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Year End Tax Planning Issues

Year-end is rapidly approaching as are the holidays. So before you become distracted with the seasonal celebrations, it may be in your best interest to consider year-end tax moves that can benefit you for both 2022 and 2023.

Having the Congressional members preoccupied with the November mid-term elections has sidelined, at least temporarily, any legislation to extend tax provisions that expired after 2021 and won't be available for 2022, including: the mortgage insurance premium deduction; increased AGI limit for charitable deductions for those itemizing deductions; the above-the-line charitable deduction for non-itemizers; tax credits for COVID sick and family leave pay for self-employed individuals; the employee retention credit (for employers); the temporary increase in the child tax credit, which reverts to $2,000, the old phase-out levels and the lower age to be a qualifying child; the child and dependent care credit that returns to pre-COVID amounts; and the enhanced earned income tax credit for taxpayers without a qualifying child.

Looking forward to 2023, the temporary allowance of a 100% deduction for business meals at a restaurant ends after 2022 and reverts to 50%; bonus depreciation on business property purchases begins to phase out and will only be 80% in 2023.
Here are last-minute tax issues you might consider:

Roth IRA Conversions – If your income is unusually low this year, you may wish to consider converting your traditional IRA into a Roth IRA. The lower income results in a lower tax rate, which provides you an opportunity to convert to a Roth IRA at a lower tax amount. Also, the decline in the stock market may provide an opportunity for some to convert where the stocks in their retirement account have had a significant decline in value.

Recognizing Capital Losses – With our current down market you should review your stock portfolio and consider selling losers to offset capital gains that would otherwise be subject to the 15% or 20% long-term capital gains tax rate. Capital losses can also offset up to$3,000 ($1,500 in the case of a married taxpayer filing a separate return) of ordinary income if capital losses exceed capital gains by at least that amount. Recognizing capital losses to offset capital gains can also reduce the amount of income subject to the net investment income surtax. Be aware of the wash sale rules that don't allow you to deduct a loss if you repurchase those loser stocks within 30 days before or after the sale date.

Take Advantage of the Zero Capital Gains Rate - There is a zero long-term capital gains rate for those taxpayers whose taxable income is below the 15% capital gains tax threshold. This may allow you to sell some appreciated securities that you have owned for more than a year and pay no or very little tax on the gain. The 2022 15% capital gains tax bracket starts at taxable income of $83,351 for married joint filers, $55,801 for those filing as head of household, and $41,676 for all other filers.

Avoid Required Minimum Distribution (RMD) Penalties - Once U.S. taxpayers reach the age of 72, they are required to take what is known as a "required minimum distribution" from their qualified retirement plan or IRA every year. If this is the first year that this rule applies to you and you haven't withdrawn the required amount yet, there's no need to panic – you don't have to do so until sometime during the first quarter of next year. Of course, if you wait until 2023 to take your 2022 distribution, you're going to end up having to take two distributions in one year – one for 2022 and one for 2023.

For those who have fallen into this category before 2022, you only have until December 31st to take the required distribution if you want to avoid penalties.

Charitable Deductions - Many people who itemize take advantage of the ability to take a deduction for their donations to their favorite charities or house of worship. Did you know that you can choose to pay all or part of your 2023 planned giving in 2022 in order to increase the amount you deduct in 2022? Though this may not be appealing to those who itemize every year, if you alternate between taking the standard deduction one year and itemizing the next, this can give you a big boost.

Charitable contributions are deductible in the year in which you make them. If you charge a donation to a credit card before the end of the year, it will count for 2022. This is true even if you don't pay the credit card bill until 2023. In addition, a check will count for 2022 if you mail it in 2022. For last minute mailings it may be appropriate to obtain a proof of mailing from the USPS.

Qualified Charitable Distributions - Those who are age 70½ or older are allowed to transfer funds (up to $100,000 annually) from their IRA to qualified charities without the transferred funds being taxable, provided the transfer is made directly by the IRA trustee to a qualified charitable organization other than a private foundation or a donor-advised fund. If you are required to make an IRA distribution (i.e., you are age 72 or older), you may have the distribution sent directly to a qualified charity, and this amount will count toward your RMD for the year.

Although you won't get a tax deduction for the transferred amount, this qualified charitable distribution (QCD) will be excluded from your income, with the result that you may get the additional benefit of cutting the amount of your Social Security benefits that are taxed. Also, since your adjusted gross income will be lower, tax credits and certain deductions that you claim with phase-outs or limitations based on AGI could also be favorably impacted.
If you plan to make a QCD, be sure to let your IRA trustee or custodian know well in advance of December 31 so that they have time to complete the transfer to the charity. If you have contributed to your traditional IRA since turning 70½, the amount of the QCD that isn't taxable may be limited, so it is a good idea to check with this office to see how your tax would be impacted.

