Episode #03 of Intentional Wealth: Tax Planning Strategies with Barb LoPresti
A Podcast from Braun-Bostich & Associates

Welcome to Intentional Wealth, a monthly podcast where, alongside notable financial professional guests, Private Wealth Advisor and Founder of Braun-Bostich & Associates, Amy Braun-Bostich, delivers useful insights and strategies that help YOU live your best financial life! Remember, when your goals are meaningful and your wealth has purpose, you can truly live with intention. Now, here's the host of Intentional Wealth, Amy Braun-Bostich.

Amy Braun-Bostich: Good morning and welcome back to intentional wealth. Today. I'm joined by Barbara LoPresti from LoPresti & Company located Just up the road from our offices in McMurry, PA. A firm that's been serving the tax planning needs of local individuals and closely held businesses since 1996.

So welcome, Barb, and thanks for joining me today!

Barb LoPresti: Thank you.

Amy Braun-Bostich: It's great to have you here to discuss current tax planning strategies set against the backdrop of near-term legal changes we'll all need to be prepared for. We're going to talk about several topics that are incredibly important for individuals, families, and business owners to consider as they look to proactively implement effective tax mitigation strategies in the wake of these pending tax law changes.

Why don't we start with you telling us a little bit about what you do and about the services offered at LoPresti & Company.

Barb LoPresti: Well, thank you Amy. As you stated, I've been around since 1997 so, I've been practicing out here for 24 years almost, and I focus on small businesses and individuals providing tax and accounting services as needed. I also do work with some trusts and estates, supporting more the legal profession on that, and I do work with a couple of private foundations which I find to be interesting.

Amy Braun-Bostich: Well, that's terrific, that's absolutely great. As a baseline for our discussion let's table some of the most obvious reasons to be proactive rather than reactive about tax preparation in today's changing environment.

Barb LoPresti: Well I think in any environment, whether it's the current one or a prior one, or what have you, we have to be proactive. Many times, I see people come in the door after year end, and there's nothing I can do to help them resolve a tax situation they've gotten into, it's too late, it's out of the tax year and being proactive is giving us the heads up given a certain circumstance in your situation that's different.

How best can we use that for today's… how best can we plan for that in the current tax year to save those current dollars? As we all try to do, the taxation planning is one of defer income

and accelerate deductions. I think that probably the most important reason to be proactive is ultimately to save you tax dollars.

Amy Braun-Bostich: Yeah. I think a lot of people look at tax as historical in nature. You know, I think I notice even with our own clients, unless we nudge them to reach out to their CPAs or we do it for them, they're just waiting until the next tax year to sort of talk to their CPA when, like you say, it's too late.

Barb LoPresti: It is, especially if there's something life changing, if you're putting a spouse… or if you're moving into a medical facility, one of the long-term care facilities and a lot of times we see excessive medical deductions. Well, we want to make sure that we use those medical deductions to offset income.

So maybe we generate income and not waste those deductions. We can't do that after year end.

Amy Braun-Bostich: Yeah, I know I have a client that was getting net operating losses from a business he invested in every year, but we weren't able to use them to withdrawal IRA money tax-free because we wouldn't get them, even though we'd ask, until the following year. So it made it really hard to do things like that.

Barb LoPresti: Absolutely. There's so many different reasons I think, to be proactive… Yeah.

Amy Braun-Bostich: Okay. So, there's a number of tax law changes coming down the pike that will have impact on our clientele. A few would be capital gains, corporate tax increases, and some things that just made it through the ways and means committee. What are some things that your firm is doing to prepare clients for these changes?

Barb LoPresti: Well, it's scary. As we've talked in the past, we never know what we're going to end up with as far as new tax laws. As you know, the Senate came out in August, House Ways and Means came out a couple of days ago, each have their own version of a bill and who knows what the government will ultimately settle on.

