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Hi Everyone,

Summer is now in full swing and the 4th of July holiday is already behind us. It's strange how time in the summer goes so much quicker than time in the winter. Hopefully you still have many great outdoor activities planned to do all the things we say we wish we could do when there is snow on the ground.

Hopefully these articles will provide some insight, or maybe raise a few questions. If you have questions or concerns regarding your situation, please don't hesitate to call. As always, if I can be of help to you or anyone you care about, please let me know.

Thank you!

Steve

July 2016

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Information to chew on...

Investors Are Human, Too

In 1981, the Nobel Prize-winning economist Robert Shiller published a groundbreaking study that contradicted a prevailing theory that markets are always efficient. If they were, stock prices would generally mirror the growth in earnings and dividends. Shiller's research showed that stock prices fluctuate more often than changes in companies' intrinsic valuations (such as dividend yield) would suggest.[1]

Shiller concluded that asset prices sometimes move erratically in the short term simply because investor behavior can be influenced by emotions such as greed and fear. Many investors would agree that it's sometimes difficult to stay calm and act rationally, especially when unexpected events upset the financial markets.

Researchers in the field of behavioral finance have studied how cognitive biases in human thinking can affect investor behavior. Understanding the influence of human nature might help you overcome these common psychological traps.

Herd mentality

Individuals may be convinced by their peers to follow trends, even if it's not in their own best interests. Shiller proposed that human psychology is the reason that "bubbles" form in asset markets. Investor enthusiasm ("irrational exuberance") and a herd mentality can create excessive demand for "hot" investments. Investors often chase returns and drive up prices until they become very expensive relative to long-term values.

Past performance, however, does not guarantee future results, and bubbles eventually burst. Investors who follow the crowd can harm long-term portfolio returns by fleeing the stock market after it falls and/or waiting too long (until prices have already risen) to reinvest.

Availability bias

This mental shortcut leads people to base judgments on examples that immediately come to mind, rather than examining alternatives. It may cause you to misperceive the likelihood or frequency of events, in the same way that watching a movie about sharks can make it seem more dangerous to swim in the ocean.

Confirmation bias

People also have a tendency to search out and remember information that confirms, rather than challenges, their current beliefs. If you have a good feeling about a certain investment, you may be likely to ignore critical facts and focus on data that supports your opinion.

Overconfidence

Individuals often overestimate their skills, knowledge, and ability to predict probable outcomes. When it comes to investing, overconfidence may cause you to trade excessively and/or downplay potential risks.

Loss aversion

Research shows that investors tend to dislike losses much more than they enjoy gains, so it can actually be painful to deal with financial losses.[2] Consequently, you might avoid selling an investment that would realize a loss even though the sale may be an appropriate course of action. The intense fear of losing money may even be paralyzing.

It's important to slow down the process and try to consider all relevant factors and possible outcomes when making financial decisions. Having a long-term perspective and sticking with a thoughtfully crafted investing strategy may also help you avoid expensive, emotion-driven mistakes.

***Note:** All investments are subject to market fluctuation, risk, and loss of principal. When sold, investments may be worth more or less than their original cost.*

1 *The Economist,* "What's Wrong with Finance?" May 1, 2015

2 *The Wall Street Journal,* "Why an Economist Plays Powerball," January 12, 2016

Q&As on Roth 401(k)s

Which is the better option, pretax or Roth contributions?

The answer depends upon your personal situation. If you think you'll be in a similar or higher tax bracket when you retire, Roth 401(k) contributions may be more appealing, since you'll effectively lock in today's lower tax rates. However, if you think you'll be in a lower tax bracket when you retire, pretax 401(k) contributions may be more appropriate. Your investment horizon and projected investment results are also important factors.

The Roth 401(k) is 10 years old! With 62% of employers now offering this option, it's more likely than not that you can make Roth contributions to your 401(k) plan.[1] Are you taking advantage of this opportunity?

What is a Roth 401(k) plan?

A Roth 401(k) plan is simply a traditional 401(k) plan that permits contributions to a designated Roth account within the plan. Roth 401(k) contributions are made on an after-tax basis, just like Roth IRA contributions. This means there's no up-front tax benefit, but if certain conditions are met both your contributions and any accumulated investment earnings on those contributions are free of federal income tax when distributed from the plan.

Who can contribute?

