

Thinking of Selling Your Home? Don't Be Surprised by Capital Gains Taxes

The Taxpayer Relief Act of 1997 provided homeowners who sell their principal residence an exclusion from capital gains taxes of \$250,000 for single filers and \$500,000 for joint filers. At that time, the average price of a new home was about \$145,000, so this exclusion seemed generous and allowed more Americans to move freely from one home to another.¹ Unfortunately, the exclusion was not indexed to inflation, and what seemed generous in 1997 can be restrictive in 2024.

Capital gains taxes apply to the profit from selling a home, so they may be of special concern — and potential surprise — for older homeowners who bought their homes many years ago and might yield well over \$500,000 in profits if they sell. In some areas of the country, a home bought for \$100,000 in the 1980s could sell for \$1 million or more today.² At a federal tax rate of 15% or 20% (depending on income) plus state taxes in some states, capital gains taxes can take a big bite out of profits when selling a home. Fortunately, there are some things you can do to help reduce the taxes.

Qualifying for exclusion

In order to qualify for the full exclusion, you or your spouse must own the home for at least two years during the five-year period prior to the home sale. You AND your spouse (if filing jointly) must live in the home for at least two years during the same period. The exclusion can only be claimed once every two years. There are a number of exceptions, including rules related to divorce, death, and military service. If you do not qualify for the full exclusion, you may qualify for a partial exclusion if the main reason for the home sale was a change in workplace location, a health issue, or an unforeseeable event.

Increasing basis for lower taxes

The capital gain (or loss) in selling a home is determined through a two-part calculation.

First, the selling price is reduced by direct selling costs, including certain fees and closing costs, real estate commissions, and certain costs that the seller pays for the buyer. (The amount of any mortgage pay-off is not relevant for determining capital gains.) This yields the *amount realized*, which is then reduced by the *adjusted basis*.

The basis of your home is the amount you paid for it, including certain costs related to the purchase, plus the costs of improvements that are still part of your home at the date of sale. In general, qualified improvements include new construction or remodeling, such as a room addition or major kitchen remodel, as well as repair-type work that is done as part of a larger project. For example, replacing a broken window would not increase your basis, but replacing the window as part of a project that includes replacing all windows in your house would be eligible. This basis is adjusted by adding certain payments, deductions, and credits such as tax deductions and insurance payments for casualty losses, tax credits for energy improvements, and depreciation for business use of the home. (See hypothetical example.)

Hypothetical Example

Pete and Joanne purchased their home for \$100,000 in 1985 and sold it for \$800,000 in 2024. This is how their capital gains might be calculated.

Capital gains	Basis
\$800,000 sales price	\$100,000 purchase price
- \$50,000 direct selling costs	+ \$8,000 purchase costs
\$750,000 amount realized	+ \$52,000 improvements
- \$150,000 adjusted basis	\$160,000 total basis
\$600,000 capital gain	- \$10,000 solar energy credit
- \$500,000 capital gains exclusion	\$150,000 adjusted basis
\$100,000 taxable gains	

At a 15% rate — which applies to most taxpayers — this would cost \$15,000 in federal capital gains taxes.

This hypothetical example of mathematical principles is for illustration purposes only. Actual results will vary.

Inheriting a home

Upon the death of a homeowner, the basis of the home is *stepped up* (increased) to the value at the time of death, which means that the heirs will only be liable for future gains. In community property states, this usually also applies to a surviving spouse. In other states, the basis for the surviving

spouse is typically increased by half the value at the time of death (i.e., the value of the deceased spouse's share).

Determining the capital gain on a home sale is complex, so be sure to consult your tax professional. For more information, see IRS Publication 523 *Selling Your Home*.

1. U.S. Census Bureau, retrieved from FRED, Federal Reserve Bank of St. Louis, 2024
2. CNN, January 29, 2024



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What's Your Real Return?

Investing can be daunting, whether you are experienced or a beginner. Even if you feel confident about your investing strategy, it can be easy to lose focus or make decisions based on emotion. Here are eight quotes from successful investors, economists, and other insightful thinkers that may help provide perspective and focus for your own investing strategy.

