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Social Security GPO: FOMO, IDK, or LOL??

Michael Wilson, CFP®, CRC®, RICP®, Integrity Financial Planning

Editor's note: This article is an adaptation of the live webinar delivered by Michael Wilson in 2021 His comments have been edited for clarity and length.

You can read the summary article here as part of the 4th Qtr 2021 Retirement InSight and Trends Newsletter, worth 1.0 CE when read in its entirety (after passing the online quiz.)

You may also choose to take the full length course "Social Security GPO: FOMO, IDK, or LOL?? for 1.0 hour continuing education (CE) credit.

By Michael Wilson, CFP®, CRC®, RICP®, Integrity Financial Planning

If you do not know the acronyms, i.e., if you do not have a teenager running around, FOMO stands for fear of missing out. When people who have worked for an agency where they did not pay into Social Security, maybe they've heard of this GPO (government pension offset), and so they are thinking, this could affect what Social Security benefit I might get. So, that is the fear of missing out.

The IDK is I don't know, as in, I don't know anything about GPO. LOL sometimes stands for laugh out loud or lots of love. In this case, it means lots of luck trying to understand this thing because, even for those in the financial industry, understanding the GPO is challenging. You can imagine somebody, say, a schoolteacher or a police officer, firefighter, or somebody working for an exempt agency trying to understand how GPO will affect them.

If you haven't done so yet, I recommend reading the sister article to this article on WEP, the Windfall Elimination Provision. These are two very, very different processes, two very different systems within the Social Security system. They have different impacts depending on whether you are subject to the WEP, you are subject to the GPO, or may be subject to both, as it turns out. It is essential to understand the different scenarios that you, your members, or your clients could run into regarding the WEP and the GPO.

How Social Security Defines Various Retirement Benefits

How does Social Security define a pension? In their lingo and system, any type of periodic lump-sum payment from an employer's retirement plan that either comes solely from the employer or that could also include employee contributions is a "pension." When those in the financial industry hear the term "pension," we think lifetime paycheck. Here's the kicker. A 401(k), a 457, or a 403(b) can also be considered a "pension" from Social Security's perspective. Again, we do not usually think of defined contributions plans as pensions. But in Social Security's world, any employer money and possibly including employee contributions to DC plans could be considered a pension.

Maybe a better way to think of a "pension" in Social Security's terminology is just any type of employer-paid retirement benefit. If the employer is paying into it, it will be considered a pension. It does not matter if it is a 401(k) plan or a 457 or a traditional pension; always going to be considered a pension from Social Security's perspective.

Now let's understand the basics of how Social Security typically works so we can contrast that with how the GPO might affect somebody's Social Security benefit. Typically, folks in the private sector, some public sector positions, cities, counties, states do pay into Social Security. It depends on the particular agency.

Typically, agencies that might not pay in are school systems, might be special service districts, like water districts or sewer districts, maybe public safety officers, maybe firefighter agencies, and maybe some cities, towns, and counties. For everybody else who pays into Social Security and pays FICA taxes and has at least ten years of what is called qualified earnings or work credits, they are entitled to a Social Security benefit.

For instance, in 2021, to count toward those ten years of work credits, you would have had to earn at least $1,470 a quarter. So, if somebody was making 20, 30, 40 thousand dollars a year in 2021 and they are paying into Social Security, they would get four work credits for the year or four quarters. Once you earn at least ten years of work credit, you will get some type of Social Security benefit. When Social Security calculates somebody's Social Security benefit, it is based on the participant's highest 35 years of earnings.

Social Security started back in 1935. It was designed as a welfare program. It was not designed to be the primary retirement resource; it was designed to supplement it. If anything, it was built to sort of slant the benefits more toward long-term, lower-income workers. That was the intent of the program. Nowadays, Social Security, in many cases, has become the primary retirement benefit for folks who do not have any other retirement savings. It was never intended to be that, but it is kind of a safety net for many folks.

When does the Government Pension Offset (GPO) Apply?

Who is impacted by the GPO? If you work for a Social Security exempt agency and you will receive a pension of some type. Again, pension, in Social Security lingo, could also mean defined contribution plans like a 401(k) or a 403(b). It will also apply if you have a spouse who is eligible to receive a Social Security benefit.

The GPO is only going to affect someone who is married. Assume I am a married exempt worker (working for an exempt agency). I am a school teacher, and I don't pay into Social Security. My spouse works in the private sector. I could be affected by the GPO.

If I am single and retiring, the GPO will not affect me whatsoever. I do have to keep in mind, though, if I get married by the time I get into retirement, or I marry in retirement, the GPO might come back into play if the person I marry is entitled to some type of Social Security benefit.

How does the GPO work? What is the impact? Say both you and your spouse work in the private sector. While we are both alive, as one option, my spouse could potentially draw half of my Social Security benefits, or she can have her benefits based on her work earnings record. The other option for benefits is that when one of us passes away, the survivor gets the higher of the two benefits. If my spouse's Social Security benefit was going to be $2,000 a month and mine is $1,500 a month, if she passes away first, my $1,500 a month goes away, and my benefit jumps to her $2,000 a month benefit. Again, these are kind of the typical scenarios: the ability to draw off of a spouse's benefit while we are both alive, or once one of us passes away, the survivor gets the greater of either their own or their spouse's benefit.

The GPO will affect me if I am an exempt worker and the Social Security beneficiary of a private-sector worker. Assume I work for a school system, and I am not paying into Social Security. My wife is working in the private sector and paying into Social Security. The GPO could affect the one-half spousal benefit or my ability to draw off her Social Security benefit. Her Social Security benefit that I would have assumed as a beneficiary if she were to pass away first will potentially be reduced.

How to Calculate the GPO's Impact and Who is Affected

Let's look at some examples. Say Tammy has worked for an exempt school district for 14 years. Before that, she worked for 16 years in the private sector. Because she worked in both the private and public sectors, the Windfall Elimination Provision (WEP) will apply to her. Her husband, Steve, works in the private sector as a mechanic. They decide to retire. Tammy's pension benefit from the school district is $1,000 a month. Because the WEP applies to her, ultimately, she is only potentially going to get $400 a month of her own Social Security benefit from the time she worked in the private sector. (See this article for more information about WEP.)

Steve's Social Security benefit is $2,000 a month. Typically, if both had paid into Social Security, Tammy would assume she would receive half of Steve's benefit, or $1,000. But the GPO comes into play. The GPO is a two-thirds Social Security benefit reduction based on Tammy's pension amount. For example, her pension is $1,000, so a two-thirds GPO reduction is about $670 a month. The $670 a month will then be subtracted from the half spousal benefit that Tammy would be entitled to from Steve's earnings record. Tammy's half spousal benefit is now only $330 a month.

She thought she would have $1,000 a month in pension benefits and $1,000 a month in the half spousal Social Security benefit from Steve's record. She does get the $1,000 pension because the GPO does not affect her pension whatsoever. But she will not get the $1,000 Social Security spousal benefit that she was expecting based on Steve's record. Her own WEP-adjusted Social Security benefits (see above) would be $400, which is more than the $330 GPO-adjusted benefit that she could collect in spousal Social Security benefits. She chooses to take the $400 WEP-adjusted benefit based on her own Social Security record.

