Does Your Retirement Plan Have these 10 Crucial Elements?

Jeff Dietz

804-608-9775

jeff@safesecureretirement.pro

safesecureretirement.pro

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1. Avoid **ALL** downside market risk and enjoy only upside market gains?

When you experience losses in your portfolio, you not only lose money on paper in the near-term, but you lose time – the time it takes to get back to where you were before the loss. Time is one thing that we cannot create more of and so losing time simply to get back to where you already were will undermine your ability to achieve your goals.

What's worse is if that loss occurs close to your planned retirement date or shortly after you retire.

• If that loss occurs in the few years before retirement, you may have to defer retirement like so many people had to do in 2008 and 2009 when the housing bubble popped and sent the stock market into a freefall.

• If you had retired in say 2006 or 2007 and then experienced that kind of loss to your retirement portfolio, such a dramatic loss could affect your **ENTIRE** retirement – the retirement that you had been working towards for 40+ years. Such an impact could mean curtailing your planned standard of living or going back to work to make up for the losses.

2. Offer fully **TAX-FREE** distributions?

You can save for retirement in one of two ways: either on a pre-tax basis in a 401k, 403b, traditional IRA or similar plan, or on an after-tax basis where there are a few options as well. The government only gets one shot at taxing your income.

If you choose to save for retirement on a pre-tax basis, money from your earnings is deposited in your 401k (or similar plan) untaxed, your taxable earnings are reduced, and your current tax burden is lightened. Upon distribution in retirement, however, not only are the contributions taxed (because they were not taxed previously) but so are all of the earnings that resulted from those contributions. While it may not feel like it in your daily life, taxes are currently dramatically lower than they have been historically.

With $28 trillion in national debt, a fresh trillion dollars of debt being added each year for the foreseeable future (in 2020 we added $4 trillion in total due to COVID-19), up to $160 Trillion of unfunded liabilities in Social Security, Medicare and Medicaid, and taxes at historically low rates now, there's really only one reasonable expectation for tax rates in the future: Higher. Much, much higher.

Pretend for a minute that you're a corn farmer. It's spring and it's time to plant seed corn for the yearly crop.

The government shows up and offers you a proposition: You can pay taxes now at a really low rate on just the seed corn … ***OR*** you can wait until the harvest and pay taxes then on the full harvest, all of the kernels on all of the ears of corn on all of the stalks in the whole field – and, oh, by the way, tax rates are going up right before the harvest begins.

Which sounds like a better deal?

Investing in a pre-tax 401k is similar to paying your taxes on the whole harvest of corn. What is even more troubling about all of this is that no one knows exactly how large that tax bill will be.

The problem there lies in the fact that in a 401k or traditional IRA, you have a partner in your retirement plan – and that partner is Congress. And it's Congress that gets to decide how much of your retirement money that you get to keep.

Wouldn't you like to not be shackled to Congress and their taxing authority? If you would allow me, I'd like to show you how to pay tax only on the seed corn and avoid a huge tax bill in the future.

3. Have SIGNIFICANT income tax diversification?

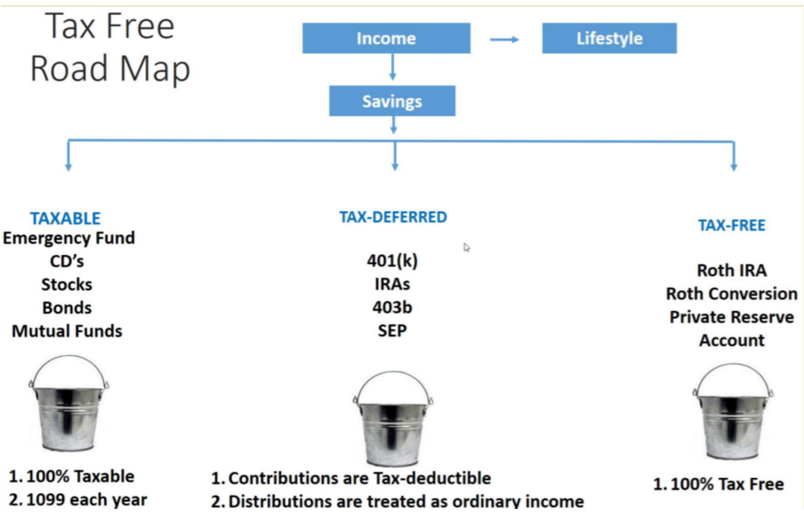
In order to minimize your overall taxation in retirement, you will need money in three different buckets of money:

1) the taxable bucket

2) the pre-tax, tax-deferred bucket

3) the tax-free bucket.