But what we do know… what I know just from years of experiences, we've spent a lot of money in these last 18 months with the pandemic. We need to replenish that pot of money that was needed. A lot of money was given away and it was needed, but we've got to replenish. And so, yes, there's going to be tax increases because realistically that's the only way we get some money back in there.

And the talk in both House and Senate is to change some taxation of capital gains, maybe hit the corporate tax increase, although yesterday, Ways and Means I was happy to see that for the real small business, and that's who I see a lot of, they're actually proposing a decrease in the corporate tax rate to 18% and then back to 21 then when it gets very large going higher. So, but that's still a positive for the small business, but when we talk about corporate tax rates, the thing we have to keep focused on is most small businesses today aren't corporate

and what I mean by that is they have made if they're a corporate entity, they've made an election to be an S-Corp, which means the income doesn't get taxed at the corporate level, it gets taxed in a personal level.

Or a lot of businesses are jumping over to the LLC environment, which again makes the income taxable at the individual level, not the corporate level. So, you have to assess the situation to see what's going to impact you. But to get back to your question, I mean, what I have focused on is to get my clients, If they feel that they're going to have any large capital gains transactions coming up in the future, let's get them maybe done now. We know those rates will go up in 2022 so, let’s get those, maybe take care of those large needs of cash, which come from the sale of securities. Let's, let's look at it in 2021, not 2022.

Although I do have to qualify that by one piece and that is that if you look closely at the House bill, they’re going to stay with a 20% tax rate on gains up through September 13th, 2021. Then anything after that is going to pop up to that, I believe it's 28%. So that's one aspect of both bills that's going to be retroactive when legislation is drafted, not when the tax bill actually goes into play.

Something else really quickly is, there’s a lot of talk about reducing our lifetime state exemption. We’re at 11 million now and I've heard talk of going back to 1 million. So I think that the people have to be focused on gifting and that's a 2021 issue, not a 2022 that there's a lot of wealth out there…Maybe it's time to move it.

Amy Braun-Bostich: So I think you're maybe referring to different trusts that they can move gift money to… Is that right?

Barb LoPresti: Well, the only way that you get money out of your estate is to give up the rights to it. So you could do it a couple of ways. Obviously you could just give it out right to your family members and be done with it, or you put it into some form of irrevocable trust.

And because there's not really a way to get it out of your estate and maintain control of it if that makes sense. Now there is, and we're probably really going off topic here, a specific type of trust out there called a defective grantor trust that's deemed to take it out of your estate, but still it's deemed to be yours for income tax purposes.

I mean, these are things that people, if they have a need, should really probably talk with an attorney who is specialized in estate planning.

Amy Braun-Bostich: Now also in the bill I thought I saw some mention of limiting the amount of Roth conversion that you can do?

Barb LoPresti: Yeah. You know, that was interesting.

Especially when you look at Roth conversions of course are taking it from a taxable to a non-taxable type of investment. So you take your taxable IRA, and you move it into a non-taxable

Roth IRA. Non-taxable meaning that it will grow tax-free in a Roth as of right now, you know, legislation can change.

But as of right now, when you take a distribution from that Roth, it's not subject to tax any of the growth. So it's a completely tax-free investment. Now you don't get a tax deduction up front when you fund it, but you do get the benefit of a non-taxation situation going forward once you fund it.

And those conversions now may be limited or, and they may be and generally they're limited based on your taxable income. That is something that you know, we've got to keep our mind, we've got to keep focused on those conversions. And I think when you do a Roth conversion, sometimes you've got to look at what you're going to do with that Roth.

And again, I'm going down a different path here, someone wants to convert a Roth when they're 62 to only turn around and take it out when they're 68. I don't know that a Roth conversion is worth doing it when they're 62, when their income is higher and they're going to pay the tax dollars on that conversion up front.

