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Last, But Not Least: Tax Considerations for Life's Milestones

March 1, 2023

Reminder:

Life Lessons webinars are designed to provide an overview of matters you may wish to consider at different stages of life.

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Life's Milestones

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- **First Steps:** Finding your financial footing
- **All's Fair in Love and Money:** Money and personal relationships
- **Building and Protecting Your Nest**
- **Getting Your Ducks in a Row:** Documents and discussions
- **Ready, Set, Retire:** Planning for your golden years
- **Death is in the Details**

Life Lessons Webinar #1

First Steps:
Finding your financial footing

- Employer Provided Fringe Benefits
  - Health and Life Insurance
  - Retirement Plans
  - Cafeteria Plans
  - Assistance Plans

Employer Provided Fringe Benefits: Health and Life Insurance

→ Health insurance

- Premiums paid by employer are not taxable
  - Includes long-term care insurance

- Itemized deductions for
  - Premiums paid by employee
    - Disability and life insurance premiums not deductible
  - Out-of-pocket expenses for co-pays, co-insurance and deductibles
  - Must exceed Adjusted Gross Income (AGI) floor of 7.5%
  - Must not be paid by a flexible spending account or health savings account

- CAUTION: Self-employed individuals eligible under spouse's plan

→ Group-term life insurance

- Premiums for $50,000 of coverage are not taxable

Employer Provided Fringe Benefits:
Retirement Plans

- Retirement plan contributions
  - Employer contributions: tax-deferred income
  - Employee contributions: tax-deferred income
  - Earnings are tax-deferred until withdrawn
  - May be in lower tax bracket in retirement

- Employer "match"

- SECURE 2.0 legislation ("Setting Up Every Community for Retirement Enhancement")
  - Roth 401(k) employer match (2023)
  - Student loan payment matching (2024)
  - Emergency savings accounts and withdrawals (2024)
  - Catch-up contributions enhanced (2025)
  - Saver's Credit (2027)

- Social Security Employer match = 7.65%

Employer Provided Fringe Benefits:
Cafeteria Plans

- Employees choose between taking cash (taxable) or benefits that are not taxable ("pre-tax")
- Flexible spending account (FSA): "Use it or lose it!"
  - Health insurance and medical expenses
  - Daycare
  - Adoption assistance
- Health savings account (HSA)
  - Medical expenses for a high-deductible plan
- Disability insurance
  - Disability benefits received are taxable if employer pays premiums
  - Employee should pay premiums "after-tax"
- Group-term life insurance

Employer Provided Fringe Benefits:
Assistance Plans

- Employer paid benefits are not taxable income
- Dependent Care: $5,000 maximum each year
- Educational Assistance Programs: $5,250 maximum per year
  - Includes student loan payments through 2025
  - Undergraduate or graduate-level courses
  - Need not be job related unless involve sports, games or hobbies

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Life Lessons Webinar #2

All’s Fair in Love and Money:
Money and personal relationships

- Income Tax Return Filing Status
  - Why does it matter?
  - Determined by marital status
  - Non-tax considerations
  - Divorce

Income Tax Return Filing Status: Why does it matter?

- Determines
  - Tax rates
  - Standard deduction (in lieu of itemized deductions)
  - Tax credits
  - Other tax benefits

- Determined by marital status and *“dependents”*
  - No deduction for personal exemptions or dependents: through 2025

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Income Tax Return Filing Status: Determined by marital status

- Married filing jointly
  - Married status on December 31st
  - Unmarried surviving spouse considered married at year end
- Qualifying widow or widower (surviving spouse)
  - Considered married for two years after year of death of spouse
  - Must not remarry
  - Must maintain household for a "*dependent child*" living in the home
- Head of household
  - Unmarried
  - Must maintain household for a *"qualified person"*
- Single
  - Unmarried
  - May qualify for Head of Household
- Married filing separately

Tax Rate Schedule: 2022

Ordinary Income

Tax Bracket/ Filing Status	Single	Married Filing Jointly or Surviving Spouse	Married Filing Separately	Head of Household
10%	$0-$10,275	$0 - $20,550	$0-$10,275	$0 - $14,650
12%	$10,275 - $41,775	$20,550 - $83,550	$10,275 - $41,775	$14,650 - $55,900
22%	$41,775 - $89,075	$83,550 - $178,150	$41,775 - $89,075	$55,900 - $89,050
24%	$89,075 - $170,050	$178,150 - $340,100	$89,075 - $170,050	$89,050 - $170,050
32%	$170,050 - $215,950	$340,100 - $431,900	$170,050 - $215,950	$170,050 - $215,950
35%	$215,950 - $539,900	$431,900 - $647,850	$215,950 - $323,925	$215,950 - $539,900
37%	Over $539,900	Over $647,850	Over $323,925	Over $539,900