"The individual investor should act consistently as an investor and not as a speculator."¹

— Benjamin Graham, investor, author, and teacher known as the "father of value investing." A speculator takes large risks in the hopes of making large quick gains. An investor focuses on risk-appropriate strategies to pursue long-term goals

"Don't try to buy at the bottom and sell at the top. It can't be done except by liars."²

— Bernard Baruch, investor and presidential adviser. Trying to time the market may be tempting, but it rarely works, because no one really knows when the market has reached its top or bottom.

"If you aren't willing to own a stock for 10 years, don't even think about owning it for 10 minutes."³

— Warren Buffett, investor, businessman, and philanthropist. Buffett, a former student of Benjamin Graham, is perhaps the most famous proponent of patient "buy and hold" investing.

"Take measured risk."⁴

— Doris P. Meister, investment manager and business leader. All investing involves risk, but risk can be managed through careful research and proven strategies such as asset allocation and diversification.

"Regardless of what happens in the markets, stick to your investment program. Changing your strategy at the wrong time can be the single most devastating mistake you can make as an investor."⁵

— John Bogle, investor and mutual fund industry pioneer. A sound investment strategy should be designed to carry you through market ups and downs.

"Know what you own, and know why you own it."⁶

— Peter Lynch, investment manager, author, and philanthropist. Your portfolio should be assembled with an eye toward meeting your long-term financial goals, not by rushing to own the "flavor of the month."

"Investing should be more like watching paint dry or watching grass grow. If you want excitement, take \$800 and go to Las Vegas."⁷

— Paul Samuelson, 1970 Nobel laureate in economic sciences. Investors often make poor decisions when they are driven by adrenalin; patience is more likely to produce positive results in the long run.

"Compound interest is the eighth wonder of the world. He who understands it, earns it ... he who doesn't ... pays it."⁸

— Albert Einstein, 1921 Nobel laureate in physics. Even though this and similar quotes are often attributed to Einstein, it's uncertain whether he ever said them. Either way, one of the most powerful tools for investors is reinvesting interest, dividends, and capital gains.

1. 6. 7. Investopedia, September 15, 2023
2. 5. BrainyQuote, accessed March 28, 2024
3. 8. Goodreads, accessed March 28, 2024
4. U.S. News & World Report, March 11, 2024

There is no guarantee that any investing strategy will be successful. All investments are subject to market fluctuation, risk, and loss of principal. When sold, they may be worth more or less than their original cost. Investments seeking to achieve higher returns also involve a higher degree of risk. Asset allocation and diversification are methods used to help manage investment risk; they do not guarantee a profit or protect against investment loss.

Eight Great Investing Quotes



Bon Voyage!

With the COVID pandemic receding in most areas of the world, Americans are traveling again. U.S. citizens took more than 98 million international trips in 2023, just short of the pre-pandemic level of 99 million in 2019 and almost three times higher than the 33 million low in 2020.

Here are the regions they visited.

Source: National Travel and Tourism Office, 2024

International destinations for U.S. travelers, 2023



After the Loss of a Loved One, Watch Out for Scams

Scam artists often prey on those who are most vulnerable. Unfortunately, this includes individuals who have recently lost a loved one and are easily taken advantage of during their time of grief. Scammers will look for details from obituaries, funeral homes, hospitals, stolen death certificates, and social media websites to obtain personal information about a deceased individual and use it to commit fraud.

A common scam after the loss of a loved one, often referred to as "ghosting," is when an identity thief uses personal information obtained from an obituary to assume the identity of a deceased individual. That information is then used to access or open financial accounts, take out loans, and file fraudulent tax returns to collect refunds. Typically, a ghosting scam will occur shortly after someone's death — before it has even been

reported to banks, credit reporting agencies, or government organizations such as the Social Security Administration (SSA) or Internal Revenue Service (IRS).

