

**Silicon Valley Chapter
American Association of Individual Investors**

Fred's Financial Planning Workshops
Taxes

www.siliconvalleyaaii.org/financialplanning/

Email: fred.svaaii@gmail.com

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Silicon Valley Chapter

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Please check us out!

- **Chapter website: www.siliconvalleyaaii.org**
- **Meetups: www.meetup.com/AAll-Silicon-Valley-Meetup**
- **Facebook: www.facebook.com/sv.aa**
- **YouTube Channel**

www.youtube.com/channel/UC4GepcU8lzx8rZMaWNBeJtA

- **AAll National website: www.aaii.com**
- **My email address: fred.svaaii@gmail.com**

Our Next Event and Special Interest Group Webcasts

- **The U.S. Economy in 2021:** Robert Valletta, SF Fed
 - Saturday January 9th at 9:00am; webcast only
- **Financial Planning Discussion Group**
 - Fred Smith: Second Wednesday of each month at 6:30pm
- **Investing Discussion Group**
 - Lynn Gillette: Fourth Monday of each month at 6:30pm except Dec.
- **Computerized Investing Group**
 - Bill Paseman, Don Mauer: First Thursday of each month at 6:30pm
- **Fintech/Realtech Discussion Group**
 - Roland Chow: To be determined.

Financial Planning Workshops

We cover a full range of topics in the cycle:

- **Financial Planning ... The Big Picture**
- **Investing 1: Modern Portfolio Theory, Building a diversified portfolio**
- **Investing 2: Efficient Market Hypothesis; Can you beat the market?**
- **Taxes: TCJA, SECURE Act, Tax diversification, Asset location, QCDs**
- **Retirement Planning 1: Tax-advantaged plans, RMDs**
- **Retirement Planning 2: Safe withdrawal rates, Bengen's 4% rule**
- **Risk Management/Insurance: Annuities, Long-term care, Litigation**
- **Social Security and Medicare: Claiming strategies, Medicare traps**
- **Estate Planning: Probate, Executor/trustee duties, Philanthropy**
- **Wrap-up: Case study reviewing previous material**

Overview for Today's Workshop

- **What taxes do we pay?**
- **Recent Federal tax acts**
 - **Tax Cuts and Jobs Act, TCJA**
 - **Setting Every Community Up for Retirement Enhancement Act, SECURE**
 - **Families First Coronavirus Response Act, FFCRA**
 - **Coronavirus Aid, Recovery, and Economic Stability Act, CARES**
- **Tax Tips**
 - **Tax saving strategies**

What Taxes Do We Pay?

- **Federal taxes**
 - Income
 - Interest
 - Short-term and long-term capital gains
 - Qualified and non-qualified dividends
 - Net investment income surcharge
 - Import/export taxes, Tariffs, Excise tax, etc.
- **State and local income tax**
- **Sales tax**
- **Property tax**

Tax Cuts and Jobs Act, TCJA

- **Signed into law in December 2017**
 - **Most significant revision to tax code in four decades**
 - **Effective 2018 tax year**
 - **Most changes to the individual tax code sunset in December 2025**
- **Corporate taxes cut from 35% maximum in 2017 to 21% maximum in 2018**
 - **Possibly revert back to 28% maximum by Biden administration in 2021**

TCJA: Income Tax Brackets and Rates

Rate	2020 Single	2020 MFJ	2021 Single	2021 MFJ
10%	Up to \$9,875	Up to \$19,750	Up to \$9,950	Up to \$19,900
12%	\$9,876 to \$40,125	\$19,751 to \$80,250	\$9,951 to \$40,525	\$19,901 to \$81,050
22%	\$40,126 to \$85,525	\$80,251 to \$171,050	\$40,526 to \$86,375	\$81,051 to \$172,750
24%	\$85,526 to \$163,300	\$171,051 to \$326,600	\$86,376 to \$164,925	\$172,751 to \$329,850
32%	\$163,301 to \$207,350	\$326,601 to \$414,700	\$164,926 to \$209,425	\$329,851 to \$418,850
35%	\$207,351 to \$518,400	\$414,701 to \$622,050	\$209,426 to \$523,600	\$418,851 to \$628,300
37%	\$518,401 and above	\$622,051 and above	\$523,601 and above	\$628,301 and above

