Creative
wealth maximization strategies*

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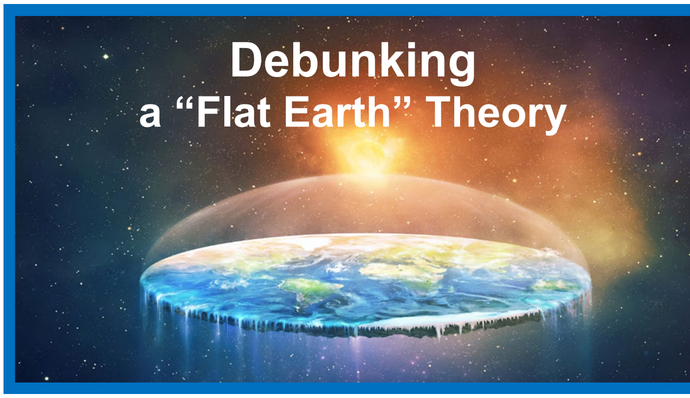

and Debunking "You will be in a Lower Tax Bracket at Retirement" Theory…

Due to some ambiguously provocative statements from a few celebrities and professional athletes, there has been a revival of "Flat Earth" theories in public discussion. In one form or another, these ideas postulate that the Earth is not a sphere, but a flat disc that bends on itself.

Even though there is strong evidence to discredit them, Flat Earth theories persist because they align with our perception that the Earth is flat. So when a "new" version of Flat Earth comes along, it's easy for us to say, "Well, you know…that sort of makes sense" – even though this iteration isn't much different than others that have been discredited.

The "Flat Earth" Statement of Retirement Planning

Similarly flawed theories exist in personal finance. Despite facts to the contrary, these ideas persist because, at first hearing, they sort of make sense. For example, there's this one, which first appeared in the mid-1970s, with the introduction of the Individual Retirement Account (IRA):

"You'll be in a lower tax bracket in retirement."

Sounds like it ought to be true, right? A primary motivation for making tax-deferred contributions today is the belief that the taxes due when the funds are withdrawn will be less than the deduction received on the deposits.

When IRAs (and their employer-sponsored cousins, like 401(k)s and 403(b)s) first appeared, no one really knew if "You'll be in a lower tax bracket" was true. But after 40-plus years, enough individuals who saved in qualified retirement accounts have transitioned to retirement, to arrive at a definitive conclusion: **Those who do a good job saving during their working years will most likely *not* be in a lower tax bracket in retirement.**

What the Numbers Say

In November 2018, The Nationwide Retirement Institute released findings from a "Tax and Retirement Income Survey," based on data collected by The Harris Poll. The respondents came from three groups: Those retired for more than 10 years, those retired for 10 years or less, and those who expected to retire in the next 10 years.

Each group was asked to assess their tax rate in the first five years of retirement compared to either their current tax rate if still working, or their tax rate in the five years prior to retirement. Across the board, **three out of five respondents said their tax rates were either about the same or higher in retirement.**

> Taxes at distribution can make two accounts with the same balance spend differently.

In This Issue…

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Here are the exact percentages:

Retired for 10 or more years: **59 percent**
Retired for 10 years or less: **58 percent**
Planning to retire within 10 years: **61 percent.**

Why might this be? Well, consistent savers most likely have other good financial habits. They systematically reduce or eliminate debt, and live within their means. By the time they retire, these households have accumulated enough money to continue living as they did when they were working. And there aren't any compelling reasons to further delay gratification or decrease lifestyle just to stay in a lower tax bracket. Realistically, the only retirees who can anticipate a lower tax bracket are those who didn't save enough while they were working.

Another possible reason many retirees find themselves at the same level of taxation or higher: They ignored the distribution aspect of retirement planning. Believing the lower-tax-bracket-in-retirement mantra to be accurate, savers sought retirement plans offering up-front deductions, assuming whatever taxes to be assessed at distribution would be less.

In hindsight, many retirees recognize they should have given taxes a closer look. The survey found that only 25 percent of older retirees (those who had been retired for more than 10 years) considered themselves knowledgeable or very knowledgeable about how their retirement income was impacted by taxes. The numbers for the other cohorts were slightly higher, but across all groups, there was an expressed need for better tax planning.

These comments highlight a critical nugget of financial wisdom: taxes at distribution can make two accounts with the same balance spend differently. For example, the true after-tax cost of a bucket-list trip to Europe could be $20,000 or $25,000, depending on which account is used to pay for the trip.

Eric Henderson, a Nationwide executive, points to the disproportionate public emphasis on accumulation as telling only half the retirement planning story: “It is also important to determine how to spend your retirement income. Building tax flexibility into a retirement income plan is crucial. Doing so allows you to use different types of investments and retirement accounts (taxable, tax-deferred, and tax free) to potentially avoid higher tax brackets.”

Based on the evidence, successful savers are probably ***not*** going to be in a lower tax bracket in retirement. A better approach: consider retirement accumulation options with different tax treatments on distributions. ❖

Flat Earth Theories Persist as well as Retiring in a Lower Tax Bracket, but That Doesn’t Make Them True

With 60 percent of retirees finding they aren’t in a lower tax bracket, it’s perhaps prudent to retire the idea of “You’ll be in a lower tax bracket,” or at least be a bit skeptical about the claim. Yet just like the persistence of Flat Earth theories, some in the financial service industry continue to exhort consumers to maximize contributions to a qualified retirement plan.

