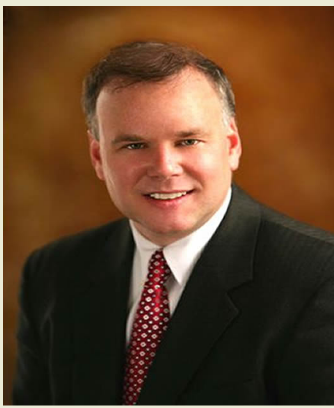

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February 2015

Key Numbers for 2015
10 Financial Terms Everyone Should Know
Should Life Insurance Be Part of Your Retirement Plan?
Should I be worried about a Federal Reserve interest rate hike?

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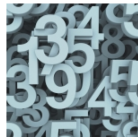

Every year, the Internal Revenue Service (IRS) announces cost-of-living adjustments that affect contribution limits for retirement plans, thresholds for deductions and credits, and standard deduction and personal exemption amounts. Here are a few of the key adjustments for 2015.

Retirement plans

- Employees who participate in 401(k), 403(b), and most 457 plans can defer up to $18,000 in compensation in 2015 (up from $17,500 in 2014); employees age 50 and older can defer up to an additional $6,000 in 2015 (up from $5,500 in 2014)
- Employees participating in a SIMPLE retirement plan can defer up to $12,500 in 2015 (up from $12,000 in 2014), and employees age 50 and older will be able to defer up to an additional $3,000 in 2015 (up from $2,500 in 2014)

IRAs

The limit on annual contributions to an IRA remains unchanged at $5,500 in 2015, with individuals age 50 and older able to contribute an additional $1,000. For individuals who are covered by a workplace retirement plan, the deduction for contributions to a traditional IRA is phased out for the following modified adjusted gross income (AGI) ranges:

	2014	2015
Single / head of household (HOH)	$60,000 - $70,000	$61,000 - $71,000
Married filing jointly (MFJ)	$96,000 - $116,000	$98,000 - $118,000
Married filing separately (MFS)	$0 - $10,000	$0 - $10,000

Note: *The 2015 phaseout range is $183,000 - $193,000 when the individual making the IRA contribution is not covered by a workplace retirement plan, but is filing jointly with a spouse who is covered.*

The modified AGI phaseout ranges for individuals making contributions to a Roth IRA are:

	2014	2015
Single / HOH	$114,000 - $129,000	$116,000 - $131,000
MFJ	$181,000 - $191,000	$183,000 - $193,000
MFS	$0 - $10,000	$0 - $10,000

Estate and gift tax

- The annual gift tax exclusion remains $14,000
- The gift and estate tax basic exclusion amount for 2015 is $5,430,000, up from $5,340,000 in 2014

Personal exemption

The personal exemption amount has increased to $4,000 (up from $3,950 in 2014). For 2015, personal exemptions begin to phase out once AGI exceeds $258,250 (Single), $309,900 (MFJ), $284,050 (HOH), or $154,950 (MFS).

Note: *These same AGI thresholds apply in determining if itemized deductions may be limited. The corresponding 2014 threshold amounts were $254,200 (single), $305,050 (MFJ), $279,650 (HOH), and $152,525 (MFS).*

Standard deduction

The standard deduction amounts have been adjusted as follows:

	2014	2015
Single	$6,200	$6,300
HOH	$9,100	$9,250
MFJ	$12,400	$12,600
MFS	$6,200	$6,300

Note: *The 2015 additional standard deduction amount (age 65 or older, or blind) is $1,550 if filing as single or HOH (unchanged from 2014) or $1,250 (up from $1,200 in 2014) for all other filing statuses. Special rules apply if you can be claimed as a dependent by another taxpayer.*

See disclaimer on final page

10 Financial Terms Everyone Should Know

Understanding financial matters can be difficult if you don't understand the jargon. Becoming familiar with these 10 financial terms may help make things clearer.

1. Time value of money

The time value of money is the concept that money on hand today is worth more than the same amount of money in the future, because the money you have today could be invested to earn interest and increase in value.

Why is it important? Understanding that money today is worth more than the same amount in the future can help you evaluate investments that offer different potential rates of return.

2. Inflation

Inflation reflects any overall upward movement in the price of consumer goods and services and is usually associated with the loss of purchasing power over time.

Why is it important? Because inflation generally pushes the cost of goods and services higher, any estimate of how much you'll need in the future--for example, how much you'll need to save for retirement--should take into account the potential impact of inflation.

