medical expense deduction is \$2,100 (\$5,475 minus \$3,375).



Some big-ticket items are deductible medical expenses, like long-term care insurance premiums, nursing home payments and Medicare costs — including Medicare Part B, Medigap policies, Medicare Advantage programs and Part D Prescription plans.

In addition, any health insurance you pay out of pocket can be deducted.

But that can't include coverage you pay for with before-tax dollars, which is often the case with employer-sponsored medical plans.

Another big deductible item is co-payments for prescription drugs — and also out-of-pocket fees for doctors, dentists, physical therapists and other health-care professionals not covered by Medicare or any other health insurance. Add in prescription eyeglasses, hearing aids and wheelchairs, and transportation costs to and from medical appointments, as well as alcohol and drug treatment programs.

Medical expenses are deductible only if they alleviate or prevent a physical or mental defect or illness, including dental and vision. So, you cannot deduct a gym membership if it is to promote your general wellness. However, if a doctor diagnoses you with a specific medical condition, such as obesity or hypertension, then the expense of the prescribed treatment may indeed be tax-deductible. Give us a call to discuss this topic further. ●

Interest Rate Inflection Point

(Continued from page 1)

stock, the future may be very different, which especially affects the demographic bubble of baby-boomer retirees, who have long favored bonds for producing reliable income.

To understand the effect the new rising rate cycle might have on your portfolio in the years ahead, this table gives you the key facts.

The annual returns on stocks and Treasury Bills stayed approximately the same through both the rising and falling interest rate cycles. However, the average annual return of bonds in the rising rate cycle from 1948 to 1981 was less than half the that of bonds during the 1982 to 2017 period. This poses a new kind of risk that

many investors have never experienced before.

During the rising rate cycle, when the average annual return on bonds was a measly 3.83%, stocks and 90-day Treasury Bills averaged about the same annual return as they did in the falling rate cycle. The performance of stocks, bonds, and cash over this period demonstrates why diversification and a strategic approach are so important to long-term investing.

In light of this trend, we have been utilizing bonds with shorter maturities — due in 3 to 7 years, as opposed to 10, 20, or 30 — which are less susceptible to interest rate risk. Floating rate bonds are another option — they invest in bank loans, and can actually do well in rising interest rate environments. If your FSA

accounts invest in bonds, you are likely to see several short-term and floating rate bond funds in your portfolio.

The takeaway here is that rates may be at the start in a new long-term cycle and clients can rely on our advice on the best way to manage this risk. Please do not hesitate to contact us with questions. ●

Large-cap US equity represented by the S&P 500 Index. Small-cap US equity represented by the Ibbotson Small Companies Index from 1970-1978, and the Russell 2000 Index starting in 1979. Non-US equity represented by the MSCI EAFE Index. Real estate represented by the NAREIT Index from 1970-1977 and the Dow Jones US Select REIT Index starting in 1978. Commodities represented by the Goldman Sachs Commodities Index (GSCI). As of February 6, 2007, the GSCI became the S&P GSCI Commodity Index. U.S. Aggregate Bonds represented by the Ibbotson Intermediate Term Bond Index from 1970-75 and the Barclays Capital Aggregate Bond index starting in 1976. Cash represented by 3-month Treasury Bills.