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TILIA NEWS

INVESTMENT MANAGEMENT | FIDUCIARY ADVICE | FINANCIAL PLANNING

IRS Punts on Catch-Up Contribution Changes

As a result of legislation included in the SECURE Act 2.0, a popular tax deferral method for savers is going away. For the last 22 years, savers aged 50 and above have been allowed to make extra contributions into retirement accounts on a pre-tax basis. The allowed amount varied from an extra $1,000 a year in a traditional IRA, to $7,500 a year in a 401k plan for 2023.

The rule change was slated to become effective on January 1, 2024, but the IRS just announced a 2 year delay to give more time to retirement plan platforms to update their systems.

Starting in January 2026, the catch-up contribution will no longer be available for people earning over $145,000 in annual wages. While this is a negative for those looking to save on taxes in the short-run, the news isn't all bad. Workers earning above $145k will still be allowed to make the extra

Low Coupon Bonds Look Attractive

Today's bond market looks drastically different and more attractive than it has for the last 15 years. During the era of 2010 - 2021, companies issued long-term bonds at incredibly low rates, allowing them to borrow money from investors at rates as low as 1 - 3%. Following the rapid rise in interest rates over the last 2 years, these low "coupon" bonds are left trading at large discounts to their maturity value.

To dispense with the jargon, "coupon" is just another word for the fixed interest rate that a corporate bond pays an investor. For example, The Goldman Sachs Group has a bond that matures in February of 2032 and it pays a fixed interest rate of 2% (1% paid twice a year). While the return on the interest rate alone is paltry, the asking price for that bond today is just north of 73 cents on the dollar. So roughly $730,000 invested in this bond would pay the investor $20,000 a year, and the investor would receive $1,000,000 in just over 8 years. That works out to be a yield to maturity of 6.08% - not bad for a bond that carries an A2 rating from Moody's.

The potential return is not unique in today's bond will instead be directed into a post-tax "Roth" bucket within the retirement plan. So while you'll pay taxes on those wages in 2026, you'll then be able to escape taxation on all future growth & income on that money in the future.

Upcoming Tilia Events

Tilia has several events coming up this fall that are open to clients. Below is a quick rundown:

1) "Key Financial Insights for Small Businesses" - Ryan Casey will be one of four panelists. Ryan's portion of the presentation will be focused on exit planning for owners preparing for a business sale. This event will take place on November 9th from 4:30 - 6:00pm at Azalea Station at 1502 Castle St. The event will be ticketed via Eventbrite. We'll be sending out invitations to clients and friends who operate small businesses in the area.

2) "Cairn Travels Advisory: Reducing Travel Stress". Elizabeth & Darryl Rogers of Cairn Travels will be presenting travel tips and insights to clients of Tilia at Banter at 19 S. 2nd St. on October 4th from 4:30 - 6pm. This should be a fun event, and we look forward to hearing some great ideas for ways to "invest" in memories via travel.

market. There are plenty of high-quality bonds offering 6%+ returns for 7-12 years these days. Some of these even carry a high fixed interest rate of 5 - 6%. While that is music to the ears of an investor who is thirsty for current income, taxation is where investors in the accumulation phase can benefit from buying low interest rate bonds like the Goldman Sachs bond referenced above.

The two return components (gain in value of a bond and interest payments) are taxed differently. While the interest payments are taxed as ordinary income to investors in the current year, any gains in value of the bond are not taxed until the bond is sold or it matures. When one of those two things happen, that gain is taxed at the long-term capital gains rate, which is more favorable than the rate on ordinary income.

In what cases are these low coupon bond appropriate? They make the most sense for investors who have taxable accounts, are still in the accumulation phase, and need a diversifier beyond stocks in their portfolio. They also make sense for tax-conscious retirees that have a low current distribution rate.

If you have questions about low coupon bonds, or bonds in general, feel free to reach out to your advisor!

Sources:

www.irs.gov

advisorservices.schwab.com