

Smart Money

NEWSLETTER

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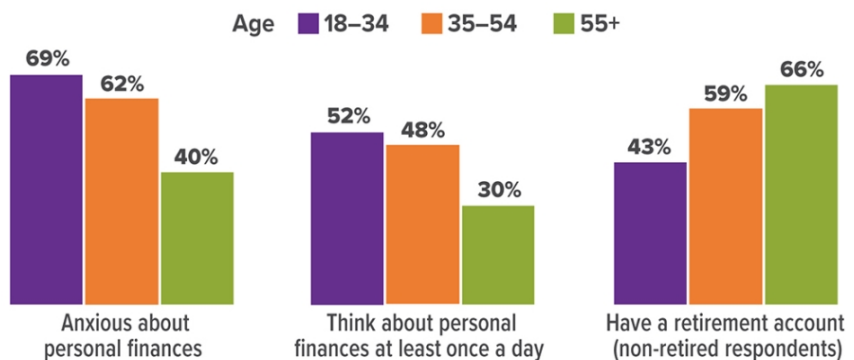
Percentage of Americans who said they spent more than their income in 2021; 34% said they spent about equal to their income, and 43% said they spent less. These responses were almost exactly the same as in 2009, 2012, 2015, and 2018 — suggesting that people are spenders or savers regardless of economic conditions.

Source: FINRA Investor Education Foundation, 2022

Anxious About Your Finances?

A study of financial capability found that older Americans were significantly less anxious about personal finances than younger people. However, about one-third of non-retired people 55 and older had no retirement account.

A comparison of the percentages regarding financial anxiety and retirement accounts suggests that having sufficient resources to contribute to a retirement account is an important aspect of feeling less financial stress for older people. However, many younger people feel stress regardless of whether they have retirement savings. This is especially true of those ages 35 to 54 who may have large mortgages, children in college, and other financial stressors.



Source: FINRA Investor Education Foundation, 2022 (2021 data)

How Taxes Impact Your Retirement-Income Strategy

Retirees face several unique challenges when managing their income, particularly when it comes to taxes. From understanding how taxes relate to Social Security and Medicare to determining when to tap taxable and tax-advantaged accounts, individuals must juggle a complicated mix of factors.

Social Security and Medicare

People are sometimes surprised to learn that a portion of Social Security income becomes federally taxable when combined income exceeds \$25,000 for single taxpayers and \$32,000 for married couples filing jointly. The taxable portion is up to 85% of benefits, depending on income and filing status.¹

In addition, the amount retirees pay in Medicare premiums each year is based on the modified adjusted gross income (MAGI) from *two years earlier*. In other words, the cost retirees pay for Medicare in 2023 is based on the MAGI reported on their 2021 returns.

Taxable, Tax-Deferred, or Tax-Free?

Maintaining a mix of taxable, tax-deferred, and tax-free accounts offers flexibility in managing income each year. However, determining when and how to tap each type of account and asset can be tricky. Consider the following points:

Taxable accounts. Income from most dividends and fixed-income investments and gains from the sale of securities held 12 months or less are generally taxed at federal rates as high as 37%. By contrast, qualified dividends and gains from the sale of securities held longer than 12 months are generally taxed at lower capital gains rates, which max out at 20%.

Tax-deferred accounts. Distributions from traditional IRAs, traditional work-sponsored plans, and annuities are also generally subject to federal income tax. On the other hand, company stock held in a qualified work-sponsored plan is typically treated differently. Provided certain rules are followed, a portion of the stock's value is generally taxed at the capital gains rate, no matter when it's sold; however, if the stock is rolled into a traditional IRA, it loses this special tax treatment.²

Tax-free accounts. Qualified distributions from Roth accounts and Health Savings Accounts (HSAs) are tax-free and therefore will not affect Social Security taxability and Medicare premiums. Moreover, some types of fixed-income investments offer tax-free income at the federal and/or state levels.³

The Impact of RMDs

One income-management strategy retirees often follow is to tap taxable accounts in the earlier years of retirement in order to allow the other accounts to continue benefiting from tax-deferred growth. However, traditional IRAs and workplace plans cannot

grow indefinitely. Account holders must begin taking minimum distributions after they reach age 73 (for those who reach age 72 after December 31, 2022). Depending on an account's total value, an RMD could bump an individual or couple into a higher tax bracket. (RMDs are not required from Roth IRAs and, beginning in 2024, work-based plan Roth accounts during the primary account holder's lifetime.)

