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MONEY AT WORK

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What is Your 'Personal Inflation Rate'?

You're probably well aware that inflation is running near 9%, but depending on how you spend, your own personal rate could be much lower – or higher.

I've been reading a lot about inflation lately and the potential impact it can have on households. I've also received questions from clients about inflation projections going forward. Some of the current thoughts around this issue relate to a "personal inflation rate." In other words: How does the current inflationary environment affect individuals?

This makes sense to me, as everyone spends their money differently. Budgets tend to be more impacted in the areas where you absolutely need to spend money, or the non-discretionary part of your budget. Of course, if the high levels of inflation continue, the potential for inflation to impact the discretionary part of your budget may also become an issue.

Breaking it down, non-discretionary expenses are things like mortgage or rent payments, insurance premiums, car payments, food, energy usage, water, school tuition, etc. Discretionary expenses potentially include personal travel, dining out, club dues, alcohol consumption, new cars, new homes, etc. – all things that consumers can adjust their spending habits on to account for the sensitivity of their household budget to inflation.

My 'Personal Inflation Calculator'

In the interest of trying to work through this on my own, and to provide guidance to our clients who are concerned about the impact of inflation on their own planning, I created a "Personal Inflation Calculator" using the latest numbers from the Bureau of Labor Statistics. If you've never looked at the monthly reports from the BLS, they are quite extensive, and cover quite a few common budget items. They are also broken down into "seasonally adjusted" and "unadjusted" inflation rates for each item.

Seasonally adjusted numbers take into account normal inflationary increases due to seasonal adjustments and removes their impact from the calculation. For example, gas prices tend to increase around holidays and the summer vacation travel period. Other items' prices may increase or decrease around the winter holidays. Unadjusted rates just look at the raw numbers and increases in prices from period to period.

Based on the current economic environment, and the rapid pace of inflation, I'm focusing only on the unadjusted inflation numbers from May '21 to May '22. Seasonally adjusted estimates will most likely differ in some respects, but the unadjusted rate should give us a worst-case scenario. As stated in the BLS May report, "The unadjusted data are of primary interest to consumers concerned about the prices they actually pay."

The worksheet I created takes some of the most common categories of household expenditures and allows us to enter annual amounts for those categories. The inflation factor for each item is than applied, resulting in an estimated price for that item or service in the current period. We then total all of those budget items up and develop a personal inflation rate from the difference. I think this can be most enlightening if we enter budget items based on the prior year's estimates, to illustrate how prices are changing in real time. I've also added a few line items for occasional purchases, like a new or vacation home, or a new car, so that we can look at the effect of inflation on those particular items.

The end result is that we can fine-tune an inflation rate for a particular individual or family, as opposed to the blanket rate that is typically quoted for the entire economy. For example, if someone has a very low-cost lifestyle but relies on fuel oil to heat their home, they will have a higher personal inflation rate than someone heating their home with electricity.

A Test Case

I approached my test analysis assuming that we would start with budget estimates for the 2021 calendar year and attempt to predict how a typical household budget would be affected in 2022. Some interesting observations came to light.

In case No. 1, I considered a family of four with two young children and an annual household budget of $108,400. This includes such things as (in 2021 annual amounts):

Mortgage: $18,000
Auto loans: $7,200
Credit card payments: $2,000
Property tax: $4,000
Groceries: $10,000
Gasoline: $3,600
Natural gas: $1,200
Electricity: $1,800
Airfares: $3,000
Lodging away from home: $1,500
Dining out: $6,000
Pet food: $1,200
Veterinary costs: $600
Wireless telephone services: $1,400
Cable TV: $1,800

By my calculation, based on their budgeted expenditures, this family's inflation rate comes out to 8.53%, which brings their 2022 budget up to $117,650. This family may have to take steps to limit this projected increase, and chances are, they are already feeling it.

Your Own Inflation Rate Will Differ

When figuring your own personal inflation rate, you should realize that some budget items are not going to increase for the foreseeable future, such as fixed debt payments (home mortgage, auto loan, etc.). However, credit card interest rates are certainly going to increase – along with the general rise in interest rates related to inflation, as are many other things, such as food, travel, gasoline and utilities.

And the costs of some of the budget items are actually expected to decrease, such as "Food at Elementary and S econdary Schools" and "Computers, Software, and Smartphones."