Saving is a good thing, but so is tax flexibility. ❖

Age might be just a number, but age-related numbers are important markers in personal finance, particularly in retirement. For example:

- **59½** is the age at which penalty-free withdrawals can be made from qualified retirement plans.
- **62** is when most Americans become eligible to receive reduced Social Security Benefits.
- Sometime between **66** or **67**, depending on your birthday, is your Full Retirement Age, when you can receive your full Social Security benefit.
- In the year you turn **70½**, you must commence with Required Minimum Distributions from qualified retirement plan accumulations.

These age requirements for retirement benefits, like the ones that determine your eligibility to vote or right to consume alcohol, are somewhat arbitrary. But because these age-based benchmarks exist, they often become default standards for retirement planning.

However, because everyone is unique, retirement planning should also consider one’s biological age as well.

Chronological vs Biological Age

Chronological age is simply how long someone has lived, measured in hours, days, months and years. **Biological age**, sometimes referred to as ***physiological age***, is an assessment of your physical and mental function relative to your chronological age. A 65-year-old leading a healthy and active life may be physiologically similar to the average person who is 55 chronologically. Thus, we might say this healthy 65-year-old has biological age of 55.

There are any number of ways to measure biological age, from on-line self-assessments to comprehensive medical evaluations. Most biological age assessments are based on a combination of:

- physical condition (measurables like height, weight, blood pressure, vision, physical fitness)
- lifestyle (exercise and diet habits, stress levels, relationship status, i.e., single, married or divorced)
- heredity (the lifespans of others in the family tree, and the prevalence of specific diseases or illnesses)
- location (the climate, level of personal safety, and access to health services).

Impact on Personal Finance

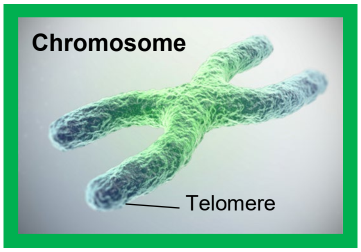
None of these biological age measurements are as exact as chronological age. But your biological age could be the deciding factor in many retirement decisions. For example…

1. A biological age lower than chronological age projects to a longer life expectancy. This probability could change your retirement planning in several ways, such as:

- Anticipating a longer life, you might need to save more.
- Or, with the expectation of good health, you might want to work longer.
- A lifetime annuity could be attractive for retirement income, because there’s a financial benefit for living beyond chronological life expectancy.

2. Conversely, a biological age that is higher than your chronological one might prompt other decisions.

- Taking Social Security at 62, rather than waiting until you reach Full Retirement Age.



- Selecting an aggressive spend-down schedule that increases your retirement income.
- Restructuring your life insurance plans to ensure a death benefit for a surviving spouse.

You Can Change Your Biological Age

Chronological age is immutable; the only way to change it is with a fake ID (which is both sketchy and illegal). On the other hand, most individuals can adjust their biological age through better lifestyle choices. It's all about taking care of your telomeres.

Telomeres are protective structures at the end of our DNA strands. As we age, our telomeres get shorter. When telomeres get too short, the DNA is no longer protected, and cell regeneration processes break down, leading to cancer and other chronic medical conditions.

Fortunately, we can preserve telomere length and reverse aging at the cellular level. Dr. John Day, a cardiologist and author of "The Longevity Plan," lists six actions that improve telomere health, and the degree to which these changes can adjust your biological age.

1. Managing stress saves up to 10 years of telomere decay. A University of California at San Francisco study found that "Those who perceived they were under the most stress for the longest periods of time, prematurely aged their telomeres by about 10 years." Another study from the same researchers showed that meditation and relaxation techniques could reverse this premature aging.

2. Exercise can preserve 10 years of telomere life. An English study of 2,401 twins found that regular exercising slowed telomere aging by about 10 years when compared to their non-exercising sibling.

3. A healthy diet can reverse telomere aging by 5 years. Diets high in vegetables, fruits, fish, nuts, seeds, and legumes can protect our telomeres. Sugar, processed foods, and processed meats have the opposite effect.

4. Maintaining an ideal weight is worth 9 years. Obesity is another cause of premature aging. Excess weight causes oxidative stress, or "rusting," which results in telomere shortening. Maintaining an ideal body weight can lengthen telomeres by 9 years.

5. Sleep at least 7 hours. Sleep is recuperative. One study found that older people who slept at least seven hours each night had the telomeres of middle aged people.

6. Maintain social connections. Social isolation is a strong predictor of heart disease and telomere shortening. Staying connected to friends and family slows the aging process.

Biological Age Is a Huge Planning Variable

Because it can't be quantified on a spreadsheet, biological age doesn't get much attention in retirement planning. But health and wealth are intertwined. Adjusting your biological age could dramatically impact every facet of retirement planning.

Particularly for those who haven't been able to accumulate adequate savings, lowering your biological age could play a key role in catching up, because it theoretically expands your window for working and saving. And in retirement, a lower biological age translates to a higher quality of life, for a longer time. ❖

> Chronologically, time marches on, but by adjusting your biological age, you have some control over the cadence of your life, both physically and financially. Manage your biological age like a financial asset.

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