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Tax Rate Schedule: 2022
Capital Gains & Qualified Dividends

Tax Bracket/ Filing Status	Single	Married Filing Jointly or Surviving Spouse	Married Filing Separately	Head of Household
0%	$0-$41,675	$0 - $83,350	$0-$41,675	$0-$55,800
15%	$41,676 - $459,750	$83,351 - $517,200	$41,676 - $258,600	$55,800 - $488,500
20%	$459,751+	$517,201+	$258,601+	$488,501+

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Standard Deduction

Filing Status/Standard Deduction	2022	2021	2020	2019	2018	pre-TCJA 2017
Married filing jointly	$25,900	$25,100	$24,800	$24,400	$24,000	$13,000
Qualifying widow or widower	$25,900	$25,100	$24,800	$24,400	$24,000	$13,000
Married filing separately	$12,950	$12,550	$12,400	$12,200	$12,000	$ 6,500
Head of household	$19,400	$18,800	$18,650	$18,350	$18,000	$ 9,550
Single	$12,950	$12,550	$12,400	$12,200	$12,000	$ 6,500

Increase in standard deduction offsets loss of deduction for personal and dependency exemptions through 2025

- Example: (2) parents + (1) child = $4,000 x 3 = $12,000

Intended to reduce IRS examinations of itemized deductions

Income Tax Return Filing Status:
Non-tax considerations

- → Married filing separately does not provide tax advantages
  - EXCEPTION: One spouse has significant uninsured medical expenses
- → Married filing separately may be beneficial for non-tax reasons
  - No joint & several liability
    - "Spendthrift" spouse
    - Spouse with separate debt; bankruptcy history
    - "Innocent spouse" vs. ignorant spouse
  - Prenuptial agreement
    - Separate wealth
    - Second marriage
    - Use of pre-nuptial does not require married filing separately
- → Federal and state laws regarding marriage

Income Tax Return Filing Status: Divorce

- Property settlement
  - Transfers between spouses are “gifts”
  - Gifts are not taxable income to recipient
  - Gifts are not deductible by the payer
- Child support
  - Not taxable income to recipient
  - Not deductible by the payer
- Alimony
  - Divorce decrees dated January 1, 2019, and after
  - Not taxable income to recipient
  - Not deductible by the payer
- Dependents
  - Usually claimed by custodial parent
  - Form 8332: one parent grants exemption to the other

Life Lessons Webinar #3

Building and Protecting Your Nest

- Home Ownership
- Raising Your Family
- Education Expenses
- Section 529 Plans
- Financial Protection

Home Ownership

- Mortgage interest expense
  - Primary and secondary home <u>acquisition</u>
  - Debt secured by residence: “acquisition debt, home equity loan, home equity line of credit (HELOC) or second mortgage”
  - Debt used for deduction capped at $750,000
  - After 2025, cap = $1M + $100,000 of home equity debt
- Real estate property taxes plus state income taxes, personal property taxes limited to $10,000 through 2025 ($5,000 MFS)
- Utilities, maintenance and insurance: not deductible
- Casualty losses: not deductible unless in federally declared disaster area through 2025
- Sale of home: $500,000 of gain may not be taxable for <u>principal</u> residence; Capital gains rates may apply to taxable gain

Raising Your Family

- No deduction for personal exemptions or dependents through 2025
- Adoption: $15,950 for expenses in 2023
  - Tax free employer assistance for expenses OR
  - Tax credit
- Child tax credit
  - $2,000 for each qualifying child under age 17 AND
  - $500 for any other dependent (through 2025)
  - “Additional (refundable) child tax credit” of $1,600 for 2023
- Daycare expenses
  - $1,050 per child under age 13 or other qualifying dependent
  - Incurred to be gainfully employed

Education Expenses

- Employer educational assistance $5,250: employee only
- Scholarships
  - Ignored in determining support of a dependent
  - Taxable if spent for room and board
- Savings
  - (Coverdell) Education Savings Account a/k/a “Education IRA”
  - Section 529 Plans: states vary for tax deduction, investment options and fees
  - U.S. savings bond interest income not taxable if spent on education
- Student loans
  - Maximum deduction of $2,500 for interest expense
  - Debt forgiveness
- Gifts: do not include direct payments to educational institution
- Tax credits
  - American Opportunity
  - Lifetime Learning

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Section 529 Plans vs. Uniform Gifts/Transfers to Minors (UG/TMA)

Section 529 Plan

- Tax treatment
  - Tax-free growth & withdrawals
  - Unlimited annual contributions, may have lifetime limits
  - Contributors may receive income tax benefits for their home state plan
- Beneficiary can be changed anytime
- Adult owns property for FAFSA purposes
- State manages investment options, usually age-based
- Must be used for qualified education expenses
  - Up to $10,000 for K-12 education and student loan payments

