Casey Mullooly: Welcome back to the Mullooly Asset podcast. This is your host, Casey Mullooly, and we're back for episode 387. I'm joined by Tom and Brendan this week, and we get into a discussion about an article from Christine Benz at Morningstar. She wrote about her 2022 financial planning tips. She broke it out by month. But since we're already midway through January here we broke it out quarter by quarter. This week's episode is going to be covering quarter one and quarter two, so we get you through the first half of this year.

Casey Mullooly: We talk about reviewing how 2021 went from a saving and investing standpoint. We talk about getting ready to file those 2021 tax returns, all the documentation you need for that. We generally just talk about financial planning tips, financial planning best practices, things to consider to set yourself up for a successful 2022. It's good to review this stuff at the beginning of the year and get headed on the right path. Here we go. Here's episode 387 of the Mullooly Asset Podcast, we hope you enjoy.

Tom Mullooly: I want to say if you're paying half attention and you see that the market's down, today it's down a lot, down 500, you start to get preoccupied with, "Oh my God, what's the market doing?" It takes you away from what you really ought to be doing, which is this stuff.

Casey Mullooly: Yeah, it's interesting there are no bullet points that said, check what your-

Brendan: Check how the S&P is doing. What was your Sortino ratio versus the S&P 500 last year.

Casey Mullooly: Right. Yeah, while it is important and the first bullet point is to review your numbers. It's more about things that are actually within your control. Like how much did you save? Where did you save? If you retired how much did you withdraw from your portfolio? How much did you spend on average per month?

Casey Mullooly: I know that that's a big thing that we bake into our financial plans. Yes, look back at your investment portfolio and see what worked and what didn't work. But I think the year time horizon is a much healthier and a much less stressful way to look at investment returns than by looking at that stuff every single day.

Brendan: Yeah. I think that if you're looking at your portfolio and how it did, it's probably wiser to consider it within the context of rebalancing than it is to say, "Oh, this didn't work. Let's get rid of it." Because if you had a philosophy to begin with, let's say that, you had allocations to different areas of the market for a reason, and one of them lagged while the other led for a year, really all the result should be for you as the end user of the portfolio is to take some money out of what worked and add it back to the other thing that didn't for a year. Because odds are whether it's this calendar year or sometimes soon, those roles are going to reverse and you have targets in a portfolio for a reason.

Casey Mullooly: Right. You, you're jumping ahead of me here but that was good.

Brendan: I know but then you're talking about the numbers. I mean, if you are going to get into portfolio minutia, that's the degree to which you should do it, I think, or it's actually useful.

Casey Mullooly: Right. So you're saying if you have an asset allocation, what worked probably is going to be more of that allocation now just based on the performance and what didn't perform well is going to be less of that allocation. So just bring it back to the target of what you started with. Yeah, I think the first quarter is a good time to take stock of that and see where things stand.

Brendan: The other numbers you're talking about though, are like-

Casey Mullooly: Right.

Brendan: ... if you sent your contributions into your 401(k), probably easy because you did so in percentage terms, but if you hit your max, then it starts to throw things off. So like, what was your savings rate? You can think of that both in terms of maybe what you sent to your 401(k), but also if you're sending money elsewhere to a brokerage account or to a bank account to add to emergency funds things there more short term goals kind of savings, overall, what were you saving over the course of the year as a percentage of your gross income and how do you feel about that?

Tom: Question maybe off track, and I'm sorry. But question, if you are paying down debt through the year, and you're also trying to save, should you count that towards your savings goal? Reducing debt.

Brendan: While they're both good things, no.

Casey Mullooly: Yeah. I think they're different things but-

Brendan: I don't think so. I see where you're going. You could definitely make a case that it is because if you're paying down a debt, I mean, it's basically a guaranteed return on whatever the interest rate of that debt is, but it's not the same in the sense that it's not an asset that's growing for you, that you're accumulating. If anything, it's the other side of the balance sheet that you're making less, which all feeds through to your net worth. It's all important.

Tom: It's a liability that's shrinking, but it's not necessarily savings because you can't like dip back into a debt-

Brendan: Bingo.

Tom: ... again, but it does help future cash flow.

Casey Mullooly: Right. It is interesting because I think both are expenses. I know some people don't really think about savings as an expense, but I think you could argue that savings and paying down debt are probably the two most important expenses that you're going to have on a month to month basis.

Tom: If you have a good income in a certain year and you use a good chunk of that income to get rid of debt, it's a little deflating when you get to the end of the year or the beginning of next year, when you're mapping out your next year and you say, "Oh, for crying out loud, I made all this money, I've got nothing to show for it."

Tom: So sometimes looking at your net worth statement, your balance sheet from last year, and seeing the progress you made can be a lot more rewarding if you are in that debt paying down, debt reduction phase. So it's important because you can make a lot of money, pay down a lot of debt. You're doing something really good, but if you say, "Wow, I didn't save anything."

