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Resolute Connections

In this month's newsletter our first article, *Roth Conversions Reconsidered*, reviews how The SECURE Act of 2019 impacted the benefits of inherited IRAs, and as a result perhaps improved the benefits of the Roth IRA conversion.

How Significant is the Latest Market Decline? concerns the new bout of volatility impacting the U.S. stock market, which from a historical perspective is common in September when Wall Street returns from summer vacations. However, this year it is perhaps more troubling as it reminds uneasy investors of the sharp downturn of this past March.

COVID Update provides the status of the quest for a vaccine, and *Spending for Your Future Health* looks at how much one might expect to spend on medical and healthcare services in retirement.

Please be safe and we wish you continued health. If you have any questions about anything we have covered in the articles, or a specific situation please feel free to give us a call, or visit our website, www.ResoluteFinancial.com.

Roth Conversions Reconsidered

The SECURE Act significantly reduced the benefits of an inherited traditional or Roth IRA, by requiring the non-qualified heir (typically anyone other than the spouse) to take the full amount out of the account within ten years of receipt. Interestingly, that provision makes it somewhat more beneficial for some people to make Roth conversions today.

Chances are you know the difference between a traditional IRA and a Roth; the gist of it is that contributions to a traditional IRA are tax-exempt, but when the money is taken out of a traditional IRA in retirement, it is taxed at the retiree's current tax rate. In contrast, contributions to a Roth are not tax-exempt, but the money comes out tax-free. If you convert from traditional to Roth, then you have to pay ordinary income taxes on the money that is shifted over at ordinary income rates, as the price for getting tax-free distributions in the future.

In general, you don't want to convert assets from a traditional IRA to a Roth IRA unless you can pay those taxes with outside funds; otherwise you're reducing the money that can accrue tax-free until the money is needed. The traditional calculation is that the conversion only makes sense if the person's tax rate today is lower than the future tax rate—and if you have a crystal ball which tells you what future tax rates will be, we would like to have a conversation about it. But some bets are better than others. The years between when a person leaves work and age 72 (when that person has to take required minimum distributions out of the traditional IRA) can be ideal for a conversion. The tax rate during those years when no employment income is earned can be low, and partial conversions up to certain tax brackets can be very attractive. This reduces the required minimum distributions (RMDs)

So, what's the additional argument for a Roth conversion post-SECURE Act? Some people don't need their IRA assets to pay for retirement. As a result, they take the lowest amount possible—the RMD—out each year, maintaining a balance, which they will leave to their heirs. The additional benefits accrue to the heirs, particularly if the heirs would inherit the account during their peak earning years.

Under SECURE, if the Roth IRA account is inherited, it still has to be liquidated within ten years of receipt—just like the traditional IRA. But the Roth beneficiaries face a simpler set of choices regarding the payment of taxes. If they inherit a traditional IRA, they have to decide whether to take the money out all at once at the end of 10 years, and risk having a huge tax bill because the distribution puts them in the highest tax bracket, or take the money out gradually and forego years of tax-free compounding. If the new owner of the account is in their prime earning years, then they may already be in a high tax bracket and be pushed higher no matter what they do. A big part of the bequest would be lost to taxes.

The Roth IRA beneficiary, meanwhile, has the luxury of allowing the full 10 years of compounding to proceed without any tax consequences to worry about. He or she is never pushed into a higher bracket during peak earning years. A Roth conversion by the parents is thus a way to transfer more assets to the heirs.

Everybody considering a Roth conversion should talk with a professional to get a full analysis of the potential benefits and drawbacks—understanding, of course, that this analysis requires modeling the unknown future tax code and income levels of potential heirs. Paying taxes now for benefits in the future could be a great strategy under a variety of circumstances which are, alas, still essentially unknowable.

How Significant is the Latest Market Decline?

The U.S. stock market has suddenly been hit by a new bout of volatility, reminding uneasy investors of the sharp downturn last February and March. We are nowhere near that level of decline at this point, but the fact that it happened once means that it could, conceivably, happen again.

Market analysts were at a loss to explain how the major indices were constantly breaching new record highs when the U.S. economy was wounded by the pandemic, and they seem not to be much better at explaining the recent—so-far-brief—selloff. But the answer is always the same: investors, particularly quick-twitch traders, suddenly started feeling less bullish and started taking some of their profits off the table. Whether this newly-cautious psychology will take hold and turn into a panic, or pass and allow the market to resume its climb, is impossible to predict.

What we DO know is that the unemployment rate is continuing to fall as the jobs picture has improved for the fourth month in a row. But that still means that roughly 8.5% of able-bodied Americans are out of work, which cannot be good for overall economic productivity. We know that the Federal Reserve Board, which has pockets of unlimited depth, is committed to keeping interest rates low and pursuing the stabilization of the markets. Congress is debating another round of relief for Americans hit hard by job loss and pandemic-related economic hardship, which could stimulate consumer spending similar to the previous stimulus bill. There is great uncertainty about whether we will see a resurgence in the pandemic, and the shadow of the November election has created its own levels of anxiety on both sides of the political divide. Depending on how you feel about these factors, positive or negative, likely colors your view of the current market valuations.

The decline has been led by (largely unanticipated) drops in some of the largest technology companies, which make up a huge percentage of the S&P 500 index—and it was precisely these stocks which had previously been responsible for the soaring index. Apple shares fell more than 6%, while Facebook and Amazon were down more than 4%. Microsoft slid 5.4% and Netflix closed 1.8% lower. Alphabet (Google) lost 3.6% of its value.

