Oakcrest Insight

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RISK PERSPECTIVE

Risk is a factor in any investment decision that you make. Your tolerance for risk is something that you will want to consider when you make decisions alongside your trusted financial professional. Your risk tolerance is balanced against your time horizon, meaning the time between now and when you anticipate needing your money.

But is it possible to avoid a loss? No, not completely, but you can take steps to manage that risk when investing. This is where conversations about your risk tolerance are critical.

What would you rather have, $500 right now or a 50% chance at $2,000? Many people go for the $2,000 and rightfully so. Since you have a 50/50 chance, a decision tree shows the $2,000 answer carries a potential value of $1,000.

But let's add a few zeros and see if that changes your perspective.

What would you rather have, $50,000 right now or a 50% chance at $200,000? The decision tree says the opportunity to win $200,000 has the highest potential value. But in reality, many people second-guess that decision because $50,000 is a lot of money.

Remember, there is no correct answer to these questions. They simply help you better understand the concept of risk.

Investment risk can be managed, but it can't be eliminated entirely. All investments carry some level of risk. And in general, the greater the risk an investment carries, the higher its potential return.

Risk happens, but don't let it get in the way of your dreams. Ultimately, these concerns should only serve to inform you and the questions that you ask the financial professional you are working with. The conversation should include your questions about the risks for each strategy presented as well as questions from your professional about the investment goals you want and the aspirations you hope to realize.

RETURNS (AS OF 01/31/23)

ASSET CLASS	INDEX	4 WEEK	YTD	1 YEAR	3 YEAR
US Large Cap	S&P 500 TR	6.18%	6.18%	-9.72%	8.12%
US Large Cap	Dow Jones TR	2.38%	2.38%	-2.98%	6.45%
US Small Cap	Russell 2000 TR	9.69%	9.69%	-4.76%	6.18%
International	MSCI EAFE NR USD	8.05%	8.05%	-5.49%	1.75%
Taxable Bonds	Barclays US Agg Bond TR	3.33%	3.33%	-8.30%	-2.39%

Market indexes listed are unmanaged and are not available for direct investment.

WHAT IS A ROTH 401(K)?

While many people are familiar with the benefits of traditional 401(k) plans, others are not as acquainted with Roth 401(k)s.

Since January 1, 2006, employers have been allowed to offer workers access to Roth 401(k) plans. And some have introduced offerings as part of their retirement programs.[1]

As the name implies, Roth-401(k) plans combine features of 401(k) plans with those of a Roth IRA.[2,3]

With a Roth 401(k), contributions are made with after-tax dollars – there is no tax deduction on the front end – but qualifying withdrawals are not subject to income taxes. Any capital appreciation in the Roth 401(k) also is not subject to income taxes.

What to Choose?

For some, the choice between a Roth 401(k) and a traditional 401(k) comes down to determining whether the upfront tax break on the traditional 401(k) is likely to outweigh the back-end benefit of tax-free withdrawals from the Roth 401(k).

Please remember, this article is for informational purposes only and is not a replacement for real-life advice, so make sure to consult your tax professional before adjusting your retirement strategy to include a Roth 401(k).

Often, this isn't an "all-or-nothing" decision. Many employers allow contributions to be divided between a traditional-401(k) plan and a Roth-401(k) plan – up to overall contribution limits.

Considerations

One subtle but key consideration is that Roth 401(k) plans aren't subject to income restrictions like Roth IRAs are. This can offer advantages to high-income individuals whose Roth IRA has been limited by these restrictions. (See accompanying table.)

