

# Beyond the Basics

Customized Wealth Strategies



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## What's Causing the Consumer Blues?

Each month, researchers at the University of Michigan interview hundreds of consumers about their opinions on current economic conditions, as well as their personal finances, buying intentions, and expectations for the future. Survey results are captured in the Index of Consumer Sentiment, which is a closely watched economic indicator because household spending accounts for about two-thirds of U.S. gross domestic product.

Despite a strong labor market, the index fell to an all-time low in June 2022, before starting to improve in the third quarter. High inflation, the specter of rising interest rates, and stock market declines are some of the reasons consumers have felt pessimistic about their economic prospects.



Source: University of Michigan, 2022 (data from January 1978 through September 2022)



**-21%**

Drop in smartphone prices during the 12 months that ended September 2022 — despite the high level of general inflation. Television prices fell 18% over the same period. Better yet, large retailers have reported bloated inventories of electronics and other consumer goods that are likely to result in attractive discounts for holiday shoppers.

Sources: U.S. Bureau of Labor Statistics, 2022; *The Wall Street Journal*, August 30, 2022

# When Should Young Adults Start Investing for Retirement?

As young adults embark on their first real job, get married, or start a family, retirement might be the last thing on their minds. Even so, they might want to make it a financial priority. In preparing for retirement, the best time to start investing is now — for two key reasons: compounding and tax management.

## Power of Compound Returns

A quick Internet search reveals that Albert Einstein once called compounding "the most powerful force in the universe," "the eighth wonder of the world," or "the greatest invention in human history." Although the validity of these quotes is debatable, Einstein would not have been far off in his assessments.

Compounding happens when returns earned on investments are reinvested in the account and earn returns themselves. Over time, the process can gain significant momentum.

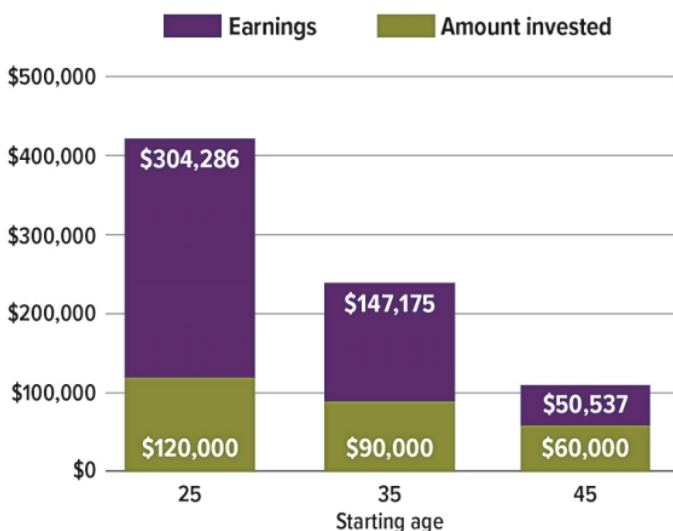
For example, say an investor put \$1,000 in an investment that earns 5%, or \$50, in year one, which gets reinvested, bringing the total to \$1,050. In year two, that money earns another 5%, or \$52.50, resulting in a total of \$1,102.50. Year three brings another 5%, or \$55.13, totaling \$1,157.63. Each year, the earnings grow a little bit more.

Over the long term, the results can snowball. Consider the examples in the accompanying chart.

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## A Head Start Can Be a Strong Ally

This chart illustrates how much an investor could accumulate by age 65 by investing \$3,000 a year starting at age 25, 35, and 45 and earning a 6% annual rate of return, compounded annually.



These hypothetical examples of mathematical compounding are used for illustrative purposes only and do not reflect the performance of any specific investments. Fees, expenses, and taxes are not considered and would reduce the performance shown if they were included. Rates of return will vary over time, particularly for long-term investments. Investments offering the potential for higher rates of return also involve a higher degree of investment risk. Actual results will vary.

## Tax Management

Another reason to start investing for retirement now is to benefit from tax-advantaged workplace retirement plans and IRAs.

**Lower taxes now.** Contributions to traditional 401(k)s and similar plans are deducted from a paycheck before taxes, so contributing can result in a lower current tax bill. And depending on a taxpayer's income, filing status, and coverage by a workplace plan, contributions to a traditional IRA may result in an income tax deduction.

