AWM Financial Planning

A few Secure Act 2.0 provisions

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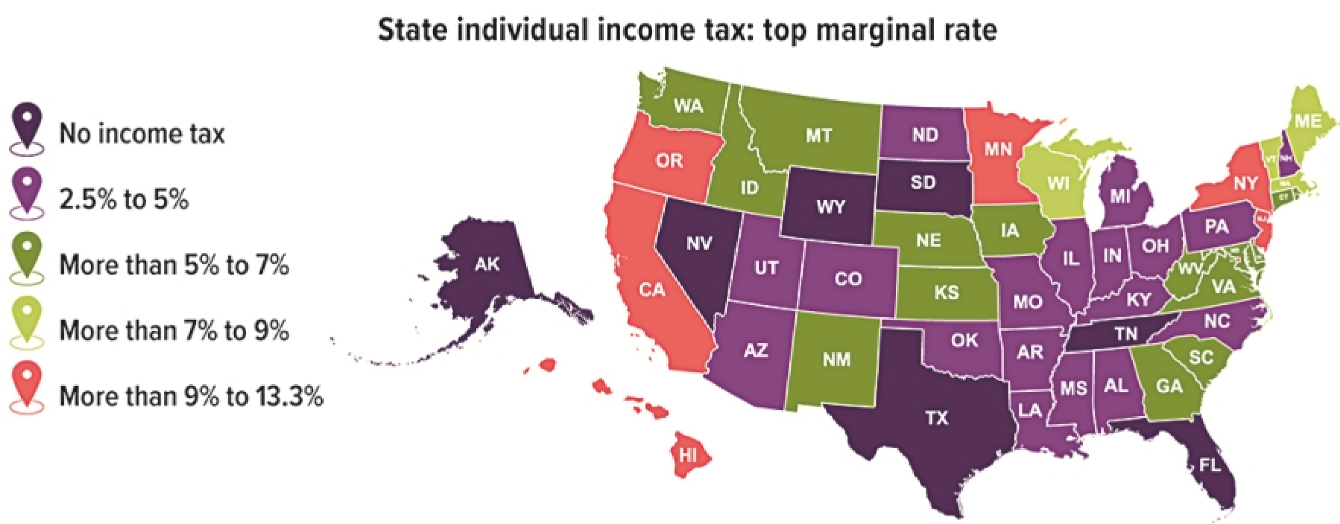
A few ways that Secure Act 2.0 may impact your retirement:

- **401(k) catch-up contributions for high earners must go into Roth accounts.** Beginning in 2026, participants in 401(k) plans who are 50 and older and whose annual income exceeds $145,000 will have to make their catch-up contributions on a Roth basis. The income benchmark is indexed to inflation.
- **Roth contributions to SEP and Simple IRAs.** These are retirement plans used by small employers and the self-employed. Before 2023, all contributions to SEPs and Simples were required to be on a pretax basis. Now Roth contributions, which are after tax, are allowed.
- **Employer matches can be a Roth.** Previously, employer matching contributions to a 401(k) were made on a pretax basis. Since 2023, if an employer offers this option, an employee can elect to have it make Roth contributions. The employee must pay the income tax on the contribution but would receive the benefits of a Roth.

Please give us a call if you have any questions.

State Income Tax Across the Map

Seven states have no state income tax. Of the 43 states with a state income tax (and the District of Columbia), the top marginal income tax rate ranges from 2.5% to 13.3%. Most states (and D.C.) with an income tax have multiple tax brackets with graduated rates; 14 states have only a single tax rate. New Hampshire only taxes interest and dividends, and Washington only taxes capital gains.



Source: Tax Foundation, February 2024

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Making the Most of Your Credit Card

A growing number of Americans are moving towards a "cashless" society. As a result, credit cards are being used more often than ever — especially by those with higher incomes.[1]

Credit cards are no longer viewed solely as a debt instrument for cash-strapped individuals. Instead, they are prized for a variety of benefits, such as earning rewards and travel perks, protecting purchases, building credit, and gaining additional insurance coverage.

Reap the rewards

Using a rewards credit card for everyday purchases can provide you with valuable perks. Some rewards cards will offer a percentage of cash back for every dollar spent on certain purchases (e.g., dining; travel) or the ability to apply rewards towards a statement credit. Others offer travel rewards that can be used to purchase airline miles and hotel accommodations. Certain rewards cards can even provide you with entrance into VIP airport lounges and early access to purchase tickets for concerts and sporting events. Many rewards cards offer additional sign-up bonuses, such as double cash back or bonus miles/points for new customers if you charge a certain amount on the card within a specified period of time.

