Warren Wealth Wisdom

Putting Clients First

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For Sue and Chris, one of the rare positives of Covid has been the chance to spend extra time with their son Garrett who has been doing his college studies from home. They wish everyone well and hope to see you all in person when possible.

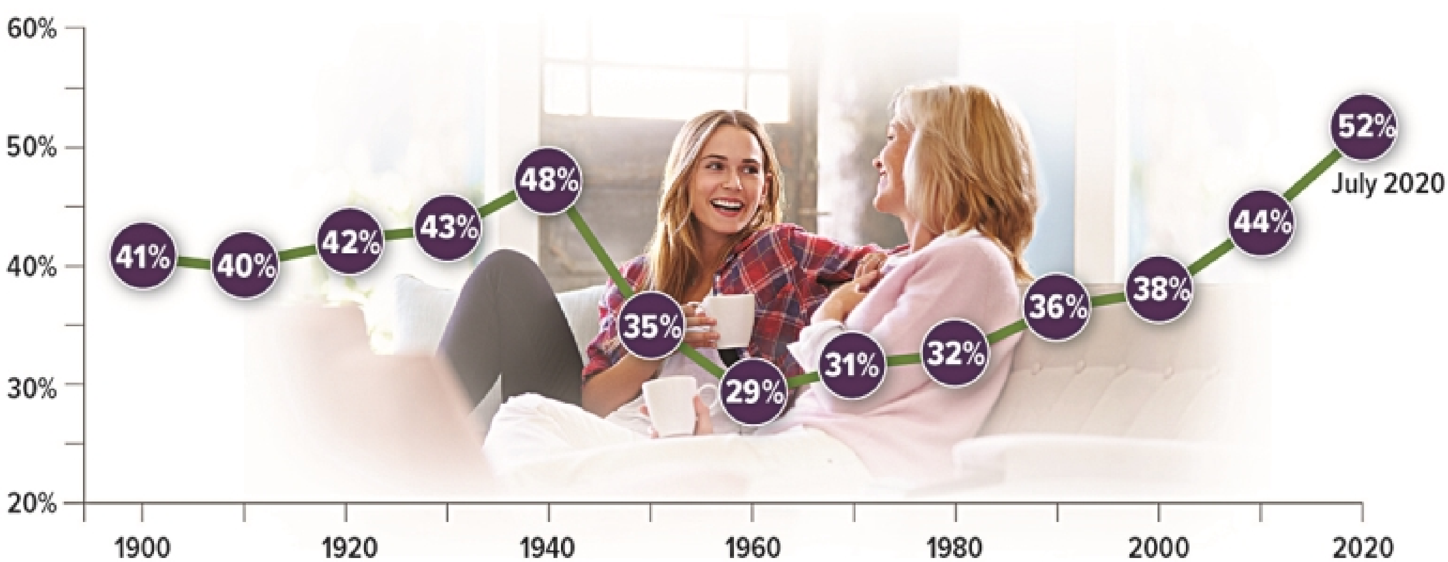
With warmer weather arriving, Scott, Jen and Eleanor look forward to spending more time outdoors – namely parks, farmers markets, and walks, and they hope to see Jen's family in Michigan soon, as it's been over a year since Scott spent time with his outlaws!

Ronnie is pleasantly settling into her position here at WWA and enjoying getting to know our clients. As with most others, life has been low key, though happy that gyms are open! She is looking forward to being able to spend more time outdoors with family, friends and her dogs.

Jenica has been spending her weekends with close friends and family and free time at the gym. She has made a lofty list of home projects and looks forward to working with the Save Coastal Wildlife foundation this spring.

Majority of Young Adults Living at Home

In 2020, a record number of 18- to 29-year-olds lived at home with their parents. In July, 52% of young adults were living at home, surpassing the previous high of 48% recorded in 1940 at the end of the Great Depression. This record return to the family home has been driven by the coronavirus pandemic and exacerbated by the overall economic downturn, record-low housing inventory along with a shortage of affordable entry-level homes, and high levels of student debt. The number of young adults living with their parents grew across the board for all demographic groups and regions of the country.



Source: Pew Research Center, 2020

Key Retirement and Tax Numbers for 2021

Every year, the Internal Revenue Service announces cost-of-living adjustments that affect contribution limits for retirement plans and various tax deduction, exclusion, exemption, and threshold amounts. Here are a few of the key adjustments for 2021.

