EVERYDAY CENTS®

LIFE, LAUGHTER, AND PERSONAL FINANCE

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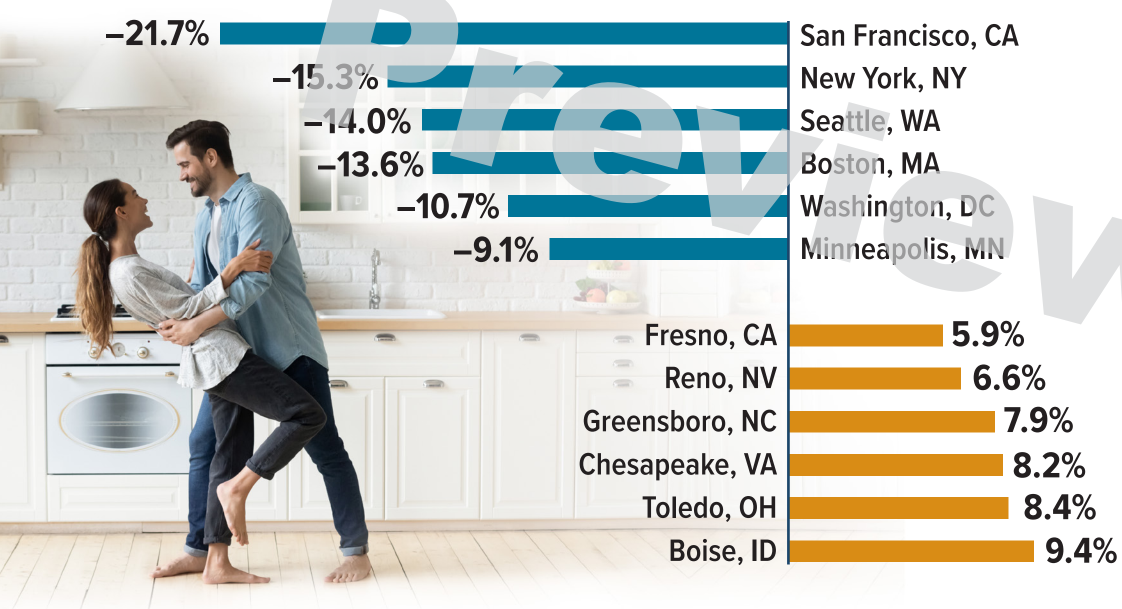
Silver Lining for Big-City Renters

By October 2020, rents had fallen nationwide (–1.4%) from the previous year due to economic effects of the pandemic, but the impact varied widely from place to place. For example, rents fell sharply in many of the nation's largest cities while rising faster than normal in some midsize cities and suburban areas.

Change in median 2-bedroom apartment rent from March to October 2020



Source: Apartment List, 2020

Cause for Concern

A 2020 survey found that half of U.S. adults live in fear that a significant health crisis in their household could lead to a bankruptcy. Already, 15% of respondents have medical debt that will not be repaid in the next 12 months.

Source: Gallup, September 1, 2020

A Strategy to Help Guarantee Lifelong Income

Most people can only guess how long their retirement savings might need to last. Those who withdraw too much or live longer than expected could run out of money; others may withdraw too little and live more frugally than might be necessary.

A qualified longevity annuity contract (QLAC) is a special type of deferred income annuity purchased in a qualified retirement account such as a traditional IRA or a 401(k). Lifelong income payments are delayed until the contract owner reaches a specific age (up to age 85), so the payouts are typically higher than they would be if the annuity income was received immediately. Funds used to buy a QLAC are removed from future required minimum distribution (RMD) calculations that normally apply to tax-deferred plans starting at age 72.

With a QLAC, retiring workers can use a relatively small portion of their tax-deferred savings to create a larger income stream later in life, when they might have little or no ability to work and often face a greater risk of needing long-term care services.

Regulations in Play

QLACs are limited to the lesser of $135,000 (adjusted for inflation) or 25% of an individual's combined retirement account balances. Payments can begin any time after age 70½, but no later than the first day of the month following the participant's 85th birthday.

The rules also allow for the continuation of income payments throughout the lifetime of a surviving spouse and/or the return of premiums (minus payouts) as a death benefit. Of course, these options will either cost more upfront or reduce income payments later in life. Without the optional death benefit, insurers may keep the premiums paid if the annuity owner dies, unless the annuity offers a return of premium feature or the payouts continue throughout the lifetime of a second individual.

Cash-out provisions are not allowed in QLACs. Investors should understand that the money invested in the annuity is no longer a liquid asset, and they may sacrifice the opportunity for higher investment returns that might be available in the financial markets. (Nonqualified annuities purchased outside of a retirement plan may offer a cash-out option that permits withdrawals during the deferral phase, but surrender charges typically apply.)

Like other distributions from tax-deferred retirement plans, payments from QLACs are taxable as ordinary income unless a portion of the distribution represents a return of after-tax contributions. With nonqualified annuities, only the earnings portion is taxed.