Brendan: There's no tangible thing to point to like make the account where it all is. Or if you were spending it and not doing debt paydown or savings, there's no boat to point to say, that's where all the money is.

Casey Mullooly: But it's an important feeling. I think like that is one of the things that keeps people going towards anything financial or otherwise is just feeling like you're making progress toward to your goals. So it is good to look back at your balance sheet, look back at your account statements see where you were in the start of 2021 and where you are now and take stock of that. If you're not where you want to be, figure out what adjustments you need to make, but if you are where you want to be, then yeah, you should feel good about that. Yeah,

Brendan: I think so, like talking about savings rate or paying down debt, I mean, often when we're talking to folks about their cashflow, we think it's probably more useful to focus on the savings rate. Meaning that if you're reviewing these numbers and you hit your savings percentage goal for the year, say you want to save 15% or 20% of your gross income or wherever the number is, if you did that and you're happy with it, then it doesn't necessarily matter where the rest of the money went, per se.

Brendan: However, if you want to take the traditional ... We call that reverse budgeting what I just described. If you don't want to do the reverse budgeting mentality, and you do want to do more of an audit let's say, one of the recommendations was to look at the bank statements for the year. A simple thing would just be to add up all the spending and divide by 12. But even if you're reviewing the monthly statements to see outliers, if you just list out the 12 totals and then to visit those months that were outliers specifically, if you don't want to come through all 12 of these statements to be like, "All right, what the heck happened this month?"

Brendan: Because maybe we did a good job of budgeting of the fixed and regular expenses. However, what was this? Try not to make excuses, because that's not what it's about. We all have one time expenses that crop up through the year and one time can be air quotes here because the thing is different each and every time. But I think the repeatability of these non budgetable expenses is not.

Brendan: So if you can just maybe start to feel out what those are looking like more so that you can just maybe even build in, if you're doing cashflow planning to say, "Hey, we need like a miscellaneous category and on average over the last year, two years," however long you have been doing this, you can say, "on average, there's been this much extra stuff. I can't tell you ahead of time what it's going to be, but it's going to be there." I think that can go a long way towards making a budget or cashflow plan, whatever you want to call it work better.

Casey Mullooly: Yeah. I know you've talked about that on podcast before where you're like, "Oh, but that month was that thing, and we don't do that every month. So that month doesn't count." It's, yeah, the one time emergencies or the one time expenses, your car breaking down, the hot water heater not working. Those things are going to happen every year, but you're right in the sense that you're not going to be able to predict what they are ahead of time.

Brendan: Those conversations have happened right here at this table.

Casey Mullooly: Yeah.

Brendan: So this is real life.

Casey Mullooly: Yeah.

Brendan: This really happens and you need to have that kind of miscellaneous account. That's important.

Casey Mullooly: We talk about having an emergency fund and having 3, 6, 12 months worth of expenses in that emergency fund. So I think in instances of one time expenses cropping up. If you dip into that emergency fund, then you have to replenish it at some point too. So if you have a miscellaneous fund and an emergency fund, is that what you're recommending there? Brendan I think just have both.

Brendan: Maybe this is just like a mentality thing for me, but if you're looking at these one time expenses and a lot of them are just repairs on things in the home, let's say. Home maintenance is not an emergency. So you should have an emergency fund and if you realize that you're spending a few thousand dollars a year, but in lump sum increments to do things around the house and you have the financial wherewithal to do it, you can set up an account where you're channeling the money in little increments every two weeks when you're getting paid to make it painless. So that when there is some sort of thing in the house that needs to be addressed, at least you have something to put towards it so it's not such a big one off expense.

Casey Mullooly: Yeah.

Brendan: But you're not going to know if you don't comb back through the statements and be like, "Oh yeah, that happened in March last year." I mean, these last two years especially, I feel like everything's been slow motion. Looking at the review doesn't feel the same as it maybe did in years prior. So it's easy to forget projects, things that you were doing around the house even this time last year.

Casey Mullooly: Yeah.

Brendan: Seems like a million years ago.

Casey Mullooly: Yeah. So an emergency fund is more about a true, true emergency. Maybe like you lose your job and don't have any income type situation you have those. You at least leave yourself a couple of months of runway there-

Brendan: Yeah.

Casey Mullooly: ... to figure things out. It's not necessarily like regular maintenance type items.

Brendan: Yeah. I mean, listen, at the end of the day, cash is cash and if you need money for something and it's in the special bucket for emergencies or home maintenance or whatever, yeah, it's all fungible you can use it for whatever you want. But just there are a lot of one time lump sum expenses that you can make into budgetable items if you want to. But to just fill up the budget with the actual recurring expenses and neglect these things that happen not frequently or not on a regular schedule, I think you're setting yourself up for a bad time when it comes to cashflow and budgeting if you're just ignoring them.