TCJA: Capital Gains and Dividend Taxes

	Taxable Income	Taxable Income	Taxable Income
Single	< \$40,000	\$40,000 - \$441,450	> \$441,450
Married filing jointly	< \$80,000	\$80,000 - \$496,600	> \$496,600
Short-term cap gains	Taxed as income	Taxed as income	Taxed as income
Long-term cap gains	0%	15%	20%
Qualified dividends	0%	15%	20%

TCJA: Standard Deduction and Personal Exemption

	Pre-TCJA	2020	2021
<u>Standard deduction</u>			
Single	\$6,500	\$12,400	\$12,550
Married filing jointly	\$13,000	\$24,800	\$25,100
Additional > age 65			
Single	\$1,600	\$1,650	\$1,650
Married filing jointly	\$1,300	\$1,300	\$1,300
<u>Personal exemption</u>			
Single	\$4,150	Eliminated	Eliminated
Married filing jointly	\$8,300	Eliminated	Eliminated

TCJA: Itemized Deductions

- **Medical deduction floor 10% AGI → 7.5% AGI**
- **New SALT deduction limit = \$10,000**
 - **State and local income tax**
 - **Property tax**
- **Mortgage interest on \$1M property → \$750,000**
- **Interest on home equity loans only deductible if used to build or improve your home**
- **Gifts to charity still deductible**
- **Eliminated deductions for ...**
 - **Tax preparation fees and other misc deductions**
 - **Theft and other casualty losses**
- **Pease limitation on itemized deductions eliminated**

TCJA: Estate Taxes

- **Exclusion**
 - \$11.580M per spouse in 2020, \$11.700M in 2021
 - Exclusion is portable for use by second spouse
- **Tax rate**
 - Maximum 40% rate for taxable amounts >\$1M
- **Challenge**
 - How do you do estate tax planning (inherently long-range) with a tax law that sunsets in 2025?
 - Hint: There's a lot more to estate planning than saving taxes

TCJA: Miscellaneous Issues

- Roth IRAs
 - Recharacterization of a Roth IRA conversion has been repealed by TCJA
- Alimony payments
 - No longer deductible by paying spouse, nor reportable as income by receiving spouse

• AMT exemption	<u>Pre-TCJA</u>	<u>2021</u>
• Single	\$54,300	\$73,600
• Married filing jointly	\$84,500	\$114,000
• Phaseout: Single	\$120,700	\$518,400
• Phaseout: MFJ	\$160,900	\$1,036,800

Setting Every Community Up for Retirement Enhancement (SECURE) Act

- **Signed into law in December 2019**
 - effective on January 1, 2020
 - Largest retirement reform since 2006
- **Required minimum distributions, RMDs**
 - Begin at age 72 instead of 70.5
 - Applies to those who turn 70.5 in 2020 or later, i.e. born on or after July 1, 1949
- **Traditional IRAs**
 - No age limit for contributing to an IRA provided you have earned income

SECURE Act: Inherited Retirement Accounts

- **Stretch IRA is gone, except for ...**
 - **Surviving spouse of original owner**
 - **Minor child < age of majority**
 - **Person >10 years younger than the decedent**
 - **Disabled individuals**
 - **Chronically ill individuals**
- **For all others the account must be completely distributed within 10 years of the original owner's death, but there are no annual RMD requirements**

The Families First Coronavirus Response Act (FFCRA)

- **Signed into law in March 18, 2020**
 - **Operational from April 1 thru December 31, 2020**
- **Mandates that employer must provide leave for a coronavirus illness or quarantine**
- **Provides payroll tax credits to reimburse employers for up to 2 weeks**
 - **Enables employers to keep workers on their payrolls**
 - **Workers do not have to choose between paychecks and public health**
- **Credits are also available for self-employed**