Another scam involves scam artists using information from an obituary to pass themselves off as a friend or associate of the deceased — sometimes referred to as a "bereavement" or "imposter" scam. These individuals will falsely claim a personal or financial relationship with the deceased in order to scam money from grieving loved ones. Scam artists will also pose as government officials or debt collectors falsely seeking payment for a deceased individual's unpaid bill.



Source: Federal Trade Commission, 2024

If you recently experienced the loss of a loved one, consider the following tips to help reduce the risk of scams:

- **Report** the death to the SSA and IRS as soon as possible.
- **Notify banks** and other financial institutions that the account holder is deceased.
- **Contact your state's department** of motor vehicles and ask them to cancel the deceased's driver's license.
- **Ask the major credit reporting bureaus** (Equifax, Experian, and TransUnion) to put a "deceased alert" on the deceased person's credit reports and monitor them for unusual activity.
- **Avoid putting too much personal information** in an obituary, such as a birth date, place of birth, address, or mother's maiden name.
- **Be wary of individuals** who try to coerce or pressure you over alleged debts owed by the deceased.

Empty Nesters Own Outsized Share of Big Homes

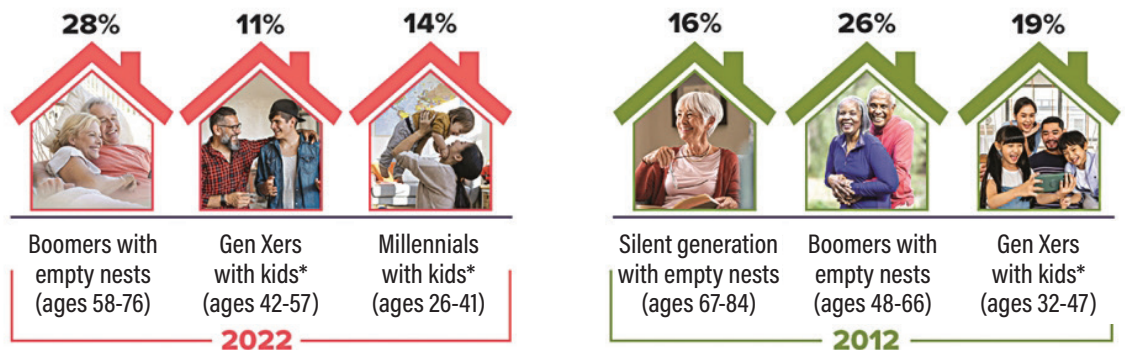
Empty-nest baby boomers owned twice as many large homes (with three bedrooms or more) as young families with kids in 2022. Careerwise, many boomers benefited financially from the 90s economic boom and/or bought their first

homes when it was much more affordable. In recent years, boomers have had little reason to downsize, as many own their homes outright or have mortgages with lower rates than they could get for a replacement home. Millennials' earnings

were negatively impacted by the Great Recession, and they've had to spend more of their incomes on housing. Ten years ago, the older generation owned a smaller share of large homes than families that were raising children.

Share of large U.S. homes owned by each generation (owner-occupied)

Source: Redfin, 2023



* Minor children under the age of 18

It's Complicated: Inheriting IRAs and Retirement Plans

The SECURE Act of 2019 dramatically changed the rules governing how IRA and retirement plan assets are distributed to beneficiaries. The new rules, which took effect for account owner deaths occurring in 2020 or later, are an alphabet soup of complicated requirements that could result in big tax bills for many beneficiaries.

RMDs and RBDs

IRA owners and, in most cases, retirement plan participants must start taking annual required minimum distributions (RMDs) from their non-Roth accounts by April 1 following the year in which they reach RMD age (see table). This is known as their required beginning date (RBD).

Likewise, beneficiaries must take RMDs from inherited accounts (including, in most cases, Roth accounts). The timing and amount of an individual beneficiary's RMDs depend on several factors, including the relationship of the beneficiary to the original account owner and whether the original owner had reached the RBD.