Don't Forget State Taxes

State taxes are also a factor. Currently, seven states impose no income taxes, while New Hampshire taxes dividend and interest income and Washington taxes the capital gains of high earners. Twelve states tax at least a portion of a retiree's Social Security benefits.

Eye on Washington

Finally, both current and future retirees will want to monitor congressional actions over the next few years. That's because today's historically low marginal tax rates are scheduled to revert to higher levels in 2026, unless legislation is enacted (see table).

Help Is Available

Putting together a retirement-income strategy that strives to manage taxes is a complex task indeed. Investors may want to seek the help of a qualified tax or financial professional before making any final decisions.⁴

Tax Rates Scheduled to Rise

Unless legislation is enacted, federal marginal income tax rates are scheduled to rise in 2026.

Current rate	2026
10%	10%
12%	15%
22%	25%
24%	28%
32%	33%
35%	35%
37%	39.6%

1) Combined income is the sum of adjusted gross income, tax-exempt interest, and 50% of any Social Security benefits received.

2) Distributions from tax-deferred accounts and annuities prior to age 59½ are subject to a 10% penalty, unless an exception applies.

3) A qualified distribution from a Roth account is one that is made after the account has been held for at least five years and the account holder reaches age 59½, dies, or becomes disabled. A distribution from an HSA is qualified provided it is used to pay for covered medical expenses (see IRS publication 502). Nonqualified distributions will be subject to regular income taxes and penalties.

4) There is no guarantee that working with a financial professional will improve investment results.

SECURE 2.0: Big Impacts for Small Businesses

An AARP study released in July 2022 found that nearly half of all private sector employees ages 18 to 64 had no access to a retirement plan at work. It also found that small businesses are more likely to lack a work-based plan, putting their workers at a significant disadvantage when it comes to retirement preparations (see chart).

Last December, Congress passed a \$1.7 trillion omnibus package that included the SECURE 2.0 Act of 2022, a sweeping set of provisions designed to improve the nation's retirement-planning health. Here is a brief look at some of the tax perks, rule changes, and incentives included in the legislation to help small businesses and their employees.¹

Tax Perks for Employers in 2023

Perhaps most appealing to small business owners, the Act enhances the tax credits associated with adopting new retirement plans, beginning in 2023.

For employers with 50 employees or less, the pension plan start-up tax credit increases from 50% of qualified start-up costs to 100%. Employers with 51 to 100 employees will still be eligible for the 50% credit. In either case, the credit maximum is \$5,000 per year (based on the number of employees) for the first three years the plan is in effect.

In addition, the Act offers a tax credit for employer contributions to employee accounts for the first five tax years of the plan's existence. The amount of the credit is a maximum of \$1,000 per participant, and for each year, a specific percentage applies. In years one and two, employers receive 100% of the credit; in year three, 75%; in year four, 50%; and in year five, 25%. The amount of the credit is reduced for employers with 51 to 100 employees. No credit is allowed for employers with more than 100 workers.

Rule Changes and Relevant Years

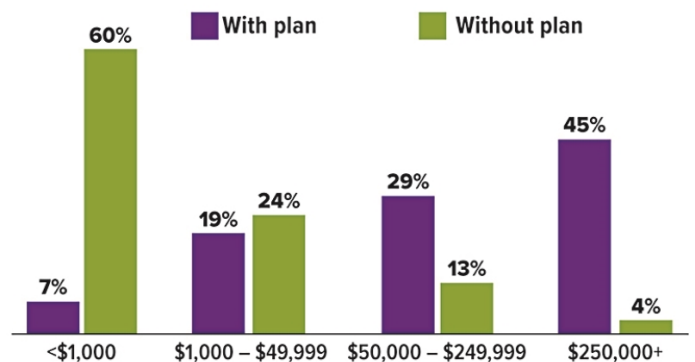
In 2024, employers will be able to adopt a starter 401(k) or similar 403(b) plan, an auto-enrollment plan for employee contributions only. The plan may accept up to \$6,000 per participant annually (\$7,000 for those 50 and older), indexed for inflation. Designed to be lower cost and easier to administer than traditional plans, these programs impose minimum and maximum contribution rates and other rules.