	Traditional 401(k)	Roth 401(k)	Roth IRA
Contributions	Contributions are made with *pretax* dollars	Contributions are made with *after-tax* dollars	Contributions are made with *after-tax* dollars
Income Limits	No income limits to participate	No income limits to participate	For 2022, contribution limit is phased out between $204,000 and $214,000 *(married, filing jointly)*, and between $129,000 and $145,000 *(single filers)*
Maximum Elective Contribution*	Contributions are limited to $20,500 in 2022, ($27,000 for those over age 50)*	Aggregate contributions are limited to $20,500 in 2022, ($27,000 for those over age 50)*	Contributions are limited to $6,000 for 2022, ($7,000 for those over age 50)
Taxation of Withdrawals	Qualifying withdrawals of contributions and earnings *are* subject to income taxes	Qualifying withdrawals of contributions and earnings *are not* subject to income taxes	Qualifying withdrawals of contributions and earnings *are not* subject to income taxes
Required Distributions	In most cases, distributions must begin no later than age 72	In most cases, distributions must begin no later than age 72	There is no requirement to begin taking distributions while owner is alive
* This is an aggregate limit by individual rather than by plan. The total of an individual's aggregate contributions to his or her traditional and Roth 401(k) plans cannot exceed the deferral limit – $20,500 in 2022 ($27,000 for those over age 50).			

Source: IRS.gov, 2022

Roth-401(k) plans are subject to the same annual contribution limits as regular 401(k) plans – $20,500 for 2022; $27,000 for those over age 50. These are cumulative limits that apply to all accounts with a single employer; for example, an individual couldn't save $20,500 in a traditional 401(k) and another $20,500 in a Roth 401(k).[4]

Another factor to consider is that employer matches are made with pretax dollars, just as they are with a traditional 401(k) plan. In a Roth 401(k), however, these matching funds accumulate in a separate account, which will be taxed as ordinary income at withdrawal.

Setting money aside for retirement can be part of a sound personal financial strategy. Deciding whether to use a traditional 401(k) or a Roth 401(k) often involves reviewing a wide range of factors. If you are uncertain about what is the best choice for your situation, you should consider working with a qualified tax or financial professional.

Citations

1. To qualify for the tax-free and penalty-free withdrawal of earnings, Roth 401(k) distributions must meet a five-year holding requirement and occur after age 59½. Tax-free and penalty-free withdrawal also can be taken under certain other circumstances, such as a result of the owner's death or disability. Employer matches are pretax and not distributed tax-free during retirement. Once you reach age 72, you must begin taking required minimum distributions.

2. In most circumstances, you must begin taking required minimum distributions from your 401(k) or other defined contribution plan in the year you turn 72. Withdrawals from your 401(k) or other defined contribution plans are taxed as ordinary income, and if taken before age 59½, may be subject to a 10% federal income tax penalty.

3. Roth IRA contributions cannot be made by taxpayers with high incomes. In 2022, the income phaseout limit is $144,000 for single filers, $214,000 for married filing jointly. To qualify for the tax-free and penalty-free withdrawal of earnings, Roth IRA distributions must meet a five-year holding requirement and occur after age 59½. Tax-free and penalty-free withdrawal also can be taken under certain other circumstances, such as a result of the

owner's death or disability. The original Roth IRA owner is not required to take minimum annual withdrawals.

4. IRS.gov 2022

HEALTHCARE COSTS IN RETIREMENT

In a 2022 survey, 35% of all workers reported they were either "not too" or "not at all" confident that they would have enough money to pay for their medical expenses in retirement. Regardless of your confidence, however, being aware of potential healthcare costs during retirement may allow you to understand what you can pay for and what you can't.[1]

Healthcare Breakdown

A retired household faces three types of healthcare expenses.

1. The premiums for Medicare Part B (which covers physician and outpatient services) and Part D (which covers drug-related expenses). Typically, Part B and Part D are taken out of a person's Social Security check before it is mailed, so the premium cost is often overlooked by retirement-minded individuals.
2. Co-payments related to Medicare-covered services that are not paid by Medicare Supplement Insurance plans (also known as "Medigap") or other health insurance.
3. Costs associated with dental care, eyeglasses, and hearing aids – which are typically not covered by Medicare or other insurance programs.

It All Adds Up

According to a HealthView Services study, a 65-year-old healthy couple can expect their lifetime healthcare expenses to add up to around $597,389 before accounting for inflation.[2]

Should you expect to pay this amount? Possibly. Seeing the results of one study may help you make some critical decisions when creating a strategy for retirement. Without a solid approach, healthcare expenses may add up quickly and alter your retirement spending.

Prepared for the Future?

Workers were asked how much they have saved and invested for retirement – excluding their residence and defined benefit plans.

Source: EBRI.org, 2022

Citations

1. EBRI.org, 2022
2. HVSFinancial.com, 2022