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REGISTERED INVESTMENT ADVISER

FINANCIAL NEWSLETTER

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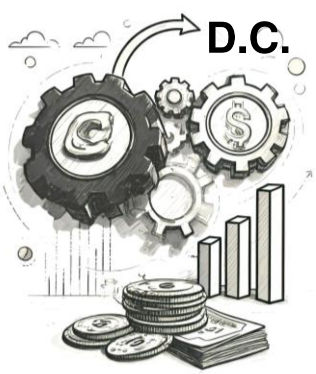
THE CRYSTAL BALL

Coming into the end of the year, there is change in the air. For one thing, we will have a new President of the United States. By the time you read this, we might know who it is, but as of this writing, it is an unknown. When it comes to investment, which is the purpose of this column, what will make a difference is the policies that are enacted, not the policies that are promised during the campaign.

While most people aren't in favor of tax increases, it is very likely that we will see some of the money in our pockets being redirected to Washington D.C. The reason is crystal clear: the federal budget deficit is $1.8 Trillion, that's trillion with a "T". While that is bad enough, it comes at a time when things are going relatively well, there is no financial crisis or war directly involving our troops. And during this time, total tax revenues hit almost 5 trillion dollars. One thing in the government's favor is that there should be a windfall in capital gain taxes that will be due April 2025. That should give a little breathing room (although taxpayers won't be too happy).



This deficit issue and the gigantic debt that the United States has accumulated are starting to make the news. People are becoming aware that there will be a tipping point… maybe soon, maybe later. But sooner or later, the piper will be paid. There's an old saying, "It's not a problem, until it becomes a problem, then it is the only problem." So, look for tax increases, more inflation, or a stagflation economy in the coming year. We may even have a bond market debacle, where a treasury auction fails. That will shake things up big time and make our leaders finally realize that the most obvious answer to deficits and debt is to cut spending. No one said it would be easy, but this is a problem that can be managed and must be managed.

What do you do? If the economy really cools, stocks will generally be impacted in a negative way. Bonds will likely hold their own as the Fed will be forced to cut interest rates further. Inflation is trending down, but this invisible tax increase hasn't gone away. You want to own things in inflationary times; real estate and select commodities should benefit. Gold has hit new highs and although it could go higher, a pullback wouldn't be unexpected, so there will probably be a better time to buy the precious metal. Cash is not trash. It allows you to sleep well at night and provides you with the ability to take advantage of the periodic panic selloffs in the financial markets. Stay patient and avoid making decisions based on emotion and what you hear the talking heads on TV are touting. Don't buy what Wall Street is selling and avoid unnecessary risk (unless it involves a speculation for which you can afford the loss).

Right now, the stock market is at all-time highs. The Federal Reserve is cutting interest rates. Mortgage rates are falling. There is a real rate of return on the interest bonds pay. Investor portfolios are flush with gains. No recession, inflation is falling. Doesn't that sound like investor paradise? So why do things feel all out of whack to many people? The reason is simple: There's more to life than the financial markets. That said, let's all stay optimistic and look to the future with excitement and not with trepidation.

Quote:

"The arc of the moral universe is long, but it bends toward justice."

Martin Luther King

MAXIMIZING ROTH CONTRIBUTIONS

In many employer plans, participants have the option to make Roth (after-tax) deferrals to fund the plan directly from payroll. In 2026, if you are over 50 and make catch up contributions (the additional $7,500 in 2024 over the $23,000 base), those will have to be made on a Roth basis. For now, the decision to fund the plan on a Roth or pre-tax basis is optional.

Historically, a “bird-in-the-hand” approach was to maximize pre-tax contributions as you knew what your tax bracket was in that year and could look to reduce income tax then. However, many investors have built significant amounts of pre-tax assets within their plans and possibly creating a tax windfall in the future. With Required Minimum Distributions (RMDs) now for those age 73 (and later for those age 75), that can further defer taxes due, but can also create larger, tax-deferred balances which could then generate more taxable income in the future. When there are employer contributions made to the plan, those are done on a pre-tax basis, and that further inflates the tax-deferred balance.

In recent years, there has been a growing trend by retirement plan participants forgoing the tax savings today and funding their retirement plans on a Roth basis. A primary driver on this is the ability to later withdraw Roth contributions on a tax-free basis. For years, there was a thought that your tax bracket might be lower in retirement providing future tax-savings on the pre-tax contributions, but more and more retirees are not finding that to be the case. While tax brackets can, do, and will change, retirement also can provide the benefit of time where you have more of it to spend on things you enjoy. There, even if a bracket dropped but income increased (via retirement plan distributions), the perceived savings may not materialize.