The bottom line on all this is that Tammy probably thought she would have $2,000 a month after she retires, and instead, she only winds up with $1,400 a month or $600 a month less than expected. That is about a 30 percent drop in income. If Tammy has not planned for this, this could significantly impact their retirement income. Therefore, it is essential to understand how the GPO can come into play.

Let's look at a different example. Say Tammy has worked her entire career for the school district. She never paid into Social Security. Steve is still in the private sector as a mechanic. They decide to retire.

Tammy's pension benefit is now $2,500 a month because she worked in the school system for 32 years. She isn't entitled to a Social Security benefit, so she doesn't have to worry about the WEP. Steve's Social Security is still $2,000. Tammy might think, "Oh, I get a spousal benefit of half of Steve's Social Security, so we'll have another $1,000 a month." But the GPO comes into play. Two-thirds of Tammy's $2,500 pension is $1,675 a month. Based on Steve's record, this amount is subtracted from the half spousal benefit she was expecting. The GPO adjustment wipes out any spousal Social Security benefit. This $1,000 a month reduction is roughly about a third of their expected income. This could obviously be a huge surprise for her.

How Does the Government Pension Offset Affect Social Security Survivor Benefits?

What happens when Steve dies? Does Tammy get Steve's full benefit? Theoretically, Tammy could "inherit" Steve's Social Security. The GPO factor is still a two-thirds Social Security benefit reduction.

Tammy's pension is $2,500 a month, and a two-thirds GPO reduction of that is $1,675 a month. Normally, Tammy might expect to receive Steve's entire $2,000 a month survivor Social Security benefit. If Tammy had never worked outside the home for pay, she would still be entitled to 100 percent of Steve's Social Security benefit as the survivor. But because Tammy had her entire career working for an exempt agency, the GPO applies.

When Tammy's $2,000 a month survivor benefit is reduced by the GPO by $1,675 a month, she now only gets $325 a month of Steve's benefit if Steve were to pass away. This can be a very, very big surprise because Tammy thought she would have her $2,500 pension and a $2,000 a month survivor Social Security benefit, or $4,500 a month retirement income. Instead, her monthly income drops to $2,825. This significant percentage drop can significantly impact Tammy's survivor lifestyle if Steve were to pass away first.

As another example, let's say Tammy retires, and she gets her pension benefit. Maybe she has a little bit of Steve's spousal benefit. Steve, meanwhile, has paid into Social Security his entire career. If Tammy passes away first, the nonmember spouse, Steve, could still pick up a pension survivor benefit if Tammy had chosen an option where Steve gets all or part of her pension if she were to pass away first.

Steve also still gets his Social Security benefit, and there is no impact on him because he paid into Social Security his entire career. So, spouses of exempt members are just fine; there is no GPO impact on them whatsoever.

But what happens if you have some years where you paid into Social Security and maybe some years where you worked in an exempt agency like our first scenario? Tammy worked 14 years in an exempt school district, and she worked 16 years in the private sector. At that point, if you are trying to dial in some more specific numbers, you will probably have to go to Social Security and ask them to create an estimate for you.

In general, the more years that you pay into Social Security, you will have a lower GPO reduction. The logic is simply that if you are paying more years into Social Security, you are probably not working for a Social Security exempt agency. If you are not working for many years for an exempt agency, you wind up with a smaller pension and a smaller potential GPO reduction.

If you want to know more, you can go to the Social Security website, SSA.gov. You can type GPO into the search box at the top of the page, and you will get a lot of different resources. One I would recommend is a two-pager on the Government Pension Offset. It is pretty much plain English for the most part, something worthwhile reading. You also may want to make it available to your members or direct it to your employees.

Ways of Potentially Reducing the Impact of the Government Pension Offset (GPO)

If you do not work for an exempt agency for the last five years of your career, then the GPO goes away.

Think of it this way. Let's say you have worked as a public safety officer for 25 or 30 years for your city. If everybody else in the city, i.e., the maintenance workers, the accountants, HR, etc., all pay into Social Security, and just public safety does not, theoretically, in the last five years of your career, you could jump over to the public employee side. Now you are no longer a public safety officer. You stepped away from being in an exempt agency, and you are paying into Social Security for those last five years.

Before making the switch, one factor to consider is if the public safety pension benefit system is richer than, say, the public employee maintenance benefit system. You also have to think about salary changes and benefits. Does it affect your commute? If you were a cop for 25 years, you get to pick when you want to go on vacation because you have seniority. If you join the maintenance department, you are the low person on the totem pole. However, the bottom line is that there is a way to entirely get out of the GPO.

The other thing to think about is supplemental employer plans. "Supplemental" as defined by Social Security means it is not the primary retirement benefit. But it could be a voluntary one or one that your agency pays into on top of the primary benefit.

Say I am a cop. I am not paying into Social Security. The city pays for my pension plan, but they also allow me to put money into a 401(k) or a 457, whatever it might happen to be. The 401(k), 457, or 403(b) are considered supplemental plans. Any of these plans that just have contributions that I have made do not affect the GPO. They are not going to make that two-thirds reduction get any bigger. Anything that I voluntarily put into a 401(k), a 457, 403(b), as long as it is just money from me, does not get counted in that GPO calculation. If there are matching contributions from the employer, that would potentially increase the GPO.

If you are a Social Security exempt member working for a system where you are not paying into Social Security and if your employer makes contributions into a 401(k), 457, a 403B, if you have a choice, do not put your money with their contributions because it is potentially going to increase the GPO. If the city is putting money into a 401(k) for me, and they happen to have a 457, I probably want to put my money in the 457 because my money in the 457 will not increase the GPO.

Summary of Key Points about the Government Pension Offset (GPO)

The GPO only affects a married Social Security exempt member. It does not affect their spouse's Social Security benefits.

Suppose I am a married policeman working for the city, and I am not paying into Social Security. In that case, I must watch out if I am entitled to a one-half Social Security spousal benefit; it could also affect my survivor benefit. It does not take a whole lot of an agency-provided benefit to reduce or even eliminate the one-half spousal benefit, primarily if I worked my entire career working in a Social Security exempt agency.

The GPO has no impact whatsoever on the benefit provided by your agency.

Now here are some things about which to think. Say I am the policeman working for the city. Let's say my spouse began in the private sector, and she has a pension plan available to her. If there are joint, married payout options for her, I may want to encourage her to pick one of those so that if she were to pass away first, I would still get her pension because I may lose that Social Security survivor benefit.

The exempt member may want to talk to their spouse about picking a joint payout pension option. For exempt members themselves, if your system allows a pension option where if your spouse passes away first, you revert to a higher pension amount. That might be something you want to consider. If your pension benefit were to increase when your spouse passes away, that could help again offset that reduction in the survivor benefit from Social Security. Not all systems will offer these reversion options, and they go by different names.

Can you minimize the effect of the GPO? Just work more years in a Social Security paying job. The WEP, by the way, works the same way, so that is kind of a win-win. The more years you work in a Social Security paying job helps the GPO to go down and potentially help the WEP to go down.

