CURRENTS
SPRING 2019

A NOTE FROM JILL

While the New Year is off to a benevolent start, in sharp contrast with December's extreme volatility, we remain watchful of the uncertainties that caused the market dip in the 4th quarter of 2018. Some of the events contributing to the market highs and lows have seen progress towards resolution, while others remain variable with a potentially profound impact to markets and market sentiment. Given the exacerbating impact of sentiment on market movements, we remain guarded in our outlook for stocks for 2019 despite their healthy rebound virtually across the board.

While it is impossible to predict the end of a market cycle or a correction with certainty, over the past year and a half we have been taking steps to position portfolios for increased volatility. At the same time, it is important that each of our clients understands the risks inherent in the equity markets and are comfortable that their target allocation to stocks is appropriate given their investment horizon, risk tolerance, and individual goals. Market volatility, while uncomfortable to many, also presents opportunity. We have taken this opportunity to introduce more active management into our portfolios in areas of the investment space where they have the potential to add value particularly in turbulent markets: emerging markets and smaller company stocks. You can read more about the diligent process we follow in selecting managers in "The Science and Art of Creating Your Investment Portfolio" on page 3 of this newsletter.

A solid financial plan, an appropriate investment allocation and high quality investments are the cornerstones of a successful investment strategy. Equally important is the discipline to stay invested through market cycles. While it may not always be comfortable, time has shown that staying the course is the best way for you to meet your long term goals. We are here to help you accomplish those goals in any way we can.

Jill

Jill Fopiano, CFA, CFP®
President, CEO, and CIO

ANNUITY OPTIONS AND 1035 EXCHANGES

By Tim Pilczak

Annuities receive and deserve plenty of attention. They are complicated, come in many shapes and sizes, and differ greatly from issuing company to issuing company. In many cases they are misunderstood, and in some cases they are unfairly portrayed. High fees, commissions, and lack of transparency are frequently some of the disadvantages, but in the right circumstance annuities offer advantages as well. When thoughtfully implemented into a client's financial plan, annuities can provide guaranteed income that can remediate potential shortfalls in future cash flow.

Not all annuities are bad.

While many annuity products have an appropriate place in one's financial plan, the focus of this article is on those annuities that no longer make sense, or perhaps never did in the first place.

Our job as financial advisors is to work with clients to conduct an annuity review - to analyze the details of a particular annuity and present a better understanding of how the annuity contract works. 'I'm not sure why I bought this, and I'm not sure why I still own it' or 'I don't understand how this works' are frequent comments we have received. In many cases these annuities were bought at some point in time and never reviewed, which is not good for any investment. Regular monitoring of portfolios is critical to ensure long term goals remain on track.

In the case where a client wants to take action to dissolve the existing annuity contract there are many, often conflicting considerations. Depending on the type of annuity, taxes can be a big hurdle. The growth in certain annuity contracts is taxed at ordinary income tax rates rather than the capital gains tax rate you might experience on other after tax investments. In addition, the gains may need to be withdrawn from the contract before you can access the initial investment amount. This oftentimes puts a client into a situation where they have to decide whether to keep a contract they no longer want, or pay a potentially large tax bill.

One potential option is a 1035 exchange. A 1035 exchange is defined by an IRS rule allowing a tax-free transfer of an existing annuity contract, life insurance policy, long-term care insurance policy, or endowment, for a solution of like kind. Using this option a client may continue to retain the tax deferral and other benefits of an annuity contract while exchanging an old contract for a more cost effective, transparent policy. There are explicit tax rules and guidelines that apply to 1035 exchanges to receive the tax benefits, and it is important to be aware of these before taking any action.

> **"When thoughtfully implemented into a client's financial plan, annuities can provide guaranteed income that can remediate potential shortfalls in future cash flow."**

As fiduciaries, the ideal outcome of an annuity review that we conduct is to help a client feel confident about their investments, including any annuity products they may hold. We enter the analysis unbiased as to whether the annuity contract remains in place, is exchanged or is dissolved. Our goal is to provide guidance and clarity to make sure the investment provides the highest possible quality at the most reasonable cost.