Coronavirus Aid, Relief, and Economic Security (CARES) Act

- **Signed into law on March 27th, 2020**
 - **\$2.2T economic stimulus bill to fight the nationwide impact of the coronavirus pandemic**
 - **Largest economic stimulus package in U.S. history**
 - **10% of total U.S. gross domestic product**
- **Unemployment benefits**
 - **Additional \$600 per week on top of state benefits**
 - **Benefits up to 39 weeks**
 - **Also available to gig workers**

CARES Act: Personal and Business Help

- **Stimulus checks**
 - Grants up to \$1,200 per adult, \$500 per child
 - Available for workers with 2019 AGI < \$75,000
 - Phased out for AGI from \$75,001 - \$99,000
- **Charitable donations**
 - Allows up to \$300 to be deducted above the line
 - Useful for those who take the standard deduction
- **Paycheck Protection Program for small businesses**
 - Lends up to 8 weeks expenses
 - Loan converts to a grant if used for payroll, rent, or utilities

CARES Act: Retirement Plans

- **Enables COVID-19 affected people to withdraw up to \$100,000 from their IRA or 401(k) plan without a 10% early withdrawal penalty**
 - **Taxes must still be paid on the withdrawal, but can be stretched over a 3-year period, 2020 - 2022**
 - **Funds can be paid back into the account within 3 years**
- **Required minimum distributions**
 - **RMDs for IRAs and 401(k)s waived for 2020**
 - **Window to return RMD already taken expired 8/31/20**
 - **Also applies to inherited IRAs**

Tax Tips: Start With The Basics

- **Traditional IRA**
 - Contribution limit of \$6,000 in 2020 and 2021 plus additional \$1,000 for age 50 and older
 - Deduction phased out if covered by employer plan
MAGI > \$65,000 for singles and \$104,000 for MFJ
 - Growth is tax deferred
 - Distributions are taxed at ordinary income level
- **Roth IRA**
 - Same combined contribution limit as traditional IRA
 - Income limit \$124,000 - \$139,000 for singles and \$196,000 - \$206,000 for MFJ in 2020
 - No tax deduction for contribution
 - Appreciation and distributions are tax-free

Tax Tips: Employer Retirement Plans

- **401(k) and 403(b) plans**
 - Defer \$19,500 contribution in 2020 and 2021 plus additional \$6,500 for age 50 and older
 - Growth is tax deferred
 - Distribution is taxed at ordinary income level
- **SIMPLE plan**
 - Defer \$13,500 contribution in 2020 and 2021 plus additional \$3,000 for age 50 and older
 - Growth is tax deferred
 - Distribution is taxed at ordinary income level

Tax Tips: Health Savings Account, HSA

- **Eligibility: Must have a high-deductible health insurance plan**
 - Cannot be on Medicare
- **Triple tax benefits**
 - Contributions are tax-deductible
 - Investments grow tax-free
 - Qualified medical distributions are tax-free
 - Distributions for non-medical expenses are taxed as ordinary income
- **Contribute up to \$3,550/person, \$7,100/family plus \$1,000 catch-up if age 55 or older (2020)**
- **Can make withdrawals in retirement after you no longer qualify for contributions**

Tax Tips: Be Aware of Tax Efficiency

- **Tax-inefficient assets, e.g. CDs, bonds, REITs, etc.**
 - Spin off interest
 - Non-qualified dividends
 - Short-term capital gains
 - Taxed as ordinary income (37% maximum)
 - Most suitable for tax-advantaged accounts
- **Tax-efficient assets, e.g. muni bonds, stocks, etc.**
 - Spin off qualified dividends
 - Long-term capital gains
 - Taxed at preferential rate (20% maximum)
 - Suitable for taxable accounts

Tax Tips: Asset Location

	<u>Trad. IRA</u>	<u>Taxable a/c</u>	<u>Roth IRA</u>
Contributions	Deductible	Income	Income
Distributions	Income	Inc./Cap Gains	No tax
Inheritances ...	Worst	Good	Best
... taxed as ...	Income	Step-up	No tax
Tax-inefficient assets	*****	*	*
Tax-efficient assets	****	*****	****
High growth, REITS, etc.	*	*	*****