3. Volatility

Volatility is a measure of the rate at which the price of a security moves up and down. If the price of a security historically changes rapidly over a short period of time, its volatility is high. Conversely, if the price rarely changes, its volatility is low.

Why is it important? Understanding volatility can help you evaluate whether a particular investment is suited to your investing style and risk tolerance.

4. Asset allocation

Asset allocation means spreading investments over a variety of asset categories, such as equities, cash, bonds, etc.

Why is it important? How you allocate your assets depends on a number of factors, including your risk tolerance and your desired return. Diversifying your investments among a variety of asset classes can help you manage volatility and investment risk. Asset allocation and diversification do not guarantee a profit or protect against investment loss.

5. Net worth

Net worth is what your total holdings are worth after subtracting all of your financial obligations.

Why is it important? Your net worth may fund most of your retirement years. So the faster and higher your net worth grows, the more it may help you in retirement. For retirees, a typical goal is to preserve net worth to last through the retirement years.

6. Five C's of credit

These are character, capacity, capital, collateral, and conditions. They're the primary elements lenders evaluate to determine whether to make you a loan.

Why is it important? With a better understanding of how your banker is going to view and assess your creditworthiness, you will be better prepared to qualify for the loan you want and obtain a better interest rate.

7. Sustainable withdrawal rate

Sustainable withdrawal rate is the maximum percentage that you can withdraw from an investment portfolio each year to provide income that will last, with reasonable certainty, as long as you need it.

Why is it important? Your retirement lifestyle will depend not only on your assets and investment choices, but also on how quickly you draw down your retirement portfolio.

8. Tax deferral

Tax deferral refers to the opportunity to defer current taxes until sometime in the future.

Why is it important? Contributions and any earnings produced in tax-deferred vehicles like 401(k)s and IRAs are not taxed until withdrawn. This allows those earnings to compound, further adding to potential investment growth.

9. Risk/return trade-off

This concept holds that you must be willing to accept greater risk in order to achieve a higher potential return.

Why is it important? When considering your investments, the goal is to get the greatest return for the level of risk you're willing to take, or to minimize the risk involved in trying for a given return. All investing involves risk, including the loss of principal, and there can be no assurance that any investing strategy will be successful.

10. The Fed

The Federal Reserve, or "the Fed" as it's commonly called for short, is the central bank of the United States.

Why is it important? The Fed has three main objectives: maximum employment, stable prices, and moderate long-term interest rates. The Fed sets U.S. monetary policy to further these objectives, and over the years its duties have expanded to include maintaining the stability of the entire U.S. financial system.

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Should Life Insurance Be Part of Your Retirement Plan?

As with most financial decisions, there are expenses associated with the purchase of life insurance. Policies commonly have mortality and expense charges. In addition, if a policy is surrendered prematurely, there may be surrender charges and income tax implications.

Any guarantees associated with payment of death benefits, income options, or rates of return are based on the claims-paying ability and financial strength of the insurer.

Most of us think of life insurance as protection against financial loss should we die prematurely. But if and when we reach retirement and the kids are all self-sufficient, do we still need life insurance? The answer is maybe--or maybe not. Here are some situations where life insurance may make sense for retirees, or those close to retirement.

Benefits at death

Provide for a dependent family member

Sometimes, even in retirement, there are family members who'll depend on you for financial and/or custodial support. Should you die unexpectedly, life insurance may help provide funds needed to support dependent family members who are physically or mentally challenged.

Income replacement for surviving spouse

Generally, Social Security retirement benefits are paid to both spouses, either based on their individual work records or on the work record of one spouse, with spousal benefits available for the other spouse. At the death of a spouse, his or her benefits end, reducing the total benefits available to the surviving spouse. Life insurance can be used to replace the loss of income for the surviving spouse.

Pay off debt

While past generations often retired with little or no debt, it is not uncommon for today's retirees to leave the workforce while still carrying a mortgage, car loan, and credit-card debt. Life insurance can provide the cash to pay off these debts, which is especially beneficial for a surviving spouse.

Provide a legacy

For many approaching retirement, as well as for those already there, a primary concern is having enough savings to provide income needed to live comfortably. While conserving savings and keeping track of spending in retirement are important, all too often retirees will forgo spending on themselves in order to fulfill a desire to leave a legacy. The death proceeds from a life insurance policy can provide a legacy for surviving family members, while allowing retirees to spend a little more on themselves, with the knowledge that they'll be leaving something for their loved ones.