I think that when you do a Roth conversion in my mind, I think you have to do it when there's a long-term situation, or maybe you put it into a Roth thinking that you'll never touch it and give it to your children or grandchildren as an estate planning vehicle. So we always have to be aware of the cost of doing it, similar to people going out and refinancing a mortgage, you know, is there a lot of costs to do it? Maybe it isn't worth it at the end just to reduce an interest rate by 1%. So that's something I think you have to be aware of, but definitely if there is somebody out there with money and they would like to convert Roth, you have to look at.

And the other issue is where we always talk, and again, stop me if I'm going off here, but there's another type of Roth out there we call it backdoor Roth, and that's where someone… they can't fund, they don't have money in an IRA to convert. So they put it into what's called a traditional non-deductible IRA, meaning it goes into a traditional IRA, but it's not deductible because of income limits.

And then they turn around and they converted into a Roth and that's a backdoor Roth. And the problem with that is, you gotta make sure that when you do that conversion to a Roth, if you have a non-deductible and a deductible IRA, the entire IRAs are considered when doing that backdoor conversion.

So maybe not all of it can be converted there without a tax cost. So that's something to think about too.

Amy Braun-Bostich: Yeah, and there's Mega-Backdoor Roths too, but we don't, there's not a lot of people that take advantage of those utilizing, you know, after tax 401k accounts, but that's probably for another subject.

Barb LoPresti: Absolutely.

Amy Braun-Bostich: Maybe we'll talk, we'll talk about all that at another time. The current administration has sorta said that, you know, if you have income less than 400,000, then your taxes are not going up. Have you, do you think that's true? Do you, with some of these new proposals, do you think only people, you know, that are making 400,000 plus are going to be hit with higher taxes?

Barb LoPresti: I think yeah. Yeah, I'm going to say yes now there's two different factors. So, if you look at the ways of means bill, I think married filing joint was 450. Whereas a single is 400,000. I think that I believe that they will stay with that but what hit me very hard is when you look at this, we're back to a marriage penalty situation, a significant marriage penalty situation for tax purposes only because there's many other factors, but for tax purposes only, why would you be making.

If I'm single and my partner is single, we each have taxable income of 400,000. Whereas if we're married, we're limited at 450, I was saddened to see how drastic of a marriage penalty situation has come back into play. To me that's very unfair, but you know you are right and those are the levels that they're focused on.

Amy Braun-Bostich: Okay. Now thinking strategically, let's talk about charitable giving is one strategy to consider. How would someone plug into charitable goals in order to, to plan for, you know, unique opportunities and deductions.

Barb LoPresti: Yeah, I think what we have to… you know, charitable giving is an interesting area. I think in the tax return, but number one, what we have now is, we have a standard deduction that's very high.

So we may find someone who's extremely generous, but if their contributions, charitable giving doesn't exceed the standard deduction, they in essence waste as deductions, they're going to get a deduction at the standard level, whether they make those charitables or not. So, one item with charitables is maybe you bunch them in one year as opposed to giving them say 5,000 to the church each year, maybe one year you give them 25,000 in one year, along with other deductions you can get a tax deduction for. You know, right now the big push is 20 and 21 here. We have the 100% deductible contributions and basically when you do charitable contributions, the amount that your able to deduct in a given year. Not that you lose the deduction, but in a given year as limited to different levels of your adjusted gross income. For 20 and 21, people can basically wipe out their adjusted, gross income, wipe out their taxable income by giving cash contributions and electing a special provision where 100% of the charitable contribution would be considered deductible so that you can certainly use that provision.

And again, that's only in 21 now; it will be gone in 22. That was to promote the people that still continue to give during our pandemic. One aspect of charity, oh, well, let me, before I, let me say this, the other aspect of charity is to always go to the outside items. So donor advise fund a private foundation, things of those, those types of structures allow you to bunch, a lot of charity deduction in one year, as I had said before, maybe you want to put a hundred thousand into a donor advised fund. You can do that in one year and enjoy a deduction for

that in one tax year. Then as the money sits in the donor advised fund, you might be able to participate in a little bit as to how you want that money to disperse.

Amy Braun-Bostich: Now, do you still get the hundred percent deduction if you put it in a donor advised fund?