If you have questions about annuities, or an annuity contract that you would like us to review, please reach out to your O'Brien Advisor.

Tim Pilczak, CFP®
Advisor

DID YOU KNOW?

O'Brien Planning Dashboard

Over the past year, we have invested in a client-focused planning platform that allows our advisors to work with clients in a more dynamic way. Advisors are able to illustrate a range of financial planning scenarios in real time to help clients think through a variety of financial questions. A few of the key benefits for our clients include:

1. Account aggregation: Clients can link outside accounts including checking accounts, savings accounts, and even college savings accounts. Additionally, clients can link liabilities including mortgages, home equity loans, student loans and credit cards. Aggregating all accounts on one platform allows clients to see a more complete snap shot of their overall financial picture.
2. Interactive projections: Whether you are sitting in our office or at home, our screen share function makes seeing your plan easier than ever.
3. Real-time data: Account balances are updated daily allowing clients to see current balances on all of their linked accounts and liabilities.
4. The Client Site – Usage: The client-specific site allows clients to log in and see their accounts, link new accounts, access O'Brien quarterly statements and explore the client-designed budgeting tools. The client site can be accessed on any device allowing you to view information at any time.
5. The Client Site – Secure Date Storage: The client-specific site allows clients to store, share and access secure documents. Storing estate documents or birth certificates, sharing tax returns or accessing advisor-run financial projections is made easy and secure through this feature.

Our Planning Dashboard is designed to give clients greater visibility to their financial plan and a way to connect all of the pieces of their financial picture. If you would like more information about the client site, please reach out to your O'Brien advisor. We are here to help and look forward to sharing this platform with you.

5 QUESTIONS ABOUT...CAPITAL GAINS AND LOSSES

By Lis Zimmerman

Throughout the year we receive many questions about the tax implications of the transactions we make in your portfolio. Just as you pay taxes on your earned income, taxes are also a necessary consequence of successful investment performance. Recognizing capital gains, and paying the resulting taxes, allows for rebalancing of your portfolio to your target, and also for taking some profits off the table when holdings perform well. We try to strike a balance between tax efficiency and adhering to our portfolio "best thinking" and gains are invariably part of that equation.

1. What is a capital gain or loss? There are two types of capital gains and losses on your investments. The first, a realized gain, occurs when a security is sold at a price greater than what it was purchased for. If the security is sold at a loss, that loss differential is a capital loss. The second, a capital gains distribution, occurs when a mutual fund distributes a capital gain even though you still own the fund. This will happen if the fund manager sells holdings within the fund at a gain, even when the fund as a whole may have declined in value. Any gains are distributed to the shareholders based on their percentage of ownership of the fund.

2. How are capital gains taxed? If the security was held for more than a year before it was sold, the gain is considered long term. Otherwise the gain is short term. This is true for both realized gains and capital gains distributions. Short term gains are taxed as ordinary income and long term gains are taxed at the long term capital gains tax rate which is either 0%, 15% or 20% depending on your adjusted gross income. Gains are also subject to state income taxes.

3. Why do I owe taxes on a fund that has declined in value? Capital gains distributions are taxed even though the shareholder continues to hold the fund. If the gain is reinvested the cost basis is increased by the amount of the distribution so that the gain is not taxed again when the fund is sold. It provides the advantage of spreading the tax burden from the gain over a longer period of time rather than paying a potentially larger tax at the time the fund is sold.

> "As portfolio managers, our goal is to create growth in your portfolio. That is how we increase your wealth."

4. What is tax loss harvesting? When the general market has declined, causing a fund to decline in value, we may sell your investment at a loss. We will then replace the fund with a substitute in the same asset category, and after a period of 30 days or more we will buy the original fund back. These losses can be used to offset capital gains, reducing the tax burden on any gains taken. We purchase the substitute fund, rather than holding cash, so that you remain invested and we are not timing the market. For many who were clients during the two most recent declines of 2000-2002 and 2008, you may remember that we realized many losses in your portfolios. These losses were used to offset gains once the market and your portfolios grew during the recovery periods. Because these losses do not have to be used in the year they were taken and can be carried forward until they are used up, many can offset their gains for a few years, easing their long term tax burden.

