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Retirement Planning Insights

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Contact Us

www.tenonfinancial.com

hello@tenonfinancial.com

T: 732-902-0066

Tenon Financial LLC
33 Wood Ave South, Suite 600
Iselin, NJ 08830

Up Front

"TERP" is now a thing

Hear ye, hear ye! On September 5, 2020, I proclaimed to the world (via Facebook, LinkedIn and Twitter) the creation of the word TERP.

No, I didn't actually claim to be the first person to combine the letters T, E, R and P. In fact, TERP is already an acronym for many things such as the exciting sounding "Thermal Effective Response Parameter" used in the chemistry world. Also, the University of Maryland's mascot is a terrapin turtle, otherwise known as a Terp.

What I staked my claim to is the origination of TERP as an acronym for **T**ax-**E**fficient **R**etirement **P**lanning.

As you all know, I do retirement planning & investment management. Yes, lots of financial advisors do retirement planning & investment management. The difference with my approach is that I do it with tax-efficiency in mind throughout the process. Because it's not just what you get, it's what you keep…taxes always matter!

So, what's the point of making an acronym out of tax-efficient retirement planning??? Beats me…I figure it could come in handy at some point. For now, I at least made it into a cool t-shirt! And yes, that's me modeling below.

My goal is to not just be good at tax-efficient retirement planning but to make it educational and fun. I like to think any shirt with an "I ❤ *<insert something here>*" on it is automatically fun. With that said, here's to a fun October!

-Andy

Retirement Planning News

Proposed tax changes to be aware of

In a non-political kind of way, I'd like to share with you the parts of Joe Biden's proposed tax plan that are most likely to impact your retirement planning IF they end up becoming law. But first, keep in mind these are all just *PROPOSALS*…they're still far from even becoming draft bills, let alone laws.

The future of these proposals is heavily dependent on not just the outcome of the presidential election but also the outcomes of the Senate and House elections. As we all know, presidential candidates always have lofty goals and often make outright promises. However, without also wrangling the support of Congress, goals and promises will never materialize.

Then why am I even commenting on Biden's tax agenda??? Because some parts of it are significant enough that they should at least be on your retirement planning radar.

Below are the items of Biden's proposed tax changes that are most likely to impact retirement planning:

- Increasing the top marginal income tax rate from 37% back up to 39.6% (it's already planned to go back up in 2026…Biden's proposal accelerates it)
- For those earning more than $1,000,000 per year, taxing gains on investments held longer than a year at ordinary income rates instead of the lower "capital gains" tax rates that currently top out at 20%
- Capping the amount of itemized deductions for those with income over $400,000

The above three items would only apply to taxpayers with high income. Therefore, these changes likely won't affect the majority of retirees. However, there is one change that could potentially impact everyone:

- Elimination of the "step-up in basis"

"Basis" is tax speak for the price you paid for something. When you own an asset whose price has increased since you bought it, you have a gain. That gain will be taxable if/when you sell the asset. For example, if you bought a stock for $10 and sold it for $15, you will have to pay tax on the $5 gain.

However, the tax code currently allows you to pass on that stock to your heirs without anyone having to pay tax on the $5 gain. Instead, when your heirs receive that stock from your estate, the basis in their hands will be whatever the stock's price was at your death. In other words, your heir's basis will be "stepped-up" to $15 in this case. The $5 taxable gain that you would have had if you sold the stock during your lifetime magically goes away upon your death.

On the surface, it might look like the potential elimination of the step-up in basis would not so much affect you as it would your heirs. However, this would nonetheless impact your estate planning and the planning around which assets you choose to sell (or not) during your retirement years.

As of the publishing of this newsletter, there is still more than a month until the elections and obviously anything can happen. With that in mind, don't take any of Biden's proposals as foregone conclusions. But nonetheless keep them in mind.

Practical Retirement Planning

Exceptions to the 10% penalty when taking distributions from your IRA before age 59 ½

With a tax-deferred Individual Retirement Account, or "IRA," you typically can't take money out of the account prior to age 59 ½ without paying a 10% penalty. Since IRAs are meant to help you save for retirement, taking money out of them before 59 ½ often isn't ideal. But sometimes you don't have any alternatives.

Thankfully, the IRS grants nine exceptions the early withdrawal penalty. You'll still have to pay tax on your distributions, but you won't have to pay the 10% penalty in the below cases:

1. Paying for unreimbursed medical expenses that are more than 7.5% of your Adjusted Gross Income, or "AGI"
2. Paying for medical insurance premiums during your unemployment
3. Distributions while you are totally and permanently disabled
4. Distributions from an inherited IRA
5. Distributions under a formal plan of Substantially Equal Period Payments, or "SEPP"
6. Paying for qualified higher education expenses for you, your spouse, your children or your grandchildren
7. Using the money to buy, build or rebuild the first home for you, your spouse, your children, your grandchildren or your parents. There is a $10,000 lifetime limit on such amounts
8. A levy from the IRS
9. A "qualified reservist distribution," which only applies to those in the military reserves who are called to duty for more than 179 days

For more information about each of these, check out my recent video:

If you have questions about any of these exceptions or want to discuss the possibility of taking early withdrawals from your IRA, **Contact Us.**