Anyone! If you're eligible to participate in a 401(k) plan with a Roth option, you can make Roth 401(k) contributions. Although you cannot contribute to a Roth IRA if you earn more than a specific dollar amount, there are no such income limits for a Roth 401(k).

Are distributions really tax free?

Because your contributions are made on an after-tax basis, they're always free of federal income tax when distributed from the plan. But any investment earnings on your Roth contributions are tax free only if you meet the requirements for a "qualified distribution."

In general, a distribution is qualified if:

- It's made after the end of a five-year holding period, *and*
- The payment is made after you turn 59½, become disabled, or die

The five-year holding period starts with the year you make your first Roth contribution to your employer's 401(k) plan. For example, if you make your first Roth contribution to the plan in December 2016, then the first year of your five-year holding period is 2016, and your waiting period ends on December 31, 2020. Special rules apply if you transfer your Roth dollars over to a new employer's 401(k) plan.

If your distribution isn't qualified (for example, you make a hardship withdrawal from your Roth account before age 59½), the portion of your distribution that represents investment earnings will be taxable and subject to a 10% early distribution penalty, unless an exception applies. (State tax rules may be different.)

How much can I contribute?

There's an overall cap on your combined pretax and Roth 401(k) contributions. In 2016, you can contribute up to $18,000 ($24,000 if you are age 50 or older) to a 401(k) plan. You can split your contribution between Roth and pretax contributions any way you wish. For example, you can make $10,000 of Roth contributions and $8,000 of pretax contributions. It's totally up to you.

Can I still contribute to a Roth IRA?

Yes. Your participation in a Roth 401(k) plan has no impact on your ability to contribute to a Roth IRA. You can contribute to both if you wish (assuming you meet the Roth IRA income limits).

What about employer contributions?

While employers don't have to contribute to 401(k) plans, many will match all or part of your contributions. Your employer can match your Roth contributions, your pretax contributions, or both. But your employer's contributions are always made on a pretax basis, even if they match your Roth contributions. In other words, your employer's contributions, and any investment earnings on those contributions, will be taxed when you receive a distribution of those dollars from the plan.

Can I convert my existing traditional 401(k) balance to my Roth account?

Yes! If your plan permits, you can convert any portion of your 401(k) plan account (your pretax contributions, vested employer contributions, and investment earnings) to your Roth account. The amount you convert is subject to federal income tax in the year of the conversion (except for any after-tax contributions you've made), but qualified distributions from your Roth account will be entirely income tax free. The 10% early-distribution penalty generally doesn't apply to amounts you convert.[2]

What else do I need to know?

Like pretax 401(k) contributions, your Roth contributions can be distributed only after you terminate employment, reach age 59½, incur a hardship, become disabled, or die. Also, unlike Roth IRAs, you must generally begin taking distributions from a Roth 401(k) plan after you reach age 70½ (or, in some cases, after you retire). But this isn't as significant as it might seem, because you can generally roll over your Roth 401(k) money to a Roth IRA if you don't need or want the lifetime distributions.

[1] Plan Sponsor Council of America, *58th Annual Survey of Profit Sharing and 401(k) Plans* (2015) (Reflecting 2014 Plan Experience)

[2] The 10% penalty tax may be reclaimed by the IRS if you take a nonqualified distribution from your Roth account within five years of the conversion.

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Market losses on the front end of your retirement could have an outsized effect on the income you might receive from your portfolio.

Be Prepared to Retire in a Volatile Market

In an ideal world, your retirement would be timed perfectly. You would be ready to leave the workforce, your debt would be paid off, and your nest egg would be large enough to provide a comfortable retirement--with some left over to leave a legacy for your heirs.

Unfortunately, this is not a perfect world, and events can take you by surprise. In a survey conducted by the Employee Benefit Research Institute, only 44% of current retirees said they retired when they had planned; 46% retired earlier, many for reasons beyond their control.[1] But even if you retire on schedule and have other pieces of the retirement puzzle in place, you cannot predict the stock market. What if you retire during a market downturn?

Sequencing risk

The risk of experiencing poor investment performance at the wrong time is called sequencing risk or sequence of returns risk. All investments are subject to market fluctuation, risk, and loss of principal--and you can expect the market to rise and fall throughout your retirement. However, market losses on the front end of your retirement could have an outsized effect on the income you might receive from your portfolio.

If the market drops sharply before your planned retirement date, you may have to decide between retiring with a smaller portfolio or working longer to rebuild your assets. If a big drop comes early in retirement, you may have to sell investments during the downswing, depleting assets more quickly than if you had waited and reducing your portfolio's potential to benefit when the market turns upward.