Make Business Purchases - You can reduce taxable income if you make last-minute business purchases such as for office equipment, tools, machinery, and vehicles and write them off using the 100% bonus depreciation or Sec. 179 expensing, provided you place the item(s) into business service by the end of the year. However, you must consider the impact that expensing the items will have on your taxable income and the Sec. 199A 20% pass-through deduction. It may be appropriate to contact this office in advance of any last-minute business acquisition.

You might also make sure you are taking advantage of the de minimis safe harbor rule that allows small businesses to expense rather than capitalize the purchase of tangible property up to $2,500.

Employer Health Flexible Spending Accounts – If you contributed too little to cover expenses this year, you may wish to increase the amount you set aside for next year. As a reminder, feminine menstrual products and COVID personal protective equipment now qualify. The maximum contribution for 2022 is $2,850. The amount that may be carried to 2023 is $570 and must be used in the first 2½ months of 2023.

Maximize Health Savings Account Contributions – If you become eligible to make health savings account (HSA) contributions late this year, you can make a full year's worth of deductible HSA contributions even if you were not eligible to make HSA contributions for the entire year. This opportunity applies even if you first become eligible in December. In brief, if you qualify for an HSA, contributions to the account are deductible (within IRS-prescribed limits), earnings on the account are tax-deferred, and distributions are tax-free if made for qualifying medical expenses.

Pay Outstanding Medical or Dental Bills - Taxpayers who itemize their deductions are able to deduct qualified medical and dental expenses that exceed 7.5% of their adjusted gross income. If you have reached that threshold or are close, then it may make sense for you to pay off any of those types of bills that are still outstanding rather than paying them over time. If you are near or above the limit, it may also make sense to look at what your medical and dental expenses will likely be for the next year and move those that you can into 2022 to increase the deduction. These expenses could include dental work or eyeglasses. An additional important issue: if you are thinking of doing this by paying using a credit card and you're not going to pay the balance immediately, make sure that you're not paying more in interest than you're saving with the increased tax deduction.

Maximize Education Tax Credits – If you qualify for either the American Opportunity or Lifetime Learning education credits, check to see how much you will have paid in qualified tuition and related expenses in 2022. If it is not the maximum allowed for computing the credits, you can prepay 2023 tuition if it is for an academic period beginning in the first three months of 2023. That will allow you to increase the credit for 2022. This is especially effective for students just starting college who only have tuition expense for part of the year.

Remember the Annual Gift Tax Exemption - Though gifts to individuals are not tax deductible, each year, you are allowed to make gifts to individuals up to an annual maximum amount without incurring any gift tax or gift tax return filing requirement. For tax year 2022, you are able to give $16,000 (up from $15,000 in 2021) each to as many people as you want without having to pay a gift tax. If this is something that you want to do, make sure that you do so by the end of the year, as you are not able to carry the $16,000, or any unused part of it, over into 2023. Such gifts need not be in cash, and the recipient need not be a relative. If you are married, you and your spouse can each give the same person up to $16,000 (for a total of $32,000) and still avoid having to file a gift tax return or pay any gift tax.

Avoid Underpayment Penalties - If you think there's a chance that the income taxes you've paid to date for 2022 are insufficient, it's a good idea to increase your withholding in the time that's left to make up for it. Underpaying taxes makes you vulnerable to an underpayment penalty that is assessed quarterly. The good news is that even if you have underpaid for any or all of the first three quarters of the year and will owe taxes when you file your 2022 return, you can make up for it by boosting your year-end withholding, since federal withholding is deemed paid ratably throughout the year. Plus, increased withholding and possible payment of estimated taxes can also reduce the fourth quarter underpayment penalty.

Divorced or Separated During the Year – A divorce or separation can have a significant impact on a couple's tax filings. Filing joint or separate returns, who claims the children, the tax rules related to whether to take the standard deduction or itemize, how income and tax prepayments are allocated, and more are issues to be considered. Best to figure that all out in advance.

Every taxpayer's situation is unique, and the suggestions offered here may not apply to you. The best way to ensure that you are putting yourself into a tax-advantaged position is to seek advice from an experienced, qualified tax professional. Please contact this office if you need assistance.

Managing Gains and Losses in a Turbulent Year

It's been a rough ear for the stock market. So much so that you should probably carefully review your portfolio and other capital transactions to minimize gain or maximize losses for the year. Remember, capital gains and losses are not just limited to stock transactions. For example, stock losses can offset the gain from the sale of a rental. So you may want to consider other capital transactions you've already made this year or could make before the end of the year that would result in a gain that can be offset with stock losses. There can be any number of scenarios that might benefit from year-end planning.

Any transaction you plan must be completed by the end of the year, which is right at the conclusion of the Holidays. Thus, it is probably appropriate to have your planning strategies in place well in advance of the Holidays.

But first here's a review of the various tax rules and strategies that apply during this severely down stock market.

