MONTHLY
NEWSLETTER

The Advisor

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I am happy to present this month's market commentary from our Investment Team. The goal is to give our clients and friends a simple way to see everything they need to know about the financial markets on a weekly basis, in 5 minutes or less. After all, investing should be simple, not complicated.

THE IMPORTANCE OF TAX PREPARATION FOR RETIREMENT

While many retirement plans do not require taxes during the accumulation phase, as the old saying goes; "nothing can be certain except death and taxes." At some point, taxes are paid on income. There is no skirting it. The benefit of many retirement plans is that they are tax-deferred.

During retirement planning, many workers don't anticipate the effects of taxes during that phase of their lives. They forget that any consideration of living expenses must still be net of taxes.

The benefit of tax deferral on many retirement plans is that taxes don't have to be paid on the income at the time it is earned; often during the time you are at your highest tax rate. The theory is that when you retire, you will be at a lower tax rate and you can pay taxes on your deferred income at that lower rate. As long as the federal, or your state government, does not raise tax rates, that theory should hold.

There is also the deferral of the tax obligation on the earnings within many retirement plans, such as 401k plans. Also, many employers will make a contribution into the plan, and that money usually remains tax deferred also until it is actually withdrawn. These employer funds often come with a vesting schedule, so the employee does not walk away with that portion until they have worked for that employer for a certain number of years.

This all works out well in theory, and absent of some new taxes that would throw a fly in the ointment, it does currently benefit retirement savers. Under the current marginal tax rates, a worker may squirrel away a dollar into a retirement plan that they might have paid thirty cents in taxes on. Upon withdrawing that dollar, they might only pay fifteen cents in taxes on it; which sounds like a good deal. The money management issue then becomes how to best deal with that fifteen cents. In retirement, anything that depletes income cannot be easily compensated for.

Retirement Plans and Taxes

Just as with IRA's, many 401k plans offer the choice between a traditional and a Roth. The tax treatment of the two is very different. The contributions, that you make as an employee into a traditional 401k plan, are contributed pre-tax and those amounts are treated like a deferred salary. The contributions that are made into a Roth 401k plan are made with money that has already been taxed. With the traditional 401k, you are presently taxed on the income you receive, which has been reduced by the

contributions into your retirement plan.

At withdrawal, the tax implications are reversed. On those contributions and earnings in your traditional plan, you would pay income taxes as you withdraw them as ordinary income. On withdrawals from a Roth 401k, there are no taxes. The money must have remained in the account for at least five years though.

There may be some penalties when you make withdrawals from your traditional 401k also. There is a 10 percent penalty on withdrawn amounts prior to age 59 1/2. On the other end of the retirement age spectrum are the penalties associated with not taking enough money out of your traditional retirement plans. When you reach age 70 1/2, you are required to take required minimum distributions from your traditional accounts. Depending on the size of these funds, you might want to begin earlier than this age to avoid paying too much tax on a large amount of accumulated funds.

While you might be paying ordinary income on those traditional retirement funds, based on the existing marginal tax rates, you would be paying capital gains rates on the sale of investments. The tax rate depends on the length of time you have held that investment. Again, as with marginal tax rates, the rates on capital gains could change in the future as well.

There are considerations for social security funds, annuities and pensions that all need to be considered as well. Getting the advice and direction of a professional can help navigate this complex subject.

HOW TRUMP'S INFRASTRUCTURE SPENDING COULD BOOST THE U.S. ECONOMY

In 1933, President Franklin Roosevelt moved quickly to put into place a series of experimental public works projects which became known as the New Deal. One in four Americans was out of work at the time. In May of that year, he signed the Tennessee Valley Authority Act (TVA) into law. The new agency worked on projects to improve navigation, flood control, electricity generation, fertilizer manufacturing, and economic development.

Additional large scale projects were launched in 1935, which became known as the Second New Deal. Additional agencies were created, like the Public Works Administration, and later, the Works Progress Administration. The Public Works Administration funded almost 34,000 projects.

In 1956, president Dwight D. Eisenhower signed the Federal-Aid Highway Act into law. The bill authorized enough funding — $26 billion — to construct and repair approximately 41,000 miles of highways, roads, and bridges.

While the new Trump administration will aim to reduce government's role in the lives of the average American, the emphasis on infrastructure spending and projects will introduce a degree of interventionist government that was popular with Roosevelt's supporters. And much like FDR's first 100 days, president Trump is taking executive actions and proposing projects that will stimulate the economy and put Americans back to work. Unlike FDR, he is not expanding the Federal government.

Infrastructure Proposals and Solutions

Make work projects have been used throughout much of America's history to stimulate the economy and create

jobs.

The president's infrastructure proposals include the goal of transforming "America’s crumbling infrastructure into a golden opportunity for accelerated economic growth and more rapid productivity gains with a deficit-neutral plan targeting substantial new infrastructure investments."

The proposal includes "investments in transportation, clean water, a modern and reliable electricity grid, telecommunications, security infrastructure, and other pressing domestic infrastructure needs."

By providing maximum flexibility to the states and the creation of "thousands of new jobs in construction, steel manufacturing, and other sectors to build the transportation, water, telecommunications and energy infrastructure needed to enable new economic development in the U.S., all of which will generate new tax revenues," the new administration will emphasize using American steel made by American workers.

Specific steps are mentioned in the proposal to control costs and cut wasteful spending. "Link increases in spending to reforms that streamline permitting and approvals, improve the project delivery system, and cut wasteful spending on boondoggles," according to the Trump website. "Employ incentive-based contracting to ensure projects are on time and on budget."

The Keystone XL and Dakota Access pipeline projects are projected to create thousands of permanent and temporary new jobs. These jobs would result from the construction of the pipelines and the additional new hires

at the refineries. New jobs mean more spending on commodities, as a one-off effect and increased spending means a stimulated economy. Retail spending would benefit also.

Considering that growth in domestic GDP has been lethargic over the past eight years, any initiatives, that would increase employment substantially, would have a domino effect on the sales of goods and services and the profits of corporations and small business. While there is some risk of inflation, U.S. GDP would increase beyond the stagnant 1.5 or 2 percent that has been typical recently.

While there was even opposition to FDR's infrastructure projects, which was an effort to dig America out of a depression, there is also opposition to president Trump's initiatives. With infrastructure spending comes safer highways and bridges and more tax revenues. If there is an uptick in jobs creation, then the overall impact is good.

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About the Author

K Richard Douglas has worked in the financial services industry for 26 years, with an additional 10 writing about financial and economic topics. He’s a former series 9, 10, and 26 registered principal and series 6, 7, and 63 registered representative. Richard has held many financial service industry designations, especially in the retirement planning and compliance mechanism areas.