The disadvantages of a rewards card are that it can often come with a higher interest rate or charge an annual fee. So if you tend to carry a balance on your card, you could end up paying more in interest than you would earn in rewards. In addition, it is important to read the fine print and fully understand the terms and conditions of the rewards offered. You'll also want to periodically check in with your card issuer to see if any of the terms and/or conditions of the offer have changed.

Protect your purchases

One of the main advantages of using a credit card is that you have greater protection for your purchases than you would if you use cash or a debit card. If your credit card is lost or stolen, you generally are liable for no more than $50 in fraudulent/unauthorized charges. Credit cards also come with additional fraud protection in the form of fraud alerts that are sent immediately to you by email or text message when suspicious charges are detected.

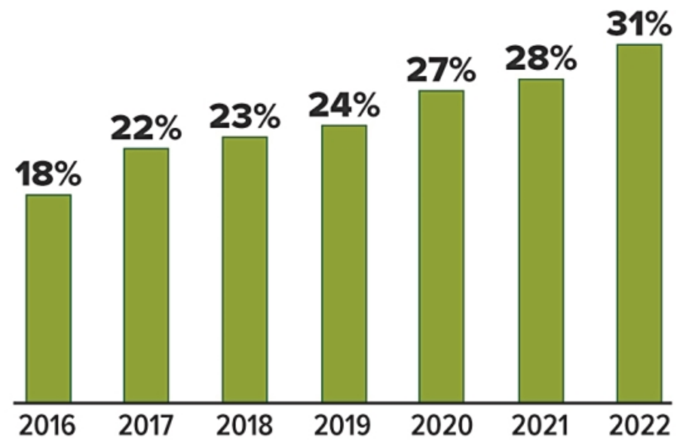
Your credit card may also provide extended warranties and/or extra purchase protection for high-cost items bought with the card, such as a TV or laptop.

Build your credit

Using a credit card is an excellent way to build credit and improve your credit score. There are a variety of factors that go into determining your credit score, such as your payment history, outstanding debt, and how close your balances are to their account limits.

In order to use a credit card to build and/or improve your credit, you should be sure to consistently pay your full monthly balance on time and keep your balance below your credit limit.

Share of payments made by credit card



Source: Federal Reserve, 2023

Gain additional insurance coverage

Many credit cards provide you with additional insurance coverage for particular circumstances. For example, if you use your card to rent a car, you may be covered by auto rental insurance to protect you in case of damage or theft. If you use your card to purchase a trip, it may offer travel interruption insurance if your trip is canceled for a covered reason. Your credit card may even provide coverage for a lost or damaged cell phone if you purchased your cell phone or pay your cell phone bill with your card.

Use your card wisely

The key to making the most of your credit card is to use your card wisely and avoid falling into common credit card traps. Here are three tips for using your credit card responsibly:

- Only charge what you can afford and pay the full balance due each month.
- Avoid missing payments by signing up for automatic payments and account alerts.
- Try to keep your balance well below your credit limit.

1) Federal Reserve, 2023

It's Complicated: Inheriting IRAs and Retirement Plans

The SECURE Act of 2019 dramatically changed the rules governing how IRA and retirement plan assets are distributed to beneficiaries. The new rules, which took effect for account owner deaths occurring in 2020 or later, are an alphabet soup of complicated requirements that could result in big tax bills for many beneficiaries.

RMDs and RBDs

IRA owners and, in most cases, retirement plan participants must start taking annual required minimum distributions (RMDs) from their non-Roth accounts by April 1 following the year in which they reach RMD age (see table). This is known as their required beginning date (RBD).

Likewise, beneficiaries must take RMDs from inherited accounts (including, in most cases, Roth accounts). The timing and amount of an individual beneficiary's RMDs depend on several factors, including the relationship of the beneficiary to the original account owner and whether the original owner had reached the RBD.

Three key points apply to both owners and beneficiaries: (1) individuals must pay income taxes on the taxable portion of any distribution, (2) the larger the RMD, the higher the potential tax burden, and (3) failing to take the required amount generally results in an additional excise tax.[1]

Date of birth	RMD age
Before July 1, 1949	70½
July 1, 1949, through 1950	72
1951 to 1959	73
1960 or later	75

The age that determines an account owner's RBD depends on the account owner's date of birth.

Spouse as sole beneficiary

Spouses who are sole beneficiaries have the most options for managing inherited accounts. By default, a surviving spouse beneficiary is treated as what's known as an eligible designated beneficiary (EDB) with certain advantages (see next section, "EDBs and DBs"). And if the deceased spouse died before the RBD, a surviving spouse EDB who is the sole owner can wait until the year the deceased would have reached RMD age to begin distributions.