Three key points apply to both owners and beneficiaries: (1) individuals must pay income taxes on the taxable portion of any distribution, (2) the larger the RMD, the higher the potential tax burden, and (3) failing to take the required amount generally results in an additional excise tax.¹

Date of birth	RMD age
Before July 1, 1949	70½
July 1, 1949, through 1950	72
1951 to 1959	73
1960 or later	75

The age that determines an account owner's RBD depends on the account owner's date of birth.

Spouse as sole beneficiary

Spouses who are sole beneficiaries have the most options for managing inherited accounts. By default, a surviving spouse beneficiary is treated as what's known as an eligible designated beneficiary (EDB) with certain advantages (see next section, "EDBs and DBs"). And if the deceased spouse died before the RBD, a surviving spouse EDB who is the sole owner can wait until

the year the deceased would have reached RMD age to begin distributions.

Alternatively, a surviving spouse who is the sole owner can generally roll over the inherited account to their own account or elect to be treated as the account owner (rather than as an EDB). In these cases, the rules for account owners would apply. However, there is a potential drawback to this move: if the surviving spouse is younger than 59½, a 10% early distribution penalty may apply to subsequent withdrawals unless an exception applies.

EDBs and DBs

The SECURE Act separated other individual beneficiaries into two groups: EDBs and designated beneficiaries (DBs). EDBs are spouses and minor children of the deceased, those who are not more than 10 years younger than the deceased, and disabled and chronically ill

individuals. DBs are essentially everyone else, including adult children and grandchildren.

EDBs have certain advantages over DBs. If the account owner dies before the RBD, an EDB is able to spread distributions over their own life expectancy. If the account owner dies on or after the RBD, an EDB may spread distributions over either their own life expectancy or that of the original account owner, whichever is more beneficial.²

By contrast, DBs are required to liquidate inherited assets within 10 years, which could result in unanticipated and hefty tax bills. If the account owner dies before the RBD, the beneficiary can leave the account intact until year 10. If the owner dies on or after the RBD, a DB must generally take annual RMDs based on their own life expectancy in years one through nine, then liquidate the account in year 10.

Other considerations

Work-sponsored retirement plans are not required to offer all distribution options; for example, an EDB may be required to follow the 10-year rule. However, both EDBs and DBs may roll eligible retirement plan assets into an inherited IRA, which may offer more options for managing RMDs.

This is just a broad overview of the complicated new rules as they apply to individual beneficiaries. If an account has multiple designated beneficiaries, or if a beneficiary is an entity such as a trust, charity, or estate, other rules apply. Beneficiaries should seek the assistance of an estate-planning attorney before making any decisions.

1. The IRS has waived this tax as it applies to the DB 10-year rule through 2024.
2. An inherited account must be liquidated 10 years after an EDB dies or a minor child EDB reaches age 21.



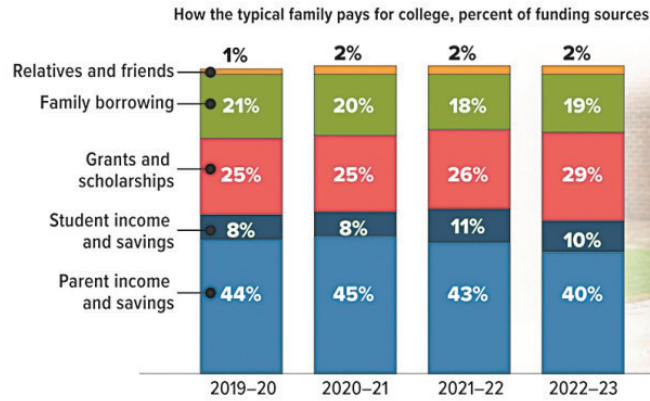
Financial discussions lead to important questions. We would be pleased to assist.

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How the Typical American Family Pays for College

The typical family uses a combination of income, savings, grant aid, and loans to pay for college. For the past several years, income and savings from parents and students have consistently covered about half of the total cost, with grant aid covering about one quarter of the total cost and loans covering most of the remainder.

Starting a college fund early and aggressively looking for grant aid from colleges can help families reduce the amount they may need to borrow. A net price calculator, available on every college website, can help families estimate how much grant aid a student might receive at a particular college.