Final expenses

Unfortunately, the expense of dying is often overlooked or underestimated. Uninsured medical bills, funeral costs, debts, and estate administration costs can add up. Typically, these expenses are paid in a lump sum, which can reduce savings for surviving spouses and dependent family members. Proceeds from life insurance can be used to help pay for these final expenses, which may help preserve savings for other needs.

Living benefits

Source of retirement income

While life insurance is designed to protect against unexpected economic loss, cash-value life insurance also may provide a source of income during retirement. Earnings in life insurance accumulate tax deferred, and in some instances cash-value distributions can be income-tax free. However, loans used to access cash values from a life insurance policy will reduce the policy's cash value and death benefit, could increase the chance that the policy will lapse, and might result in a tax liability if the policy terminates before the death of the insured.

Income you can't outlive

Your financial circumstances may change during retirement, and the need for the policy's death benefit may not be as important as the need for a steady income. One option that may be available is to exchange a portion or all of your policy's cash value for an immediate annuity that can provide a fixed income for the rest of your life, and for the life of your spouse if you choose. If the policy is not a modified endowment contract and there are no outstanding policy loans, the exchange to an annuity should be income-tax free. But exchanging your cash value for an annuity will likely decrease or eliminate the policy's death benefit. And these exchanges work only one way--you can't exchange an annuity for a life insurance policy.

Long-term care benefits

Some cash-value life insurance policies provide multiple sources of protection. Along with the death benefit and potential cash value, these policies may also provide a long-term care benefit. Often, these policies allow for a portion or all of the death benefit to be "accelerated" if used for the payment of qualifying medical and long-term care expenses.

Life insurance provides protection for your family's financial future should you die during your working years. However, life insurance may provide other benefits that can be useful during your retirement. Whether life insurance should be part of your retirement plan is best determined based on your individual circumstances and goals. You may want to talk with an insurance or financial professional before making this decision.

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Should I be worried about a Federal Reserve interest rate hike?

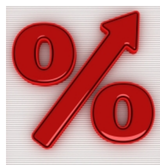
After years of record-low interest rates, at some point this year the Federal Reserve is expected to begin raising its target federal funds interest rate (the rate at which banks lend to one another funds they've deposited at the Fed). Because bond prices typically fall when interest rates rise, any rate hike is likely to affect the value of bond investments.

However, higher rates aren't all bad news. For those who have been diligent about saving and/or have kept a substantial portion of their portfolios in cash alternatives, higher rates could be a boon. For example, higher rates could mean that savings accounts and CDs are likely to do better at providing income than they have in recent years.

Also, bonds don't respond uniformly to interest rate changes. The differences, or spreads, between the yields of various types of debt can mean that some bonds may be under- or overvalued compared to others. Depending on your risk tolerance and time horizon, there are many ways to adjust a bond portfolio to help cope with rising interest rates. However, don't forget that a bond's total return is a combination of its yield and any changes in its price; bonds seeking to achieve higher yields typically involve a higher degree of risk.

Finally, some troubled economies overseas have been forced to lower interest rates on their sovereign bonds in an attempt to provide economic stimulus. Lower rates abroad have the potential to make U.S. debt, particularly Treasury securities (whose timely payment of interest and principal is backed by the full faith and credit of the U.S. Treasury), even more attractive to foreign investors. Though past performance is no guarantee of future results, that's what happened during much of 2014. Increased demand abroad might help provide some support for bonds denominated in U.S. dollars.

Remember that bonds are subject not only to interest rate risk but also to inflation risk, market risk, and credit risk; a bond sold prior to maturity may be worth more or less than its original value. All investing involves risk, including the potential loss of principal, and there can be no guarantee that any investing strategy will be successful.



How can I try to manage the impact of an interest rate hike?

With higher interest rates a distinct possibility in 2015, you may want to think about whether the bond portion of your portfolio is positioned appropriately given your time horizon and risk tolerance. One factor you might consider is which types of bonds may be most vulnerable to a rate hike.

Some investors forget that a bond's principal value may fluctuate with market conditions. When interest rates rise, longer-term bonds may feel a greater impact than those with shorter maturities. When interest rates are rising, bond buyers may be reluctant to tie up their money for longer periods if they anticipate higher yields in the future. The longer a bond's term, the greater the risk that its yield may eventually be superseded by that of newer bonds.

