QUARTERLY RETIREMENT REVIEW

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SPRING 2021 ISSUE

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Establishing an Emergency Fund

The right amount for your emergency fund and the reasons you may need to use it often depends on whether you're still working or if you've already retired. Unexpected expenses, like an unplanned home repair or a medical emergency, can happen at any time. With an emergency fund in place, you won't have to run up a balance on your credit card or tap in to your retirement savings to get through a period of uncertainty.

While you're working: In case you lose your job, suffer a temporary decline in income, or come upon large unexpected expenses.

After you've retired: To cover your living expenses in periods of an extended market downturn or when any major unexpected expenses arise

Where to hold it: Savings or money market accounts; short-term bond funds; short-term certificates of deposit (CDs); or, if you are in a high tax bracket, tax-free short term funds.

How much do you need: Dual-income households should save three to six months' worth of living expenses. Single-income households (or those with unpredictable income) should have six months or more of living expenses in savings. After you have retired, however, you should consider holding one to two years of household living expenses.

What Should You Do With Your Old 401(k)?

You have four options for what to do with an old 401(k) account. Some things to consider before making a decision include: whether you're changing jobs or retiring from your career, as well as your financial circumstances and long term goals. Keep in mind that preserving the tax benefits of your investments when you leave your job may substantially improve your ability to build wealth over the long term. Here are the options:

1. **Leave your assets where they are**. If the plan allows, you can leave the assets in your former employer's 401(k) plan, where they can continue to benefit from any tax-advantaged growth. Find out if you must maintain a minimum balance and understand the plan's fees, investment options, and other provisions, especially if you may need to access these funds at a later time.

2. **Roll your assets into your new employer's plan.** If you're changing jobs, you can roll your old 401(k) account assets into your new employer's plan (if permitted). This option maintains the account's tax-advantaged status. Find out if your new plan accepts rollovers and if there is a waiting period to move the money. Also, review the differences in investment options and fees between your old and new employers' 401(k) plans.

3. **Roll over your assets to an IRA.** For more investment options and to maintain the tax-advantaged status of the account, you can roll your old 401(k) into an individual retirement account (IRA). IRAs allow for greater flexibility over access to your savings (although income taxes may apply, along with early withdrawal penalties, if you are under age 59½). Review the differences in investment options and fees between an IRA and your old and new employer's 401(k) plans.

4. **Cash out your assets.** Cashing out your old 401(k) may have significant financial consequences. Not only are those funds considered taxable income and subject to an immediate tax withholding, but you also may be subject to a 10% early withdrawal tax penalty if you cash out before age 59½. Additionally, withdrawals will lose the potential for tax-deferred growth.

If possible, choose an option that allows you to continue to benefit from your savings' tax-advantaged status and preserve and increase growth potential of your wealth. Other factors to consider include fees and expenses, available services, protection from creditors, and special tax considerations for employer stock. Please consider consulting with a tax advisor.

Weighing Your Options

Here are some pros and cons to help you make the right choice for your situation.

1. Leave your assets where they are

ADVANTAGES

- Offers familiar investment options.
- Maintains your plan account's tax-advantaged status.
- Generally allows for penalty-free withdrawals if you leave your job in the year that you turn age 55 or older (although distributions are still subject to income taxes).
- May provide access to investment choices and plan services that aren't available elsewhere.

CONSIDERATIONS

- May have a minimum balance requirement of $5,000 to remain in the plan.[2]
- Subject to plan withdrawal provisions.
- May have limited investment options.

2. Roll your assets into your new employer's plan

ADVANTAGES

- Maintains your plan account's tax-advantaged status.
- May permit loans.[2]
- Generally allows for penalty-free withdrawals if you leave your job in the year that you turn age 55 or older (although distributions are still subject to income taxes).
- May provide access to investments that may not be available elsewhere.
- If you are still working at age 72, you may not have to take required minimum distributions from your current employer's plan.[3]

CONSIDERATIONS

- Limits investment options to those in the new plan.
- Limits your access to withdrawals.[2]
- May involve a waiting period prior to moving assets from a former employer's plan.[2]
- Generally, rollover contributions to a new plan (if permitted) can be withdrawn at any time and do not have to meet a permissible distribution event. Taxes and penalties may apply.

3. Roll over your assets to an IRA

ADVANTAGES

- Maintains your plan account's tax-advantaged status.
- Often offers access to a wider range of investment options (versus keeping the assets in an employer-sponsored plan).
- Permits penalty-free withdrawals after age 59½ and under limited circumstances.
- Allows you to consolidate multiple accounts into a single IRA.

