Waypoint Monthly

Brought to you by Our Team

James R. Schaffer, Jr., AIF®, CRPC®
Waypoint Partners
28601 Chagrin Blvd • Suite 300 • Cleveland • OH • 44122
216-591-2367
james.schaffer@LFG.com • waypointpt.com

Baby Boomers Buying More Online

The coronavirus pandemic has forced consumers to change many habits, including how they shop. This is particularly true for baby boomers (ages 56 to 74). Nearly half (45%) said they shop online more, with some product categories seeing a large shift in online purchases.

Source: National Retail Federation, 2020

Year-End 2020 Tax Tips

Here are some things to consider as you weigh potential tax moves before the end of the year.

Defer income to next year

Consider opportunities to defer income to 2021, particularly if you think you may be in a lower tax bracket then. For example, you may be able to defer a year-end bonus or delay the collection of business debts, rents, and payments for services in order to postpone payment of tax on the income until next year.

Accelerate deductions

Look for opportunities to accelerate deductions into the current tax year. If you itemize deductions, making payments for deductible expenses such as medical expenses, qualifying interest, and state taxes before the end of the year (instead of paying them in early 2021) could make a difference on your 2020 return.

Make deductible charitable contributions

If you itemize deductions on your federal income tax return, you can generally deduct charitable contributions, but the deduction is limited to 60%, 30%, or 20% of your adjusted gross income (AGI), depending on the type of property that you give and the type of organization to which you contribute. (Excess amounts can be carried over for up to five years.) For 2020 charitable gifts, the normal rules have been enhanced: The limit is increased to 100% of AGI for direct cash gifts to public charities. And even if you don't itemize deductions, you can receive a $300 charitable deduction for direct cash gifts to public charities (in addition to the standard deduction).

Bump up withholding

If it looks as though you're going to owe federal income tax for the year, consider increasing your withholding on Form W-4 for the remainder of the year to cover the shortfall. The biggest advantage in doing so is that withholding is considered as having been paid evenly throughout the year instead of when the dollars are actually taken from your paycheck.

Maximize retirement savings

Deductible contributions to a traditional IRA and pre-tax contributions to an employer-sponsored retirement plan such as a 401(k) can reduce your 2020 taxable income. If you haven't already contributed up to the maximum amount allowed, consider doing so. For 2020, you can contribute up to $19,500 to a 401(k) plan ($26,000 if you're age 50 or older) and up to $6,000 to traditional and Roth* IRAs combined ($7,000 if you're age 50 or older). The window to make 2020 contributions to an employer plan generally closes at the end of the year, while you have until April 15, 2021, to make 2020 IRA contributions. (*Roth contributions are not deductible, but Roth qualified distributions are not taxable.)

Avoid RMDs in 2020

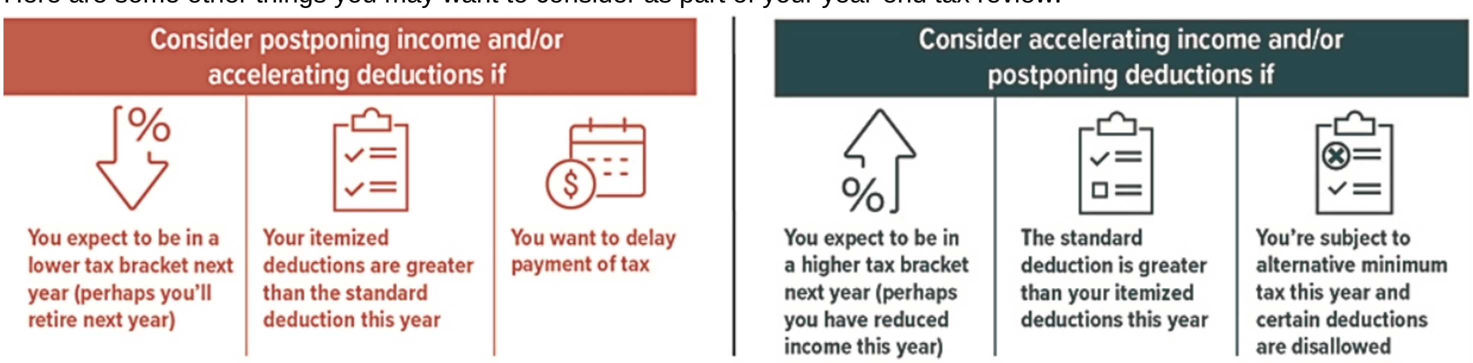
Normally, once you reach age 70½ (age 72 if you reach age 70½ after 2019), you generally must start taking required minimum distributions (RMDs) from traditional IRAs and employer-sponsored retirement plans. Distributions are also generally required to beneficiaries after the death of the IRA owner or plan participant. However, recent legislation has waived RMDs from IRAs and most employer retirement plans for 2020 and you don't have to take such distributions. If you have already taken a distribution for 2020 that is not required, you may be able to roll it over to an eligible retirement plan.

Weigh year-end investment moves

Though you shouldn't let tax considerations drive your investment decisions, it's worth considering the tax implications of any year-end investment moves. For example, if you have realized net capital gains from selling securities at a profit, you might avoid being taxed on some or all of those gains by selling losing positions. Any losses above the amount of your gains can be used to offset up to $3,000 of ordinary income ($1,500 if your filing status is married filing separately) or carried forward to reduce your taxes in future years.

More to Consider

Here are some other things you may want to consider as part of your year-end tax review.



Is Now a Good Time to Consider a Roth Conversion?