**Tax-deferred compounding.** IRAs and workplace plans like 401(k)s compound on a tax-deferred basis, which means investors don't have to pay taxes on contributions and earnings until they withdraw the money. This helps drive compounding potential through the years.

**Future tax-free income.** Roth contributions to both workplace accounts and IRAs offer no immediate tax benefit, but earnings grow on a tax-deferred basis, and qualified distributions are tax-free. A qualified distribution is one made after the Roth account has been held for five years and the account holder reaches age 59½, dies, or becomes disabled.

**Saver's Credit.** In 2022, single taxpayers with adjusted gross incomes of up to \$34,000 (\$66,000 if married filing jointly) may qualify for an income tax credit of up to \$1,000 (\$2,000 for married couples) for eligible retirement account contributions. Unlike a deduction — which helps reduce the amount of income subject to taxes — a credit is applied directly to the amount of taxes owed.

**Avoiding penalties.** Keep in mind that withdrawals from pre-tax retirement accounts prior to age 59½ and nonqualified withdrawals from Roth accounts are subject to a 10% penalty on top of regular income tax.

## Additional Fuel for the Fire

Workplace plans that offer employer matching or profit-sharing contributions can further fuel the tax-advantaged compounding potential. Investors would be wise to consider taking full advantage of employer matching contributions, if offered.

## Don't Delay

With the power of compounding and the many tax advantages, it may make sense to make retirement investing a high priority at any age.

# Three Stretch IRA Alternatives

The passage of the SECURE Act in 2019 effectively eliminated the stretch IRA, an estate planning strategy that allowed an inherited IRA to continue growing tax deferred, potentially for decades. Most nonspouse beneficiaries, including children and grandchildren, can no longer stretch distributions over their lifetimes. Moreover, proposed IRS regulations require most designated beneficiaries to take annual required minimum distributions (RMDs) within the 10-year distribution period if the original account owner died on or after his or her required beginning date. This shorter distribution period could result in unanticipated and potentially large tax bills for nonspouse beneficiaries who inherit high-value IRAs.

You may be looking for alternative ways to preserve your wealth and pass it on to your beneficiaries. Here are three options you might consider.

## Roth Conversion

If you are willing to pay income taxes now instead of your beneficiaries paying them later, you could convert your IRA to a Roth IRA. Anyone can convert a traditional IRA to a Roth IRA. However, you generally have to include the amount you convert in your gross income for the year converted. Not only would you have to pay taxes on the amount converted, but the beneficiaries of your Roth IRA will generally have to liquidate the account within 10 years of inheriting it, although they won't pay federal income taxes on the distribution(s).

## Life Insurance

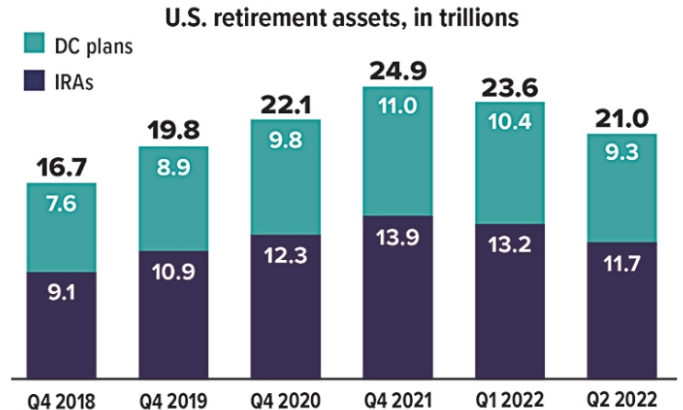
You could take distributions from your IRA and use them to buy life insurance on your life. The beneficiaries you name in the life insurance policy will receive those proceeds tax-free at your death. The policy beneficiaries could use the tax-free proceeds of the life insurance to pay any income taxes they would owe on the balance of the IRA they inherit from you. Or, if you've been able to liquidate or spend down your IRA during your lifetime, the tax-free life insurance death benefit would replace some or all of the taxable IRA that otherwise would have been inherited by the beneficiaries.

