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TAX MOVES TO MAKE NOW IF YOU THINK BIDEN WILL BE PRESIDENT

"I'm going to get rid of the bulk of Trump's $2 trillion tax cut, and a lot of you may not like that, but I'm going to close loopholes like capital gains and stepped-up basis." — Joe Biden, in a speech to potential campaign donors on June 29..

After a period of historically low tax rates and an exploding national debt, an era of higher taxation could arrive with a Joe Biden presidency next year, or with another progressive in five years. How does this potential change affect those entering or near retirement? Perhaps not favorably: You will be on a fixed income, but your taxes could increase, creating an additional drag on your retirement funds.

These same higher taxes could have a potentially negative impact on stock and dividend growth. Heavy-handed taxes at the corporate level could result in a dramatic slowing in GDP and spur multinational companies to leave our shores for a more favorable tax environment.

Biden's proposals could just the beginning. His first steps, as **outlined in his tax plan**, could be the end of historically low taxes for all of us. In other words, you may never again pay as little in taxes as you are today. Taxes are truly on sale right now.

The good news is there are things you can do. You don't have to be a victim of potential tax hikes. But you may need to take action sooner rather than later.

So, let's take a look at some current proposals from Biden. As you read, keep in mind that it's Congress — not the president — that has the power to determine what happens to taxes. Presidents can recommend changes to tax laws, but only Congress can make the changes. With that said, **let's look at where we may be headed and then talk about what you can do about it.**

1. PROPOSAL: HIGHER TAX RATES FOR THE WEALTHIEST AMERICANS

Although low- and middle-income earners would get some breaks under Biden's plan, he proposes to roll back the Trump tax rates to the pre-Trump era on those earning $400,000 or more. That means the top tax bracket will go up from 37% to 39.6%.

While that change would be incremental and only affect America's highest earners, a bigger change is coming regardless of who wins the White House, and it could affect us all. In 2025, if no action is taken, the Tax Cuts and Jobs Act will "sunset," meaning all tax brackets will go back up to the higher rates that existed prior to the Trump tax package. This increase will happen automatically on Jan. 1, 2026, simply by the Congress doing nothing.

2. PROPOSAL: NO MORE CAPITAL GAINS TAX BREAKS FOR HIGH EARNERS

Biden proposes taxing all dividends and capital gains at ordinary income rates for those earning $1 million or more. This means that the tax on selling a stock for those high earners would go from 20% now to 39.6%. That's nearly a 100% tax increase! And, certain high earners may be hit with an additional 3.8% net investment tax. According to Joy Taylor, editor of The Kiplinger Tax Letter, "As a result, under his tax plan, filers reporting over $1 million in income could pay a 43.4% federal tax rate on their long-term capital gains compared with 23.8% now."

3. PROPOSAL: ELIMINATING THE "STEP-UP IN BASIS"

This tax provision is a tax saving that allows you to pass on certain assets — such as stocks and real estate — to your heirs, with little to no tax implications. It allows you to pass on your life's savings to your heirs so they can benefit from your lifetime of hard work.

Here is how it works. An individual holds an asset for many years, watches it appreciate and passes it to an heir at death. The basis value — the owner's original investment in the asset — rises to the market value as of the date of death and the heir inherits this "stepped-up basis." If the heir turns around and sells the asset, he can do so with little to no capital gains tax.

"It's an enormous loophole in the law, the step-up in basis," said Jonathan Blattmachr, Estate Attorney and Principal at InterActive Legal, in a recent Business News report. "You get the step-up in basis even if you don't pay the estate tax."

This step-up in basis is not just used by the wealthy but by anyone who has spent their life saving and building an investment account with the hope of passing it on to their heirs in a tax-efficient manner. It is important to know that this step-up in basis applies not just to stocks but also to:

1. Mutual funds
2. Bonds
3. Your businesses
4. Real estate

A progressive candidate such as Biden could try to eliminate your step-up in basis on all investments in the future. (Remember: This could happen only if Congress passed a law to do so.) That means when you pass on, it is likely your family would have to pay ordinary income taxes on the total gains of any of your assets listed that your family inherits. This could easily push them in to the top tax bracket, currently proposed to be 39.6% by Biden.

BEFORE YOU DESPAIR, HERE ARE SOME MOVES YOU CAN MAKE

So, what can we do? There are three key steps you can take that would potentially minimize the impact on both you and your family's lives.