Estate, Gift, and Generation-Skipping Transfer Tax

- The annual gift tax exclusion (and annual generation-skipping transfer tax exclusion) for 2021 is $15,000, the same as in 2020.
- The gift and estate tax basic exclusion amount (and generation-skipping transfer tax exemption) for 2021 is $11,700,000, up from $11,580,000 in 2020.

Standard Deduction

A taxpayer can generally choose to itemize certain deductions or claim a standard deduction on the federal income tax return. In 2021, the standard deduction is:

- $12,550 (up from $12,400 in 2020) for single filers or married individuals filing separate returns
- $25,100 (up from $24,800 in 2020) for married individuals filing joint returns
- $18,800 (up from $18,650 in 2020) for heads of households

The additional standard deduction amount for the blind or aged (age 65 or older) in 2021 is:

- $1,700 (up from $1,650 in 2020) for single filers and heads of households
- $1,350 (up from $1,300 in 2020) for all other filing statuses

Special rules apply if you can be claimed as a dependent by another taxpayer.

IRAs

The combined annual limit on contributions to traditional and Roth IRAs is $6,000 in 2021 (the same as in 2020), with individuals age 50 and older able to contribute an additional $1,000. The limit on contributions to a Roth IRA phases out for certain modified adjusted gross income (MAGI) ranges. For individuals who are covered by a workplace retirement plan, the deduction for contributions to a traditional IRA also phases out for certain MAGI ranges. (The limit on nondeductible contributions to a traditional IRA is not subject to phase-out based on MAGI.)

MAGI Ranges: Contributions to a Roth IRA

	2020	2021
Single/Head of household	$124,000–$139,000	$125,000–$140,000
Married filing jointly	$196,000–$206,000	$198,000–$208,000
Married filing separately	$0–$10,000	$0–$10,000

MAGI Ranges: Contributions to a Traditional IRA

	2020	2021
Single/Head of household	$65,000–$75,000	$66,000–$76,000
Married filing jointly	$104,000–$124,000	$105,000–$125,000

The 2021 phaseout range is $198,000–$208,000 (up from $196,000–$206,000 in 2020) when the individual making the IRA contribution is not covered by a workplace retirement plan but is filing jointly with a spouse who is covered. The phaseout range is $0–$10,000 when the individual is married filing separately and either spouse is covered by a plan.

Employer Retirement Plans

- Employees who participate in 401(k), 403(b), and most 457 plans can defer up to $19,500 in compensation in 2021 (the same as in 2020); employees age 50 and older can defer up to an additional $6,500 in 2021 (the same as in 2020).
- Employees participating in a SIMPLE retirement plan can defer up to $13,500 in 2021 (the same as in 2020), and employees age 50 and older can defer up to an additional $3,000 in 2021 (the same as in 2020).

Kiddie Tax: Child's Unearned Income

Under the kiddie tax, a child's unearned income above $2,200 in 2021 (the same as in 2020) is taxed using the parents' tax rates.

Estate Planning Strategies in a Low-Interest-Rate Environment

The federal government requires the use of certain interest rates (published by the IRS) to value various items used in estate planning, such as an income, annuity, or remainder interest in a trust. The government also has interest rates that a taxpayer may be deemed to use in connection with certain installment sales or intra-family loans. These rates are currently at or near historic lows, presenting several estate planning opportunities. Low interest rates generally favor certain estate planning strategies over others and may have a detrimental effect on others.

Grantor Retained Annuity Trust (GRAT)

In a GRAT, you transfer property to a trust, but retain a right to annuity payments for a term of years. After the trust term ends, the remaining trust property passes to your beneficiaries, such as family members. The value of the gift of a remainder interest is discounted for gift tax purposes to reflect that it will be received in the future. Also, if you survive the trust term, the trust property is not included in your gross estate for estate tax purposes. If the rate of appreciation is greater than the IRS interest rate, a higher value of trust assets escapes gift and estate taxation. Consequently, the lower the IRS interest rate, the more effective this technique generally is.

Charitable Lead Annuity Trust (CLAT)

In a CLAT, you transfer property to a trust, giving a charity the right to annuity payments for a term of years. After the trust term ends, the remaining trust property passes to your beneficiaries, such as family members. This trust is similar to a GRAT, except that you get a gift tax charitable deduction. Also, if the CLAT is structured so you are taxed on trust income, you receive an upfront income tax charitable deduction for the gift of the annuity interest. Generally, the lower the IRS interest rate, the more effective this technique is.