Alternatively, a surviving spouse who is the sole owner can generally roll over the inherited account to their own account or elect to be treated as the account owner (rather than as an EDB). In these cases, the rules for account owners would apply. However, there is a potential drawback to this move: if the surviving spouse is younger than 59½, a 10% early distribution penalty may apply to subsequent withdrawals unless an exception applies.

EDBs and DBs

The SECURE Act separated other individual beneficiaries into two groups: EDBs and designated beneficiaries (DBs). EDBs are spouses and minor children of the deceased, those who are not more than 10 years younger than the deceased, and disabled and chronically ill individuals. DBs are essentially everyone else, including adult children and grandchildren.

EDBs have certain advantages over DBs. If the account owner dies before the RBD, an EDB is able to spread distributions over their own life expectancy. If the account owner dies on or after the RBD, an EDB may spread distributions over either their own life expectancy or that of the original account owner, whichever is more beneficial.[2]

By contrast, DBs are required to liquidate inherited assets within 10 years, which could result in unanticipated and hefty tax bills. If the account owner dies before the RBD, the beneficiary can leave the account intact until year 10. If the owner dies on or after the RBD, a DB must generally take annual RMDs based on their own life expectancy in years one through nine, then liquidate the account in year 10.

Other considerations

Work-sponsored retirement plans are not required to offer all distribution options; for example, an EDB may be required to follow the 10-year rule. However, both EDBs and DBs may roll eligible retirement plan assets into an inherited IRA, which may offer more options for managing RMDs.

This is just a broad overview of the complicated new rules as they apply to individual beneficiaries. If an account has multiple designated beneficiaries, or if a beneficiary is an entity such as a trust, charity, or estate, other rules apply. Beneficiaries should seek the assistance of an estate-planning attorney before making any decisions.

1) The IRS has waived this tax as it applies to the DB 10-year rule through 2024.

2) An inherited account must be liquidated 10 years after an EDB dies or a minor child EDB reaches age 21.

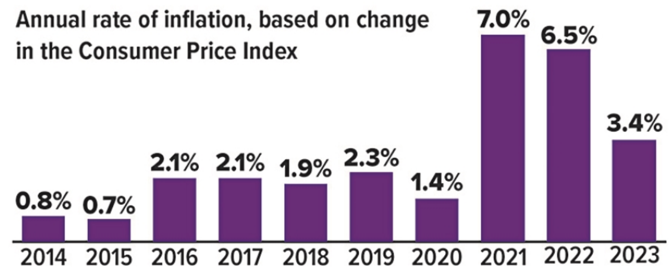
What's Your Real Return?

As an investor, you probably track the return on your investments. But it's likely that you look at the *nominal return,* which is the percentage increase or decrease in the value of an investment over a given period of time, usually expressed as an annual return. To estimate actual income or growth potential in order to target financial goals, such as a certain level of retirement income, it's important to consider the *real return,* which includes the effects of taxes and inflation.

Let's say you want to purchase a bank-issued certificate of deposit (CD), because you like the lower risk and fixed interest rate that a CD can offer. CD rates have risen substantially with the Federal Reserve's aggressive increases in the federal funds rate, so let's say you find a CD that offers 5% annual interest. That could be attractive. However, if you're taxed at the 22% federal income tax rate, 1.1% will be gobbled up by federal income tax on the interest.

That still leaves an interest rate of 3.9%, but you should consider the purchasing power of the interest. For example, inflation slowed to 3.4% in 2023 after hitting 40-year highs in 2021 and 2022 (see chart). But a 3.4% inflation rate would leave a real return of just 0.5%. If inflation slows further, the real return on this hypothetical CD would increase. However, if the Fed were to lower the benchmark federal funds rate in response, rates on CDs and other fixed-income investments might decline, reducing the real return on future CD and fixed-income purchases.

Eroding Purchasing Power



Source: U.S. Bureau of Labor Statistics, 2024

This hypothetical example doesn't represent the performance of any specific investment, but it illustrates the importance of understanding what you're actually earning after taxes and inflation. In some cases, the lower risk offered by an investment may be appealing enough that you're willing to accept a low real return. However, pursuing long-term goals such as retirement generally requires having some investments with the potential for higher returns, even if they carry a higher degree of risk.

The FDIC insures CDs and bank savings accounts, which generally provide a fixed rate of return, up to $250,000 per depositor, per insured institution. All investments are subject to risk, including the possible loss of principal. When sold, investments may be worth more or less than the original cost.