UG/TMA

- Tax treatment
  - Investment income subject to “Kiddie Tax”
  - Transfers subject to federal gift tax annual limits: $17,000 in 2023
  - Alternative to trust funds for families with limited assets
- Beneficiary cannot be changed anytime
- Child owns property for FAFSA purposes
- No limitations on investment options
- Unrestricted use of funds (not limited to education)
  - Parent is custodian until child reaches age of majority

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Financial Protection

- Trusts: consult an attorney
  - "Spendthrift" children
  - Special needs children
- Disability insurance
  - Benefits are taxable unless the employee pays the premiums
  - Premiums are <u>not</u> a deductible medical expense
- Life insurance
  - Not taxable to the beneficiary
  - Premiums are <u>not</u> a deductible medical expense
  - Employer may provide $50,000 group-term coverage
- Long-term care insurance
  - Premiums are a deductible medical expense up to age-based limit

Life Lessons Webinar #4

Getting Your Ducks in a Row:
Documents and discussions you need to have

- Legal Documents
- Titling of Accounts
- “Convenience Accounts”
- Beneficiary Designations

Legal Documents

- Engage an attorney: CPAs cannot “practice law”
  - Financial Power of Attorney
  - Wills
  - Trust documents
- Income tax consequences
- Estate and gift tax consequences
- “Survivor’s Notebook”

Titling of Accounts

- Account holders may override will provisions

- Individual account holders: provisions of the will control

- Joint Tenants with right of survivorship (JTWROS)
  - Commonly used by married couples
  - “Simple” estates not subject to estate tax
  - Override provisions of the will
  - Adding a child for aging parents may be a gift
  - Lose the benefit of “step-up in basis”

“Convenience Accounts”

- → Account holder wants security of trusted person having access
  - Example: Adult child assisting elderly parent to pay bills
- → Parent does not intend for child to inherit the entire account
- → No right of survivorship; ownership transfers pursuant to provisions of the will
- → Functions like a Power of Attorney limited to a particular account
- → Half the states have adopted the Uniform Multiple-Person Accounts Act

Beneficiary Designations

→ "Beneficiary designation assets" - transfer upon death via beneficiary form, irrespective of will provisions

- Life insurance
- Qualified retirement plans, i.e., 401k and 403b plans
- Individual retirement accounts (IRAs)
- Annuities

→ Non-beneficiary designation assets: "after-tax assets"

- Bank accounts
- CDs outside of an IRA
- Brokerage accounts outside of an IRA

Life Lessons Webinar #5

Ready, Set, Retire:
Planning for your golden years

- Medical Expenses
- Taxation of Social Security
- Retirement Plan Distributions
- State Residency

Medical Expenses

- Itemized deduction for:
  - Self-insured/COBRA premiums
  - Medicare Parts B and D
  - Long-term care insurance premiums up to age-based limit
  - Medical portion of long-term care facility charges

- IRA distributions to fund HSA
  - One-time, tax-free transfer of otherwise taxable IRA distribution
  - Amount limited to annual HSA contribution maximum
    - $7,750 for family in 2023
  - Must be HSA eligible for following 12 months
  - Penalties may apply

Taxation of Social Security

- Working while receiving Social Security
  - Benefits decrease if you are younger than full retirement age
    - For the entire year: Benefits decrease $1:2 earned in excess of $21,240 (2023)
    - For part of the year: Benefits decrease $1:3 earned in excess of $56,250 (2023)
    - No decrease in benefits upon reaching full retirement age

- Social Security taxes must be paid on earnings regardless of age or eligibility

- Social Security benefits received may be taxable if:
  - Adjusted gross income (AGI)
    + nontaxable interest
    <u>+ 1/2 of Social Security benefits</u>
    = greater than $32,000 (married filing jointly), then up to 50% of benefits are taxable
    = greater than $44,000 (married filing jointly), then up to 85% of benefits are taxable

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Retirement Plan Distributions

- Required minimum distributions (RMD) must be withdrawn over life expectancy after beginning date to avoid penalties
- Secure 2.0 (new law)
  - RMD age 73 for 2023; age 75 by 2033
  - Roth accounts in employer retirement plans will be exempt from the RMD requirements (2024)
  - Distributions for terminally ill avoid penalties (2022)
  - Roth rollover of $35,000 lifetime limit for Section 529 plans (2022)
- Qualified Charitable Distributions (QCD) from IRA
  - Age 70½ or over
  - $100,000 tax-free distribution to charity