SIMPLE plans may benefit from two new contribution rules. First, employers may make nonelective contributions to employee accounts up to 10% of compensation or \$5,000. Second, the annual contribution limits (standard and catch-up) for employers with no more than 25 employees will increase by 10% more than the limit that would otherwise apply. An employer with 26 to 100 employees would be permitted to allow the higher contribution limits if the employer makes either a

matching contribution on the first 4% of compensation or a 3% nonelective contribution to all participants, whether or not they contribute. These changes also take effect in 2024.

Beginning in 2025, 401(k) and 403(b) plans will generally be required to automatically enroll eligible employees and automatically increase their contribution rates every year, unless they opt out. Employees will be enrolled at a minimum contribution rate of 3% of income, and rates will increase each year by 1% until they reach at least 10% (but not more than 15%). Not all plans will be subject to this new provision; exceptions include those in existence prior to December 29, 2022, and those sponsored by organizations less than three years old or employing 10 or fewer workers, among others.

Worker Savings Amounts: With Retirement Plan vs. Without



Source: Employee Benefit Research Institute, 2023. "With plan" includes workers with a defined contribution plan, IRA, or defined benefit (DB) plan. Total assets include savings and investments other than the value of their home and DB plan. Numbers may not add up to 100% due to rounding.

Participant Incentives on the Horizon

SECURE 2.0 drafters were creative in finding ways to encourage workers to take advantage of their plans. For example, effective immediately, employers may choose to offer small-value financial incentives, such as gift cards, for joining a plan, or beginning in 2024, they may provide a matching contribution on employee student loan payments. Also starting in 2024, workers will be able to withdraw up to \$1,000 a year in an emergency without having to pay a 10% early distribution penalty, which may ease the fear of locking up savings until retirement (restrictions apply).

1) SECURE stands for Setting Every Community Up for Retirement Enhancement and originated with the SECURE Act of 2019.

As Your Parents Age, Help Them Protect Their Finances

It's heartbreaking to hear stories of people losing money (even their life savings) as a result of fraud or financial exploitation, especially if they are older and financially vulnerable. In fact, it's quite common. People age 70 and older reported losses of \$567 million in 2022.¹ You know your parents could be at risk, and you want to protect them, but how?

One place to start is by looking for warning signs that your parents have been victimized, or are at risk of being influenced, manipulated, or coerced by a stranger or someone they know.

- Unusual bank account activity, including large or unexplained withdrawals, and nonsufficient fund notices
- Missing checks, credit cards, or financial statements
- Unpaid bills
- Lost money or valuables that can't be located after a thorough search
- Relationships with people who seem to have undue influence
- Unexplained changes to legal documents
- Declining memory and decision-making skills

Regularly checking in with your parents may help you spot issues that need to be addressed. If your parents have fallen victim to a financial scam or are being pressured for money from someone they know, they may be embarrassed or reluctant to tell you, even if

you ask. Do your best to remain objective and nonjudgmental, and patiently listen to their views while expressing your own concern for their well-being.

Laying some groundwork to help prevent future incidents is also important. For example, talk to your parents about how they might handle common scams. Let them know it's a good idea to get a second opinion from you before acting on any request for information or money, even if it seems to come from their financial institution, a well-known company, law enforcement, a government agency such as the IRS or Social Security Administration, or even a grandchild in trouble.

Encourage them to set up appointments with their elder law attorney or financial professional to talk about concerns and legal and financial safeguards. They might also want to add layers of protection to their financial accounts, such as naming a trusted contact or setting up account alerts.

People are often reluctant to report financial fraud or exploitation, either out of embarrassment or fear of being wrong. But if you suspect your parents have been victimized, you can get help from many sources, including the National Elder Fraud Hotline, sponsored by the U.S. Department of Justice. You can call (833) 372-8311 to be connected with case managers who will assist you and direct you to additional resources.

1) Federal Trade Commission, 2022

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