Take a look at the diagram below to better understand the buckets and what can go into them.



The best scenario during the distribution phase of your retirement looks as follows:

1. As much money as possible coming from tax-free sources

2. Any money accumulated in tax-deferred plans (in order to get the “free” dollars from the employer match) and any funds accumulated prior to discovering “safe money and tax-free” alternatives being taxed at the lowest rate possible

3. A taxable (cash) source for a rainy day or emergency fund

What I often uncover during planning sessions with my clients is that most people have the largest portion of their assets in the tax-deferred bucket and little to no money in tax-free bucket.

This will expose their retirement assets to maximum levels of taxation, depleting their income generating assets far more quickly, as more of their account balance must be withdrawn in order to meet their after-tax income needs.

By blending previously accumulated tax-deferred assets with new sources of tax-free assets, you can reduce your overall tax rate in retirement and preserve your assets to produce income for you for far longer.

4. Have unlimited contributions?

In 2022, the IRS has limited 401k contributions to $20,500 for workers under age 50 while workers 50 and above can contribute as much as $26,000 through "catch-up" contributions.

While those limits will not matter much to the average American worker, chances are if you're reading this then you could meet or surpass those limits.

Because of future taxation, and the fact that today's tax rates are so low which provides very little immediate tax relief, there are better places to save for retirement than in a pre-tax 401k (again, you'd probably still want to contribute enough to get the matching contribution, if one is available).

To save enough for retirement and avoid the oncoming tax freight train, you need a vehicle that allows for virtually unlimited contributions AND has tax-free distributions in retirement.

The pre-tax 401k certainly is not this vehicle (it fails both tests), and neither is the Roth IRA. The rich and the ultra-rich, however, utilize a strategy that is almost unheard of to everyone else.

5. Have no earnings limit for contributions?

The 401k does not have a limit on how much you earn so that you can contribute, but IRAs certainly do.

The combined contributions to a traditional and Roth IRA are capped at a $6,000 contribution for 2022 ($7,000 for workers 50 and older) and for a Roth IRA you can only contribute the full amount if you earn less than $129,000 as a single person or $204,000 as a married couple.

The Roth IRA has tax-free distributions, but contributions are severely restricted. Therefore, the Roth IRA is not a viable vehicle for saving your retirement to a large degree.

You need a vehicle that will allow for unlimited contributions and is not restricted by income limits in order to save enough for retirement in an efficient manner.

6. Avoid counting against you and your child(ren) for college financial aid qualification?

One of the financial challenges that face many families is the dual goal of paying for college and saving for retirement.

When being considered for financial aid, the assets of both the parent(s) and the child(ren) are considered in calculating total financial resources.

This includes workplace retirement plans; they don't care that you can't actually access these funds. Fortunately, there is one unique exception, clearly spelled out right in the financial aid application, that allows an unlimited amount of assets to be excluded from the financial aid qualification calculations.

This means dollars held in this unique asset are excluded for both the parent and the child. This means that you can not only save towards your retirement, but these very savings can help the family qualify for more financial aid. If properly structured, these dollars can serve two functions; they can help pay for college without setting retirement accumulation off track. If you have children who are college-bound, we should talk.

7. Avoid taxation of Social Security benefits?

When Social Security was originally created, it was intended to be a tax-free benefit to senior citizens.

Now, however, with even modest amounts of income, a retiree can be taxed on up to 85% of their Social Security benefits.

To add insult to injury, half of your Social Security benefit is included in this “provisional income” calculation!