The biggest increases (unadjusted) are in the following areas:

Home prices: +20%
Rent: +5.2%
New car prices: +12.6%
Used car prices: +16.10%
Gasoline: +48.70%
Fuel oil: +106.7%
Electricity: +12%
Natural gas: +30.2%
Airfares: +37.8%
Lodging away from home: +19.3%
Dining out: +9%
Food / groceries: +11.9%
And, the perennial favorite, health insurance: +13.8%

As you can see, there are some discretionary items in this list, and some non-discretionary items. So, depending on your particular spending plans, your personal inflation rate will vary. For instance, if our hypothetical family of four decided last year that they would buy a new home this year, costing around $300,000, their personal inflation rate becomes closer to 15.03% on a seasonally adjusted basis and 16.96% on an unadjusted basis (of course, if they had been renting, and through their home purchase were able to reduce their annual outlay in the process, they've just reduced their personal inflation rate).

If they had planned to buy a $35,000 new car this year, their personal inflation rate rises to 9.53% on an unadjusted basis. If our family of four had plans for more extensive family vacations this year, and we increase their airfares to $7,000 and their lodging away from home to $5,000, their inflation rate goes to 9.87% This is without buying a house or a new car.

Some Quick Takeaways:

- Depending on the sensitivity of your budget to items that are showing higher inflation rates, you may want to consider delaying purchase of those items, assuming they are discretionary in nature, such as homes, cars and increased travel.
- Take steps to pay off adjustable-rate debt, such as credit cards.
- Consider making your home more energy efficient (although this may expose you to higher inflationary costs from remodelers), and if you start to see higher utility bills, think about shopping energy providers.
- Renting vs. buying a home is a tricky challenge right now, because even as rents increase, mortgage rates and home prices are rising as well. However, considering that the projected rise in rents is +5.2% and the year-over-year increase in the price of homes nationwide was +20% in February, possibly delay buying a home until home prices fall to a more reasonable level.
- If you have an adjustable-rate mortgage, meet with your adviser to determine whether this should be refinanced to a fixed rate.
- Possibly delay purchasing a vacation or second home until this situation resolves itself.
- The cost of groceries is rising at a slightly higher rate than the costs of dining out. This may give you pause when thinking about cooking all of your meals at home. However, maybe consider cutting back on the more expensive menu items, as well as high-cost beverages.

In conclusion, the constant drumbeat of scary inflation numbers has everyone worried. However, if you take a few minutes to revisit how you spend your money and calculate your own personal inflation rate, you may come up with some solutions to put your mind at ease.

Remember, You're Worth More Than Your Money

When it comes to estate planning, it's time for us all to look beyond the money … with an ethical will.

Let's admit it, the financial industry has spent far too long treating end-of-life planning like a mathematical exercise. Rather than viewing it as the very human process it should be, conversations often center around taking an inventory of people's money and assets followed by a functional decision about where different parts of their estate should go.

This is missing the point because, in truth, the things that make us who we are reach far beyond the number of properties we own or the amount of money we earn. Just ask the families of Dr. King or, more recently, the millions of health care professionals and volunteer community workers who helped us through the pandemic.

In fact, the experiences we have, the beliefs we hold and the decisions we make are as important a part of our legacy as any monetary inheritance we leave behind. And the way to capture all this non-financial worth is by crafting an ethical will to augment your traditional will.

The ethical choice

Ethical wills first began to appear in the 1990s, usually in the form of a "legacy letter" written just before a person died and then bolted onto their main will as an appendix. Such letters are designed to define a person's non-financial legacy – from details of the key milestones, places and relationships in their life to the thoughts, feelings, obstacles and lessons they experienced along the way. They can even be a place to ensure important family traditions and values are preserved and continued in future.

But valuable as a legacy letter can be, how can you communicate everything about someone's life in a page or two? And can you really remember, so late in life, all of the events from years before that you wanted to share and what they meant to you? The answer to both questions is you can't, which means the idea of the ethical will has to evolve.

Instead of hastily writing it in hindsight during old age, you should be constantly capturing major milestones, lessons and experiences in your life as they happen. That way, future generations of your family can read, watch and, crucially, learn from them further down the line.

Perfectly imperfect

Naturally, many of the stories you'll want to share in your ethical will would be achievements – both professional and personal. Buying a house. Starting a business. The tale of how you met your partner and went on to build a loving relationship. All of which have incredible emotional value to everyone coming next.

