MEMO

WASHINGTON'S GROWING ROLE IN YOUR RETIREMENT

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Washington has been busy over the past few years debating a host of new tax and spending priorities. These debates have given us insight into what may be in store for popular retirement savings vehicles like 401(k)s and IRAs.

As savers plan for retirement, they often consider what kind of lifestyle they want, how much income they'll need, and what tax bracket that income may put them in.

But these savers are making decisions inside an ecosystem prescribed from Washington. After all, the bills being passed by Congress and the President can have a direct impact on a saver's retirement approach.

I've found that while many savers consider the individual ways their taxes may change in retirement, they often aren't prepared for legislative changes that could be coming from Washington.

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Why is this important?

Americans who have saved all or the majority of their retirement assets in tax-deferred vehicles, like IRAs and 401(k)s, have agreed to pay their retirement tax bill in the future, rather than today. In essence, they have made a bet their taxes will be lower in retirement than they are currently.

But the actions of Washington could upset this calculation. In fact, we may be entering a rising tax environment for U.S. savers.

It's important for savers to understand what higher taxes could mean for their retirement approach: Will they still have enough income to meet their needs? How will their legacy plans be impacted?

LEGISLATIVE RISK IN RETIREMENT

All of this amounts to savers understanding Legislative Risk in retirement.

Legislative Risk is the risk that Congress changes the rules around taxes or retirement vehicles, and those changes negatively impact a saver's retirement approach.

Legislative Risk is comprised of two related considerations:

- **Tax Class,** which is the level of taxation a saver experiences in retirement. This is the risk a saver's taxes may be higher in retirement than planned, leaving them with less income to spend.
- **Tax Structure**, which is the structure of taxes a saver experiences in retirement. This is the risk our government changes what is taxed, when it's taxes, and how it's taxed.

We've seen heightened legislative risk during key debates in the past few years, and savers should understand what is being considered in Washington when it comes to taxes in retirement.

RISING TAX RISK?

Many experts agree Congress will need to raise additional tax revenue in the near term to offset spending priorities and address the federal debt. And recent Congressional debate shows retirement accounts are a key place Congress may look for this revenue.[1]

> **The U.S. debt currently sits at more than $31 trillion.[2] The debt has grown rapidly in recent years, due in part to Congressional spending on economic stimulus bills and pandemic-related legislation in 2020 and 2021.**

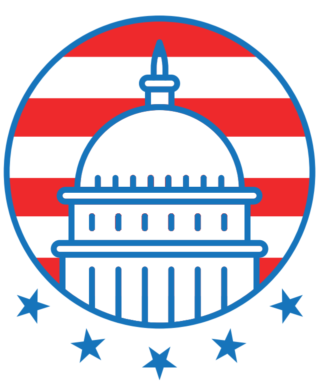
However, it's not just appropriated spending that is driving our nation's debt. As the large Baby Boomer generation retires, our country is seeing increased pressure on government benefit programs like Medicare and Social Security.[3] In short, our government is currently spending more funds than it is bringing in - and future projections suggest this will continue.[3]

As Congress considers both the federal debt and economic health of our country, I believe they will need to look at increasing tax revenue to the government. And in fact, over the past 24 months, we have seen a number of significant tax and spending proposals out of Congress.[4]

Let's examine a few of those proposals, and how they could potentially lead to higher taxes for savers.

TAX BACK BETTER?

In 2021 and 2022, Congress engaged in multiple debates over the **Build Back Better** agenda, a $3.5 trillion spending bill covering priorities like expanded health care coverage, education, family leave benefits and climate change initiatives. To help offset the cost of these priorities, Congress also considered $2.9 trillion in new taxes - some of which were aimed squarely at retirement savings vehicles.[1]



For example, Congress proposed a new Required Minimum Distributions (RMD) applicable at any age for certain savers. Under this proposal, savers would add up the total value of all their retirement accounts.

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If that value exceeded a government-determined cap, the saver would be required to withdraw from their accounts 50% of the excess above the cap. This would end the tax-preferred status of these funds, delivering new tax revenue to the government and leaving individual savers to potentially pay taxes on those funds each year going forward.

Another proposal stipulated that once a saver reached the retirement asset cap, they would be prohibited from saving any additional funds in Traditional or Roth accounts - regardless of their age or career status. Congress also discussed limiting the ability of certain savers to convert tax-deferred assets into Roth accounts, limiting their ability to grow and access funds tax free in the future.[5]

WHAT COMES NEXT

Thankfully for savers, these new tax proposals on retirement savings accounts were not passed into law. However, that doesn't mean savers should breathe a sigh of relief.