5. How should I view capital gains in my portfolio? As portfolio managers, our goal is to create growth in your portfolio. That is how we increase your wealth. Growth creates capital gains and you are taxed on the growth of your portfolio. The capital gains tax is currently lower than your income tax rate and therefore any growth in your portfolio is taxed at a lower rate than your earned income including wages, annuity income, pension income, and your required minimum distribution. During periods of economic growth there tend to be more capital gains that build up in the portfolio. We have the capability to create a capital gains budget for each client for two reasons. First, so that we take gains regularly to spread out a client's tax burden and second, so that clients may budget for any necessary estimated taxes. During periods of economic decline, we may have opportunities for tax loss harvesting.

We hope this gives you some perspective on the role of capital gains in your portfolio. If you have any further questions, please reach out to your O'Brien Wealth Partners Advisor.

Lis Zimmerman,
CFP®, CASL®, CRPC®

Senior Vice President, Client Relations & Financial Planning

Principal

SAVING ON TAXES: CHARITABLE CONTRIBUTIONS AND RMDS

By Cindy Kuppens

If you are age 70 ½ or older and take annual Required Minimum Distributions (RMDs) from your IRA, and you also make charitable contributions each year, you may be able to save on your federal taxes when you make a Qualified Charitable Distribution (QCD) directly from your IRA. Depending on where you live, you may also save on state taxes.

Required Minimum Distributions from a pre-tax traditional, rollover, SIMPLE, or SEP- IRA are generally taxable to you as ordinary income. In addition, the taxable distribution amount counts as income for purposes of determining your Medicare Part B premium. For some who have a significant RMD each year, the increase in the Medicare Part B premium can be material. This, combined with the disappearance of itemized deductions for most filers, has increased taxes for some.

However, if you make a Qualified Charitable Contribution **directly from your IRA**, the amount of the distribution that is donated to a qualified charity will not count as taxable income. Using this approach you will not be able to deduct your charitable contribution, but you will lower your taxable income and thus your overall tax burden. In addition, you will still be able to take advantage of the higher standard deduction under the recent tax law.

Following are the rules for Qualified Charitable Deductions:

- You must be 70 ½ or older.
- A QCD may be made from a traditional or Rollover IRA, an Inherited IRA, an inactive SEP plan or an inactive SIMPLE plan. (A SEP or SIMPLE plan is considered inactive if you are no longer making contributions to it.) Please note this does not include 401(k)s or 403(b)s.
- The maximum QCD amount is $100,000 per year (to one or more charities). If you are married, your spouse can make an additional $100,000 QCD from his or her IRA.
- You can contribute more than your RMD but the excess amount cannot be counted toward your RMDs in future years.
- The distribution must be made directly from your IRA custodian to the charity. Funds that are payable to you are not counted as a QCD.
- To qualify as a QCD, the distribution must be to a Section 501(c)(3) organization. Donor advised funds and private foundations do not qualify.
- You will receive 2019 1099R tax reporting on your distributions from your custodian in early 2020. Custodians will not differentiate a QCD from a taxable distribution.

If you have questions or would like to use your RMD to make a Qualified Charitable Donation, please call your O'Brien Advisor. We would be happy to talk with you about this process and the most efficient way to make your contribution.

Cindy Kuppens, CFP®, AEP®

Senior Vice President
Client Relations

Principal

THE SCIENCE AND ART BEHIND CREATING YOUR INVESTMENT PORTFOLIO

By Jill Fopiano

More than thirty years of investing across many market cycles has enabled us to carefully hone our investment process into the institutional-quality standard we follow today. While choosing good investments is a science that begins with quantitative data analysis, there is also an art to interpreting and screening the plethora of information available on the economy, the markets and the investments themselves. While we do our utmost to filter this information into risks and opportunities, we are smart enough to know what we do not know, and we continue to believe that a diversified portfolio of high quality investments will ultimately serve our clients best.