Barb LoPresti: Yes, because remember donor advised fund is irrevocable. I don't get any benefit back from that. Now there are other types of like what we call CRUTs and CRATs charitable remainder type trusts, which allow you to put money into them but you as the donor may get a certain amount of income back each year from that money that you've put in, in that case, you don't get 100% of the deduction because you're still benefiting from that trust. Whereas in a private foundation or a donor advised fund, you're giving, you don't have rights to any.

That goes, it's gone. So once again, you can take a full deduction. One other aspect I've gone to mentioned. I think people have to focus on is the provision for anybody over 70 and a half years old, you are able to divert your required minimum distribution to a charity and not take that required amount in income in a given year.

And you know, if you're limited to a standard deduction, a $10,000 charity to a 10,000 contribution to your church, isn't going to matter. But if you can say, hey if my RMD could divert 10,000 of it to my church, well, not only do you have the standard deduction you can take, but you have 10,000 less of income, you have to recognize.

I think that's an awesome provision in our code.

Amy Braun-Bostich: Yeah, and it's very helpful to for people on Medicare because premium B and D are means tested so, we can have people really get over that threshold and start paying more for Medicare very easily.

Barb LoPresti: Absolutely.

Amy Braun-Bostich: That’s awesome. Okay. Are there any other tax mitigation strategies for high earners and businesses that you can think of at this point?

Barb LoPresti: I think it's, it's tough. I see so many people right now you know, when the company sponsored plans really started to go away and the 401k came into play, we pumped as much money as we could into our 401ks, and that was a very wise thing to do. I see so many people now who have made good money over their lifetime that are now stuck with a situation where everything's taxable and that being their IRAs, that's where all their assets are sitting and they are 100% taxable, I don't know what else we can do out there. What I will say, and I had made this note earlier and maybe going back to a previous discussion, but you know, things to consider is there's something out there called an installment sale.

If you sell your business or you sell an interest or something down the road where you have an income recognition, but you're going to receive payments for that sale over a number of years, you're automatically into something called an installment sale. You have, you recognize the gain on that sale as you receive your gross proceeds. Something people need to do is think about revoking that installment sale provision, you are permitted to do that in the year the installment sale starts. Revoke it, bring all that cash in, bring all that gain into this year at these lower tax rates and not in the future. You know, so maybe when you say high income, maybe one of those individuals has that high-income because they're selling the business.

Amy Braun-Bostich: So for an installment sale, if you revoke it, you still are receiving income over a period of years, but you're paying all the tax upfront?

Barb LoPresti: Absolutely. I had a client in 2020 that had a big sale of an investment and, we absolutely took that provision because we knew that there would be higher rates down the road.

Amy Braun-Bostich: Now, what about folks planning for retirement? What are some common practices you could share with our audience about how to adjust tax planning for retirement?

Barb LoPresti: I think you have to first start with what their needs are. You know, how much money will they need in retirement and where is that going to come from?

You know, probably bouncing back to the IRA situation or the 401k situation. If that's where all their retirement money sits. Then they have no choice but to pick it all up as income, ordinary income. Maybe planning from an investment strategy is any other type of investment income they have, maybe they go into tax exempts, and that's exactly where you guys are there saying, you know, hey, we've got to be careful here because we don't want you to have everything taxable. I believe that comes into play, you know, and I think the other items that come into play is social security, when to start when not to start. I do feel that planning for retirement is different for every person, every tax payer, because I think there's a lot of outside influences and sometimes they have to make decisions that aren't tax motived.

Amy Braun-Bostich: Yeah, right. I mean, there's a, a spouse survival need maybe where you would, you know, what defer your social security so that if you die first or spouse can get a higher step up in social security.

Barb LoPresti: Yes, I do. I feel that way. I feel that you have to look at each situation. And again, going back to your opening comment, let's be proactive and not reactive.

Amy Braun-Bostich: I don't think people actually realize the tax penalty for widowers. So their tax rates go up and their income comes down and it's, it can be pretty, pretty devastating for some.