> **There's an old saying in Washington: tax proposals never die, they just go on the shelf for future use.**

Once Congress starts debating certain tax provisions, those provisions are easier to insert into future legislative proposals. In fact, each year the Congressional Budget

Office (CBO) publishes its “Options for Reducing the Deficit,”[6] which is a list of new and expanded taxes and regulations Congress can consider to increase government revenue. The most recent version of this document, released in December 2022, includes reforms focused on retirement savings and Social Security.[6]

Needless to say, savers should watch Congress closely in the next few years as they debate new tax and spending legislation.

ADDRESSING LEGISLATIVE RISK

Successful retirement planning involves identifying and addressing risks you may face in the future. Rising taxes and legislative changes can pose a big risk in retirement - but I find many U.S. savers aren’t protected against them.

So how can savers start addressing legislative risk? A good place to start is through diversification. Much like most savers don’t have all their retirement assets invested in a single stock, savers may want to diversify the tax status of their retirement accounts as well. (Savers interested in this approach should consult with qualified professionals about their individual needs.)

There are two areas of potential diversification savers may consider:

Diversification to address the risk of rising taxes: Tax-free savings vehicles, like Roth accounts,[5] can help savers hedge against rising taxes in the future. Since these types of accounts are funded with after-tax dollars, no taxes are due on the funds when they're withdrawn in retirement. So if Congress raises taxes in the future, these funds won't be impacted.

Diversification to address the risk of legislative changes: Some savers may want to further diversify the kinds of vehicles they use for their retirement assets. This could include evaluating options that potentially have lower exposure to legislative changes, like CDs or cash value life insurance.[7]

WHY NOW?

If you're concerned about tax and legislative risk in retirement, now is the time to get educated. The news from Washington suggests that higher taxes are coming, so savers may want to make adjustments ahead of any legislative changes.

Additionally, individual income tax bracket rates are set to rise in the next few years. The individual tax bracket reductions passed in 2017 as part of the Tax Cuts and Jobs Act (sometimes called the "Trump Tax Cuts") are set to expire in 2025.[8] That means in 2026, tax bracket rates will revert to their older, higher levels. If you are considering changing the tax status of any of your retirement assets, you may want to do so today at the lower rates.

WHAT'S NEXT?

If you're ready to address tax and legislative risk in your retirement approach, it's important to work with a financial professional who understands these risks. Below are three questions to discuss with them. These questions will help you better understand your exposure to legislative risk, and your options for addressing it.

- **Based on my needs and today's legislative environment, are my taxes in retirement likely to be lower, the same, or higher than they are today?**
- **How will my income be impacted if taxes are different than I expected? Can I still meet my retirement goals?**
- **Are the vehicles I've used to save for retirement exposing me to legislative risk or protecting me from it?**

If your goal is to be prepared for all the risks you may face in retirement, it's important you've evaluated your exposure to Legislative Risk. Washington can have a big impact on a saver's retirement approach, and now could be a valuable time to take action.

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Becky Ruby Swansburg is Chief Executive Officer of Stonewood Financial, a noted public speaker, and co-author of several industry-leading books including *The New Holistic Retirement.* She has built a career in communication and policy, working in the White House under George W. Bush, and on Capitol Hill for the Speaker of the House and other Members of Congress.

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This document is not intended to provide a complete overview of product features, benefits and limitations of any particular savings vehicle or product. Traditional and Roth accounts are subject to qualifications and limitations by the IRS. This document is not endorsed by any government agency or department. This document should not be deemed a representation of past or future events or results, and is no guarantee of any future performance or occurrence.

1 "Build Back Better Act," House Committee on the Budget, Accessed 03/06/2023 and available online at https://democrats-budget.house.gov/issues/build-back-better

2 "What is the National Debt?" U.S. Treasury Fiscal Data, updated daily. Accessed 03/06/2023 and available online at https://fiscaldata.treasury.gov/americas-finance-guide/national-debt/

3 "Status of Social Security and Medicare Programs," Social Security Administration, 2022. Available online at https://www.ssa.gov/oact/TRSUM/tr22summary.pdf

4 Publications, Congressional Joint Committee on Taxation. Accessed 03/03/2023 and available online at https://www.jct.gov/publications/

5 "Options for Reducing the Deficit," Congressional Budget Office, December 2022. Available online at https://www.cbo.gov/publication/58164

6 Roth Accounts are funded with after-tax dollars. Roth Accounts may involve qualifications, fees, limitations and restrictions. Please consult with a qualified professional about your individual situation.

7 The primary purpose of life insurance is death benefit protection. Please note life insurance is subject to insurability and other suitability factors. Policies include fees, limitations and restrictions. Please see a complete carrier illustration for information regarding your specific situation.

8 "Tax Cuts and Jobs Act, 2017," as proposed for reconciliation and signed into law. Accessed 03/06/2023 and available online at https://www.congress.gov/bill/115th-congress/house-bill/1/text