Our investment analysis begins broadly with the belief that stocks are the key driver of returns over the long run. There are areas of the market that may be more or less attractive at certain times given relative valuations, macroeconomic environments, geopolitical factors, and investment opportunities. The first question we ask is where are the risks that are worth taking given the potential rewards? These considerations help determine the tactical shifts we make in client portfolios; for example, how we weight U.S. stocks versus their global counterparts. We use the analogy of "dimmers and dials" to describe the materiality of these decisions. In keeping with our commitment to diversification they are tweaks around the margins rather than radical exits or doubling down. Once we have decided which asset categories, geographies or sectors present opportunity the challenge becomes selecting the right investment vehicles by which to gain access.

> "It is important to look at the investment landscape from both a quantitative and qualitative lens."

In the next level of our analysis we begin to narrow the thousands of available mutual funds and exchange traded funds (ETFs) from which we can choose to implement our investment thesis. The universe of investment options is expansive, with thousands of managers offering tens of thousands of funds in any area you can imagine (interestingly, you can even find ETFs that invest only in companies with the word "cat" in their name). Our goal is to narrow the universe to about 20-40 viable options. It is important to look at the investment landscape from both a quantitative and qualitative lens. We have created an expansive set of screening criteria to analyze the quantitative aspects of the funds. They provide both tools for focusing our research and useful information about the how different funds and ETFs might be expected to behave in our portfolios. We examine factors like long-term performance relative to a benchmark or the risk/return dynamics of different funds, keeping in mind that past performance is not necessarily an indicator of future results. We also take into account correlations, or how the investments may perform relative to one another, as overly correlated portfolios can add unnecessary risk. By comparing the investment philosophies and analyzing the outcomes of buy and sell decisions, we can learn more about the fund managers and their discipline. Do they jump ship quickly at the sign of bad times, or do they have the conviction to maintain core holdings even when all signs point south?

After the preliminary quantitative narrowing, we are left with only about 10-20% of the funds we began with. At this point, we apply a rigorous fundamental due diligence screening process. We really want to get to know the firms we are considering in depth, to ensure that they are who they represent themselves to be and that they are committed to the strategies they postulate. We screen the portfolio management team for tenure, depth, and breadth of analyst coverage, compensation metrics, and experience and knowledge. By looking into the operational side of the businesses, we gather information on whether the firm has the appropriate risk management tools in place, understand their compliance function, disaster recovery plans, and other aspects of their business management. By reviewing the funds' corporate structures, we can see how fees compare to competitors, get an understanding of whether they are a growing or contracting player in the market, and monitor any distractions that could impede their ability to serve our clients going forward, like a merger announcement or high turnover within the company itself.

After these assessments, our search is often narrowed down to less than 10 managers. We conduct extensive interviews with each firm with whom we invest, whether it means bringing them into our office or, more often, visiting theirs. This allows us to get a sense of the intangibles; their motivations and ideologies, their commitment to the organization, whether they have any skin in the game or whether they are just incentivized to sell. We can gain insights from these meetings to determine whether investment decisions are made as a team with challenges to leading opinions or whether groupthink rules the firm. These critically important unquantifiable factors can actually underpin the success or failure of a firm.

With all these components in mind, we then can select which fund fits our needs best. After receiving sign-off from our Chief Investment Officer, the fund is then presented to our internal Investment Committee for approval. A lot goes into choosing every fund for our firm, and deservedly so. We are entrusted with your assets, and we take the time to make sure our diligence is aggressively thorough, both when we add a fund to a portfolio and as we monitor our holdings on an on-going basis. As long-term, high quality investors, our investment team works diligently to ensure the investment choices made are the best available for our clients.

Jill Fopiano, CFA, CFP®

President, CEO, and CIO

TAKE A CLOSER LOOK...

How Can I Save More?

One of the most common questions we hear from clients is "How can I save more?" We understand it can be difficult to save when you have many competing goals.

