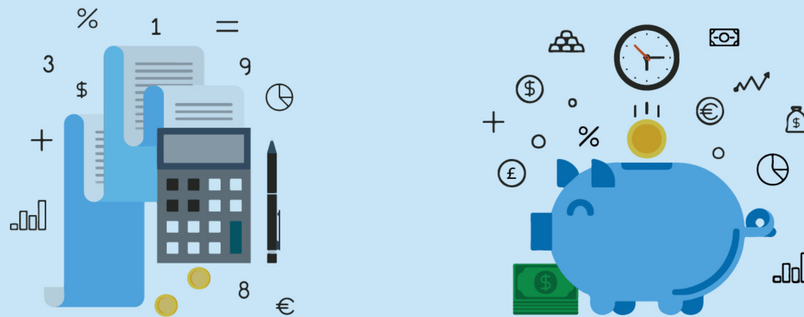

Saturday, September 17, 2016

Ask the Experts: Financial FAQs (Fall 2016)

In the fall issue, we address reader questions about how to make the most out of open enrollment season at work, year-end tax planning, and expectations for the stock and bond markets in the years ahead.

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Q. It is time for open enrollment at work. What should I be thinking about as I make my benefit elections for the new year?

A. The 2016 Aflac WorkForces Report found that 93 percent of employees choose the same benefits year after year, even when the benefits themselves change — sometimes significantly. The same study found that 57 percent of employees spent less than 30 minutes making open enrollment benefit decisions.

These are shocking statistics considering that the choices you make during your employer's open enrollment period can affect almost every aspect of your financial life. The benefit elections you make impact everything from retirement planning to life, health, and disability insurance to tax and estate planning — so don't take them lightly. Some of the questions you may need to address include:

- Am I taking full advantage of my employer's retirement plan?
- Should I be making Roth contributions?
- Are my beneficiaries up to date?
- Should I be using our health savings account (HSA) or flexible spending accounts (FSAs)?
- Do I need more life or disability insurance?
- Are there new benefits that I should consider using?

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- Am I withholding enough in taxes?

Make no mistake: open enrollment is a major event. Take the time to review and analyze your options every year and consult your professional advisors as needed.

Q. We are coming up on the end of the year. Are there any tax-planning ideas that I should consider?

A. While many investors believe their taxable income is out of their control, they can often exert some control with the help of their tax and financial advisors. Taking advantage of small tax-planning tactics can have a cumulative effect and may generate significant savings in the long term.

Reduce Taxable Income: Selling investments with unrealized losses this year is one way to reduce taxable income. Several sectors of the equity market, such biotechnology stocks, may present tax-loss-harvesting opportunities in 2016, but please consult your tax advisor about wash sale rule considerations before taking action.

Gifting to charitable organizations is another strategy for reducing taxable income at the end of the year. Pre-funding planned charitable gifts may considerably reduce taxable income. And don't restrict your thinking to gifts of cash. You may want to explore gifting appreciated securities as a way to both reduce income and avoid realizing gains.

Increase Taxable Income: Despite being counterintuitive, increasing income in a given tax year may actually create tax savings in the long run if executed properly. This could be the case if you are in an abnormally low tax bracket this year, expect higher taxable income next year, or expect the sale of a business or a low-cost-basis asset in a future tax year.

You may want to pull taxes forward by selling securities with unrealized gains—perhaps stocks or estate investment trusts that you have held for several years. And if you are years away from retirement, consider converting some or all of a traditional individual retirement account (IRA) to a Roth IRA. This can benefit investors who expect higher tax rates — or who expect to be in a higher tax bracket — when they retire. While you must pay income taxes on the converted amount, funds in the Roth IRA will grow and can be withdrawn tax free so long as you wait five years and are at least 59½ years of age.

Tax planning hasn't become more fun in recent years, but it has become more important. Tax rates, especially for high earners, have gone up — bringing tax management back into vogue. As always, please consult your tax and financial advisors for help.

Q. Despite the doom-and-gloom predictions of many pundits, stocks and bonds have done pretty well this year. What do you see going forward?

A. While returns for both stocks and bonds have been strong since the financial crisis (not just this past year), investors should prepare themselves for underwhelming results over the next few years. They may have to take more risk to achieve the level of returns to which they have become accustomed.

Stocks: Analysis of price-to-earnings (P/E) ratios is one way to estimate future returns. While it is a poor predictor of one-year returns, P/E is more reliable for longer periods. Our analysis of the P/E ratios for U.S. large-capitalization stocks (as measured by the Standard & Poor's 500 Index) and their subsequent 10-year returns since 1970 suggests that investors should expect annual average returns in the mid-to-high single digits. This rough measure is in line with CAPTRUST's forecast 6.9 percent return for large-cap stocks over the next five to seven years.

Bonds: The 10-year U.S. Treasury yield has proven to be a reliable proxy of future fixed income returns, especially high-quality, investment-grade bond returns. With the 10-year Treasury yielding 1.6 percent (at the end of September), we believe investors should expect low-single-digit returns from their bonds in coming years. Over the

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next five to seven years, CAPTRUST forecasts an annual return of 2.8 percent for U.S.core fixed income.

Have questions? Need help? Call the CAPTRUST Advice Desk at 800.967.9948 or schedule an appointment with a retirement counselor today.