Better Your Odds

The Employee Benefit Research Institute used a simulation to test the theory that using a portion of a 401(k) plan balance to fund a deferred income annuity at age 65 (with payments delayed until age 85) might help improve retirement savings outcomes. The results suggest that low-wage workers, who depend more on Social Security, may have little need for longevity protection. For higher-income participants (the top 50%), the probability of running out of money decreases when an annuity is purchased with 5% to 25% of assets.[1]

Despite federal regulations designed to promote wider adoption of QLACs, few retirement plan sponsors currently offer them to participants.[2] Consequently, employer plan investors who are considering this retirement strategy might have to roll their retirement plan funds into an IRA before they can buy a QLAC.

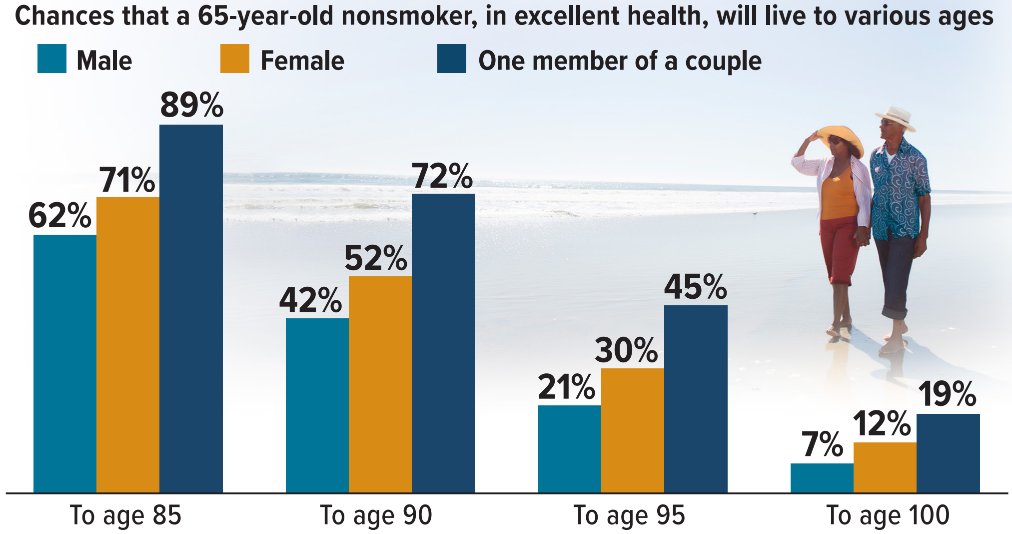
Annuities are insurance-based contracts that have exclusions, contract limitations, fees, expenses, termination provisions, and terms for keeping them in force. Any guarantees are contingent on the financial strength and claims-paying ability of the issuing insurance company.

1) Employee Benefit Research Institute, 2019
2) 2020 Defined Contribution Trends Survey, Callan Institute

How Long Will Your Retirement Last?

The average U.S. life expectancy at age 65 is about 18.1 years for men and 20.7 years for women. Mortality tables are based on the population as a whole, including people who smoke, suffer from health problems, or work in risky occupations. For this reason, many healthy people need to be financially prepared to live well beyond the averages.

Chances that a 65-year-old nonsmoker, in excellent health, will live to various ages



Source: U.S. Centers for Disease Control and Prevention, 2020 (2018 mortality data); Society of Actuaries, 2020

Renovation Nation

According to Harvard's Leading Indicator of Remodeling Activity, U.S. spending on home improvements and repairs is projected to reach nearly $338 billion in the first quarter of 2021, a 4.1% rise over the previous year.[1]

Home-improvement spending normally lags during recessions, but COVID-19 sparked an unexpected surge in do-it-yourself renovation and maintenance projects. Many households whose finances held up during the pandemic devoted time and money to making their indoor and outdoor living spaces more functional and comfortable for working, learning, and recreation.[2]

Homeowners who intend to stay in their homes for the long haul have more freedom to make choices that will enhance their own lives. However, those who plan to sell in the next year or two should pay close attention to which upgrades tend to attract buyers and provide the largest return on investment. Rising home values make it easier to obtain financing for major projects, but it's important to make responsible borrowing decisions and keep costs under control.

Kitchens and bathrooms are among the most popular and expensive home improvements. But notably, homeowners tend to get a better return on low-cost cosmetic renovations (such as paint, fixtures, and counters) than they would for major kitchen reconstruction and/or upscale finishes, according to *Remodeling Magazine*.[3]

Projects that increase a home's curb appeal tend to provide the biggest payback at the time of sale.

Payback Time

Project costs and percentages recouped

Project	Cost	Recouped
Manufactured stone veneer	$9,357	96%
Garage door replacement	$3,695	94%
Minor kitchen remodel	$23,452	78%
Siding replacement (fiber cement)	$17,008	78%
Window replacement (vinyl)	$17,461	72%
Deck addition (wood)	$14,360	72%
Entry door replacement	$1,881	69%
Major kitchen remodel (mid-range)	$68,490	59%

Source: Cost vs. Value Report 2020, *Remodeling Magazine* (national averages)

Nevertheless, preferences and costs for materials and labor vary significantly by region, and a homeowner's actual return on investment will depend on conditions in the local housing market, the home's overall appeal, and buyers' expectations for the neighborhood and price point.