Higher taxable income in retirement can have other concerns like pushing you to a higher tax bracket, leading to taxation of social security benefits, and increasing your Medicare premiums. By building a core of Roth funds within your retirement plan, you can help curb this. With both Roth and traditional savings, you’ll have the ability in retirement to decide on which funds to use and when. In some cases, savers will draw down the taxable portions of their retirement assets before tapping social security or starting Medicare. Beginning this year, RMDs are only required on pre-tax money within a qualified plan while designated Roth deferrals avoid RMDs. With more funds accumulated as Roth, that can lower the RMD due from a plan.

Finally, while Roth IRA contributions are limited to a $7,000 base (with $1,000 age 50+ catch-up) in 2024, the Roth deferral option in a qualified plan is over 3x higher at $23,000 base (with $7,500 catch-up). Thus, the Roth deferral can provide a means to greatly accelerate your Roth savings. All in all, if your plan at work permits Roth deferrals, you might see if maximizing Roth deferrals can work for you. We’re here to help you decide what can work well for your situation.

Distributions from traditional IRAs and employer sponsored retirement plans are taxed as ordinary income and, if taken prior to reaching age 59 ½, may be subject to an additional 10% IRS tax penalty. To qualify for the tax-free and penalty-free withdrawal or earnings, a Roth IRA or Roth deferrals must be in place for at least five tax years, and the distribution must take place after age 59 ½ or due to death, disability, or a first-time home purchase (up to a $10,000 lifetime maximum). Depending on state law, Roth IRA distributions may be subject to state taxes.

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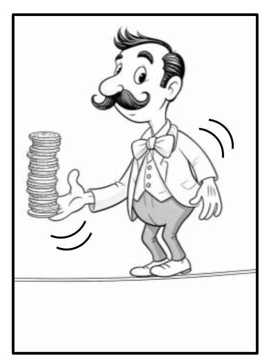
THE IMPORTANCE OF LIFE EXPECTANCY IN PLANNING FOR RETIREMENT

Retirement is often seen as a time for relaxation and enjoying life after decades of work. However, the length of time you expect to live can significantly impact your retirement planning. Understanding how long you may live influences your financial decisions, lifestyle choices, and even your health management.

When planning for retirement, individuals typically consider their desired lifestyle, estimated expenses, and sources of income such as Social Security, pensions, and savings. A crucial aspect often overlooked is life expectancy, which can vary significantly based on factors like genetics, health, lifestyle choices, and socio-economic status.

The longer you expect to live, the more savings you’ll need to maintain your lifestyle. This includes ongoing expenses for housing, healthcare, and leisure activities. Underestimating your lifespan can lead to depleted savings, forcing you to make difficult financial decisions later in life.

As life expectancy increases, so do healthcare costs. Planning for health insurance and out-of-pocket medical expenses is crucial, as these can dramatically affect your budget. Understanding your potential health needs can guide you in selecting appropriate insurance plans and saving for medical expenses.



Retirement planning isn’t a one-time task. Regularly reassess your financial situation, lifestyle, and health as you age. Be prepared to adjust your plans as needed. Life expectancy is a crucial component of your planning. Embracing this reality empowers you to create a sustainable and fulfilling retirement, so that you can enjoy the years ahead without excessive financial worry.

THE BENEFITS OF A HEALTH SAVINGS ACCOUNT (HSA)

A Health Savings Account (HSA) offers significant tax advantages, making it an excellent tool for managing healthcare expenses while also serving as a long-term financial asset. Contributions to a HSA are tax-deductible, the balance grows tax-free, and withdrawals for qualified medical expenses are also tax-free. In 2024, the maximum contribution limit is $4,150 for individuals and $8,300 for families, with an additional catch-up contribution of $1,000 for those aged 55 and older. However, you can only contribute if you're enrolled in a high-deductible health plan (HDHP).

HSA funds can be utilized to cover healthcare costs for your spouse and dependents, including children. You can withdraw the funds tax-free for a wide range of qualified medical expenses, such as doctor visits, prescription medications, dental care, and surgeries. Beyond immediate healthcare needs, a HSA can play an important role in your retirement planning. After age 65, HSA funds can be used to cover several Medicare expenses, including premiums for Medicare Part B (medical insurance), Medicare Part D (prescription drug coverage), and Medicare Advantage (Part C) plans. You can also use HSA funds for other healthcare-related expenses, such as long-term care insurance premiums. However, HSA funds cannot be used to pay for Medicare Supplement (Medigap) premiums or funeral expenses. While withdrawals for non-medical expenses after age 65 are subject to income tax, they are penalty-free, making the HSA function similarly to a traditional IRA, but with added flexibility for healthcare costs.

When you pass away, if your spouse is named the beneficiary, they will inherit the HSA as their own account and preserve its tax benefits. However, if someone other than your spouse, such as a child, inherits the account, the HSA is dissolved, and its balance is added to their taxable income for the year. This is often a surprise.