High-yield bonds (also known as junk bonds) may be affected disproportionately because they involve greater risk. Issuers must pay those higher yields because they are seen as having a greater risk of default, especially if a company already has a high debt burden and/or a relatively short history of successful debt repayment, or is otherwise on shaky financial footing. Investors may be reluctant to purchase risky debt if they foresee receiving a comparable yield from an issuer seen as more trustworthy.

Bonds redeemed prior to maturity may be worth more or less than their original value; however, if you hold a bond to maturity, you would suffer no loss of principal unless the issuer defaults. Bond investments also may be laddered. This involves buying a portfolio of bonds with varying maturities; for example, a five-bond portfolio might be structured so that one of the five matures each year for the next five years. As each bond matures, you might be able to reinvest the proceeds in an instrument that carries a higher yield.

Don't forget that all investing involves risk, including the potential loss of principal, and there can be no guarantee that any investing strategy will be successful. In addition to interest rate risk, bonds also face credit risk, inflation risk, and market risk.

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Financial Habits And Net Worth

What does it take to achieve financial prosperity?

You already know that our financial habits determine our financial fate. If we avoid credit card debt, spend less than we earn and create a financial buffer against the unexpected, we tend to thrive financially. If we carry a lot of debt or live constantly on the edge, with little savings, then our financial future is much cloudier.

Recently, a paper published by the Federal Reserve Bank of St. Louis proved these truisms in the real world. For eight individual years between 1992 and 2013, the Fed's Survey of Consumer Finances has posted a series of financial questions to thousands of people in all walks of life, at all income levels and ages. Among them:

1) Did you save any money last year?
2) Did you miss any loan or mortgage payments in the last year?
3) Did you have a balance on your credit card after the last payment was due?
4) Do liquid assets make up at least 10% of the value of your total assets?
5) Is your total debt service—the cash you devote each month to paying principal and interest—less than 40% of your income?

The paper scored the answers, giving every positive answer (yes for 1, 4 and 5, no for 2 and 3) one point, assigning zero points to the "wrong" answers. Then they added up the scores for each household and looked at a financial health score taken from the same survey, and compared the two. They found what you would probably expect: that good financial habits are highly correlated with the accumulation of wealth. A small chart at the back of the study, which divided people according to age and ethnic profile, found that individuals who averaged a score of 2.63 had a median net worth of $25,199, while those who averaged a 3.79 score enjoyed a median net worth in excess of $800,000. The average score: 3.01, associated with a net worth somewhere in the $70,000 to $75,000 range, which happens to fall neatly in between the median for people age 35-44 ($51,575) and those age 45-54 ($98,350).

How Corporate Buybacks Are Driving Stock Prices

The invisible force behind the bull market

The U.S. stock market has delivered positive returns to investors for six consecutive years, and in five of those years, the returns were in the double-digits. Aggregate revenues and profits have soared to record levels and grown much faster than the slow growth of the underlying economy. Each month, the S&P 500 tests new record highs, while the underlying economy putters along at 2-3% growth rates.

How is that possible, since America's corporations, to a large extent, ARE America's economy?

One answer is share buybacks. These are exactly what they sound like: a company uses some of its extra cash to buy back outstanding shares of its own stock. Or, in many cases recently, companies issue bonds in the current low-interest-rate environment and use the cheap money to make aggressive stock purchases.

Big picture, there are two ways for a company to give back some of its profits to shareholders. The most straightforward is to return some of that money in the form of dividends which, if "qualified", receives preferential tax treatment.

Buying back stock is the other alternative. A share buyback reduces the number of shares available to be purchased. This, in turn, raises the average revenues and profits per share. It also reduces the supply of stock available to investors, which tends to raise demand for increasingly scarce shares. The total number of shares outstanding for all S&P 500 firms, after rising dramatically from around 1990 to around 2005, has gone into an unprecedented decline over the last 10 years.

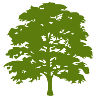
Fewer shares, and higher earnings per share, both tend to cause the price of a stock to go up, even if the company isn't any more profitable than it was before. This explains what would otherwise be a mathematical anomaly: how stocks and profits per share can rise faster than the economic growth of the country as a whole.