Let's say if my employer is making contributions to the 457 on my behalf and if I have another retirement plan defined contribution plan option, I may want to put my money in that other plan voluntarily. It might not help a lot, but it could certainly help some. The whole idea is here is that you are separating employer money from employee money. If they are not mixed, any employee money will be invisible as far as the GPO is concerned. If the employer is putting money into a 401(k) and I also have a 457 available to me, I may want to use the 457. Again, not a huge impact, but every little bit helps.

What about matching contributions? Let's say you have a 457 plan, and your employer says if you put 4 percent into the 457, they will match 2 percent. Go ahead and take the match. Yes, the GPO will bite you a little bit, but you are getting a 100 percent return in essence on those matching contributions that are free money from the employer. Take the dollars in that scenario. If the match is up to 4 percent, put in up to 4 percent. I probably want to stop at 4 percent. If I have another defined contribution plan available, I will put the rest of my savings in a plan with employee-only money because that will help a little bit with the GPO.

There is that final five-year option to switch to another state or local government agency that pays into Social Security. Anybody who is thinking about doing that ought to call Social Security first and tell them exactly what your scenario is and what it is you are thinking about before you go. Avoid doing anything extreme like quitting one job to take the other job because it can get a little grey, especially if you are moving between different agencies and employers. But it is an option and can work for some folks.

Say we have a Social Security exempt worker. They have a stay-at-home spouse who has never worked outside the home and paid into FICA. If so, there is no Windfall Elimination Provision (WEP). There is no GPO because neither the worker nor the spouse has ever paid into Social Security.

If you have a client or member in this situation, it gets complicated when the worker has some years where they did not pay into Social Security and some years where they did pay into Social Security. For that stay-at-home spouse, now the WEP could apply to the worker. (Read this article on the Windfall Elimination Provision (WEP) for more information.)

The WEP could apply to the exempt worker, but not the GPO, as the GPO is based on a working spouse's Social Security benefit. If you are an exempt worker with a spouse working full time in the private sector, they have paid into Social Security. The GPO may and probably will impact my survivor benefit if my spouse passes away first, and it will likely also affect my one-half spousal benefit.

What if we have mixed years? If some years I did not pay into Social Security and some years I did, and I still have the spouse who has been in the private sector their entire career and paid Social Security the entire time. The WEP may affect me now because there were some years I did not pay into Social Security, and the GPO will probably also affect me.

Other Government Pension Offset (GPO) Resources

Another resource for you on this topic is Kitces.com. Michael Kitces is a financial advisor, private sector, super sharp guy, and does a lot of good research understanding on a whole host of different financial planning topics. He has this quick summary of how the WEP and the GPO apply and when it does not.

On the Social Security website, there are WEP calculators. That is probably one of the best tools out there for somebody who will be subject to the WEP. There is a GPO calculator. In my opinion, it is not as helpful, as it does not probably do justice to coming up with how the GPO might impact somebody. But there is one there.

There are also designations/certifications out there. So again, if you want to go deeper into Social Security, there is the National Social Security Advisor Certificate program.

It has a more academic understanding of how Social Security works. I have had some colleagues who have gone through this program, and they really liked it.

The second one there, the Registered Social Security Analysts, is a little more practice-oriented, more maybe for financial advisors trying to help their clients understand when to draw Social Security. It also covers the basics, and you get short-term access to some pretty sophisticated Social Security optimization software.

Social Security WEP: FOMO, IDK, or LOL?? – Michael Wilson

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Mike Wilson is the owner and founder of Integrity Financial Planning, which specializes in personal retirement planning. In one form or another, Mike has been in the training and financial services industry for 30 years. He earned his MBA in Finance from Baylor University and is a Certified Financial Planer®, Certified Retirement Counselor® and a Retirement Income Certified Professional®.

Mike and his wife Nancy reside in Salt Lake City, where he enjoys hiking and mountain biking whenever possible.

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Care Planning Prevents Tearing Families Apart

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Editor's note: This article is an adaptation of the live webinar delivered by Carroll Golden in 2021. Her comments have been edited for clarity and length.

You can read the summary article here as part of the 4th Qtr 2021 Retirement InSight and Trends Newsletter, worth 1.0 CE when read in its entirety (after passing the online quiz.)

You may also choose to take the full length course Care Planning Prevents Tearing Families Apart for 1.0 hour continuing education (CE) credit.

By Carroll Golden, CLU, ChFC, CLTC, CASL, LECP, FLMI, LACP, the Executive Director, Limited and Extended Care Planning Center (LECP Center) for the National Association of Insurance and Financial Advisors, C. Golden Consulting, LLC

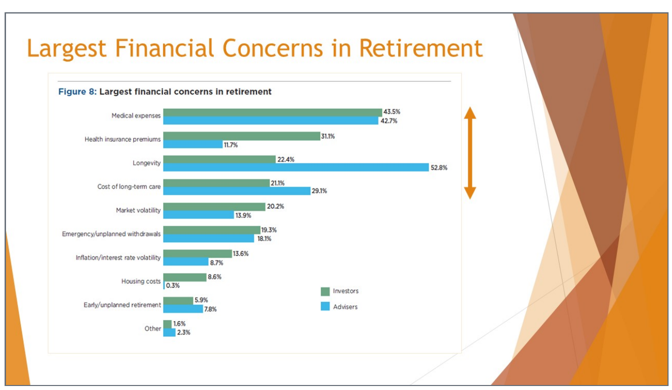
Now is a good time for us to look at a retirement security framework as we approach the most significant surge in the number of people aged 65 and over. This framework should include extended and long-term care because all generations, from the Silent to the Millennial, are caught up in the unpreparedness of aging adults with growing care needs. Retirement itself is changing along with its effect on extended and long-term care and vice versa.

Experience is an excellent teacher, but it can be a harsh master. We're all living longer, and aging takes its toll on our ability to remain independent. No matter how we define family, chances are that all of us will find ourselves, our current and our future clients, in the role of the caregiver or being cared for at some point in time, as well as needing care for the caregiver.

During the pandemic, we saw two realities confirmed. First, no one is immune to a sudden, unexpected care event. Secondly, as is true of so many things in life, preparation is key. Better preparation could have helped many families cope with the situations in which they found themselves.

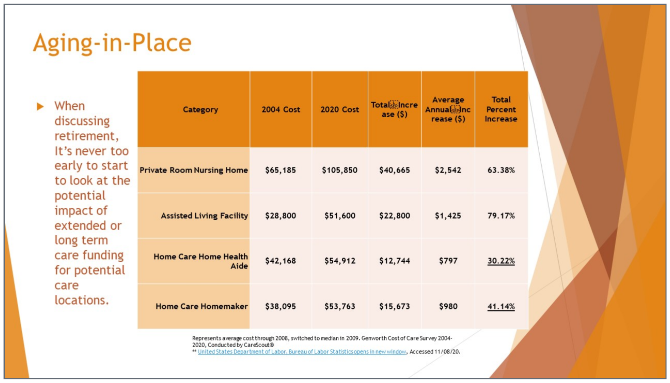
Starting a conversation about aging or becoming unable to manage incapacities is challenging for planning for extended and long-term care. Today I'm going to offer you a framework: *3 Simple Steps*. I hope they will help you kick-start critical conversations as a professional. I also hope they will help you expand your role since the three steps create relationships with multiple generations in families and friends of the families. Anyone who is going to be involved in caring for someone they love.

