Share Forward

COUTO DEFRANCO, P.A.
CERTIFIED PUBLIC ACCOUNTANTS & ADVISORS

ONLINE ADVISOR

JUNE 2020

This month's newsletter details several reasons why you should look for other sources of cash instead of tapping into your retirement funds, along with identifying potential tax surprises if you are using any of the pandemic-related relief programs, including unemployment benefits.

There are also some tips on how you can help local businesses as they re-open their doors and an overview of changes coming to your banking experience.

Please call if you would like to discuss how this information could impact your situation. If you know someone who can benefit from this newsletter, feel free to send it to them.

Financial Questions

Think Before

to Ask
Mom and Dad

Many Americans have been focused on their own finances over the past several months. But don't neglect helping those closest to you with their finances as well, especially aging parents. Here are some questions to ask your parents to help them sort through their financial picture.

Have you decided when you'll start taking Social Security benefits?
If your parents have not started taking Social Security, a discussion in this area will help both of you. Generally, Baby Boomers can receive their full amount of benefits at age 66, but benefits increase gradually if they wait longer, reaching the peak at age 70. Conversely, if your parents intend to retire early, they may wish to start receiving reduced benefits as soon as age 62. To add more complexity, a spouse can take retirement benefits from their partner's work history. Often a rule of thumb is if you expect to live past 80, consider delaying when you first receive benefits, if you can afford to do so.

Do you have a durable power of attorney?
If you need to act on behalf of your parents regarding financial matters, you will need a power of attorney. Without this document in place, you'll have to go to court to get guardianship of your parents in order to access their financial accounts.

Is there an executor?
Who is responsible for going through everything when necessary? You don't really need to know who it is, just that there is someone in place with a potential backup executor if the primary executor is unwilling or unable to help.

Tapping 401(k) as Emergency Fund

Do you need a quick infusion of cash?

Under the Coronavirus Aid, Relief, and Economic Security (CARES) Act, you may be able to take money out of a qualified plan, like a 401(k), or an IRA, with favorable tax consequences. But should you do it? You might view withdrawing money from a retirement account as a last resort.

Background
Among other changes in the CARES Act relating to qualified plans and IRAs, a participant can withdraw up to $100,000 of funds without paying the usual 10% tax penalty on distributions before age 59½. Plus, you can take as long as three years to pay the resulting tax bill, spread out evenly over the three years. If you repay the full amount within three years, you owe no tax.

To qualify for this program, you or your spouse must be diagnosed with COVID-19 or experience adverse financial consequences due to the virus such as being laid off, having work hours reduced or being quarantined or furloughed.

What are the pitfalls?

Where do you keep financial records?
Does someone, other than your parents, know where financial documents and information are kept? This includes bank account numbers along with usernames and passwords for websites.

Who are key advisors?
The executor will need the names and contact information for each member on your parents' team of trusted advisors. Ideally your parents have introduced their executor to each of the members of their team.

How are you planning to pay for long-term care?
One of the main financial concerns is the possibility of paying exorbitant amounts for long-term care in a nursing home or with stay-at-home assistance that will drain all your parents' assets. Traditionally, this was handled by long-term care insurance to absorb at least some of the cost. Unfortunately, these policies are now very expensive. But there are other ideas that can help, including certain tax advantaged insurance policies and establishing a trust to shield assets from nursing home costs (subject to certain restrictions for Medicaid assistance).

Do trusts need to be created or updated?
Although there are numerous types of trusts, each with a various purpose, your parents may use a trust to preserve assets for their heirs. They are also used to avoid probate. An irrevocable trust can fully protect assets, but your parents must give up all control over their assets. In contrast, a revocable trust can be modified (where your parents can still change beneficiaries), but offers less protection.

Remember, your goal is not to pry into your parents' finances, but to help ensure a plan is in place. And as an added benefit, many of the questions outlined here are great to apply to your own situation!

Be Prepared for Pandemic Tax

There are several reasons why you may want to avoid taking money out of your retirement accounts unless it's an absolute emergency:

You're diluting your retirement savings.
Although the money comes in handy now, you're chipping away at your nest egg and forfeiting growth. For example, if you withdraw the maximum amount of $100,000 that would have earned 6% annually tax-deferred for ten years, the value would have been $179,000.