Arguably, this is a more efficient way to return money to investors than simply writing a dividend check. When the stock goes up, it generates capital gains for long-term (more than 12 months) investors in the stock, and these capital gains are taxed at preferential levels of 0% for lower income earners, up to 20% for those in the 39.6% bracket. Better yet, these capital gains can be deferred until the investor sells the stock. They might even be deferred into a year when the investor is in a lower tax bracket.

Over the last 33 years, companies have tended to pay slightly lower dividends as a percentage of net income, and have dramatically raised the amount they're spending to buy their own stock. In fact, during the long bull market following the Great Recession, the largest buyer of stocks, in aggregate, has actually been Corporate America itself.

The numbers are pretty dramatic. In 2013, the companies listed in the S&P 500 index spent $478 billion on share repurchases, a 24% increase over 2012. Last year, that figure rose to an estimated $565 billion. In 2007 and 2008, companies, in aggregate, managed to pay out, in total, more than they earned—borrowing some of the money that they returned to shareholders.

Is this borrowing-to-buy-your-own-stock activity sustainable in the long-term? Probably not. When interest rates rise, companies will almost certainly slow down their debt issuance, and some of the money funding share buybacks will no longer be available. By then, however, the economy may be in full recovery, and companies won't need to buy their shares in order to keep their stock prices on an uptrend. Then all of us will go back to a more normal relationship between growth of the economy and growth of our investments.



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Protecting Yourself From Identity Theft

Some of the best ways to safety are free and relatively easy.

We're hearing a lot more about identity theft these days—from hackers stealing credit card numbers from big banks and retail stores to individuals opening up credit card or bank accounts in your name, which they can use to write bad checks or make expensive purchases. Criminal identity thieves may also take out a loan in your name for a car or even a house, and some have managed to receive Social Security benefits or tax refunds that rightfully belong to others.

In some cases, when arrested for some other crime, hackers have helpfully provided a victim's name to the arresting officers, showing the police a falsified driver's license with that person's number and their picture. They post bail and skip town. When their victim doesn't show up for a court date he was never informed of, he could be arrested.

How do you protect yourself?

According to the National Crime Prevention Council, the biggest threats are coming from places that might surprise you. A study by Javelin Strategy and Research found that most identity thefts were taking place offline, where someone managed to steal your credit cards, or found social security information or credit card information in a dumpster, or filed bogus change of address forms to divert a victim's mail to their address, where they can gather personal and financial data at their leisure.

Even more surprising, 43% of all identity thefts were committed by someone the victim knows.

An organization called IdentityTheft.net estimates that over 10 million people are victimized by identity theft each year, although that number may be boosted by the aforementioned mass hacking incidents.

The Council and an organization called IdentityTheft.net say that you do a reasonable job of protecting yourself by taking a few common sense steps that make it much harder for someone to make purchases in your name or withdraw funds from your accounts.

1. First, never give out your Social Security number, and don't carry your social security card, birth certificate or passport around with you.
2. Copy your credit cards and your driver's license, and put the data in a safe place, to ensure you have the numbers if you need to call the companies.
3. When you use a credit card to buy something in a retail store, take the extra copy of the receipt with you and shred it.
4. Create complicated passwords for your online bank and investment accounts, and don't write them down on hard copy paper. Try not to use the same password for every website you access. (Can't remember 50 complicated passwords? A free program called LastPass lets you save all your user names and passwords in an encrypted format, so you only have to remember a single strong pass phrase. You can also store security questions and answers.)
5. Don't let anyone look over your shoulder when you're using an ATM machine.
6. Be skeptical of websites that offer prizes or giveaways.

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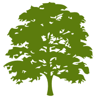
7. Tell your children never to give out their address, telephone number, password, school name or any other personal information.
8. Make sure you have a virus and spyware protection program on your computer, and keep it updated.
9. Check your account balances regularly to make sure no unexplained transactions have occurred.

These simple precautions will keep you safe from many of the criminal efforts to hack into your life. If you feel like you need additional protection, there are a variety of protection services on the marketplace, which basically all do the same thing: they regularly monitor your credit scores, looking for changes and odd debts that might be a clue that someone has stolen your identity, and check public record databases to see if your personal information is compromised. Some will prevent preapproved credit card offers from being sent to your mailbox, patrol the black market internet where thieves buy and sell credit card numbers, and the fancier services will provide lost wallet protection, identity theft insurance and keystroke encryption software.