The Largest Financial Concerns in Retirement



This graph shows the largest financial concerns in retirement. The cost of long-term care is listed as one of the largest financial concerns in retirement (number four). The three above it are also intricately linked to long-term care: medical expenses, health insurance premiums, and longevity. All of these things start to become very evident as we get into the aging process and the issues that come along with it.

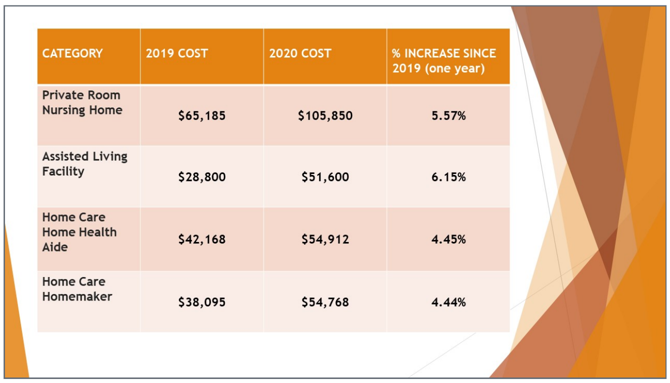
Having seen what we saw during the pandemic, everyone wants to age in place. Everyone. We must include in retirement planning the impact of trying to fund long-term care.



Category	2004 Cost	2020 Cost	Total Increase ($)	Average Annual Increase ($)	Total Percent Increase
Private Room Nursing Home	$65,185	$105,850	$40,665	$2,542	63.38%
Assisted Living Facility	$28,800	$51,600	$22,800	$1,425	79.17%
Home Care Home Health Aide	$42,168	$54,912	$12,744	$797	30.22%
Home Care Homemaker	$38,095	$53,763	$15,673	$980	41.14%

This slide compares the last 15 years' change in cost. There has been almost an 80% increase in the cost of assisted living facilities in the last 15 years. Take a look at the increase in home care/home health aide cost. Everyone wants to age in place. How will they manage that if the cost for home healthcare aides has increased 30 percent in the last 15 years?

Home Care Homemakers help people manage all of the things involved in aging, such as medication management and paying bills. Those costs have increased a little more than 40 percent since 2004. Do we think that that is going to change?



CATEGORY	2019 COST	2020 COST	% INCREASE SINCE 2019 (one year)
Private Room Nursing Home	$65,185	$105,850	5.57%
Assisted Living Facility	$28,800	$51,600	6.15%
Home Care Home Health Aide	$42,168	$54,912	4.45%
Home Care Homemaker	$38,095	$54,768	4.44%

Let's look at the increase in costs of just this one year, 2019 to 2020. Specifically, see what's happening with assisted living facilities. The bottom line, aging in place is going to be expensive.

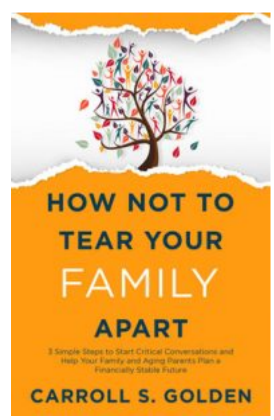
Ask your clients their thoughts about where they expect to retire. How far are they going to be from family and friends? Are they going to be able to afford an assisted living facility or a CCRC (continuing care retirement community)? What exactly do they have in mind? How many physical limitations will they have?

Longevity is Redefining Retirement

Let's now address the effect of longevity because here is the crossroads between long-term care, extended care, and retirement planning. The increases in longevity are genuinely unprecedented. I recently saw John Hancock's Vitality research; Vitality is a wellness program. With 50 years of research and data, they have concluded that while people live longer, they're not necessarily living healthier.

Funding longevity in retirement is a significant cost of retirement. Extended and long-term care absolutely must be included in planning, and it should also include long-term care.

The question is: Are your future clients involved? Will your client become what I call a presumptive generational caregiver?



We will go through a book I wrote (available on Amazon) that uses a story. The main character, Jody, is typical of most caregivers. Her parents are living in their home. Her dad is in pretty good shape; her mom is more wobbly and not all that steady on her feet. Jody is the on-call caregiver.

As so often happens, when people begin to feel the effects of poorer health and aging, they become more dependent. What was just a phone call now becomes an on-site caregiving responsibility. You have to drive over and help them with certain things. Maybe they don't want to drive long distances on a highway. Maybe they need help going to the doctor. It's very gradual.

There is also an "on a flight" caregiver. When my mother needed care, my sisters and I all lived in different states, and none of us lived where my mother needed care. We became "on a flight" caregivers. And if you think that that doesn't interrupt funding retirement, maybe you haven't had the experience yet.

In 2017, caregiving provided was worth about $470 billion, according to AARP. Can you imagine how much is being devoted to caregiving not only in terms of money but of hours?

What is the real issue? The real issue is starting the conversation with clients. Right along there with them, I don't want to talk about aging and needing help, etc. I have created a book that is a story because storytelling is telling. You, the advisor, can step into the role of a moderator, sometimes a mediator (unfortunately), sometimes a facilitator, or a guide along the way so that as they're looking at retirement, you bring up the subject. Frankly, it is a fiduciary responsibility. You are helping them with investments, retirement planning, and insurance. You also need to mention extended and long-term care planning because it impacts so much of their lives.

How to Start Conversations with Clients that Address Extended and Long-Term Care

How are you going to start these conversations? When starting the conversations, you must be aware that caregiving, extended care, or long-term care is never done in isolation. While people retire from work, they do not retire from their families, and they may find that their family will have to help them through this.

This is beyond just a math problem. We already looked at the rising costs for aging in place or going in a facility or, frankly, needing nursing care. But it's more than that. In my book. Jody is caught up and is already the on-call caregiver, and she's heading straight towards being the full-time caregiver.

Why haven't they started the conversation? Parents often aren't sure how to approach it without sounding as if they do not want to share this situation. Maybe they're in denial. Jody isn't starting the conversation, but she wonders if her parents are even sharing the current needs, let alone where they'll be in the future, or if they even have plans.

The rest of the family doesn't know how to discuss this either. They're seeing the impact on Jody, and they don't want to sound invasive. In addition, Jody has two children. The two children don't want to say to their mom, "Well, don't you want to talk about this?" Because they don't want to have Jody think that they're being critical.

What's the reality of what's happening to Jody? Almost all caregivers wind up impacting their work on their career. So many will also wind up being forced into giving up work entirely.

In Jody's case, it is her children who notice that not only is their mom now out of the running for her promotion, but she's not eating right. She has given up going to the gym. She is not visiting with her children, and Jody has young grandchildren. But Jody is caught. She's the sandwich generation, and the sandwich generation is now becoming a club sandwich because it's four generations involved in extended and long-term care.

We're starting to realize how many people retired early during the pandemic, and we weren't anticipating this number of Baby Boomers to retire. We all know that when they retire, it starts to impact the retirement plan. Whether you've worked with them as to whether they're going to retire or not, it falls on the retirement plan to support it.

I don't have to tell you that the caregivers may be sacrificing years of future earnings and contributions to the investment accounts you manage, to the retirement plans you have so carefully put together, to the insurances that you thought they would purchase or ladder as they got older.