This year has been challenging on many fronts, but one financial opportunity may have emerged from the economic turbulence. If you've been thinking about converting your traditional IRA to a Roth, now might be an appropriate time to do so.

Conversion Basics

Roth IRAs offer tax-free income in retirement. Contributions to a Roth IRA are not tax-deductible, but qualified withdrawals, including any earnings, are free of federal income tax. Such withdrawals may also be free of any state income tax that would apply to retirement plan distributions.

Generally, a Roth distribution is considered "qualified" if it meets a five-year holding requirement and you are age 59½ or older, become permanently disabled, or die (other exceptions may apply).

Regardless of your filing status or how much you earn, you can convert assets in a traditional IRA to a Roth IRA. Though annual IRA contribution limits are relatively low ($6,000 to all IRAs combined in 2020, or $7,000 if you are age 50 or older), there is no limit to the amount you can convert or the number of conversions you can make during a calendar year. An inherited traditional IRA cannot be converted to a Roth, but a spouse beneficiary who treats an inherited IRA as his or her own can convert the assets.

Converted assets are subject to federal income tax in the year of conversion and may also be subject to state taxes. This could result in a substantial tax bill, depending on the value of your account, and could move you into a higher tax bracket. However, if all conditions are met, the Roth account will incur no further income tax liability and you won't be subject to required minimum distributions. (Designated beneficiaries are required to take withdrawals based on certain rules and time frames, depending on their age and relationship to the original account holder, but such withdrawals would be free of federal tax.)

Why Now?

Comparatively low income tax rates combined with the impact of the economic downturn might make this an appropriate time to consider a Roth conversion.

The lower income tax rates passed in 2017 are scheduled to expire at year-end 2025; however, some industry observers have noted that taxes may rise even sooner due to rising deficits exacerbated by the pandemic relief measures.

Moreover, if the value of your IRA remains below its pre-pandemic value, the tax obligation on your conversion will be lower than if you had converted prior to the downturn. If your income is lower in 2020 due to the economic challenges, your tax rate could be lower as well.

Any or all of these factors may make it worth considering a Roth conversion, provided you have the funds available to cover the tax obligation.

As long as your traditional and Roth IRAs are with the same provider, you can typically transfer shares from one account to the other. When share prices are lower, as they may be in the current market environment, you could theoretically convert more shares for each dollar and would have more shares in your Roth account to pursue tax-free growth. Of course, there is also a risk that the converted assets will go down in value.

Using Conversions to Make "Annual Contributions"

Finally, if you are not eligible to contribute to a Roth IRA because your modified adjusted gross income (MAGI) is too high (see table), a Roth conversion may offer a workaround. You can make nondeductible contributions to a traditional IRA and then convert traditional IRA assets to a Roth. This is often called a "back-door" Roth IRA.

As this history-making year approaches its end, this is a good time to think about last-minute moves that might benefit your financial and tax situation. A Roth conversion could be an appropriate strategy.

All investing involves risk, including the possible loss of principal, and there is no guarantee that any investment strategy will be successful.

If your federal tax filing status is:	Your 2020 Roth contribution is reduced if your MAGI is:	You can't contribute to a Roth IRA for 2020 if your MAGI is:
Single or head of household	More than $124,000 but less than $139,000	$139,000 or more
Married filing jointly or qualifying widow(er)	More than $196,000 but less than $206,000	$206,000 or more
Married filing separately	More than $0 but less than $10,000	$10,000 or more

Note that your contributions generally cannot exceed earned income for the year. (Special rules apply to spousal IRAs.)

Should You Pay Off Student Loans Early or Save More for Retirement?

For adults with student debt and extra money on hand, deciding whether to pay off student loans early or put those funds toward retirement can be tricky. It's a financial tug-of-war between digging out from debt today and saving for the future, both of which are very important goals. This decision is relevant today considering that roughly 65% of college graduates in the class of 2018 had student debt, with an average debt of $29,200.[1] This amount equates to a monthly payment of $295, based on a 4% interest rate and standard 10-year repayment term.

Let's assume you have a $300 monthly student loan obligation. You have to pay it each month — that's non-negotiable. But if you have extra money available, what's the better course: pay more toward your student loans each month to pay them off faster or contribute extra funds to your retirement? The answer comes down to optimizing how those dollars can be put to work for you.

The first question to consider is whether you are taking full advantage of any 401(k) match offered by your employer. For example, let's say your employer matches one dollar for every dollar you save in your 401(k), up to 6% of your pay. If you make $50,000 a year, 6% of your pay is $3,000. So by contributing $3,000 per year to your 401(k), or $250 per month, you will get the full employer match of $3,000. That's a 100% return on your investment.

If you are already contributing enough to get the full match, next compare the interest rate on your debt to the rate of return you could be earning on any extra funds you invest. When you make extra payments on a specific debt, you are essentially earning a rate of return equal to the interest rate on that debt. In the student loan example, the interest rate is 4%, so by applying extra money toward that debt you are "earning" a 4% return. If you think you can earn a higher rate of return by investing extra money in your retirement account, then those funds might best be put to work for you there.

Of course, no one can predict their expected rate of return with certainty. But generally speaking, if the interest rate on your debt is relatively low, the potential long-term returns you might earn in your retirement account could outweigh the benefits of shaving a year or two off your student loans. If you have time on your side when saving for retirement, the long-term growth potential of even small amounts can make contributing to your retirement account a smart financial move.

All investing involves risk, including the possible loss of principal, and there can be no guarantee that any investing strategy will be successful.

1) The Institute for College Access and Success, 2019