Brendan: So at least try to figure out what they've looked like over the last year if you're reviewing this stuff and maybe make some adjustments going forward as a result.

Casey Mullooly: Yeah. So some of the other suggestions for quarter one financial planning topics to consider is to revisit your retirement plan contributions because the contributions are bumping up in 2022. The contribution limit for 401(k)s is now going to be $20,500. For those over age 50 is going to be $27,000.

Brendan: I know that if you work for a big company, they're probably going to send you a reminder in December for payroll purposes that, "Hey, if you want to max out, you've got to do X amount of dollars out of each paycheck." But we're a small business, I would usually sit down on January 16th in previous years and say, "Oh man, I didn't change that." Now I have to try and figure out how to cram all of that into 23 paychecks instead of 24 paychecks. Is things like that.

Casey Mullooly: Yeah.

Brendan: You really want to be on top of that. It would be best if you did that before the end of the year and not wait until the beginning. Don't wait too long.

Casey Mullooly: Yeah. It's important to stay on top of this stuff. The big one at the end of the first quarter is to ... You can start doing this now if, or at least in the next couple of weeks. Is to start gathering your tax information, your tax documentation, check in with your tax professional to see what they need at the very least make sure you have any 1099s you might have, your W2 for the year and gather your receipts for any possible deductions that you might have. The standard deduction for 2021 tax year is $12,550. If you're married, it's going to be $25,100.

Casey Mullooly: I just wanted to pause and talk about examining your W2s and how much inform you can glean from those. I know that that's one of the things that we talk about when we're gathering documentation for new clients that we're onboarding. I think that some people just get their paychecks and then they know what the direct deposit is, but they don't actually look at the checks. They don't open the checks themselves. They might just file them in a filing cabinet or stick them in a folder. There's a lot of information, especially tax withholding information that can be found on there. So what should people be looking for on their W2s?

Brendan: First thing that comes to mind, if you're just let looking at the paystub versus what you get on W2s, if you're a high earner and you make more than the threshold for what social security collects. That can be a discrepancy based on, if you're looking at your paycheck in October, it may not look the same as your paycheck in January and the W2's going to tell the actual tell. Meaning they'll show you when you hit the cap for social security earnings that no longer is deducted from your pay automatically. So you get a raise until the end of the year.

Brendan: Same would go for your 401(k), if you hit the maximum this year coming up as Casey mentioned, 20,500. If you hit that maximum at any point throughout the year, instead of hitting it on the button with your last contribution, you're going to have more on your paycheck then. So the paycheck is great and it's going to tell you breakdown of what's happening for that snapshot and time, but it might not speak to the broader picture if you're trying to understand over the course of the calendar year, what the heck happened. So W2 can be useful to review from that standpoint.

Tom: I'll also add that. I think a lot of people in past years they would fill out a W4 form and they would calculate how many exemptions they were going to take. I just think that's such a convoluted way of doing things. I think a good practice for folks would be to look at your paycheck, see how much is taken now for federal tax and divide that number back into the gross amount of your check and see how much, like what percent of your paycheck is going off the top for federal taxes. I think you'd be surprised.

Tom: Then keep that number in the back of your mind when you get your tax return back from your tax preparer and see how much tax actually was paid.

Brendan: I think a lot of people will probably be surprised in a positive way, if what they're calculating there is their effective rate. A lot of people are more concerned with their marginal tax bracket. Meaning where in the bracket system do I fall? Which isn't necessarily-

Casey Mullooly: The top number. Yeah.

Brendan: Yeah, exactly. So I think that that can definitely be a helpful exercise to do. I guess whenever I'm looking in at W2 form, I guess the wage number that's probably simplest for people to use, depending on all the other different pre-tax contributions they're doing is there's a line for your Medicare wages, which would be the correct one to use, because that is your gross income prior to ... If you're looking at the W2, they spit out for your federal return, it's not going to include like your 401(k) contributions, contributions for health insurance. If you're doing an HSA, things like that.

Brendan: Even the New Jersey and the federal one will disagree on some items and so that Medicare line should be the same on all of them and that should be the top and number I guess to use in that recommended.

100%, that's that is the number to use. Use the Medicare number all the time.

Casey Mullooly: So we've talked about marginal versus effective tax rate before. So we'll link that up in the show notes if you need a refresher on that. Moving into quarter two here. April 18th is tax day for 2020-2021 taxes. But something that we've ran into in the last couple weeks is you can still make 2021 contributions to IRAs and HSAs up to tax day in which will be April 18th. So you can make 2021 contributions to IRAs and HSAs up to that day.