An early retiree making $80,000 per year forgoes about $80,000 in savings over a decade. By the same token, they're now missing out on the 5 percent of salary contribution to the employer-sponsored plan. If they were also earning a retirement match that now they're not, that just exacerbates the entire thing.

So now you have clients who are retiring. If your client isn't the one retiring, they have retired parents. Again, it's a trickle-down effect.

3 Simple Steps Provide a Planning Framework for Consumers/Clients to Seek Advisement

Planning for extended and long-term care is a generational problem. I went into some detail about each generation in the book because, as we know, where you come from determines how you interpret and how you learned words. Each generation learned things according to the environment they were in. There will be many boomers who are going to live a long time and who are going to depend on either Gen Xers or Millennials and Silents who will depend on Boomers. That means when you're talking about extended and long-term care, you will have to learn to work with all of these different generations.

During my career, I noticed that if consumers had any knowledge about extended and long-term care, they tended not to talk about it or would walk away if only one solution were offered. So, I broke down the process to talk about care into three steps. Frankly, it doesn't matter which step you start with, whether you start helping them create a care guide, a care squad (which is inclusion for people in the family), or a care planning team.

Let's talk about *Step One: The Care Guide*. Life can only be understood backwards, but it must be lived forward. Family members may not remember what you said as an advisor, but they will remember how you made them feel. The process of suggesting that they create a care guide is a perfect ice breaker. Why? Because when you talk to them about the care guide, you're not just talking about healthcare.

For Jody, she needs to determine if her parents have a do not resuscitate (DNR) order in place. She needs to find out the family's history and find out if their wills are up to date. The care guide is far more than just what is your current medication.

What is Jody gaining? She's gaining insight into her family's medical history on both sides of the family. This can be a non-invasive exercise because they don't have to share everything. In my book, one of the granddaughters helps the grandfather put it all together, but he holds back a certain amount, and Jody is aware of that. The grandfather has the option to share some of it with just his advisor and maybe his daughter – preferably the three of them.

So, why are you, the advisor, helping with this? It's a caring conversation, and it uncovers facts and influencers for various generations of the families who will face retirement and who need to start to plan.

What about *Step Two: The Care Squad*? What do we work for, if not to make life less difficult for each other? That's the "what if" conversation. In the book, I shared that in planning for parents, sometimes – as in the case with my husband – he was made the executor of his mom's trust. Long story short, he didn't consult with the brother. He and his brother were at odds quite often. As a result, they're still not speaking with one another.

The Care Squad is designed so that when an incident occurs – and I assure you in the book, an incident occurs – instead of everybody panicking and running in directions and starting to be counterproductive, it pulls everybody into a role. When you give people a role and responsibility when there is an extended long-term care incident, everyone benefits. Jody won't be the only caregiver. We saw during the pandemic how overwhelmed many caregivers (the Jodies of this world, the Gen-Xers who were trying to help people who were in care facilities) were and how overwrought they became. Planning for the Care Squad will avoid that. For you, the advisor, you will get to know the generational family members.

In the case of Jody, they brought in a friend – Jackson – because he has been a lifetime friend and can be there in case Jody needs help with her husband or with her father. So, it's not necessarily just family members, and remember, we defined family in varied ways.

By familiarizing yourself with other family obligations, you can pose specific questions. The book has many questions that you can ask to help make you comfortable bringing up the topic with clients. Unless you can start the conversation and guide it along, it's not going to be as well incorporated into their retirement plan as it needs to be.

What about the *Third Step: The Care Planning Team*? "Fight for the things that you care about, but do it in a way that will lead others to join you." Ruth Bader Ginsburg. This is the discovery conversation. Let's say you're not a specialist in this area, so you want your client to be able to read through a story. In this story, Jody assigns to the various care planning team members, her children, her husband, herself, and her father because she needs her father to buy into whatever solution they discover. This step will help your client create a care planning team and review the different available options.

As your clients discover options, you guide, moderate, and facilitate these discussions. You're not selling them anything. You're not saying, "Here is the solution." Ultimately they might say to you, "You know? That's interesting, and that could work for me. Let's look more into that." You would respond with, "Yes, well, that's a good idea because frankly, the devil is in the details. We need to look at the details. These are just overviews."

I have included tools, research, links, and sidebars to help individuals and families see you as part of the team as you're doing these overviews,

When you're working through this with them, or they're working through it, and you're in touch with any one of them, they start to tell you their preferences, and you start to see how they envision growing older. This is a retirement issue. How do you envision yourself? This is all about behavioral finance and how people can envision their future self.

Generational Extended and Long-Term Care Planning

Above are extended and long-term care planning options for healthy people, such as Jody's son. Jody's son has two children. His wife isn't working outside the home, and she's taking care of their young children. He has a limited budget, and he discovered there is term insurance with an accelerated benefit endorsement rider. Considering that he rides a motorcycle, which completely freaks his wife out, he wanted to have the adviser look into what that would be for him.

Jody's son is two generations down from where we started helping with the grandparents. The whole idea is that once you get the conversation started by using any of the three steps, you start to not only grow your practice but think of Jody as your client or Jody's parents as your clients. You are starting to secure their retirement plan because you're looking at these various options with them, and hopefully, this is going to be something that they come to you and say, "What about this?" You may have to increase your professional network to be able to help. But isn't that a good thing, not a bad thing?

What if your client has some health issues or budget concerns? Some people just don't want insurance. They come to you, and they say, "Look, if we invest, then I think I can cover this." Somewhere along the line, the advisor said to Jody, "Okay, but right now, what if we had to invade your stock portfolio? Is there a good time?" When the market is high and it's earning well, do you want to pull it out? When the market is low, do you want to pull it out or let it sit, and maybe you'll recover? But at any rate, do you want to have to do that?

What about the tax implications of suddenly having to invade investments or funds that were growing for retirement, and now all of a sudden, boom, they're not growing. We all know that changes not only the numbers but the stress level is also terribly impacted by the sudden need to invade investments or retirement funds.

And as we saw earlier, Jody passed up a promotion, which will impact her retirement, especially long term.

What if the parents are genuinely impoverished? We can't disregard that Medicaid is there. We can't disregard that there are community, state, and county services that could also be an answer for certain clients, depending on the situation and what the family feels comfortable with.

How to Help Your Clients Not Tear Their Family or Retirement Plan Apart

If extended and long-term care isn't your area of expertise, please consider sharing the book because in it we offer overviews, links, and resources for the currently available extended and long-term care options. You can get a great deal of insight just from reading the story, but it does mean that if you send this book off to a client, you have brought up the topic.

At this point, if they don't want to go ahead with it or find that it is not a conversation they want to have with you, well, you tried. As a fiduciary, you certainly took on the responsibility of the impact that extended or long-term care could have on the planning that you're doing, and you took steps.

Remember, it doesn't matter how or in what order you use any of this. You've broadened your knowledge. Hopefully, you've become a generational advisor, and you have helped your client avoid tearing their family or their retirement plan apart.

For most of us, and certainly, for those who help plan retirement, the tricky part is that life doesn't stop while they're caught up in caring and juggling their own life. It's dynamic and ever-changing. No matter how they define caring, no matter how they define family, no matter how they define advice, this book will help them understand that you're there for them and that there isn't just one path to security. They may not only put their retirement at risk, but certainly, the impact on those who are caring for them is a big theme that pervades the book as well.