1–2) Joint Center for Housing Studies of Harvard University, 2020
3) 2020 Cost vs. Value Report, *Remodeling Magazine*

Making Sense of Tax Rates

The United States has a progressive tax system, which means federal income tax rates change at progressively higher income levels or brackets (see chart). For example, if you and your spouse file jointly for 2020 and have taxable income of $90,000 (after applicable deductions), you are in the 22% tax bracket. However, you will not pay that rate on all of your income, only on the amount over $80,250. In this case, 22% is your *marginal tax rate* or top tax rate.

People sometimes worry about being "pushed into a higher tax bracket," but only the amount of income that is in the next bracket is taxed at the higher rate. Income under the threshold is taxed at rates in the lower bracket(s).

Your *effective tax rate* — the average rate at which your income is taxed — offers a clearer picture of the portion of your income that goes to Uncle Sam. To determine your effective rate, divide your total taxes by your taxable income. Using the example above, the effective tax rate would be about 12.6% for a married couple with $90,000 in taxable income.

2020 Income Tax Brackets

Tax rate	Single filers	Married joint filers
10%	Up to $9,875	Up to $19,750
12%	Over $9,875 up to $40,125	Over $19,750 up to $80,250
22%	Over $40,125 up to $85,525	Over $80,250 up to $171,050
24%	Over $85,525 up to $163,300	Over $171,050 up to $326,600
32%	Over $163,300 up to $207,350	Over $326,600 up to $414,700
35%	Over $207,350 up to $518,400	Over $414,700 up to $622,050
37%	Over $518,400	Over $622,050

Note: 2021 taxable income thresholds are slightly higher.

Wedding Trends to Watch in 2021

In 2020, nearly two-thirds of couples with wedding plans had to rearrange them at least once because of COVID-19 safety concerns and restrictions on large gatherings.[1]

The double whammy of pent-up demand from 2020's fraught wedding season and events that would normally be scheduled for 2021 means that many venues and vendors are booked solid. Of course, higher demand means it could cost more to put together a dream wedding for the foreseeable future.

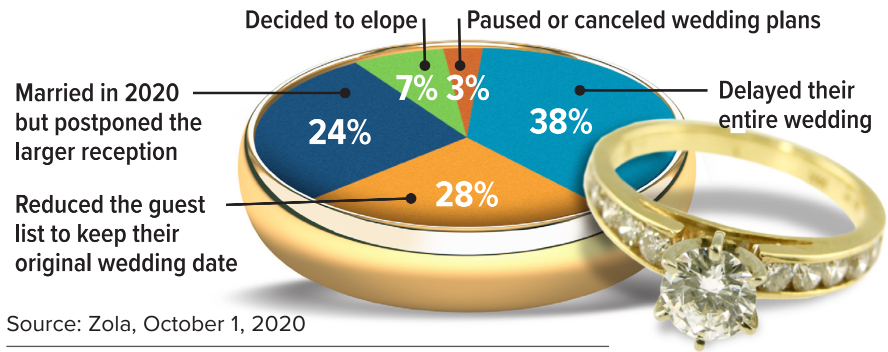
Here's how engaged couples — and supportive parents — can throw fun and memorable celebrations without breaking the bank.

Putting Safety First

As long as the virus remains a threat, outdoor spaces may be safer for guests and vendors. If there is no covered patio or pavilion, renting a tent can help ensure that poor weather won't spoil the occasion.

Receiving lines and buffet meals were becoming less common even before they became practically obsolete in 2020. Plated dinners and individualized portions still fit the bill at more formal affairs, whereas food trucks or prepacked picnics are perfect for casual shindigs. Safety protocols should make it easier for guests to maintain social distancing and access hand sanitizer.

How Engaged Couples Pivoted in 2020



Source: Zola, October 1, 2020

Being Flexible

With many weekend dates already out of reach, don't be surprised to see more weekday weddings. The good news is that engaged couples may be able to book a preferred venue at a more affordable rate for less popular days and times.[2]

Reserving a family member's backyard or a public park can save a bundle and eliminate the headaches involved with scheduling, or having to reschedule, a pricey private venue.

Keeping It Low-Key

Many couples chose micro-weddings in 2020, which means they eloped or settled for intimate ceremonies with few guests. Short and sweet "cake and champagne" receptions (held between mealtimes) also became more common. These trends may stick around for 2021 and beyond, especially if economic hardships persist.

Young people in their 20s and 30s could be invited to more weddings than they can reasonably afford to attend in 2021, and the bridal party is often asked to spend a small fortune to participate in a series of wedding festivities. Thus, cost-conscious friends and family are likely to appreciate a scaled-back celebration.

Without the pressure to host a lavish affair, newlyweds can put themselves in a better position to pursue other important financial goals. For example, the average wedding costs almost as much as the 10% down payment ($31,350) on a median-priced home.[3–4]

1) Zola, October 1, 2020
2–3) The Knot 2019 Real Weddings Study
4) National Association of Realtors, 2020 (data from Q3 2020)

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