Casey Mullooly: Also, if you need to file an extension, that is an important day, you have to have that request filed by April 18th. A lot to consider, and a lot of moving parts in the first quarter, financially speaking, as we move further out into April, May, June things start to slow down once you get your tax returns back, you can see how that went.

Casey Mullooly: One of the suggestions for the second quarter was to organize all of your statements and documentations. You had to gather a lot of information for tax time. If you are like me, you might have your medical bills from the 2014, '15 lying around in that filing cabinet. So once tax time has passed, it is a good opportunity to declutter yourself and only keep the last couple years of information that you need at hand. So you're just clean and organized and you set yourself up to move forward for the rest of the year.

Tom: I think there's always the urge at the beginning of every year, "Say, this is the year I'm going to do it right. I'm going to be totally organized and I'm going to fill everything away and I'm going to have folders set up." I can show you empty folders from 2004, 2011, 1998. So I've tried this many times in January, "This is the year that I'm going to do it." Christine Benz in this article raised a really good point. Don't do that. You should really think about doing that in April after your taxes are filed or even better in May. You've already got a couple of months now of documents, of statements, of things. You've already made a quarterly estimated payment perhaps. So this is a really good time to be doing this. April, May, June in the second quarter.

Brendan: Also probably the best time to rectify any mistakes, regardless of whether it was a withholding discrepancy or whatever caused it. If there were issues with your tax return and you owed money, which nobody is ever happy with. Once you had that information, you could begin to rectify that for the following year if there's going to be the same issue again. I mean, obviously if it was a one time thing, then it's a one time thing, but try to wrap your head around what caused you to owe money and to what extent and whether you're comfortable with that or not.

Brendan: You can make changes in the second quarter that have plenty of time to filter through to the bottom line before you years end. It's tick clock though. So the longer you wait, the shorter runway, you have to implement change. If you're a regular old W2 employee, then each pay period that passes is I think, as Tom alluded to one opportunity out the door to make a change that needs to happen more incremental.

Casey Mullooly: Yeah. That's a good point. I think on the other end, if you're getting a refund, I know we talked about the emergency fund before, but if you get a refund I think-

Tom: This Cancun money, right?

Casey Mullooly: Come on, blowing up my spot. I was going to say, you could pad your emergency fund, because if you're not doing it from cashflow, then where's it going to come from? Unless you win your fantasy football league, then you're not going to get a couple hundred bucks or you're not going to get a lump sum payment like a tax refund.

Brendan: You talking your book there Casey?

Casey Mullooly: I did win my fantasy football league this year. So I just wanted to get that in there.

Tom: You going to get 1099 for that?

Casey Mullooly: No. So think about it, maybe do something fun with it partially, or save some of it as well.

Brendan: If it's enough to split up, I'm telling you right now that you got to figure something out with your withholdings for next year. I understand that for some people, if it's one or the other, you'd rather be over withheld and get a refund than the reverse. But if you're talking like a few thousand bucks and you can figure out how to divvy it up, then you got to get better with the withholding because you're just given the government your money for no reason.

Tom: I was just going to say, I can be the old guy saying, get off my lawn. Like you just gave a free loan to uncle Sam.

Brendan: I was trying to refrain from saying that cause it's the grumpy thing to say, and everybody knows it because they've been told it a million times, but it's true. So if it's enough for it to be a windfall sort of a thing for you, figure it out. If you need to get it out of sight, out of mind, then you can automate something to send it where it should be, whether it's your emergency fund, an investment account, or it could be again like I'm a big proponent of the buckets. If we talked about the home maintenance one before you can have another one that's for like Cancun or your fun stuff, or the Atlantic City Money or whatever the case is.

Casey Mullooly: Brendan buckets.

Brendan: Yeah. That's fine. I'll accept that.

Casey Mullooly: Yeah.

Brendan: Yeah. So you can automate it and channel it to be where it needs to rather than letting payroll run that operation for you and then having it sit with the IRS for 10 months until you get it back.

Casey Mullooly: Yeah. I know we talked about organization there. These days everyone has about a dozen plus online accounts that includes financial institutions like banks or retirement accounts. So make sure you have that information on hand if you haven't logged in a year or so. It might be a good time to log in there check things and make sure you can at least access that. Yeah, Q2 is all about organization kind of making adjustments, you do still have six months plus at least to make adjustments for the rest of the year. So quarter two, April, May, June is a good time to do that.

Casey Mullooly: That's going to do it for episode 387 of the Mullooly Asset Podcast. We know that there is a lot of stuff in there, but hey, the beginning of the year is a busy time financially speaking. So we'll be back with quarter three and quarter four. So the second half of 2022, what to expect there, some things to look out for and to plan for in the later half of this year. That'll be episode 388 and we'll see you then thanks as always for listening.