My primary objective of the three simple steps was to offer an easy-to-follow, easily adaptable process to help secure retirement. Stories can simplify complexity, and generational stories allow your clients to identify with characters. Suppose they don't want to talk about their situation. Let them talk to you about what they saw in the book, how they felt about it.

Successful fiduciary relationships ensue when clients see you as a critical driver and the moderator of a plan. The three simple steps can be used in any order and tell you that if they start with stage two, they're a little hung up on creating a Care Guide and talking about medical things. Explain to them that a Care Guide doesn't have to be medical. It can be about their retirement plan and things that can affect their retirement plan.

All in all, each step is your clue and your cue to integrate your value proposition, offer guidance, and put the best solution in place for generations to come.

There are a couple of resources that I wanted to mention. I am the Executive Director of the Limited & Extended Care Planning (LECP) Center. I'd love to have you reach out to me. We have conversations, and we have blogs. We are very much into social media. We do interviews. All in all, it's a center where we have information that we hope will help you, and we have the legislative working group housed there as well.

Care Planning Prevents Tearing Families Apart – Carroll Golden

About Carroll Golden, CLU, ChFC, CLTC, CASL, LECP, FLMI, LACP, the Executive Director, Limited and Extended Care Planning Center (LECP Center) for the National Association of Insurance and Financial Advisors, C. Golden Consulting, LLC

Carroll Golden is a forward-thinking organizational consultant and business strategist with a diverse international background holding senior leadership roles within the healthcare and insurance marketplace. Carroll is recognized by industry peers for her contributions in the extended and long-term care insurance (LTCI) field and is a frequent speaker and noted author across numerous professional benefits and financial services organizations.

Carroll has an extensive business background focused on business development, solutions selling, risk management and insurance distribution. As a Senior VP in charge of a leading carrier's LTCI Sales and Marketing department, her nationwide responsibilities spanned formulation of strategic sales plans, product development, innovative and traditional marketing initiatives. She excels in developing relationships and adding value within both small, privately-owned companies and large global corporations.

Working with a Certified Public Account audience, Carroll did a local radio spot on LTCI, focusing on the Executive Carve-Out Business market and later specialized in Group/Worksite Long Term Care Insurance. For several years, she contributed a monthly feature to Benefits Selling Magazine. Carroll gained brokerage and field perspective working with East Coast, and later with West Coast, national LTCI distributors.

Carroll entered the professional world as an International translator, having spent several years as a student at the Sorbonne in Paris and continuing her studies in Reims, France. Traveling to more than 44 countries while working with a prestigious Manhattan, NY law firm, Carroll gained insight into how different customs and traditions influence governments and businesses.

As an active member of the Society of Financial Service Professionals (SFSP), Carroll served as Chapter President and taught continuing education (CE) classes. Additionally, she served as Chairperson for both the Society of Actuaries Fifth and Tenth Annual Intercompany LTCI Conferences. She currently participates on the Board of Directors of the Intercompany Long-Term Care Conference (ILTCI). Carroll is President of C. Golden Consulting, LLC and is currently working with the National Association of Insurance and Financial Advisors. NAIFA is creating the first of several Specialty Centers. Carroll is the Executive Director of the NAIFA Limited and Extended Care

Planning Center (LECP Center). LECP is an easy to access hub-dealing with all aspects relating to or impacted by extended and long term care planning-or the absence of planning.

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Are Health Savings Accounts better than a 50% employer-match on a 401(k)?

Greg Geisler, PhD, CPA, Clinical Professor of Accounting at Indiana University-Bloomington

Editor's note: This article is an adaptation of the live webinar delivered by Greg Geisler in 2021. His comments have been edited for clarity and length.

You can read the summary article here as part of the 4th Qtr 2021 Retirement InSight and Trends Newsletter, worth 1.0 CE when read in its entirety (after passing the online quiz.)

You may also choose to take the full length course Are Heath Savings Accounts better than a 50% employer-match on a 401(k)? for 1.0 hour continuing education (CE) credit.

By Greg Geisler, PhD, CPA, Clinical Professor of Accounting at Indiana University-Bloomington

The tax-efficient order to invest and pay down debts, is in other words, how to maximize the tax-efficient accumulation of wealth while you are working. There are many articles on tax-efficient decumulation once you retire, but there is a very clear tax-efficient order for accumulating wealth.

Is it possible that an employee's health savings account contribution can increase their wealth more than an employer's 401(k) match? It is quite possible, and it happens a lot whether people realize it or not. I will show you how common it is, and I will prove it mathematically and visually.

After we do that, we will get onto the tax-efficient order to invest and pay down debts to maximize wealth. This includes utilizing Roth Retirement Accounts, tax-deferred retirement accounts, often called traditional retirement accounts, health savings accounts, and 529 higher education savings accounts.

What is a Health Savings Account (HSA)?

First, a little background on health savings accounts. You can only contribute to one if you have high deductible health insurance, which for many employers, it is either the only option or one of a couple of options that they offer. There are over 30 million health savings accounts currently in the US, and the number of accounts has been growing by approximately 10 percent per year over the last few years.

Typically, people put in approximately enough to cover their qualified medical expenses for the year. Over two-thirds of contributions are withdrawn in the same year. But unlike a flexible spending account for health expenditures where you have to use or lose it, a health savings account is yours as long as you are alive, like a quasi-retirement account. You can invest it.

As of now, there are $90 billion in health savings accounts. This is about $70 billion higher than about seven or eight years ago. Only about one-third of the $90 billion is invested, so $60 billion is sitting in cash. Of the $30 billion invested, about $20 billion is in bonds, and only about $10 billion is in stocks. The opportunity being missed is putting money in these health savings accounts to the extent you do not withdraw it in the same year, investing it for the long term if you do not need the money for a good while.

I have had a health savings account since 2015. In other words, I have had high deductible health insurance through my employer every year since 2015. I put the maximum into my health savings account every year, and it has grown, and I invest it in pretty much the US stock market, just an index fund. I do not pay any attention to it. I looked at it recently. I have $60,000 in there, and I have saved since I started my health savings account at the beginning of 2015. I have saved $35,000 worth of qualified medical expense receipts. So, in other words, any time I want to go forward, I can take out up to $35,000 tax-free.

Why am I waiting? When I am retired, and let's say I get to the top of a tax bracket, and I do not want to jump to a much higher tax bracket, that will be an excellent time for me to take money out of my health savings account tax-free and just put some of those receipts that I have accumulated into that year's tax folder. A significant advantage of a health savings account is its ability to be a quasi-retirement account.

What are the amounts you can put into one of these health savings accounts if you have high deductible health insurance? In 2022, the contribution limit for someone with self-only health insurance is $3,650. This is for employer and employee contributions combined. So, in other words, if the employer puts $1,000 into the HSA, the employee can only put in $2,650. If the coverage is for more than self-only, the maximum in 2022 is $7,300. If the employer puts in $2,000, the employee can put in the maximum of $5,300. The 2021 maximum contributions are $3,600 and $7,200.

Is a Health Savings Account (HSA) Better Than an Employer Match on a 401(k)?