Dividing your portfolio

One strategy that may help address sequencing risk is to allocate your portfolio into three different buckets that reflect the needs, risk level, and growth potential of three retirement phases.

Short-term (first 2 to 3 years): Assets such as cash and cash alternatives that you could draw on regardless of market conditions.

Mid-term (3 to 10 years in the future): Mostly fixed-income securities that may have moderate growth potential with low or moderate volatility. You might also have some equities in this bucket.

Long-term (more than 10 years in the future): Primarily growth-oriented investments such as stocks that might be more volatile but have higher growth potential over the long term.

Throughout your retirement, you can periodically move assets from the long-term bucket to the other two buckets so you continue to have short-term and mid-term funds available. This enables you to take a more strategic approach in choosing appropriate times to buy or sell assets. Although you will always need assets in the short-term bucket, you can monitor performance in your mid-term and long-term buckets and shift assets based on changing circumstances and longer-term market cycles.

If this strategy appeals to you, consider restructuring your portfolio before you retire so you can choose appropriate times to adjust your investments.

Determining withdrawals

The three-part allocation strategy may help mitigate the effects of a down market by spreading risk over a longer period of time, but it does not help determine how much to withdraw from your savings each year. The amount you withdraw will directly affect how long your savings might last under any market conditions, but it is especially critical in volatile markets.

One common rule of thumb is the so-called 4% rule. According to this strategy, you initially withdraw 4% of your portfolio, increasing the amount annually to account for inflation. Some experts consider this approach to be too aggressive--you might withdraw less depending on your personal situation and market performance, or more if you receive large market gains.

Another strategy, sometimes called the endowment method, automatically adjusts for market performance. Like the 4% rule, the endowment method begins with an initial withdrawal of a fixed percentage, typically 3% to 5%. In subsequent years, the same fixed percentage is applied to the remaining assets, so the actual withdrawal amount may go up or down depending on previous withdrawals and market performance.

A modified endowment method applies a ceiling and/or a floor to the change in your withdrawal amount. You still base your withdrawals on a fixed percentage of the remaining assets, but you limit any increase or decrease from the prior year's withdrawal amount. This could help prevent you from withdrawing too much after a good market year, while maintaining a relatively steady income after a down market year.

Note: *Asset allocation is a method used to help manage investment risk; it does not guarantee a profit or protect against investment loss.*

[1] Employee Benefit Research Institute, "2016 Retirement Confidence Survey"

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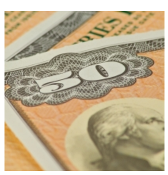

How many types of government savings bonds are there, and what's the difference between them?

While the U.S. government has issued 13 types of savings bonds, there are currently only two series available for purchase through the U.S. Treasury Department: Series EE bonds and Series I bonds. U.S. savings bonds are nonmarketable securities, which means you can't resell them unless you're authorized as an issuing or redeeming agent by the U.S. Treasury Department. Savings bonds are guaranteed by the federal government as to the timely payment of principal and interest.

You can buy Series EE bonds and I bonds in any amount from $25 up to $10,000, which is the maximum amount you can purchase for each bond type per calendar year. In other words, you may buy a total of $10,000 annually in both EE and I bonds, for an annual total of $20,000 for the two types combined.

Series EE bonds earn a fixed rate of interest as long as you hold them, up to 30 years. You'll know the interest rate the bond will earn when you buy it. The U.S. Treasury announces the rate each May 1 (for new EE bonds issued between May 1 and October 31) and November 1 (for new EE bonds issued between November 1 and April 30).

Series I bonds are similar to EE bonds, but I bonds offer some protection against inflation by paying interest based on a combination of a fixed rate and a rate tied to the semi-annual inflation rate. The fixed rate component doesn't change, whereas the rate tied to inflation is recalculated and can change every six months. The total interest (fixed and inflation adjusted) compounds semi-annually.

In any case, the interest on EE or I savings bonds isn't paid to you until you cash in the bonds. You can cash in EE bonds or I bonds any time after one year, but if you cash them out before five years, you lose the last three months of interest.

The interest earned on both EE and I bonds is generally exempt from state income tax but subject to federal income tax. Interest income may be excluded from federal income tax when bonds are used to finance higher-education expenses, although restrictions may apply.