Our experience has shown that the most successful savers are those who have a plan and don't rely solely on self motivation. If your strategy is to save what you haven't spent at the end of each month, your chance of failure is high. As Benjamin Franklin taught us, ***when you fail to plan, you plan to fail.***

Here are some steps that you can take to increase your savings.

Step One: *Identify your goals.* Are you saving for a house, your child's education, a vacation, retirement, or some combination of these? Prioritize each in order of importance.

Next, determine how much you'll need to save each month. You may want to use a savings goal calculator to set a monthly savings amount for each goal.

Step Two: *Create a budget.* There are many online budgeting tools to make it easier to track your spending. It is important to build in an expense for savings in your early working years. It never gets easier to save as you may always find a place to spend the extra income. Once savings is added to your budget, you can increase your savings as your income increases. You may have to make some difficult choices early but creating a budget is all about creating good spending habits. Financial wealth is not determined by how much you earn and spend; it's about how much you have saved.

Step Three: *Pay yourself first.* The easiest way to do this is to make savings automatic.

- For **retirement**, save into your employer's **401(k) or 403(b) plan**, where money is taken out of your paycheck and put into the plan automatically. If your employer matches your contribution make sure you contribute at least enough to receive the full match.
- If you are eligible to do so, contribute to a **Roth IRA**, which is a fabulous tool for saving. While you are taxed on the amounts you contribute, the gain on the contributions grows tax free. Again, you can make your saving automatic by having money deducted from your checking account each month to fund your Roth IRA account.
- If you are **saving for education**, open a **Section 529** savings account, and have your monthly savings amount deducted from your checking account.
- For **other savings goals** open a **savings or investment account**, or use an app to make your savings automatic.

Step Four: *Maintain, Monitor, and Stay Motivated!* Schedule time annually to review your budget and make needed adjustments. There are many blogs on budgeting and saving—you're sure to find a few that speak to you, and perhaps find a community of people online who are purposefully shaping their financial lives to meet their short and long term goals, finding balance between enjoying the here and now and saving to attain security and their life's dreams.

O'Brien WEALTH PARTNERS
ADVISORS | ANALYSTS | ADVOCATES

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INSIDE

O'BRIEN WEALTH PARTNERS

IN THE NEWS…

1. Congratulations to Whitney Van Hise who was recently promoted to Associate Advisor. Many of you know Whitney's smiling face and friendly voice! She has been a great addition to our firm and we all wish her well in this new role!
2. Welcome to Jonathan Smith who has recently joined us as an Investment Analyst Intern from Northeastern University. Jonathan will be supporting our investment team in manager due diligence and other research capacities.
3. We are thrilled to welcome back Alena Taylor who has recently transitioned from part-time to full-time as our Client Solutions Specialist. Alena first joined us in 2008. She took a break to develop her passion for baking and business and we are excited to have her back!
4. In the Press: Jill Fopiano's "Financial Infidelity & Abuse" article was published by Thrive Global in January. The same week, Jill was interviewed by NBCnews.com for an article on the "Money Taboo" and its potential harmful effect on relationships.
5. Qing Yang has joined the O'Brien team as an Associate Advisor. With his strong investment background, Qing also adds to our bench on the asset allocation and manager due diligence fronts.

ALPHABET ARITHMETIC

Are you smarter than a 6th grader? Here's a math problem from the Pierce School in Brookline:

+ × − ÷

$$\begin{array}{r} d \\ -\ a \\ \hline i \end{array} \qquad \begin{array}{r} b \\ -\ c \\ \hline g \end{array} \qquad \begin{array}{r} ac \\ +\ ic \\ \hline de \end{array} \qquad \begin{array}{r} fg \\ -\ de \\ \hline hi \end{array}$$

Each letter in the equations above stands for a different digit: 1, 2, 3, 4, 5, 6, 7, 8, or 9. They are the same in all 4 problems above. *HINT: C=4*

Can you figure out what number each letter stands for?

A: ___ B: ___ C: 4 D: ___ E: ___

F: ___ G: ___ H: ___ I: ___

Answer key can be found in the "In the News" page of our website www.obrienwp.com