It may be bad timing.
Experts say it is difficult to time the markets in the current volatile environment. If you sell some holdings right now, you may be locking in losses that would miss the recovery in the next few months or years.

You still owe income tax.
Income tax is due unless you replace the full amount within three years. Also, depending on your situation, you could end up paying tax at higher rates than you would in your retirement years.

Better options might exist.
Arranging a hardship loan from your 401(k) might be a better alternative for your situation. You avoid the taxable event of the withdrawal and you pay back yourself with interest. Other options include refinancing a mortgage with lower interest rates, taking advantage of payment relief from mortgage, rent or student loan payments or deferred credit card billing.

While it is an option, retirement plan withdrawals are not always the best choice. Think through all scenarios before withdrawing from retirement funds to cover emergency expenses.

Surprises

Numerous new laws provide economic relief to individuals and businesses hardest hit by this year's pandemic. This much-needed financial assistance, however, comes with a few strings attached.

Here are three potential surprises if you use the available economic relief packages:

- **Getting a tax bill for unemployment benefits.** While the $1,200 economic impact payments most Americans received does not have to be reported as taxable income on your 2020 tax return, there is currently no such luck with unemployment benefits. In addition to paying federal taxes on your unemployment compensation, more than half of states also impose a tax on unemployment benefits.
  What you need to do: *See if your unemployment compensation check withholds a portion of your pay for taxes. Even if your check does have withholding for income tax purposes, the withholding amount may not be enough. If possible, talk to your state unemployment office and try to get withholding amounts revised.*

- **Paying estimated tax payments.** If you normally receive a paycheck from your employer, you may have never needed to write a check to the IRS to pay estimated future taxes. Your employer withholds your taxes from your paychecks and sends it to the IRS for you. If you're collecting unemployment benefits, however, you may be required to pay tax on the unemployment benefits received during

Ideas to Help Local Businesses

Shuttered businesses are realizing that lifting lockdown restrictions doesn't mean a return to business as usual. Social distancing guidelines and a public wary of venturing into crowded environments means light customer traffic for many businesses.

Here are several ideas to help local businesses financially as they re-open their doors:

Tip more than usual. Of all industries impacted by the economic downturn, the leisure and hospitality industry is being hit the hardest. On top of the millions of workers in this industry that have filed for unemployment, even more have had their hours scaled back. When you order takeout or pay for a service,

the first six months of 2020 by July 15, 2020.
What you need to do: *Estimate the amount of tax you owe for all sources of income, then compare that number with the amount of money withheld from your income to pay these taxes. If necessary, send in quarterly estimated tax payments to the U.S. Treasury and, in some cases, state revenue departments. This must be done each quarter with the next payment due July 15. You may need to send money in on September 15, 2020 and January 15, 2021 as well.*

- **Reporting emergency distributions from retirement accounts:** You may withdraw up to $100,000 in 2020 from various retirement accounts to help cover pandemic-related emergency expenses without incurring penalties. While you will not be required to pay an early withdrawal penalty, you will still be subject to income tax when filing your 2020 tax return.
What you need to do: *If you plan to withdraw funds from your retirement account, reserve enough of the money to pay the tax! The amount you reserve depends on your potential tax situation so call for a tax review before taking money out of the account.*

consider tipping more than you normally would. It may not seem like much, but every extra dollar helps.

Shop online locally. The prices you pay might be higher, but when you add the property taxes, local employment taxes and donations to school events that local businesses fund, the added costs are worth it. Also, with many retail shops restricted to limited foot traffic because of social distancing guidelines, online sales are currently a significant source of revenue for many small businesses.

Write a review. Reviews left on Google, Yelp, and other sites are a major source of new customers for local businesses and restaurants. Take the time to leave a positive review for each of your favorite local businesses so new, potential customers can find them.

Offer your services. With the change in spending habits, businesses are forced to adapt. If you have skills and knowledge that could help a small business make the transition, consider donating some of your time. Some examples include web development, marketing strategies, cash flow management and budgeting.