So far, the drop is a small fraction of the 50% rally since the March low—down 2.3% last week — and nobody should be surprised if and when the market pulls back from record highs. Only a working crystal ball will tell us whether the markets are taking a breather or previewing yet another bear market, but perhaps the rapid recovery after the severe February/March downturn can give us some comfort. Long-term, the U.S. economy steadily builds value in public companies, and in every instance in the past—through wars, recessions and even pandemics—the markets have eventually recovered from downturns to post new highs. The next bear market, when it comes, should be no different.

COVID Update

Many people are wondering why we still don’t have a vaccine for the COVID-19 virus yet, and when we’ll finally get one. But amid the hopeful headlines, we aren’t hearing much from the deep experts who are in the trenches trying to find an effective way to prevent the virus from lodging in our bodies. What are they saying these days?

Dr. Peter Hotez, at the Center for Vaccine Development at Texas Children's Hospital, notes that the current pandemic is actually our third major encounter with a coronavirus. There was Severe Acute Respiratory Syndrome (SARS) in 2003, and the Middle Eastern Respiratory Syndrome (MERS) in 2012. Like those other viruses, COVID-19 replicates in the upper airways of the human body and is being transmitted whenever people cough, sneeze or even speak—whenever we aerosolize the virus into the air. Inside the body, scientists have found that the virus makes us sick when it attaches to something called the ACE-2 receptor that is found in the heart and lung tissue (and also in parts of the nervous system).

Developing an effective preventative is, therefore, not as complicated as you might imagine; an effective vaccine has to trigger an immune response that will prevent the coronavirus from docking to the very specific ACE-2 receptors in the body. But how do you do that in a way that is safe and effective? Hotez notes that 90% of all vaccines, for all diseases, never make it to the end of the clinical trial, often because safety concerns have emerged. Testing the safety of a virus vaccine has always, in the past, required years of human trials—in fact, decades-long timelines are more normal. The fastest vaccine ever developed in history was the mumps vaccine—which took four years.

Will we break that record? One coronavirus vaccine has already received government approval: something called Sputnik V, developed by the Gamaleya Research Institute in Moscow. But many health experts are concerned about the vaccine's safety and efficacy, since it was rushed to approval before it had entered Phase 3 clinical trials.

The Healthline website, which is tracking treatments and vaccine efforts around the world, notes that there are now more than 100 vaccine projects related to the COVID-19 virus, but most experts think the most likely timeline for a vaccine to come to market is summer or fall 2021. That timeline could be accelerated due to a "human challenge trial." Some 30,000 people in more than 140 countries have signed up to get various experimental vaccines and then voluntarily expose themselves to the coronavirus—rather than the usual trial, where people are vaccinated and then the researchers wait to see if they have contracted the virus by participating in normal life (whatever that means these days).

Several public/private partnerships are working on the problem. Operation Warp Speed is a collaboration of the U.S. Health and Human Services, the National Institute of Health and 18 biopharmaceutical companies. The COVID-19 Prevention Trials Network combines clinical trial networks funded by the National Institute of Allergy and Infectious Diseases, the HIV Vaccine Trials Network and the Infectious Diseases Clinical Research Consortium. The World Health Organization has organized a Coalition for Epidemic Preparedness Innovations working with vaccine manufacturers Inovio, Moderna, CureVac, Institut Pasteur/Merck/Themis, AstraZenica, Novavax, the University of Hong Kong, Clover Biopharmaceuticals and the University of Queensland, Australia.

The President appears to have promised that a breakthrough vaccine will be available before the November election. But people who are banking on that promise should know that the U.S. Food and Drug Administration has scheduled a public meeting of the Vaccines and Related Biological Products Advisory Agency to discuss what would seem to be an early stage of the process: the general development of COVID-19 vaccines. This meeting will review the data that would be needed to facilitate the authorization or licensure of any vaccine that might be developed in the future; in other words, what the clinical trials should cover and what their results should be.

Of course, even if somebody does manage to develop a promising vaccine, it has to be supported by the largest drug companies or the government—who sometimes have their own agendas. Hotez recalls how a vaccine that would have prevented the SARS epidemic in 2003 sat untouched in a lab freezer, because his team couldn't secure enough funding to begin clinical trials.

Spending for Your Future Health

When you create your retirement plan, and look at how much you expect to spend on food and shelter, greens fees, cruises and restaurants, what do you estimate you'll spend on medical and healthcare services?

Every year, the Milliman insurance industry consulting firm issues a report that estimates the average cost of health insurance and copays across the population of

Americans. The most recent study looked at couples who are assumed to live to age 88 and 90, respectively, and takes into account premiums and out-of-pocket expenses for a Medicare Part D plan and Medicare Supplement Plan G, assuming that medical costs overall will rise 4.9% a year.

The result? A healthy 65-year-old couple retiring in 2020 would be projected to spend $351,000 in today's dollars on healthcare over their lifetime; $535,000 in future dollars. A healthy 45-year-old couple would be projected to spend $505,000 in today's dollars—$1.4 million in future dollars.

It is important to note that this is an average, which means for people who experience significant health conditions, the numbers will be higher. And for people who manage to stay healthy until the day they die in their sleep without requiring extensive medical care or hospitalization, the costs could be much lower. But the average expenses—34% of a couple's Social Security benefits in their early years of retirement—might come as a shock to some people, and should cause some to revisit their retirement spending assumptions.

Source:
Bob Veres Inside Edition Newsletter

For more information on these topics or for a free consultation, contact Resolute Financial, LLC at (978) 463-8771 ext. 1003.