Here we will start answering the question – is a health savings account better than an employer match on a 401(k)? Specifically, I will focus on a 50 percent employer match because that is a typical 401(k) employer match percentage. So, the employee puts $100 in, and the employer puts in another $50. That is your 50 percent match. Here is the answer: Is the employee's combined tax rate over 33 1/3 percent? If it is, and the employer's 401(k) match is 50 percent or less, then the health savings account makes the employee wealthier than the employee match on the 401(k).

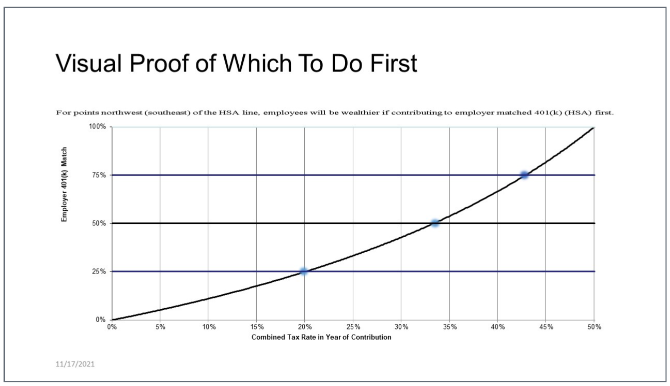
The Federal tax rate brackets start at 10 percent, then quickly go up to 12 percent, and they are there for a while, then they go to 22 percent, and they are there for a pretty good while, then they go to 24 percent. The tax rate brackets are there for quite a while, and then they go to 32, 35, and ultimately 37 percent. Those are the seven Federal income tax rate brackets under current law. And these rates have been in effect since 2018; they are scheduled to stay in effect through at least 2025.

Assume an individual is in the 22 percent Federal tax rate bracket to give you some idea of where that puts them as far as their income goes. For someone single, if their taxable income is over $40,000, which means their total income is over about $52,000-$53,000, they are in the 22 percent bracket if their total income does not go over about $100,000. Their taxable income does not go over about $86,000.

You might describe someone in the 22 percent bracket as moderate income. Assume that they are a resident of a state that also has an income tax and assume the rate there is six percent. Do not forget that this moderate-income individual has to pay 7.65 percent FICA (Federal Insurance Contribution Act) taxes on their salary, which is the 6.2 percent Social Security tax plus the 1.45 percent Medicare tax.

Add all these up – 22 plus 6 plus 7.65, and you get 35.65 percent as the combined tax rate for the moderate-income individual. That is over 33 1/3 percent. The health savings account will make the employee wealthier than a 50 percent 401(k) match. How do I know that? Take the tax savings of 35.65 percent and divide it by the after-tax contribution to the HSA, which is 64.35 percent of the total contribution. That is a 55.4 percent immediate return. That beats an immediate 50 percent return on an employer's 401(k) match.

Again, I assume the employer 401(k) match is 50 percent. If the employer 401(k) match were 75 percent or 100 percent, then the 401(k) match would make the employee wealthier. Even if the employer 401(k) match is 50 percent or less, the health savings account contribution makes the employee wealthier.



This graph was in the Wall Street Journal about five years ago. The curved line is the breakeven point. The vertical on the left-hand side is the employer 401(k) match. At the bottom, the horizontal line is the combined tax rate. You can see the second blue shaded bullet point right at the 50 percent 401(k) match line with the 33 1/3 percent combined tax rate. If the tax rate is anything above that you are in the southeast quadrant, you are underneath the curved line. That is a situation where the HSA contribution beats the 401(k) match. In contrast, the 401(k) match beats the health savings account if you are on the northwest portion.

Intuitively, you might question how a 401(k) match could not beat a health savings account contribution? The 401(k) match is extra money the employer is giving you. How can that not win? Think about any retirement account, whether a Roth retirement account or a tax-deferred retirement account like a 401(k). With the Roth, you do not get any tax savings at contribution. That is the downside to a Roth. With the 401(k) account, you must pay tax upon distribution.

In contrast with the health savings account, you get tax savings at contribution, and the distributions are tax-free if they are for qualified medical expenses. Now, qualified medical expenses for health savings accounts include your Medicare Part B and Part D premiums. Suppose you have long-term care insurance up to an amount limited by the tax law based on your age. Also, prescriptions and over-the-counter medicines. Suppose you go to the grocery store or pharmacy and buy allergy medicine over the counter. In that case, this is a qualified medical expense for purposes of HSA tax distributions, whether you pay for it with your HSA card or you reimburse yourself later for its payment. There are many more expenses than people think that qualify to be reimbursed tax-free through an HSA.

The HSA has three tax benefits: tax savings or contribution, tax-free while it is invested, and tax-free if withdrawn for qualified medical expenses. In contrast, Roth and traditional retirement accounts only have two tax benefits.

While the money is in the account, for both HSA and Roth accounts, you do not pay any tax on the dividends or interest or capital gain distributions, and with the Roth when you take the money out as a distribution. If the funds have been there long enough and meet the five-year rules, the distribution is tax-free if you are age 59 1/2 or older.

When you contribute to a 401(k), you save Federal and state income tax, but you do not save FICA taxes when you contribute to your 401(k). This is the intuition behind the triple tax benefit of contributing to an HSA because it also includes FICA tax savings versus only double tax savings if you contribute to a Roth or tax-deferred retirement account.

The Order to Invest and Pay Down Debts to Maximize Your Wealth

Contributing to the HSA and contributing the maximum to get the employer 401(k) match are steps 1A and 1B. The steps can be reversed; do not do the health savings account first and get the maximum 401(k) match first. Why? Because they both have such an incredibly good immediate return on them. Max out your health savings account if you have high deductible health insurance and get the maximum 401(k) match from your employer – steps 1A and 1B. It is not so much one beating the other; it is just doing both. Everybody needs to do both every year if possible. Why? Because you are on your way to maximizing your wealth by doing these two steps as step 1A and step 1B.

1A. Contribute the maximum to your HSA if you have high deductible health insurance. I cannot emphasize that enough.

1B. Put in just enough to the 401(k) to get the full match and then stop. Do not max out the $19,500 2021 maximum Federal law allowable contributions to your 401(k). What if the employer match is higher – 75 percent or 100 percent? Most of the time, a 100 percent match or even a 75 percent match by the employer of the 401(k) will beat the HSA. If that's the case, get the 401(k) match first and then do the HSA maximum second.

3. Pay off high-interest rate debts. Credit cards with the 20 percent or 24.99, or 29.99 percent APR. Do I not want to do that first? No. Are you saying get a 50 percent 401(k) match before paying off my high-interest rate credit cards? Yes. I thought the most important thing was to get rid of my high-interest credit card debt? No, it is the third most important thing. Why? What is the return on it? Let's call it a 24 percent interest rate. That is a guaranteed 24 percent rate of return. That is not as good as a 50 percent 401(k) match. That is not as good as a 54-55 percent return in the example we did earlier on the HSA contribution. That is why I do this third.

4. This is the only time I stray from the tax-efficient order. Contribute to a Roth IRA. You must have income that is low enough to do that. I am talking about your adjusted gross income, which is your total income minus any above-the-line deductions. Your total income cannot be too high for you to be allowed to contribute to a Roth IRA. That is why many people wait until the end of the year, see what their adjusted gross income (AGI) is for the year, make sure it is low enough that they can contribute to a Roth IRA. For 2022 your AGI has to be below $144,000 if you are single, and if you are married filing joint, your AGI has to be below $208,000 to contribute the maximum to the Roth IRA.