But at the same time, an ethical will isn't only about painting a picture of perfection. As people, we're inspired by recovery, so you must also record the times you hit a brick wall, failed and came back stronger. The moment you lost your job, got divorced or faced some other challenge.

These life experiences and snippets of advice from them will help future generations avoid the same mistakes and believe they can overcome similar deep cuts in their own lives. Plus, understanding your story can often bring a sense of ease and comfort to them as regards to who they are and what their place in the world is. Why? Because they know they're walking in the footsteps of years of family history.

Immortality … kind of

On the other side of the equation, an ethical will can enable you, as the bequeather, to fulfill that innate human desire to be eternal. To leave a legacy based not only on your material wealth, but on your relationships, intellect, ethics and life lessons. And to keep on having "conversations" with your grandkids about their financial decisions and lifestyle choices long after you die.

You can even create a matching program in which your assets are linked to a specific behavior pattern. So, if your goal is to inspire the next generation of entrepreneurs, missionaries or professors, you can expressly state in your will that anyone who decides to pursue your chosen path can reach into the family trust and get X amount of dollars to do so. In other words, you can align your financial resources to behaviors and values that are important to you from beyond the grave.

Four immediate steps to start your own ethical will

Here are four steps you can take now to begin building an ethical will:

1. Read a book on what an ethical will is and make sure your financial adviser reads it too. There are loads of good ones out there, but two I particularly like are So Grows the Tree by Jo Kline Cebuhar and Ethical Wills & How to Prepare Them by Rabbi Jack Riemer and Dr. Nathaniel Stampfer.
2. Invest in a five-year journal or use your phone to start recording moments, milestones and experiences.
3. Create a "failure résumé" of times when things went wrong and how you learned from them.
4. Make discussing your ethical will a set agenda item during your annual financial planning review.

Whatever steps you decide to take to get started on your ethical will, the key is to ensure that you're planning for end-of-life in a way that goes beyond simply passing on your financial wealth to future generations.

Instead, you should be including all the other things that have defined your life and that can go on to help your loved ones shape theirs too. Sure, the math and the money will always be important. But believe me, you're worth so much more than that!

Financial Advice I Would Give My Younger Self - Planning for Education Funding

College 529 plans vs. Roth IRAs: A financial expert shares what she wishes she had known when saving for her own law school and her son's college. Taking her advice could put you years ahead of the game.

At the end of most lectures I give, the moderator usually asks, "What else should our audience know?" I always look at the younger members in the room or on the screen and think — if only I knew this when I was your age.

While my business is in providing financial and wealth planning advice to clients who have already built a significant amount of wealth, there are many fundamental planning strategies that apply to those just starting out in their careers, things, which frankly, I wish I knew when I was growing up. Therefore, I am penning this four-part series on planning advice I would give to my younger self. The topics will range from planning for college savings, young families, retirement, to caring for aging parents. This first article focuses on planning for college savings.

Saving for college is often thought of from the perspective of the parent saving for the child, and if you are one of the lucky ones whose parents can afford to have done that for you, good for you. However, college savings, or more appropriately education savings, is not a dominion strictly reserved from parent to child. As a young adult, you can start thinking about saving for higher education and how to do that in a tax-efficient manner. Specifically, I am referring to a 529 college savings plan and Roth individual retirement account (IRA).

529 College Savings Plans Aren't Just for Kids

The 529 college savings plan is a tax-advantaged vehicle designed for education savings. Money held inside these accounts can grow income-tax-deferred, and when money is ultimately distributed for the use of qualified education expenses, it will also be income-tax-free. In other words, earnings and appreciation from investments held in a 529 account can be completely income-tax-free if used for education needs.

For many, the first experience with a 529 account is when a young parent opens one for a newborn child — that was certainly my case as my first 529 account was opened for my son a few months after his birth. Here's the advice that I wish I had known years before — you can open an account for yourself. Instead of putting your extra savings early on in your career into a savings or investment account where interest and growth would be taxable, consider instead putting those savings into a 529 account for your own benefit. If you go to graduate school, you can then use that money to pay for tuition, books and room and board. As with any tax-advantaged account, the value of compounded income-tax-free growth can be a good boost to the bottom line. In addition, certain states also offer a tax deduction or credit on contributions to a 529 account.