1. START SYSTEMATICALLY ROLLING OVER YOUR 401(K) AND IRA FUNDS TO ROTH EQUIVALENTS

This needs to be planned out carefully to be as efficient as possible. The premise of this argument is that you are now in the lowest tax brackets you will likely be in again in your life. Taxes are "on sale" right now. So, any money we can pay tax on now and move to a "tax-free" bucket is a no brainer. Get with a financial professional to build out a plan to take advantage of the current "stair step" tax system to minimize your tax hit.

2. QUIT SAVING IN A TRADITIONAL 401(K) AND START USING A ROTH 401(K) OR A ROTH IRA INSTEAD

If you're still working and saving in a 401(k), consider paying the tax now on any savings and invest into a Roth 401(k) or a Roth IRA instead.

The idea here is that traditional IRAs and 401(k)s are based on the single premise that you will retire in a lower tax bracket than you were in when you made the money. If you retire into a higher tax bracket, which now looks likely, investing in a traditional 401(k) or traditional IRA is mathematically a disaster compared to investing in the Roth equivalent.

3. LOOK FOR OTHER INVESTMENT STRATEGIES THAT WILL GROW TAX-FREE IN THE FUTURE

I predict that you will see what are known as LIRPs — Life Insurance Retirement Plans — become more popular moving forward, and they very may well be the No. 1 savings vehicle for those under 60 in the future. These are specially designed retirement plans built out and funded using specific types of cash value life insurance.

Why is this important moving forward? A true tax-free bucket is an investment strategy that will allow you to:

- Save, invest and grow your money for retirement without paying taxes. This allows compound tax-free growth.
- Take the money out in retirement, tax-free (this is a big one!).
- When you die, pass the assets to your heirs, tax-free.

In a rising-tax environment, it is all about tax-free growth, tax-free withdrawals in retirement and tax-free transfer to heirs. There are a few investment options that I call the "True Tax-Free Buckets," which allow all three of these tax efficient benefits:

- Roth IRAs limit your contributions to $6,000 a year ($7,000/year if you are 50 or older). Unlike a traditional IRA, you pay tax on the amount contributed and then can withdraw it tax-free later on. However, they are not available to higher-income earners. Other than your contributions themselves, the money in them is also not available to you without penalty until after the age of 59½, and until five years after contributing or converting it from a traditional IRA or 401(k).
- Roth 401(k)s allow for after-tax contributions of up to $19,500 a year ($26,000/year if you are 50 or older), and tax-free withdrawals. But, this type of savings vehicle is not available to many workers, and a Roth 401(k) limits your investment options. The money in them is also not available to you without penalty prior to age 59½ and before five years of it being in the account.
- LIRPs (Life Insurance Retirement Plan) is a type of life insurance policy that can provide a stream of tax-free income in retirement, similar to a Roth IRA. There are no contribution limits. You can access your account before age 59½ if needed without any penalties, and you will not be required to pay any taxes. You can even pay back the money if you choose to, allowing it to continue to grow tax-free for later. However, you must meet certain medical and financial qualifications to use this strategy. And while a LIRP can help protect against market loss, it also puts a cap on potential gains. There also typically certain internal charges and fees associated that vary between plans.
- HSAs (Health Savings Accounts) allow those who qualify to save for medical expenses. They get a triple tax break: Tax-free contributions, tax-free growth and tax-free qualified withdrawals. After age 65, you can take tax-free withdrawals from an HSA to pay for qualified medical expenses like Medicare Part B and Medicare Advantage plans, prescription drugs, a portion of long-term care insurance premiums, dental and vision care. And if you name your spouse your beneficiary, it's a tax-free transfer on death.

A paradigm shift has arrived in terms of how you build out your retirement plan. The old model of putting some money in stocks, some in bonds, placing it all in your 401(k) or IRA to be taxed in retirement could turn into a nightmare in a high-tax rate environment.

The new model will focus primarily on tax efficiency and wealth redistribution. Don't put your head in the sand and hope this goes away, because it may not. You can start preparing now!

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Dave Lopez is the Founder of ILG Financial, which has been in business for over 11 years and he has built out hundreds of Retirement Plans. Dave is a Fiduciary Investment Advisory and holds a Life, Long Term Care, and Annuity License. He has his own radio show, "Retire Your Way with Dave Lopez," currently available as a podcast. He is also a best-selling co-author of the Amazon book "Mama's Secret Recipe for Retirement Success" with Jack Canfield and has been featured in many finance periodicals.