Tax Tips: Tax Loss Harvesting

- Only useful with taxable accounts
- Sell an underperforming investment to reduce taxable capital gains, and potentially offset ordinary income up to \$3,000
- Excess loss can be carried forward to reduce gains in future years
- Can use the proceeds from sale to purchase a similar security
- Beware the wash-sale rule
 - Must not purchase a “substantially identical” security within 30 days before or after the sale

Tax Tips: Tax Bracket Management

- If you are in a low bracket this year consider filling up to the top of the range to avoid a higher tax rate in later years
 - Harvest capital gains on long-term equities
 - Roth conversion
- Beware bumping into higher Medicare bracket
 - Modified Adjusted Gross Income, MAGI
$$\text{MAGI} = \text{AGI} + \text{Tax-free income}$$
 - Must pay Income Related Monthly Adjustment Amount (IRMAA) if MAGI exceeds base
 - Base is <\$87,000 for singles, \$174,000 for MFJ
(2020 data from 2018 tax return)

Income Related Monthly Adjustment Amount, IRMAA (2020 data from 2018 tax returns)

MAGI: Single	MAGI: MFJ	Part B IRMAA	Part D IRMAA
\$87,000 to \$109,000	\$174,000 to \$218,000	\$57.80	\$12.20
\$109,001 to \$136,000	\$218,001 to \$272,000	\$144.60	\$31.50
\$136,001 to \$163,000	\$272,001 to \$326,000	\$231.40	\$50.70
\$163,001 to \$500,000	\$326,001 to \$750,000	\$318.10	\$70.00
>\$500,000	> \$750,000	\$347.00	\$76.40

Tax Tips: Qualified Charitable Distributions, QCDs

- **Donation directly from IRA to charity**
 - Skips Form 1040; Does not add to total income
 - Does not add to AGI; no Medicare increase
 - Counts against your RMD
 - Especially useful strategy for taxpayers who take standard deduction
- **Limits**
 - \$100,000 maximum contribution
 - Cannot go to a Donor Advised Fund, DAF

Tax Tips: Bunch Deductions

	Standard		Bunched	
Year 1 SALT Charities Deduction	\$10,000	\$12,000	\$10,000	\$36,000
		\$24,800		\$46,000
Year 2 SALT Charities Deduction	\$10,000	\$12,000	\$10,000	\$0
		\$24,800		\$24,800
Year 3 SALT Charities Deduction	\$10,000	\$12,000	\$10,000	\$0
		\$24,800		\$24,800
3-Year Total Deductions		\$74,400		\$95,600

Tax Tips: Consider Lifetime Gifting

- **Annual gift exclusion**
 - \$15,000 per person, \$30,000 per couple
 - Unlimited recipients
- **Excess donations reduce your lifetime estate tax exclusion**
 - Must file disclosure on Form 709 along with 1040
- **Can make direct payments to medical and educational providers on behalf of a loved one**

To Probe Further

- **Guide to Tax on Your Personal Investments, AAll Staff, AAll Journal, December 2020**
- **Tax Guide Update: Staying Current on the New Rules, Charles Rotblut, AAll Journal, December 2020**
- **Tap Into Tax-Related Information on Stocks and Funds, Charles Rotblut, AAll Journal, December 2020**
- **SECURE Act Takeaways, Schwab.com**
- **CARES Act Offers Economic Stimulus to Fight Impact of Coronavirus, Kenneth Terrell, AARP, April 2020**
- **What the Pandemic Means for the Future of Spending and Saving, Christine Benz, Morningstar.com, Q4 2020**
- **Smart Tax Moves to Make Before Year's End, Charles Rotblut, AAll Journal, December 2019**
- **How to Make Your Money Last, Jane Bryant Quinn, Simon & Schuster**

Useful Websites

- aaii.com Broad selection of investing material
- siliconvalleyaaii.org Previous presentations on various topics
- irs.gov
- morningstar.com
- www.vanguard.com
- [santaclaracountylib.org/Adults/Business & Money](http://santaclaracountylib.org/Adults/Business%20&%20Money)
Morningstar Research Center, S&P's NetAdvantage, Value Line
- obliviousinvestor.com/index-funds/ Mike Piper blog
- rickferri.com/investment-philosophy/ Rick Ferri blog

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