CONSIDERATIONS

- Does not offer loan provisions.
- Generally, you may not make penalty-free withdrawals until age 59½.
- There may be negative tax consequences of rolling over significantly appreciated employer stock to an IRA.

4. Cash out your assets

ADVANTAGES

- Provides immediate access to your retirement plan assets.

CONSIDERATIONS

- Removes the potential for continued tax-deferred growth of your assets.
- Mandatory 20% withholding on the distribution. You may be liable for a greater amount when you file your taxes if your income tax rate is higher than 20%.
- May be subject to a 10% early withdrawal penalty if you are under age 59½.[1]

SOURCE: T. ROWE PRICE

Getting More Out of Your Retirement Income Withdrawal Strategy

You will likely need to withdraw money from savings to supplement what you receive from Social Security and any other sources of income in retirement. One challenge can be funding the most advantageous way to draw down these savings while minimizing taxes. Many people hold investments in a variety of account types: Traditional and Roth versions of individual retirement account (IRAs) or 401(k)s, along with taxable brokerage accounts creates tax diversification, which can provide greater flexibility to your withdrawal strategy.

Two tax-efficient strategies that can help minimize overall tax liability from your retirement withdrawals:

1. Take full advantage of income subject to low tax rates. Consider using your low tax bracket strategically by consistently "filling up" that bracket with ordinary income from tax-deferred account distributions, such as your Traditional IRA. If you need more than these withdrawals to support your lifestyle, you can sell taxable account investments or take money from your Roth accounts.

As an example assume a married couple: Has $750,000 across their investment accounts: 60% tax-deferred, 30% Roth, and 10% taxable. Spends $65,000 (after taxes) each year. Collects $29,000 in Social Security benefits.

Using this approach, the couple supplements Social Security income each year with approximately $22,000 to $24,000 from tax-deferred accounts, and $12,000 to $14,000 from taxable or Roth assets. By fully offsetting ordinary income with the standard deduction, they completely avoid federal income taxes and save $38,000 throughout retirement. This strategy adds two years to the life of their portfolio compared with following the conventional wisdom of drawing on taxable accounts first, followed by tax-deferred accounts and then tax-free accounts.

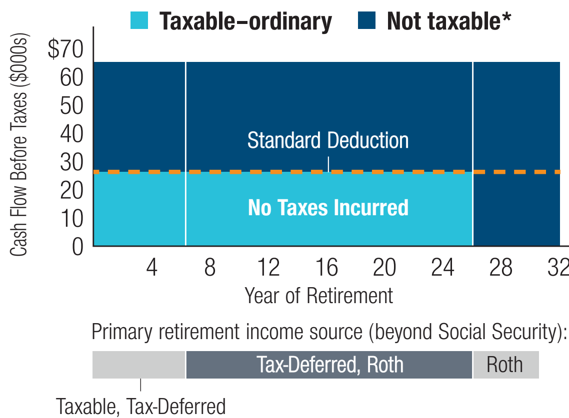
2. Make the most of untaxed capital gains. If your taxable income is $40,000 or less (for single filers) or $80,000 or less (for married couples filing jointly), long-term capital gains and qualified dividends aren't taxed.

Retirement Income Strategies Make a Difference

By pursuing a bracket-filling income strategy instead of following conventional wisdom, the couple avoids federal income taxes and adds two years to the life of their portfolio, compared with following the conventional wisdom of drawing on taxable accounts first.

BRACKET-FILLING STRATEGY

By leveling out tax-deferred distributions, the couple pays no federal income taxes.

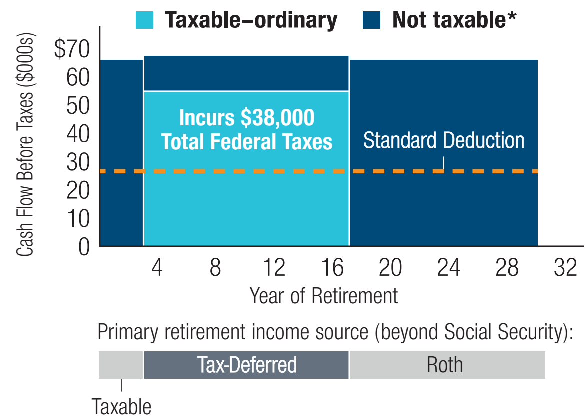


Primary retirement income source (beyond Social Security):

Taxable, Tax-Deferred | Tax-Deferred, Roth | Roth

CONVENTIONAL WISDOM APPROACH

This approach results in unnecessary taxes during years 3–17 of the couple's retirement.



