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Dear Client,

With year-end approaching, it is time to start thinking about moves that may help lower your tax bill for this year and next. Planning needs to take into account recent changes made by the Inflation Reduction Act of 2022 and potential year-end tax changes.

Whether or not tax increases become effective next year, the standard year-end approach of deferring income and accelerating deductions to minimize taxes will continue to produce the best results for all but the highest income taxpayers, as will the bunching of deductible expenses into this year or next to avoid restrictions and maximize deductions.

We have compiled a list of actions based on current tax rules that may help you save tax dollars if you act before year-end. Not all of them will apply to you, but you (or a family member) may benefit from many of them. We can narrow down specific actions when we meet to tailor a particular plan for you. In the meantime, please review the following list and contact us at your earliest convenience so that we can advise you on which tax-saving moves might be beneficial:

- The 3.8% surtax on certain unearned income. The surtax is 3.8% of the lesser of: (1) net investment income (NII), or (2) the excess of MAGI over a threshold amount ($250,000 for joint filers or surviving spouses, $125,000 for a married individual filing a separate return, and $200,000 in any other case).
- The 0.9% additional Medicare tax also may require higher-income earners to take year-end action. It applies to individuals whose employment wages and self-employment income total more than an amount equal to the NIIT thresholds, above. Employers must withhold the additional Medicare tax from wages in excess of $200,000 regardless of filing status or other income. Self-employed persons must take it into account in figuring estimated tax.
- Long-term capital gain from sales of assets held for over one year is taxed at 0%, 15% or 20%, depending on the taxpayer's taxable income. If you hold long-term appreciated-in-value assets, consider selling enough of them to generate long-term capital gains that can be sheltered by the 0% rate. The 0% rate generally applies to the excess of long-term capital gain over any short-term capital loss to the extent that, when added to regular taxable income, it is not more than the maximum zero rate amount of $89,250 for a married couple for 2023, and $44,625 for single filers.

- Postpone income until 2024 and accelerate deductions into 2023 if doing so will enable you to claim larger deductions, credits, and other tax breaks for 2023 that are phased out over varying levels of adjusted gross income (AGI). These include deductible IRA contributions, child tax credits, higher education tax credits, and deductions for student loan interest. Postponing income also is desirable for taxpayers who anticipate being in a lower tax bracket next year due to changed financial circumstances.
- If you believe a Roth IRA is better for you than a traditional IRA, consider converting traditional-IRA money invested in any beaten-down stocks (or mutual funds) into a Roth IRA in 2023 if eligible to do so. Keep in mind that the conversion will increase your income for 2023, possibly reducing tax breaks subject to phaseout at higher AGI levels.
- Many taxpayers won't want to itemize because of the high standard deduction amounts that apply for 2023 ($27,700 for joint filers, $13,850 for singles and for marrieds filing separately, $20,800 for heads of household), and because many itemized deductions have been reduced or abolished. Like last year, no more than $10,000 of state and local taxes may be deducted; miscellaneous itemized deductions (e.g., tax preparation fees and unreimbursed employee expenses) are not deductible; and personal casualty and theft losses are deductible only if they're attributable to a federally declared disaster and only to the extent the $100-per-casualty and 10%-of-AGI limits are met. You can still itemize medical expenses but only to the extent they exceed 7.5% of your adjusted gross income, state and local taxes up to $10,000, your charitable contributions, plus interest deductions on a restricted amount of qualifying residence debt, but payments of those items won't save taxes if they don't cumulatively exceed the standard deduction for your filing status.
- Some taxpayers may be able to work around these deduction restrictions by applying a bunching strategy to pull or push discretionary medical expenses and charitable contributions into the year where they will do some tax good. For example, a taxpayer who will be able to itemize deductions this year but not next will benefit by making two years' worth of charitable contributions this year, instead of spreading out donations over 2023 and 2024. For 2023-2025, the deduction for charitable contributions of individuals is limited to 60% of the contribution base (generally, AGI).
- If you expect to owe state and local income taxes when you file your return next year and you will be itemizing in 2023, consider asking your employer to increase withholding of state and local taxes (or pay estimated tax payments of state and local taxes) before year-end to pull the deduction of those taxes into 2023. But remember that state and local tax deductions are limited to $10,000 per year, so this strategy is not good to the extent it causes your 2023 state and local tax payments to exceed $10,000.

- If you were 73 or older in 2023 you must take a required minimum distribution (RMD) from any IRA or 401(k) plan (or other employer-sponsored retirement plan) of which you are a beneficiary. Those who turn 73 this year have until April 1 of 2024 to take their first RMD but may want to take it by the end of 2023 to avoid having to double up on RMDs next year.
- If you are age 70½ or older by the end of 2023, have traditional IRAs, and especially if you are unable to itemize your deductions, consider making 2023 charitable donations via qualified charitable distributions from your IRAs. These distributions are made directly to charities from your IRAs, and the amount of the contribution is neither included in your gross income nor deductible on Schedule A, Form 1040. However, you are still entitled to claim the entire standard deduction.
- Take an eligible rollover distribution from a qualified retirement plan before the end of 2023 if you are facing a penalty for underpayment of estimated tax and having your employer increase your withholding is unavailable or won't sufficiently address the problem. Income tax will be withheld from the distribution and will be applied toward the taxes owed for 2023. You can then timely roll over the gross amount of the distribution, i.e., the net amount you received plus the amount of withheld tax, to a traditional IRA. No part of the distribution will be includible in income for 2023, but the withheld tax will be applied pro rata over the full 2023 tax year to reduce previous underpayments of estimated tax.
- Consider increasing the amount you set aside for next year in your employer's FSA if you set aside too little for this year and anticipate similar medical costs next year.
- If you become eligible by December of 2023 to make health savings account (HSA) contributions, you can make a full year's worth of deductible HSA contributions for 2023.
- Make gifts sheltered by the annual gift tax exclusion before the end of the year if doing so may save gift and estate taxes. The exclusion applies to gifts of up to $17,000 made in 2023 to each of an unlimited number of individuals. You can't carry over unused exclusions from one year to the next. Such transfers may save family income taxes where income-earning property is given to family members in lower income tax brackets who are not subject to the kiddie tax.

We hope these ideas can help you with your tax planning. If you'd like to make an appointment to review any of these items, please don't hesitate to contact us!

Sincerely,

Seby & Associates, Ltd.

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