Barb LoPresti: Absolutely. And, you know, when we talked, again, going back and referring back to another discussion we had where I said about, you know, the change in a situation where you have maybe moving into a place here like friendship village, or what have you.

And you have this big write off of medical expenses in one year. Well then let's pool a bunch of that money from an IRA, let's skip that highest level of income and bring it in. Even if it's more than our RMD, we could get it out of their tax-free and let's then invest it in an invest it in such a way that you're making a growth in it but, maybe not getting taxable income from it. That's something to think about. And, the Roth conversion, I mean, that's definitely out there, but we already discussed some of the bad sides of the Roth.

Amy Braun-Bostich: if we turn our attention to the business owner, client, do you have any tips on restructuring an entity to be more strategic with tax deductions?

Barb LoPresti: Well, I think when we look at our entities, you know, I think we have four different types out there. We have the sole proprietor; we have the S Corp owner, we have a partnership, a partner in a partnership, and then we have our basic old C corporation. So, you know, the first three pay taxes at an individual level, the last one pays tax at a corporate level.

For the most part outside of maybe different plans, pension plans that are available. I think across the board, we have the ability to take a deduction for generally any, you know, if it applies in one and applies to the other, I do think, and our strategy is always deferring income and accelerate deductions.

So again, that's the same philosophy for all four of those. You know, we're in an odd situation right now because we, we as a country, converted from a C Corp to an S Corp for many, for a few reasons. First we always thought individual tax rates were lower and we always did we avoided a concept called double taxation, which is probably a discussion for another day.

But now we're seeing our C Corp rates at 21% and we think, well, why am I paying income as an S Corp on at a 35% or soon to be 39.6% when my S Corp could be 20 or my C Corp could be 21%? You have to you have to look at that. You have to pay attention. We got to remember that in the state of Pennsylvania, our corporate tax rate is 10%, whereas our personal tax rate is 3.07.

So, you know, I think again, each situation is different, and I don't know that I would run out. I know a number of individuals were saying, oh, we got to run out and change our S Corps to C Corps because now we got a lower C corporate. Eh, you know what? We need tax dollars in the future that, that C Corp rates going to go back up.

One item I do want to mention is S Corp versus partnership. You know, the big difference between those two is a partnership throws out income It's subject usually 100% self-employment tax. An S Corp is different. An S Corp, that income it throws out is not subject to self-employment tax, but you as an employee of that S Corp are required to take a salary.

And if you think of the concept of self-employment income, that is basically funding social security, Medicare, and social security. So a lot of people go to the S Corp level because only then the wages they take out are subject to the social security taxes, but any excess is not, there has been a push for a number of years to change that. To say that all of the net profits of the S Corp are going to be subject to self-employment tax as well. I think that might even be in the Senate bill. I see that that will change at some point, but other than that you know, I think a deduction as a deduction at whatever level you're in or whatever type of business entity you're in.

Amy Braun-Bostich: And like you said, the C Corp is double tax so even if I get a lower tax rate, when I take dividends, I've got to pay the corporate pays on that and I pay on that, and so I don't, I don't, I never understood where, where small businesses felt they could get away with, you know, lower tax rate with a C Corp.

Barb LoPresti: I absolutely agree. You know, maybe where they feel that it's different is maybe those dividends when they liquidate the company, those dividends will come out a year when they're in a lower bracket. Sometimes we, we see a 21% tax rate on a C Corp, and we think, well, why are we paying more on an S let's go back to a C. You have to, you have to really look at; you really do.

Amy Braun-Bostich: Well Barb, I have to tell you, this has been incredibly useful and informative so much so that I'm certain it will resonate with our listeners and pave the way for us to have you back in the near future. I, I thank you so much for all of your wonderful insight.

Barb LoPresti: Thank you. I really appreciate participating today. Have a good day!

Amy Braun-Bostich: Okay, you too… bye!