Primary retirement income source (beyond Social Security):

Taxable | Tax-Deferred | Roth

*Nontaxable sources include return of principal from sale of investments in taxable accounts, Roth qualified distributions, and the untaxed portion of Social Security.

Note: Amounts are approximate and do not depict the transition years when income sources change (or the final partial year). Primary income sources noted are those from investments, in addition to Social Security benefits.

SOURCE: T. ROWE PRICE

We've found that those who have a healthy portion of assets in taxable accounts may be better served by taking advantage of untaxed capital gains than by taking tax-deferred distributions to fill up ordinary income brackets.

Let's look at an example with a married couple that has significant taxable investments. We'll assume the couple:

1. Has $2 million across their investment accounts: 50% tax-deferred and 10% Roth and 40% taxable
2. Spends $120,000 per year
3. Collects $45,000 from Social Security

We would suggest that the best strategy might be for this couple to tap in to their taxable account in the years prior to required minimum distributions (RMDs). Then they can combine sales of taxable investments, Roth distributions, and the tax-deferred account RMDs. The Roth distribution amounts are carefully chosen (approximately $9,000 to $14,000 per year) to keep the couple's income below the capital gains tax threshold. That saves them over $31,000 throughout the retirement in taxes compared with the conventional approach.

Consider your Strategy:

As you approach retirement, keep in mind that taxes are complicated, so you will likely want to consult with a tax advisor for help in customizing a withdrawal strategy. Tax diversification can expand your options in retirement. In both strategies mentioned, the

availability of Roth assets is necessary for implementation. RMDs can significantly reduce your flexibility to manage taxes after age 72, so you need to develop a plan well ahead of that milestone.

SPOTLIGHT ON SAVING

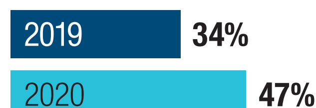
The coronavirus pandemic has affected many people's finances. In fact, according to the T.Rowe Price 2020 Retirement Savings Survey 60% of workers saving in a 401(k) plan say the pandemic has impacted their job, their income, or both with 47% reporting an increase in their financial stress. A silver lining amid these challenges: The pandemic has renewed investors' focus on the importance of short-term financial security. Many have found resilience in being resourceful, with 32% reportedly reducing their spending since February 2020. These workers are keeping an eye on the future as well and have prioritized maintain their retirement savings.

Strengthening the Foundation

The survey found that more workers are **prioritizing short-term goals**, such as saving for emergencies or setting aside money in a health savings account (HSA), than in prior years.

Saving for Emergencies

Contributing to an HSA



Managing and Budgeting

Building for the Future

The new emphasis on short-term savings hasn't come at the expense of long-term goals. **Retirement remains a top priority**, with the average contribution rate remaining steady at 8%. In addition, the number of investors saving for retirement outside of a workplace plan is increasing.

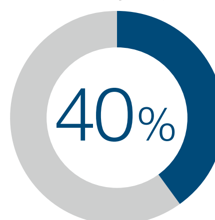
Retirement Savings via Workplace Plans

Retirement Savings Outside of Workplace Plans

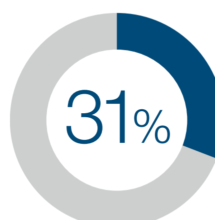
Looking Ahead

These financial patterns are **likely to continue** in the near term.

Workers who plan to increase their emergency savings



Workers who plan to increase contributions to their retirement accounts



*Those who were working part time or full time and saving in a 401(k) plan when surveyed June 5–24, 2020.

SOURCE: T. ROWE PRICE

There's Still Time to Make Your IRA Contribution

You have until May 17, 2021, to make a 2020 IRA contribution, and you can also make your 2021 contribution now. It's wise to do so as soon as possible. Why? Contributing earlier helps to maximize the compound growth potential of your investments.

IRA CONTRIBUTION LIMITS

Tax Year	Under Age 50	Age 50 or Older
2020	$6,000	$7,000
2021	$6,000	$7,000

NOTES

HAS ANYTHING CHANGED?

S.L. Reed & Company can help:

401(k) Rollover from Previous Employer
Rollover IRA out of a Retirement Plan
Traditional or ROTH IRA
Taxable Accounts
Annuities
Insurance

Additionally, we can work with you on:

Managed Accounts

For Assistance call:

Ken Kilpo (310) 893-3016

S.L. REED & COMPANY

Robert W. Nichols, CEO

Website
www.slreed.com

Telephone
(866) SLREED1
(310) 893-3030

Facsimile
(310) 893-3031

Mailing Address
11111 Santa Monica Boulevard
Suite 1200
Los Angeles, CA 90025