State Residency

- Changing state of residency upon retirement to avoid state income taxes
- State treatment of taxation of Social Security and retirement plan distributions varies
- Establishing residency: “183-day rule”
  - Own or lease a home in new state and use it as your main residence
- CAUTION: IRS factors to qualify for federal exclusion of $500K gain on sale of “primary residence”
  1. Federal income tax returns: address
  2. Voter registration
  3. Auto registration and insurance
  4. Bills and correspondence
  5. Banking relationships
  6. Social relationships

Life Lessons Webinar #6

Death is in the Details

- Disability and Final Medical Expenses
- Funeral Expenses
- Life Insurance
- Estate and Gift Taxes

Disability and Final Medical Expenses

- Financial protection
  - Disability insurance: benefits are taxable if you do not pay premiums
  - Life insurance: not taxable to the beneficiary
  - Long-term care insurance
    - Consider “self-insuring”

- Life insurance accelerated death benefits are not taxable income

- Retirement plan distributions for terminally ill avoid penalties
  - SECURE 2.0 (2022)

- Decedent’s medical expenses
  - Income tax itemized deduction subject to 7.5% AGI limitation OR
  - Estate tax deduction

Funeral Expenses

- → Do not qualify as medical expenses
- → Deductible for estate tax purposes
- → Include:
  - Tombstone
  - Mausoleum
  - Burial lot

Life Insurance

- In general, proceeds received by beneficiary are not taxable income
  - Interest income accruing on unpaid proceeds are taxable income

- In general, proceeds of life insurance are included in the estate for estate tax purposes

- Death benefit from employer is taxable
  - $5,000 exclusion eliminated in 1996

Federal Estate and Gift Taxes

- Estate and gift taxes paid by donor
  - Gifts, inheritances, and life insurance proceeds are not income taxable to the recipient
- Tax Cuts & Jobs Act (TCJA) 2017
  - Doubled estate tax exemption from $5.6M to $11.2M; adjusted for inflation
- Current exemptions/exclusions (2023):
  - Estate tax at death = $12,920,000; $12,060,000 (2022)
  - Gift tax during life = $17,000 per individual per year; $16,000 (2022)
    - Taxable gifts use up estate tax exemption
  - Amounts double for married couples due to “portability” and “gift splitting”
- Estate tax rate tiers: 18% ($10K estate) to 40% for estates > $1M
  - 2020: Only .1% of decedents filed Federal Estate Tax Return; only .04% paid tax
- Future of the “death tax”
  - TCJA changes will “sunset” (expire) in 2026
  - Step-up in basis at risk?

Last, But Not Least:
Tax Considerations for Life's Milestones

March 1, 2023

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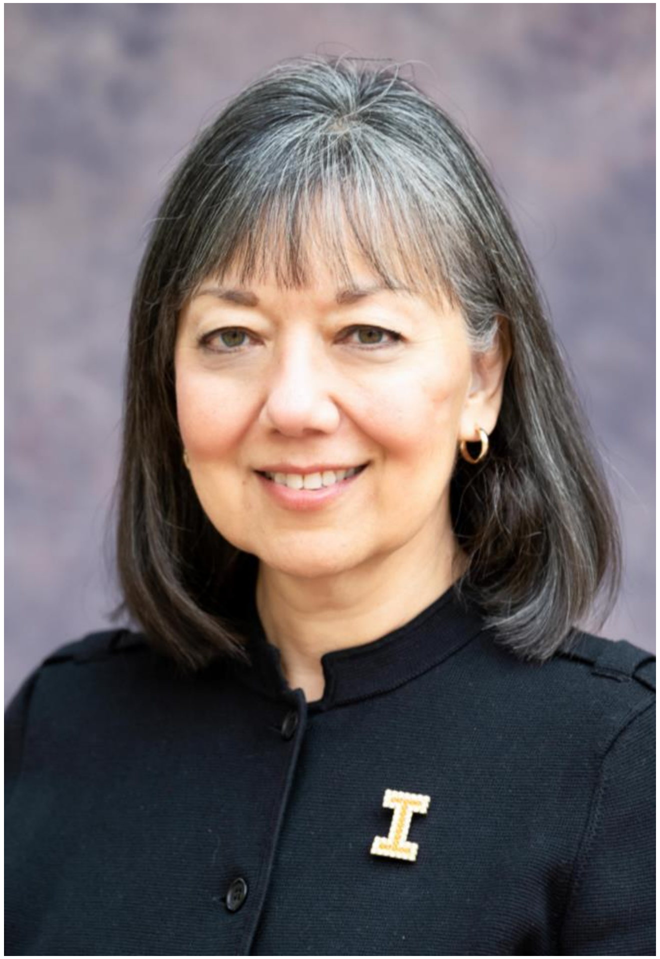

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