Source: How America Pays for College 2023, Sallie Mae

Retroactive Social Security Benefits: A Chance to Turn Back Time

Did you know that if you postpone claiming Social Security past your full retirement age, you have the option of receiving a lump-sum payment for up to six months of benefits when you finally apply?

Receiving retroactive benefits in a lump sum might be helpful if you face a change in health or need cash in an emergency. However, you'll want to think through the consequences, because taking an initial lump sum will reduce your monthly Social Security retirement benefit for the

rest of your life.

For example, let's say your full retirement age is 67, and your full retirement benefit would be \$2,400. You decide to wait to apply for Social Security. By waiting past full retirement age, you earn delayed retirement credits that will increase your benefit by 8% per year, up to age 70. You apply for retirement benefits at age 67 and 6 months. Your benefit is now \$2,496, due to the delayed retirement credits you've earned, 4% higher than at age 67.

If you opt to take benefits retroactively in a lump sum, your official Social Security start date and the amount of your monthly benefit will be rolled back by six months, and you will lose six months of delayed retirement credits. Your lump-sum benefit will be based on your age 67 benefit, so

you will receive

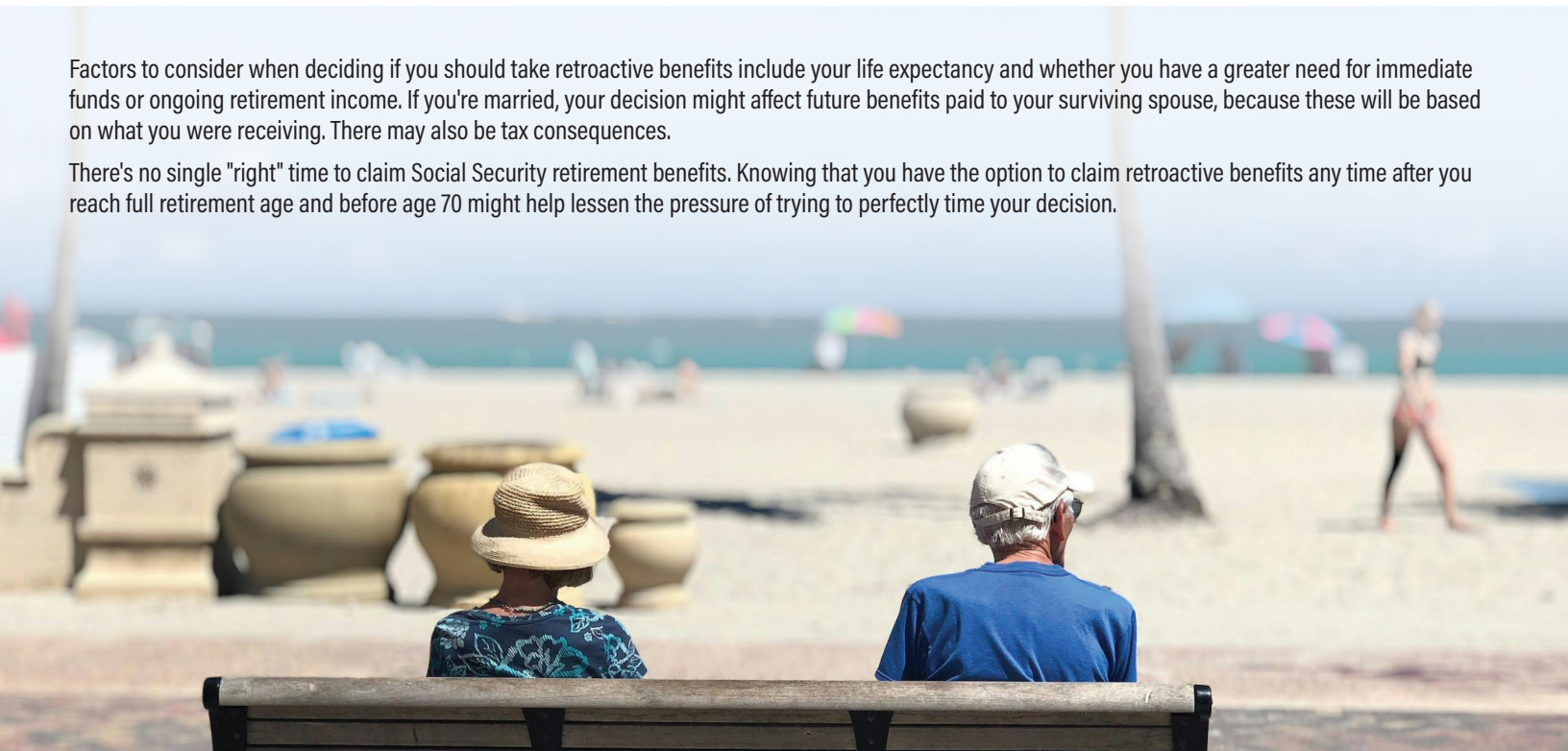
\$14,400 ($\$2,400 \times 6$) — a sizeable amount. The downside is that your ongoing monthly benefits will be permanently reduced.