You may wonder — what if I don't go to graduate school or I receive outside funding like a scholarship? Money from a 529 plan can still be withdrawn for any use (i.e., non-educational use), but the withdrawal will be subject to income tax at the time of distribution and a 10% penalty if it is not used for qualifying education expenses. Even so, you still may come out ahead, because depending on the investment growth and the length of time the 529 account has been opened, the value of the compounded income-tax-free growth throughout the years may outweigh the tax and penalty imposed for taking a non-qualifying withdrawal.

What is more likely, and where the long-term view comes in, is to think of the 529 account as a tax-advantaged vehicle not only for your education, but for any loved one's education. You can rename the beneficiary of a 529 account to a qualifying family member (e.g., another child, niece, nephew, in-laws), which means that if you ultimately do not need the money for your own education needs, you can effectively "transfer" those funds to another for his or her own education, all while earning the same income tax benefits.

In retrospect, not only should I have opened a 529 account for my own law school education, I should have continued to contribute to the account and "transferred" it to my son when he was born as the new beneficiary. Had I done that, I would have jump-started my son's college education savings by a good 15 years of tax-free compounded growth.

Roth IRAs Aren't Just for Retirement

Another tax-advantaged vehicle that may be used for education savings is a Roth IRA. These accounts are often thought of for retirement purposes, which is how they are primarily used. The advice I would give to my younger self is to consider using this strategy for education funding as well and not only for retirement.

Similar to a 529 plan, earnings and appreciation earned from investments held in a Roth IRA are income-tax-deferred, with the potential of ultimately being tax-free. The contributions you make to a Roth IRA can be accessed at any time without tax or penalty. Furthermore, when earnings and growth are distributed out of the Roth IRA, it is also income-tax-free (provided it is a qualified distribution – more on that in a bit), regardless of the use.

The Internal Revenue Service (IRS) also provides a penalty-free distribution from the Roth IRA to pay for higher education expenses for yourself, spouse, children, or grandchildren, provided that the distribution does not exceed the expenses for the year. Of course, if the assets are ultimately not needed for education, the Roth IRA can ultimately be used for retirement.

There are some key differences between 529 plans and Roth IRAs that one should consider when planning to use either for education savings purposes. The first is in timing. While you may make a distribution out of a Roth IRA at any time, there will be a 10% early withdrawal penalty if the distribution was made before age 59½, unless an exception applies. If a distribution was made within the first five years after a contribution to a Roth IRA, there will also be an income tax imposed at the time on the earnings (withdrawal of principal is income-tax-free). Therefore, the Roth IRA strategy is likely better viewed as a saving strategy for a child's education when you'll make the withdrawal after the five-year time frame from the first contribution and over age 59½ (of course, it is also available if one was to obtain higher education at a later age).

Another critical difference is on income limits. In order to qualify for contributions to a Roth IRA, one's income must be under a certain threshold. In 2022, that threshold is $144,000 for single individuals and $214,000 for those married filing jointly. A 529 plan, on the other hand, has no income limitations, so one may make contributions regardless of income level. Therefore, one should be mindful of one's income potential, because if your income starts to exceed the stated threshold amount, the Roth IRA strategy may not be available.

Of course, these two strategies are not mutually exclusive and if there is sufficient excess savings, you can always contribute to both a 529 plan and a Roth IRA.

When considering which option is right for you, there are many other factors that are beyond the scope of this article, such as:

- **Investment options offered in the plan:** 529 college savings plans may offer different investment options compared to Roths and generally may be more limited.
- **Contribution limits:** If you're younger than 50, you can only contribute up to $6,000 per year to a Roth IRA for 2022. Meanwhile, with 529 plans there are no limits, although gift taxes could come into play when contributions hit more than $30,000 per couple per year.
- **Impact on financial aid:** Eligibility and income qualification vary between 529 and Roth and will depend on many factors such as timing and ownership.

While you should always consider consulting with a financial adviser before making any final decision, I wish I knew to even ask the question when I was younger.

IRS Increases Mileage Rates Because of High Gas Prices

The higher mileage rates, which are used to calculate certain tax deductions for business and other uses of a car, took effect on July 1.

In response to rapidly rising gas prices, the IRS took the unusual step of increasing the standard mileage rates in the middle of the year (they're normally adjusted for inflation only once per year). The mileage rates that were raised are used to calculate tax deductions for the use of an automobile (i.e., a car, pickup truck, or van) for business, medical, and certain moving expenses. The new rates apply from July 1 to December 31, 2022, while the previously established rates apply for the first half of the year.

