HOW TO SET UP THE NEXT GENERATION FOR SUCCESS

AN LCR WEALTH WHITE PAPER

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Our clients often ask, ***"What can we do to help our children as they enter the US workforce?"*** The obvious answer is to continue to provide emotional support when they need it. There are also practical ways parents can assist their children, by encouraging them to set up a strong and stable financial foundation As all good parents know, there is a fine line between giving too much and giving too little, so the question becomes about strategy. Where will the money have the most impact? Teaching your children to put money away for retirement and reducing taxes is a great place to start and will accomplish the goal of building capital while reinforcing the importance of starting a nest egg early in life.

Strategy: Contribute to an IRA or a 401(k)

Contributing to an Individual Retirement Account (IRA) or a 401(k) has the triple effect of lowering taxable income, creating tax savings, and building an investment nest egg for retirement.

IRA vs. 401(k): What's the difference?

Both are tax-deferred retirement savings and investment accounts. An IRA is a retirement fund set up without employer involvement. A 401(k) is sponsored by an employer. Often a 401(k) is accompanied by an "employer matching" program in which the employer agrees to match contributions up to a preset maximum.

Annual Limits: How much can I contribute?

The limit for individual contributions (before employer matching) in 2022 for a 401(k) is $20,500. The limit for contributions in 2022 to an IRA is $6,000. You are allowed to max both.

Withdrawals: What are the limitations?

There is a 10% penalty for early withdrawals before the age of 59½. Withdrawals after the age of 59½ are taxed fully at the ordinary income tax rate, not the capital gains tax rate.

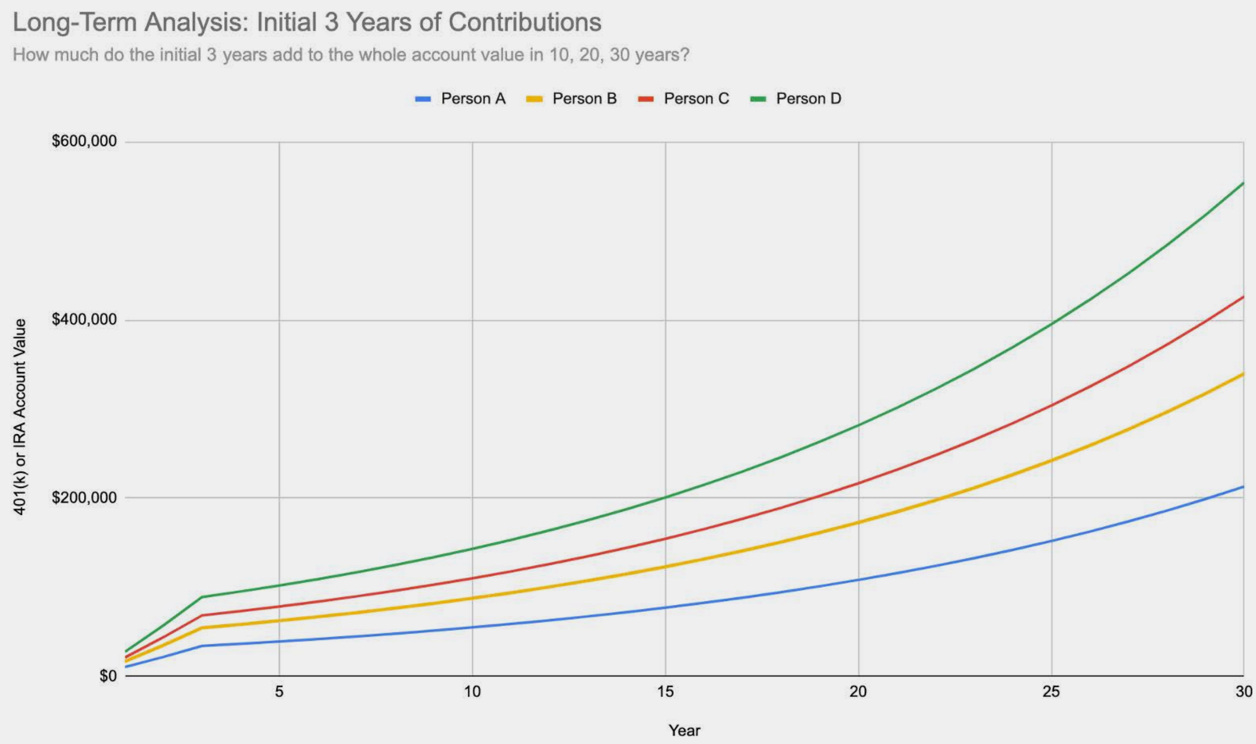
Tax-Deferred: What does this mean?

For both types of accounts, contributions are made with pretax dollars, meaning that contributions lower the investor's taxable income directly by the amount contributed.

Income Level	Tax Bracket	Annual Tax Savings from Maximum 401(k) Contribution
$40,526 to $86,375	22%	$4,510
$86,376 to $164,925	24%	$4,920
$164,926 to $209,425	32%	$6,560

Compound Growth

The example on the next page highlights the long-term benefit of contributing the maximum amount possible to your 401(k) account in the first three years of your career. Assume that three individuals each make $100,000 per year before taxes and can get a 7% market return.



End of Year 3	Contributions	Appreciation	Total Value
Person A	$30,750	$3,555	$34,305
Person B	$48,750	$5,927	$54,677
Person C	$61,500	$7,111	$68,611
Person D	$79,500	$9,687	$89,187

End of Year 30	Contributions	Appreciation	Total Value
Person A	$30,750	$182,422	$213,172
Person B	$48,750	$291,007	$339,757
Person C	$61,500	$364,845	$426,345
Person D	$79,500	$474,697	$554,197

Over time these initial contributions compound tax-free. This creates a disparity in how much these initial three years add to the value of one's retirement account. At the end of Year 30, the difference is very substantial.

Every additional $1,000 contributed to an IRA or 401(k) by the end of Year 3 represents ~$250 in tax savings and grows by **621.4%** to $6,214 by the end of Year 30, assuming a 7% annual return. If an employer does not offer a 401(k), there are options for creating a "solo 401(k) account" so that the higher annual contribution limit can be achieved.

While parents cannot contribute to their children's 401(k), they can subsidize other costs such as rent, insurance, and car payments. This enables their children to increase their 401(k) or IRA contributions. This strategy builds long-term wealth and encourages young workers to save for retirement. We have illustrated in Graph 1 both the importance of investing in the 401(k)/IRA and the benefits of maxing out those contributions. These pretax dollars grow over time and are tax-free until distributions. This strategy will help create a solidfinancial foundation early on, allowing young adults to build wealth safely and efficiently.