   The maximum you can put in in 2022 is $6,000. Now, you can put that in up until April 15, 2023. That is the latest you can put it in, and you just check a box saying I want it to be a 2022 contribution. Even though I contributed in the first three and a half months in 2023, I want that to be a 2022 contribution.

   If you are age 50 or older on December 31, 2022, you can put in an extra $1,000 or $7,000 to your Roth IRA if your income is not too high.

   Why did I move Roth IRA up to fourth? You can use it as an emergency account. We know the importance of having an emergency account. What are those rules of thumb you always hear? You should have three- to six months of expenses in an emergency account. I tell you to have zero in an emergency account and instead have a Roth IRA. This is going to be your emergency account.

   Contributions to a Roth IRA can be withdrawn tax-free at any time, not after you are 59 1/2. Any time. However, you cannot withdraw the earnings or the appreciation in value without penalty.

5. If you have children or grandchildren you want to help put through higher education, contribute to a 529 account if it provides State tax savings. Notice that if it does not provide State tax savings, this is no longer in fifth place. Why is this fifth? Why is this better than unmatched contributions to retirement accounts (sixth in the rank order)? Basically, from a tax perspective, a 529 account is equivalent to a Roth, and it is tax-free.

   You do not save any Federal income tax when you put money in. You do not pay any Federal, State income tax when you take it out for the beneficiary's qualified higher education expenses. However, if you get State income tax savings, you do not get that when you contribute to a Roth. They changed the law within the last couple of years. You can withdraw from the 529 up to $10,000 maximum per year for the beneficiary for K-12. If they go to an expensive private school that costs $25,000 a year, you can only withdraw up to $10,000 tax-free per year.

   The other rule added within the last couple of years is if you still have some money in that account after the beneficiary completes their higher education, you can take a $10,000 total out and pay down the beneficiary's student loans. Of course, you do not want to over save in a 529. Assuming you will use what you put into the 529 for the beneficiary's qualified education expenses, it beats the sixth step, contributing to unmatched retirement accounts.

   Does contributing to a 529 account not beat a Roth IRA? Yes, it does beat a Roth IRA if you get State income tax savings, but I put the Roth IRA fourth because it can be an emergency account, and that benefit is very valuable. If I stuck to my tax-efficient order, contributing to a 529 if you get state tax savings would be fourth, and contributing to a Roth IRA would be after that. But again, I am trying to open your eyes to Roth IRAs are excellent emergency accounts; contribute to them.

6. Unmatched contributions to retirement accounts. Which ones? If the tax rate you put it in is the same as the tax rate you expect when you take it out, and years in the future, then it does not matter whether you contribute to a traditional or a Roth. In contrast, if your tax rate is lower today and you expect it to be and years in the future, invest in a Roth. Many employers offer Roth 401(k) as an option in their 401(k) plan but not all employers yet. On the other hand, if your tax rate now is greater than the tax rate you expect in years in the future when you are taking money out of the retirement accounts, invest in a traditional tax-deferred retirement account, like a 401(k).

   If the best you can figure is that your tax rate should be about the same now as later, here are some other things to think about. When you contribute to a 401(k), you know the amount of tax savings you get. That is valuable because, in contrast, when you contribute to a Roth, it is uncertain until you take the money out in the future what the value will be. You know the whole thing is tax-free if it is in there long enough, but is your tax rate low or high or in the middle in the future when you take the money out of the Roth? There is uncertainty there.

   On the other hand, so many clients are so loaded up with tax-deferred retirement account money and have no or little money in Roth's, it might not be a bad idea to contribute to a Roth.

   Lastly, the after-tax dollars contributed to a Roth are greater than after-tax dollars contributed to a tax-deferred retirement account. You can put in $20,500 if you are not age 50 or older in your 401(k) or your Roth 401(k) for 2022. You get tax savings immediately when you put money into the traditional 401(k); however, you get no tax savings when you put it in the Roth. So, effectively, you can contribute a lot larger amount of after-tax dollars to a Roth.

If you have a client who can max out their contributions to their 401(k) and their tax rate now is similar to what they expect ten years in the future when they are taking money out, that would be a good idea to put money into the Roth 401(k) if the employer offers one. A more considerable amount of after-tax dollars can be contributed to the Roth 401(k) compared to the after-tax dollars going into your traditional 401(k). Again, the tax savings effectively go into the account for a traditional 401(k).

7. Pay off moderate interest rate debts. What is moderate? It depends on the client, or it depends on you, and it depends on how much risk you are willing to take.

8. Investing through taxable accounts. Why is this eighth on the list? Of course, the uncertainty of the return if you invest in stocks compared to a moderate interest rate debt has a certain return, a guaranteed return equal to the after-tax interest rate. Why do I say after-tax interest rate instead of interest rate? If the moderate rate debt is something like student loans and you get to deduct it, the after-tax interest rate is less than the before-tax interest rate. On the other hand, if the loan is a car loan for five percent, you cannot deduct any interest, so the after-tax interest rate is the same as the before-tax interest rate.

   Should you pay off that five percent auto loan before investing through taxable accounts? This is up to the client. Why? Maybe they would be better off if they invested in stocks or a balanced portfolio, or maybe not. You never know when you invest because of the uncertainty with the returns on the equities. If the client is more willing to take risks, you will not pay off that five percent loan. You would say that is a low-interest-rate debt, which is not even on this list to maximize wealth. I have a 0.9 percent car loan, and I will not pay that off early. I can do better investing.

   Why is investing through taxable accounts last? Because sooner or later, you have to pay tax on those accounts. The after-tax return is not nearly as good as it is on health savings accounts, Roth retirement accounts, and tax-deferred retirement accounts.

Why Follow This Rank Ordering to Building Wealth?

Simple. It maximizes your wealth. Further, different people run out of available cash at different points in their rank-ordering, so you need some rank order to tell you what will maximize your wealth. The more you do not spend, the more you can pay down debts and invest, and the wealthier you will be.

You must have an excellent nontax reason for not following this rank order to build wealth. If you follow it, it will maximize your wealth, given however much of your normal monthly paycheck you do not spend.

Are Health Savings Accounts better than a 50% employer-match on a 401(k)? – Greg Geisler

About Greg Geisler, PhD, CPA, Clinical Professor of Accounting at Indiana University-Bloomington

Greg received his PhD from University of North Carolina-Chapel Hill, is a Clinical Professor of tax accounting at Indiana University-Bloomington. He teaches a course called "Income Tax and Individual Financial Planning."

Retirement planning thought leadership and expertise

Greg publishes articles at the intersection of income tax and financial planning. Specifically, in the last ten years he has published 6 such articles in the Journal of Financial Service Professionals and 7 such articles in the Journal of Financial Planning (JFP), including one that received the 2017 "Montgomery-Warschauer Award" for most outstanding article contributing to the betterment of the financial planning profession.

At his previous university, he was awarded the only 2017 Chancellor's Teaching Excellence Award.

He has been quoted in the Wall Street Journal and many times in the financial press and on newscasts.

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