Annual Capital Losses Are Limited – When planning losses from selling stock, if you have losses remaining after netting losses against capital gains, you can only claim a maximum of $3,000 ($1,500 if filing as married separate) to shelter 2022 ordinary income from salaries, bonuses, self-employment income, interest income, royalties, and other sources. Any excess after the $3,000 ($1,500) is carried over indefinitely until used up to offset capital gains in future years.

Be Aware of the Wash Sale Rules – Some individuals may want to take a loss on a specific stock that's under water while still maintaining a position in the stock by selling the stock and immediately repurchasing it. Unfortunately, that strategy will not work because of the "wash sale" rules. A wash sale is a sale or other disposition of stock or securities, **resulting in a loss,** in which the seller, within a **61-day period (which begins 30 days before and ends 30 days after the date of the sale or disposition),** replaces the stock or securities by acquiring (by way of purchase or exchange on which the full gain or loss is recognized for tax purposes), or entering a contract or option to acquire, substantially identical stock or securities. The tax law says that a loss on a stock sale that meets this definition is not deductible.

The amount of any disallowed loss will be added to the basis of the repurchased securities. The rule was developed to prevent investors from creating a deductible loss without any market risk.

Off-Set Short-Term Gains with Long-Term Capital Losses - Short-term capital gains do not receive benefits of the special tax rates afforded long-term capital gains. Long-term capital losses, if used to offset long-term capital gains, reduce a gain that would be taxed at no more than 20%. The problem:

- ST capital gains are taxed at regular rates.
- LT capital losses if used to offset LTCG reduce 10% or 15% income.

Therefore, taxpayers achieve a better overall tax benefit if they can arrange their transactions to offset short-term capital gains with long-term capital losses. Although this cannot always be achieved considering investment strategies, when implemented, it will offset income that would otherwise be taxed at ordinary rates.

Planning for Zero Tax on Long-Term Capital Gains - Lower-income taxpayers and those whose income is abnormally low for the year can enjoy a long-term capital gain tax rate of zero, which provides an interesting strategy for these individuals.
Even if the taxpayer wishes to hold on to a stock because it is performing well, they can sell it and immediately buy it back, allowing them to include the current accumulated gain in the sale-year's return with no tax while also reducing the amount of taxable gain in the future. Since the sale results in a gain, the wash sale rule doesn't apply.
To determine if you can take advantage of this tax-saving opportunity, you must determine if your taxable income will be below the point where the 15% capital gains tax rate begins – see table below.

Example: Suppose a married couple is filing jointly and has projected taxable income for 2022 of $50,000. From the table below we find that the 15% capital gains tax bracket threshold for married joint filers is $83,351. That means they could add $33,350 ($83,350-$50,000) of long-term capital gains to their income and pay zero tax on the capital gains.

Of course, this strategy must be worked out based upon your projected taxable income for the year, which could end up actually being more or less than the estimated amount.
In addition, if you have any loser stocks in your portfolio, you can sell them for a loss, and thereby allow additional long-term capital gains to take advantage of the zero-tax rate.

There are some situations where the increase in adjusted gross income because of the added long-term capital gains could have unanticipated adverse effects that could reduce the overall benefit of this strategy for you. They include reducing any ACA premium tax credit you'd have, and if you are a senior, causing an increase in the Medicare premium withheld from your Social Security benefits.

Tax Rates - Capital gains vary depending on how long an investor had owned the asset before selling it. Long-term capital gains come from assets held for over a year. Short-term capital gains come from assets held for one year or less.

	2022 LONG-TERM CAPITAL GAINS TAX RATES			
Rate	**Single**	**Head of Household**	**Married Filing Jointly**	**Married Filing Separately**
0%	$0 – $41,675	$0 - $55,800	$0 – $83,350	$0 – $41,675
15%	$41,676 – $459,750	55,801 - 488,500	$83,351 – $517,200	$41,676 – $258,600
20%	$459,751+	488,501+	$517,201+	$258,601+

	2022 SHORT-TERM TAX RATES			
Rate	**Single**	**Head of Household**	**Married Filing Jointly**	**Married Filing Separately**
10%	$0 – $10,275	$14,650	$0 – $20,550	$0 – $10,275
12%	$10,276 – $41,775	$14,651 - $55,900	$20,551 – $83,550	$10,276 – $41,775
22%	$41,776 – $89,075	$55,901 - $89,050	$83,551 – $178,150	$41,776 – $89,075
24%	$89,076 – $170,050	$89,051 - $170,050	$178,151 – $340,100	$89,076 – $170,050
32%	$170,051 - $215,950	$170,051 - $215,950	$340,101 – $431,900	$170,051 – $215,950
35%	$215,951– $539,900	$215,951 - $539,900	$431,901 – $647,850	$215,951– $323,925
37%	$539,901+	$539,901+	$647,851+	$323,926+

Thank you for selecting our firm for your tax and accounting needs. We appreciate the confidence you have shown in us, and we remain ready to assist you at any time.

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