Which are the best? A research organization called NextAdvisor has recently evaluated and ranked eight of these services, with costs ranging from $20 a month down to $7 a month. The top rated was IdentityGuard (premium service price: $19.99 a month) which offers the most compete protection, including the aforementioned fancier services. But seven of the protection systems, including TrustedID, AARP (a white-labeled version of TrustedID), LifeLock Ultimate, PrivacyGuard, IDFreeze and LegalShield all received good ratings; only Experian's ProtectMyID was negatively reviewed for being expensive and only monitoring one credit reporting service.

Do you really NEED these services? Possibly not. However, with the growing publicity around identity theft, these firms have become very aggressive in their marketing efforts. What they don't tell you is that you can do many of the things they do on your own. Every quarter, you can review one of your credit bureau reports for free, or—and this is easier—simply look at your statements and balances every day. The more sophisticated services are a fancy replacement for promptly notifying your bank when a credit card is lost or stolen, or when a strange charge shows up because Citibank or the Target department store was using weak security protocols.

In the near future, as more transactions take place using thumb prints or other biometric security data, we may look back on this period as the Wild West of data security, a strange unsettling time when people had to worry about their lives being hacked by strangers. Your goal is to arrive safely, unhacked, at that more secure period in our cultural evolution.



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The Swiss Franc And Your Portfolio

A European country has dropped its peg with the Euro. So what?

You may have read about the recent drop in the global (and U.S.) stock markets, as a result of the "shocking" announcement by the Swiss central banking authority that it would not force the Swiss franc to trade at 1.2 euros. Be prepared to be shocked: you can now buy a Swiss franc with a euro.

If you're like most of us, you've probably wondered why this shocking development would have anything to do with the enterprise value of the individual companies that make up the various global indices. What's the story here?

The story is actually pretty simple—and surprisingly, isn't being told very clearly in the press. The Swiss National Bank had been artificially holding the Swiss franc at 1.2 euros for the past three years. Why? Because the value of the euro has been sinking on global markets. A lower euro means everything manufactured in the Eurozone is less expensive for outside buyers, which is great for exports. By keeping the franc at a steady cost vs. the euro, the Swiss National Bank was protecting Swiss watches, chocolate products and high-end medical diagnostic equipment from becoming more expensive in the countries where Switzerland does most of its export business.

This policy suddenly became more difficult, in part because the European Central bank is expected to announce, on January 22, what economists delicately call "monetary easing"—buying government bonds, lowering interest rates, and giving banks and corporations more access to more euros. The inevitable result would be a lower euro compared to other currencies. Every time the Swiss Central Bank buys euros and sells francs, it is putting money in the pockets of global currency traders and a variety of hot money speculators who have bet that the Swiss will continue their policy. These traders would have reaped a huge windfall if the euro dropped and the bank continued to fight an increasingly expensive battle to maintain parity. The effect would have been a transfer of billions of dollars from Swiss taxpayers to shady speculators.

But why does any of this affect the value of U.S. stocks, or stocks in Europe, for that matter? Why were floor traders on the New York Stock Exchange experiencing what one described as 'once-in-a-career' market turbulence, and others described as a 'massive flight to safety?' Certain exporting companies in Switzerland will be negatively affected and have to adjust their profit margins downward to stay competitive. But U.S. companies aren't selling their goods and services abroad in Swiss francs, and European companies will be slightly more competitive, globally, after the expected monetary easing announcement.

The only answer that makes any sense is that hot money traders dislike any kind of surprises, and they hit the "sell" button whenever they're startled by news that they didn't anticipate. Then they wait until they have a better understanding of what's going on. And, since these short-term traders make up a majority of all the actual buys and sells, the markets to trade lower even though no fundamental economic reason exists for them to.

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This provides a great opportunity for all of us to see the difference between short-term headline moves in the market and long-term fundamental shifts. Make a note to, a month from now, see if you still remember the fact that the Swiss central bank is no longer supporting the franc against the euro. At the same time, look to see if any major shift has occurred in the business operations or profitability of U.S. companies due to this adjustment in currency values overseas.

There will be consequences. Over the coming months, you might have to pay a little more for a Swiss watch, and chocolate manufactured in Switzerland might be pricier as well. You will want to steer clear of parking your money in the Swiss central banking system, which is now paying an interest rate of negative three quarters of a percent. If you're a global options trader who took the wrong side of the bet, this was terrible news for your returns this year. But the underlying value of the stocks in a diversified investment portfolio aren't likely to become less valuable based on the latest trading price of options denominated in Swiss francs.