In this example, because you received a lump-sum payment for six months of benefits, your ongoing monthly benefit will be 4% lower for the rest of your life.

Full retirement age is 66 to 67, depending on year of birth

Factors to consider when deciding if you should take retroactive benefits include your life expectancy and whether you have a greater need for immediate funds or ongoing retirement income. If you're married, your decision might affect future benefits paid to your surviving spouse, because these will be based on what you were receiving. There may also be tax consequences.

There's no single "right" time to claim Social Security retirement benefits. Knowing that you have the option to claim retroactive benefits any time after you reach full retirement age and before age 70 might help lessen the pressure of trying to perfectly time your decision.





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What's Your Real Return?

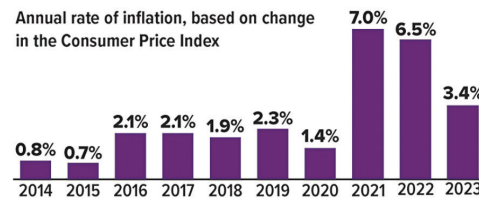
As an investor, you probably track the return on your investments. But it's likely that you look at the nominal return, which is the percentage increase or decrease in the value of an investment over a given period of time, usually expressed as an annual return. To estimate actual income or growth potential in order to target financial goals, such as a certain level of retirement income, it's important to consider the real return, which includes the effects of taxes and inflation.

Let's say you want to purchase a bank-issued certificate of deposit (CD), because you like the lower risk and fixed interest rate that a CD can offer. CD rates have risen substantially with the Federal Reserve's aggressive increases in the federal funds rate, so let's say you find a CD that offers 5% annual interest. That could be attractive. However, if you're taxed at the 22% federal income tax rate, 1.1% will be gobbled up by federal income tax on the interest.

That still leaves an interest rate of 3.9%, but you should consider the purchasing power of the interest. For example, inflation slowed to 3.4% in 2023 after hitting 40-year highs in 2021 and 2022 (see chart). But a 3.4% inflation rate would leave a real return of just 0.5%. If inflation slows further, the real return on this hypothetical CD would increase. However, if the Fed were

to lower the benchmark federal funds rate in response, rates on CDs and other fixed-income investments might decline, reducing the real return on future CD and fixed-income purchases.

Eroding Purchasing Power



Source: U.S. Bureau of Labor Statistics, 2024

This hypothetical example doesn't represent the performance of any specific investment, but it illustrates the importance of understanding what you're actually earning after taxes and inflation. In some cases, the lower risk offered by an investment may be appealing enough that you're willing to accept a low real return. However, pursuing long-term goals such as retirement generally requires having some investments with the potential for higher returns, even if they carry a higher degree of risk.

The FDIC insures CDs and bank savings accounts, which generally provide a fixed rate of return, up to \$250,000 per depositor, per insured institution. All investments are subject to risk, including the possible loss of principal. When sold, investments may be worth more or less than the original cost.

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