Three of the four mileage rates increased by 4¢ per mile (one of the rates didn't change at all). For the second half of 2022, the standard mileage rate for business use of an automobile increased from 58.5¢ to 62.5¢ per mile. The rates for deductible medical travel and moving expenses for active-duty members of the military rose from 18¢ to 22¢ per mile. The mileage rate for charitable use of a passenger car remains at 14¢ per mile, since it's fixed by law and not subject to adjustments for inflation.

Standard Mileage Rates for 2022

Deduction	January to June 2022	July to December 2022
Business Use	58.5¢ per mile	62.5¢ per mile
Medical Travel	18¢ per mile	22¢ per mile
Military Moving Expenses	18¢ per mile	22¢ per mile
Driving for Charity	14¢ per mile	14¢ per mile

In addition to calculating business expense deductions, the mileage rate for business use is also used by the federal government and many businesses to reimburse employees for the business use of their personal vehicle.

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Tax Deduction for Business Use of a Vehicle

Any self-employed person who makes deliveries, drives to a client's location or otherwise uses a personal car, van or truck for work-related purposes can claim a tax deduction for the business use of their vehicle. There are two ways to calculate the deduction – you can use the standard mileage rates listed above or your actual car expenses.

If you opt to use the actual expense method, simply add up all your car-related expenses for the year – gas, oil, tires, repairs, parking, tolls, insurance, registration, lease payments, depreciation, etc. – and multiply the total by the percentage of total miles driven that year for business reasons. For example, if your total annual car costs are $5,000 and 20% of your miles were for business, then your deduction is $1,000 ($5,000 x .2).

Note that the itemized deduction for unreimbursed employee travel expenses has been suspended until the 2026 tax year. So, the business standard mileage rate can't be used by employees to claim a deduction for their work-related travel costs. However, "above-the-line" deductions for business-related expenses were not suspended. So, for example, members of the National Guard or military reserves, state or local government officials paid on a fee basis, and certain performing artists can still deduct unreimbursed employee travel expenses and use the business standard mileage rate.

Tax Deduction for Medical Travel

If you itemize deductions on your tax return, you can deduct unreimbursed medical expenses that exceed 7.5% of your federal adjusted gross income. The list of medical expenses that qualify for the deduction is long and includes obvious expenses, such as those for doctor bills, medicine, blood tests, bandages, crutches, dental work, oxygen, nursing care, and the like. But it also includes the cost of transportation primarily for, and essential to, medical care.

If you use your own automobile for medical travel, you can deduct actual out-of-pocket expenses such as the cost of gas and oil, but you can't include depreciation, insurance, general repair, or maintenance expenses. As with the deduction for business use of your car, you can elect to use the standard medical mileage rates above instead of using your actual expenses. Either way, you can tack on parking fees and tolls, too.

According to the IRS, expenses you can't deduct include:

- Going to and from work, even if a medical condition requires an unusual means of transportation;
- Travel for purely personal reasons to another city for an operation or other medical care.
- Travel that is merely for the general improvement of your health; and
- The costs of operating a specially equipped car for other than medical reasons.

Tax Deduction for Moving Expenses of Military Personnel

It used to be that anyone could deduct job-related moving expenses if your new workplace was at least 50 miles farther from your old home than your old home was from your old workplace. However, the 2017 tax reform new tax law killed the moving expense deduction, but with one significant exception – if you're an active member of the U.S. Armed Forces, the cost of any move associated with a permanent change of station is still deductible if the move was due to a military order. This benefit for military families includes a move from your home to your first post of active duty, a move from one permanent post of duty to another, and a move from your last post of duty to your home or to a nearer point in the U.S.

You can write-off the unreimbursed costs of getting yourself and your household goods to the new location. If you drive your own car for a move in 2022, use the standard mileage rates above plus what you paid for parking and tolls. When it comes time to file your tax return, use Form 3903 to tally your moving deductions.

Tax Deduction for Charitable Use of a Car

Most people are generally aware of the charitable tax deductions available to people who itemize, but there's an often-overlooked aspect of the deduction. In addition to donations of cash or unused items in your home, you can also deduct out-of-pocket costs incurred while doing work for a charity. This includes the costs associated with driving your car for charity. For example, you can deduct car expenses if you use your own vehicle to transport food and supplies to a nonprofit organization's soup kitchen.

As with the other car-related expenses discussed above, you can either track your actual costs or use the standard mileage rate to calculate your deduction. And, of course, don't forget to add the cost of parking and tolls.

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