Sweetgum Labs

Insights

Organizing Your Pantry

In Wealth Management

Life is a long journey. Financial planning may be implemented in fits and starts and at retirement you may find yourself with multiple types of accounts (registrations.) As you enter the distribution phase of your life you will need to decide how, when and where to withdraw.

To help organize registrations, we ask that you visualize different registrations as dry goods in a pantry. In your pantry you want to rotate your stock so that expiring goods are in the front and that symbiotic goods are clumped together (spaghetti and sauce.)

Often, a can of anchovies (or other less commonly used foods) will remain on the back of the shelf only to be used in emergency, while more popular items, like peanut butter, remain up front as they’re used more often.

Once properly organized, your options can be quickly assessed, and decisions made with as little waste as possible.

> ***“Becoming a good chef is knowing what foods pair well with each other. The key to a profitable restaurant is excellent inventory management and preparation for upcoming demands.”***

Financial planning has *evolved.*

Various registrations have required distributions (IRA, 401k) and some are situationally beneficial (529, HSA) for education and healthcare cost.
It is important that registration data (the pantry) is organized so that we can maximize the utility of each of the accounts to minimize tax burden and potential penalty. There are too many scenarios to list here, but we have put together rules that we follow and a brief description of common account types to help navigate.

*We assume that you are using an asset allocation strategy. An asset location strategy matches securities with their ideal tax structure (fixed-income/alternatives) in tax-deferred accounts to avoid paying income tax until withdrawal.

Rules

Rule 1

To be tax conscious but don't let the tax tail wag the dog—make decisions based on pure economic benefit and use the calendar to your advantage (spread distributions over multiple years to lower tax impact.)

Rule 2

It's wrong to assume that because you are retired and meet penalty exemptions that you can withdraw without a strategy. Some registration types maintain their advantage into retirement, and it would be ideal to select other less beneficial registrations until you have exhausted other options.

Rule 3

Always sleep on a decision. When a disaster or an immediate need arises, using rational thought is critical to getting the most out of your assets—always seek help when you need it.

The List (common registrations)

Cash Accounts

This type of registration is fully taxable (unless you have an exempt security like a muni bond.) Selling securities from this account will automatically generate a tax implication (gain or loss.) From a tax harvesting perspective, you may want to consider selling securities with losses to lower your tax liability (if you have one.) Taxes are not the only consideration and a security may not fit into an allocation or maybe a warning sign is signaling its time to sell.

IRA/401k/SEP Tax Deferred

These are retirement assets. Exemptions from early withdraw penalties exist and a 72t allows equal and substantial payments without penalty prior to retirement age. Retirement assets will typically be behind cash accounts "in the pantry" unless the tax situation is indifferent (asset location strategy is ineffective) or you have and RMD forcing a withdraw.

Roth accounts

The crown jewel of tax treatments. Assets accumulate tax free, RMD's do not exist. This should be the last place you source withdraws from (unless forfeiting something in another registration.) Attractive withdraw rules (after 5 years) sometimes prematurely target these accounts for withdraw. Placing tax inefficient securities that have the most growth potential, in this registration type is ideal.

529s

These assets are tax deferred and are intended for K-12 and higher education expenses. Distributions are considered tax free for qualified distributions. This is a situational registration and should be matched with a tuition payment or other qualifying purchase. Beneficiary's may be changed, and special exemptions exist if the beneficiary receives a scholarship.

HSAs

Intended for healthcare expenses (tax free withdraws.) These assets should be matched only with healthcare cost unless it is the last choice and you are over the age of 65. Penalty is 20% for early with-draw. Excellent way to save for potential long-term care cost outside of insurance.

Annuities

For newer contracts they are treated as last-in-first-out (LIFO): which means growth and earnings are withdrawn first and are taxed as ordinary income upon withdraw. Early withdraw penalties may apply. This contract can be very useful when an asset location strategy cannot be effective because of a lack of assets in tax deferred registration (contribution limits in 401k etc.) Alternatives and fixed income are ideal for annuities because of their inefficient structure.

Take Away

The key to becoming a good chef is knowing what foods pair well with each other. The key to a profitable restaurant is excellent inventory management and preparation for upcoming demands. The "pantry" of account registrations is no different than a restaurant. To stretch your dollar further is it critical to foresee the types of expenses, plan for required distributions and understand your tax bracket.

This paper is not intended to be construed as com-prehensive; other registrations and rules exist and you should always consult a tax professional prior to incurring a taxable event.

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Rule 72(t) allows penalty-free withdrawals from IRA accounts and other tax-advantaged retirement accounts like 401(k) and 403(b) plans.

A required minimum distribution (RMD) is the amount of money that must be withdrawn from a traditional, SEP, or SIMPLE IRA account by owners and qualified plan participants of retirement age.

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