Funding a HSA allows you to reduce your current taxable income and pay for future healthcare expenses in a tax-advantaged way. By maximizing contributions and strategically using the funds, you and your family could benefit from this type of account. However, it is good planning to ensure that you or your spouse spends the HSA on qualified medical expenses during your lifetimes so non-spouse beneficiaries avoid taxation of the unused funds.

DON'T GET SCAMMED: AN ACTION PLAN TO PROTECT YOUR MONEY

In today's digital age, financial scams are more sophisticated than ever. The key to defending against financial scams is safeguarding your personal and financial information. Being aware of common scam tactics and staying alert to potential threats are crucial. Here are five action items to help lower the odds that you get scammed:

1. **Beware of Unsolicited Communication:** Exercise caution with unsolicited emails, calls, or texts, especially those requesting personal or financial details.
2. **Don't Click on Suspicious Links:** Avoid clicking on links or opening attachments from unknown senders.
3. **Strong Passwords & Two-Factor Authentication:** Use complex, unique passwords for all your online accounts and enable two-factor authentication whenever possible.
4. **Information Sharing:** Exercise caution when sharing personal information online or over the phone, verifying the recipient's identity beforehand.
5. **Document Disposal:** Shred or destroy any documents containing sensitive information before discarding them.

If you have concerns or questions about potential investments or suspicious activity, consult our team. If you suspect you've been targeted by a scam, report it to the relevant authorities, such as your local police. By taking these proactive measures, you can significantly reduce your risk and safeguard your financial future.

PERSONAL NOTES

Helene N. – You and your family have been good friends for a long time. You are a special person.

Tom and Lois G. – We go back a ways now. Your insights and coaching skills are treasured.

Kris and Christopher Y. – Your patience/calm demeanor is the prototype of a successful investor.

Christopher B. – Working with you and your family is a pleasure.

A STORY

A police officer pulls over a semi-truck. He gets the usual license and registration, but hears strange noises coming from the trailer, so he decides to investigate. Inside, he finds 50 penguins.

The officer asks the driver, "Sir, why do you have 50 penguins in your truck?"

"Well, they're my friends, and we like to go on journeys together in my truck," the man replies.

"I'm sorry, Sir, but you can't just own 50 penguins. I'm afraid you're going to have to take them to the zoo."

The man agrees and drives off. The next day, the same officer pulls the truck over again, and once again hears strange noises in the trailer. He goes to check and finds the same 50 penguins.

"I thought I told you to take these penguins to the zoo yesterday!" the cop angrily tells the driver.

"I did take them to the zoo. They loved it. Today we're going to the beach."

ASSESSING RISK

We think that because things are so great in the financial sector, that it is time to step back and look at things with a different perspective, but not a jaded eye. Take a look at your asset allocation and how it is positioned. Will a big drop in the stock market impact your lifestyle? If so, make changes while the getting is good and don't worry about missing out on rising asset values. It is wise to understand risk.

Many say they do but when risk invariably hits, that is when the true understanding of risk becomes real. There aren't too many reasons other than pride and ego to take more risk than you need to in order to meet your objectives. Things are going to change in the next year, some good, some not so good. Make adjustments while you can, not when you must.

Overheard:

"I don't like to complain about the customer service of any business, but I didn't appreciate being pushed over by my banker when I asked him to check my balance."

Phil's Opinions And Judgments…

On Political Worries …

The next President's biggest headache won't only be the U.S. economy. Foreign affairs will have him/her reaching for the aspirin.

On Taxes…

Each candidate is floating tax breaks (no taxes on tips/ no taxes on overtime pay/ no taxes on social security income/ no increases in taxes if you earn under a certain amount/ tax deductions on car loan interest). These "tax breaks" have a very small chance of becoming law as presented. If I were a cynic, I might think these trial balloons are being floated to buy votes. That can't be, could it?

On Journalism…

"Don't tell me what you think, tell me what you know." This was the famed journalist Edward R. Murrow's advice to young journalists. Considered by many as the father of broadcast journalism, Murrow's admonishment is as appropriate today as it was 70 years ago. The pendulum swings.

On Sports…

Two sports comments: The MLB Baseball All Star Game players wore the ugliest uniforms I've ever seen. In the Summer Olympics, the Women's Rugby bronze medal game provided as exciting an ending of any game that you will ever see. The U.S. women's team showed a determination that was off the charts and should fire up any athlete's competitive spirit. Wow!

On Music…

Van Morrison is a music treasure. He is still performing and putting out albums that showcase one of the best singing voices in the universe. His contribution to music puts him on the Mount Rushmore of the music echelon. How lucky we are to have him over the past 50 years. If you aren't a fan now, give him a listen and you'll see what I mean. If you'd like some album suggestions, let me know.

Until next time,

Phil Paul Clete Vance Sylvia

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