The money that is withdrawn from pre-tax accounts like a 401k counts as income for the year, and once you cross $34,000 in provisional income as a single person, or $44,000 for a married couple, you’ll pay taxes on 85% of your Social Security benefit – and it’ll be taxed at your highest marginal tax rate!

That is simply outrageous for a benefit that you’ve been paying into for your entire life and was intended to be tax-free. Yet that’s where we are. This situation is avoidable and can be accomplished with a well thought out retirement strategy.

8. Allow access to the account value without penalty before age 59 ½?

Getting money out of your 401k before age 59 ½ is difficult at best and may not even be possible.

Most plans offer 401k loans and hardship withdrawals, but employers are not obligated to provide these options. Most employers do not allow in-service withdrawals so that you can roll over the money to an IRA.

If you discontinue your employment, you would be able to tap into those 401k funds, but in addition to paying income taxes on any withdrawals, you'd also have to pay a 10% early withdrawal penalty if you're younger than age 59 ½. As you can see, a 401k is not a good place to go looking for a sizeable amount of money should a sudden need arise, or even for a very much expected need like paying for a child's college education.

Fortunately, there is a vehicle that allows you access to your account value at any age, without early withdrawal penalties, may or may not be paid back (your choice), grows tax-deferred and whose distributions are tax-free. Let's talk about this retirement plan so that you can have all of these benefits and not be hamstrung by the restrictive nature of the 401k

9. Let you avoid Required Minimum Distributions after age 72 if you don’t need the money?

The government has the right to tax your income exactly once.

When you invest in a 401k on a pre-tax basis you are postponing when that moment will be.

But the federal government will not let you postpone paying taxes for forever, and when you turn age 72 you must start taking what are known as RMDs – Required Minimum Distributions.

You are forced to take at least the RMD amount from your 401k and IRA each year, whether you need the money or not.

You would end up paying income tax on those distributions and now that money is in a taxable account (such as checking, savings, or money market) and no longer growing on a tax-deferred basis.

With proper planning, you can minimize those RMDs, which minimizes taxes and allows more of your assets to keep growing tax-deferred for longer. To accomplish this, we will need to plan, execute, and revisit a well thought out strategy.

10. Offer advice and guidance to safely grow your money, avoid losses, minimize taxes, and plan for the other issues related to retirement?

Not only has the burden of investment contributions and decisions shifted away from the "done for you" structure of pension plans to the "it's all on you" nature of 401ks and other workplace retirement plans, employers are usually prohibited from giving their employees any retirement planning advice or guidance.

That is where I may be of service to you and your family. As a Retirement Income Certified Professional, I have specialized training and the experience to ask you the right questions and help you arrive at the right answers and the right plan for your retirement security and success. I would be happy to meet with you to discuss the results of this checklist and answer any questions you might have about your retirement planning.
There is no cost and certainly no obligation if we meet.

ABOUT THE AUTHOR

Jeff's primary focus is in creating a secure, stress-free, and tax-free retirement for his clients. He's on a professional mission to help as many individuals as possible remove the needless risks of Wall Street we've all been told that we must endure to have a successful retirement and to keep the sticky and greedy fingers of the IRS off of his clients' hard earned money, both while you're working and - even more importantly - during your retirement years.

As a Retirement Income Certified Professional, Jeff works with his clients to not only build their retirement nest egg, but to also create an optimal strategy to manage the often-mismanaged distribution phase. The goal is to maximize spendable income, through tax minimization and significantly enhanced – yet safe – distribution rates, so that one's assets provide for their desired lifestyle for their entire life without the fear of running out of money. Conventional financial advice is geared almost exclusively towards the accumulation of assets, which is of course very important, but there's very little emphasis on how to manage those resources in retirement such that taxes are minimized, people can sleep well at night without worrying about each and every stock market gyration, and live a fulfilling retirement without the fear of running out of money.

Jeff helps his clients both accumulate their wealth and then use it optimally when they need it. Jeff holds a Bachelor's degree from Virginia Tech in Chemical Engineering and a Master's degree from The University of Virginia in Systems Engineering. He is the proud father to two outstanding sons and is a very active member of Woodlake United Methodist Church.

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