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CPAs & WEALTH ADVISORS

Year-End Tax Planning Strategies for Individuals & Businesses

Year-end is approaching, so is time to contemplate ways to help reduce your 2021 tax bill. Tax year 2021 has turned out to be a year with plenty of tax law changes. COVID-related disaster relief signed into law in December 2020 made several favorable changes to 2021 tax rules. After that, in March 2021, the American Rescue Plan Act enacted another set of major tax law changes.

Besides the changes we know about impacting 2021, there is a strong likelihood we may end the year 2021 with some other important tax law changes. President Biden and Congressional Democrats have proposed raising the ordinary income and capital gains tax rates on individuals, most likely to take effect in 2022. A corporate tax rate hike has also been proposed for tax years beginning after 2021. Currently, Congressional Democrats are negotiating to come up with a bill based on the President's proposals.

Despite the uncertainty regarding President Biden's proposals, there are still many items you might consider doing before year-end to minimize your 2021 tax bill. We will point out some strategies and things to consider in light of potentially higher tax rates in 2022. Uncertainty makes tax planning challenging, but putting it off until any pending proposals become final may provide you with little time to make any moves before year end.

Using our tax strategies, you can effectively:
• Reduce current year tax
• Defer current year tax
• Reduce future year's tax
• Maximize savings from allowable deductions
• Maximize tax credits
• Minimize Capital Gains
• Minimize tax on net investment income
• Avoid penalties for underpayment of estimated taxes

Year-end Planning Moves for Individuals

Be Prepared for Possible Higher Income Tax Rates. If you expect to be in a higher tax bracket in 2022 than in 2021, **the standard idea of deferring income and accelerating deductions is reversed.** In its place, you would want to accelerate income into 2021 (where it will be taxed at the current lower rate) and defer deductions until 2022, when they will yield a bigger tax benefit. We can help you determine if accelerating income into 2021 is advantageous in your situation. We are monitoring the proposed legislation, which is changing by the minute, out of Washington .

Group Itemized Deductions to Maximize Their Tax Value. For 2021, the standard deduction amounts are $12,550 for singles and those who use Married Filing Separate (MFS) status, $25,100 for Married Filing Joint (MFJ) couples, and $18,800 for Heads of Household (HOH). If your total annual itemizable deductions for 2021 will be close to your standard deduction amount, consider bunching your expenditures for itemized deductions so that they exceed the standard deduction in one year, and then use the standard deduction in the following year. Note that if you decide to take the standard deduction in 2021 (and bunch itemized deductions in 2022), you can still take an "above the line" deduction for charitable contributions in 2021, up to $300 ($600 if MFJ).

Determine if Selling Investment Assets before Year-end Makes Sense. No matter what your tax bracket in 2022 will be, you should review your investment portfolio held in a taxable account and determine if selling any stock before year end could make tax sense. To the extent you have capital losses that were recognized earlier this year or capital loss carryovers from before 2021, selling stock that will result in gains before year-end will not result in any tax bite. This strategy is especially advantageous when realizing short-term capital gains. Sheltering short-term capital gains with capital losses is a great deal because net short-term gains would otherwise be taxed at higher ordinary income rates. If you have investments that have declined in value, you might want to take the resulting capital losses this year since those losses would shelter capital gains, including high-taxed short-term gains, from other 2021 investment sales.

Many Valuable Tax Credits Extended through 2021. Credits are still available for: (1) energy-efficient home improvements, (2) residential energy efficient property (including solar energy equipment), (3) fuel-cell vehicles, (4) electric motorcycles, and (5) alternate fuel vehicle refueling equipment. If you're thinking about purchasing any of these, let us know. We can help you determine whether your expenditure qualifies for a credit.

Consider a Roth IRA Conversion. This may be the right time to make a Roth conversion, especially if you think you will be in a higher tax bracket in 2022. Although you will pay tax as if the assets had been distributed from the traditional IRA, your future Roth IRA distributions can potentially be tax-free. As an added benefit, unlike traditional IRAs, Roth IRAs don't have minimum distribution requirements during the account owner's lifetime.

Contribute to a Traditional IRA. Individuals over the age of 70½ who are still working in 2021 can contribute to a traditional IRA. However, if you're over age 70½ and considering making a charitable donation directly from your IRA (known as a Qualified Charitable Distribution or QCD) in the future, making a deductible IRA contribution for years you are age 70½ or older will affect your ability to exclude future QCDs from your taxable income.

Other Tax Planning Strategies:

- Maximize your health flexible spending account
- Maximize health savings account contributions
- Use a credit card to prepay expenses to generate deductions for this year including medical expenses
- If you expect to owe state and local income taxes for 2021, increase your withholding of state taxes or pay state estimated taxes before year-end if your total state and local taxes don't exceed $10,000
- Election to capitalize real estate taxes on investment property
- Make gifts of up to $15,000 to an unlimited number of individuals before year-end; this can save you gift and estate taxes
- Contribute appreciated stock to charities
- Consider giving appreciated stock to lower tax paying family members

Year-end Planning Moves for Small Businesses

In addition to planning for possibly higher tax rates in 2022, if you own a business, consider the following strategies. Keep in mind that the proposed tax rate increases mentioned above would potentially affect income earned by sole proprietors, pass-through entities, and corporations.

Establish a Tax-favored Retirement Plan. If your business doesn't already have a retirement plan, now might be the time to make this move. Current retirement plan rules allow for significant deductible contributions. But please be aware that if your business has employees, you may have to cover them as well.

Plan Asset Purchases. 100% first-year bonus depreciation is available for qualified **new and used** property that is acquired and placed in service in calendar-year 2021 (and unless the law is changed, 2022). As such, your business might be able to write off the entire cost of some or all of your 2021 asset additions on this year's return. Some assets that don't qualify for bonus depreciation are eligible for Section 179 expensing. For qualifying property placed in service in tax years beginning in 2021, the maximum Section 179 deduction is $1.05 million. The Section 179 deduction begins to phase-out when the cost of Section 179-eligible property placed in service during the year exceeds $2.62 million.

Note: If tax rates are going up in 2022, you might wait until then to place property that qualifies for bonus depreciation or Section 179 expensing in service.

Increase Basis in your Business. If you own an interest in a Partnership, LLC, or S Corporation, you may need to increase your basis in the entity so you can deduct a loss from it for this year.

Consider employing your children in the business. This will give your business additional deductions and help establish a child's retirement account.

Maximize the 20% deduction for business pass through income in 2021. Please note that pending legislation will make this deduction available to fewer taxpayers as income level increases.

Review and consider changing current accounting method and/or entity structure. There are many tax accounting method changes available under current law that can be implemented during the balance of 2021 or in early 2022 that can favorably impact the timing of your businesses income and/or deductions.

This alert only covers some of the year-end tax planning moves that could potentially benefit you, your family, and your business. Please contact us if you have questions, want more information, or would like us to help in designing a year-end planning package that delivers the best tax results for you.

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