Installment Sale

You may also wish to consider an installment sale to family members. With an installment sale, you can generally defer the taxation of any gain on the property sold until the installment payments are received. However, if the family member resells the property within two years of your installment sale, any deferred gain will generally be accelerated. The two-year limit does not apply to stocks that are sold on an established securities market.

You are generally required to charge an adequate interest rate in return for the opportunity to pay in installments, or interest will be deemed to be charged for income tax and gift tax purposes. However, with the current low interest rates, your family members can pay for the property in installments, while paying only a minimal interest cost for the benefit of doing so.

Low-Interest Loan

A low-interest loan to family members might also be useful. You are generally required to charge an adequate interest rate on the loan to avoid income tax and gift tax consequences. However, with the current low interest rates, you can provide loans — or refinance an existing loan — at a very low rate and family members can effectively keep any earnings in excess of the interest they are required to pay you.

Charitable Remainder Unitrust (CRUT)

You retain a stream of payments for a number of years (or for life), after which the remainder passes to charity. You receive a current charitable deduction for the gift of the remainder interest. Interest rates have no effect if payments are made annually at the beginning of each year. Otherwise, interest rates generally have only a minimal effect. However, in this case, a lower interest rate increases the value of the charitable remainder interest slightly less than a higher interest rate would.

The use of trusts involves a complex web of tax rules and regulations, and usually involves upfront costs and ongoing administrative fees. You should consider the counsel of an experienced estate professional before implementing a trust strategy.

More to Consider

Here is how certain factors affect the valuation of remainder interest transfers in the trusts discussed here. In addition to the interest rate, you may want to consider how the length of the trust term and the amount of the trust payments affect values.

FACTOR	GRAT	CLAT	CRUT
Lower interest rate	LV	LV	Minimal or no effect
Longer term of years	LV	LV	LV (shorten term to increase value)
Higher annuity payment	LV	LV	N/A
Lower unitrust payout rate	N/A	N/A	HV

HV = higher value for remainder interest; LV = lower value for remainder interest

Tax Filing Information for Coronavirus Distributions

In March 2020, Congress passed the Coronavirus Aid, Relief, and Economic Security (CARES) Act. The legislation included a provision that allowed qualified retirement plan participants and IRA account holders to take penalty-free early distributions totaling no more than $100,000 between January 1 and December 31, 2020. If you took advantage of this measure, here's what you need to know for tax filing.

What Is a Coronavirus Distribution?

In order for a distribution to be qualified under the CARES Act, it must have been made to a qualifying individual before December 31, 2020. You qualify if you, your spouse, or dependents were diagnosed with the virus, or if you, your spouse, or someone who shares your principal residence experienced a pandemic-related financial setback as a result of:

- A quarantine, furlough, layoff, or reduced work hours
- An inability to work due to lack of child care
- Owning a business forced to close or reduce hours
- Reduced pay or self-employment income
- A rescinded job offer or delayed start date for a job

The Three-Year Rules

A key provision in the Act allows the distribution(s) to be spread "ratably" over three years for purposes of calculating tax payments. In other words, the total can be reported in equal amounts on your 2020, 2021, and 2022 tax returns. For example, if you received a $15,000 distribution, you could report $5,000 in income for each of the three years. However, if you prefer, you can generally report the entire distribution in your 2020 tax filing.

Another provision allows you to repay all or a part of your coronavirus distribution to an eligible retirement plan within three years from the day after the date the distribution was received. Repayments will be treated as if you enacted a trustee-to-trustee transfer, and no federal income taxes will be owed. (A repayment to an IRA is not considered a rollover for purposes of the one-rollover-per-year rule.)

If you pay your income taxes prior to repaying the distribution, your repayment will reduce the amount of the distribution income you report in a subsequent year. Or instead, you may file an amended return, depending on your specific situation.

Consider speaking with a tax professional before making any final decisions.

How to Report Distribution Income

If you received a coronavirus distribution(s) in 2020, you should use Form 8915-E, Qualified Disaster Retirement Plan Distributions and Repayments, to report the income as part of your 2020 federal income tax filing. You can also use this form to report any recontributed amounts.