## Irrevocable Trust

You could create an irrevocable trust and fund it with non-IRA assets. An irrevocable trust can't be changed or dissolved once it has been created. You generally can't remove assets, change beneficiaries, or rewrite any of the terms of the trust. Often, life insurance is used to fund the irrevocable trust. You can direct how and when the trust beneficiaries are to receive the life insurance proceeds from the trust after your death. In addition, if you have given up control of the property, all of the property in the trust, plus any future appreciation on the property, is removed from your taxable estate.

## Wealth Cache

Assets held in individual retirement accounts (IRAs) and defined-contribution plans such as 401(k)s dipped in the first half of 2022 to \$21 trillion. Even so, that total was up more than 25% from year-end 2018.



Source: Investment Company Institute, 2022

*While trusts offer numerous advantages, they incur upfront costs and often have ongoing administrative fees. The use of trusts involves a complex web of tax rules and regulations. You should consider the counsel of an experienced estate planning professional and your legal and tax professionals before implementing such strategies.*

*As with most financial decisions, there are expenses associated with the purchase of life insurance. Policies commonly have mortality and expense charges. The cost and availability of life insurance depend on factors such as age, health, and the type and amount of insurance purchased. In addition, if a policy is surrendered prematurely there may be surrender charges and income tax implications. Any guarantees are subject to the financial strength and claims-paying ability of the insurer.*

*To qualify for the tax-free and penalty-free withdrawal of earnings, a Roth IRA must meet the five-year holding requirement, and the distribution must take place after age 59½ or due to the owner's death, disability, or a first-time home purchase (\$10,000 lifetime maximum). Under current tax law, if all conditions are met, the Roth IRA will incur no further income tax liability for the rest of the owner's lifetime or for the lifetimes of the owner's heirs, regardless of how much growth the account experiences.*

# Virtual Health Care Is Here to Stay

The use of telehealth skyrocketed early in the COVID-19 pandemic, with the number of remote office visits and outpatient services 78 times higher in April 2020 than in February 2020. Usage has stabilized since then, but as of early 2021 remained 38 times higher than the pre-pandemic level.<sup>1</sup>

More recent data indicates that remote health care is here to stay. In August 2022, almost 23% of adults said they had an appointment with a health professional over video or phone during the previous four weeks.<sup>2</sup>

## Remote Access

Telehealth encompasses a broad range of remote services including virtual office visits (also called telemedicine), remote patient monitoring, patient-physician communication through secure emails and websites, and online physician-to-physician consultation. Patients have immediate access to advice and treatment any time of the day or night, while avoiding unnecessary and costly emergency room visits. But telehealth is not only for emergency or off-hours situations; it also can be a more convenient and cost-effective way to get medical care that might normally be handled in a doctor's office.

Telehealth can be used to treat minor problems such as allergies and rashes, or for an urgent condition such as a high fever. It makes it easier to access therapy for mental health issues such as depression

and anxiety, and can fill gaps in the availability of specialty care. In other cases, doctors can remotely monitor the vital signs of patients with chronic conditions or follow up after a hospital discharge, and physical therapists can lead patients through exercises and monitor their progress.

In 2021, 94% of large employers offered traditional telemedicine services, 28% offered a virtual behavioral health-care network, 25% offered targeted virtual health solutions for specific conditions such as diabetes and musculoskeletal problems, and 16% offered a virtual primary-care service or network. About 12% of eligible employees used a telemedicine service in the first half of 2021.<sup>3</sup>

Original Medicare and Medicare Advantage plans also cover a wide variety of telehealth services. Some of these were specifically added to coverage because of the pandemic and are scheduled to expire at the end of 2023.<sup>4</sup> Considering the convenience and cost savings associated with telehealth, it is possible they will be extended, but that remains to be seen.

If your health plan includes telehealth services, you might take a closer look at the details, download the app, and/or register for an online account. You'll be ready to log in quickly the next time you or someone in your family faces a medical problem.

1) McKinsey & Company, July 9, 2021; 2) Centers for Disease Control and Prevention, 2022; 3) Mercer, May 12, 2022; 4) Centers for Medicare & Medicaid Services, 2022

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