

6 Year-End Tax-Smart Opportunities You Can't Afford to Miss

Tax planning identifies opportunities to help reduce or shift your tax burden so you're not paying more than your fair share. While you never want to make decisions based solely on the tax consequences, managing taxes is part of a comprehensive approach to pursuing your financial and lifestyle goals. Below are six tax-smart tips and strategies to consider before year end.

1. Determine if you can itemize on your 2023 tax return

Taking time now to determine if you will itemize or if you will take the standard deduction on your 2023 return will help ensure you're not missing tax-saving opportunities between now and year end. For 2023, the standard deduction is \$13,850 for individual taxpayers, \$27,700 for married filing jointly, and \$20,800 for heads of household. In addition, single filers age 65 and older who are not a surviving spouse can increase the standard deduction by \$1,850. Joint filers 65 and over can increase the standard deduction by \$1,500 each, or \$3,000 per couple. If your allowable deductions add up to more than the standard deduction, it makes sense to itemize. If they're close but not quite there, consider whether bunching deductions so you can itemize is a good option for you.¹

2. Bunch deductions

Bunching deductions can help you save money if you have qualified deductions that are nearly equal to the standard deduction. For example, if you have significant unreimbursed medical expenses for 2023, it may make sense to accelerate out-of-pockets costs for planned elective procedures or medical equipment into this year to bring you over the standard deduction amount. Keep in mind, you can only deduct unreimbursed medical expenses that exceed 7.5% of your adjusted gross income (AGI). So if your AGI is \$50,000, the first \$3,750 of qualified expenses (7.5% of \$50,000) don't count.

Bunching charitable deductions can be a tax-smart way to help accomplish your philanthropic goals. One way to achieve this is through the use of donor-advised funds which are established with qualified public charities. As the donor, you transfer money or appreciated stock to the fund and receive a deduction in the year the charitable donation is made. For example, if you plan to give \$3,000 per year to charity over the next five years, but that annual amount is not enough for you to itemize and take a deduction for your charitable gifts, you could donate the full \$15,000 (5 X \$3,000) in 2023. That would enable you to itemize this year's tax return and take the standard deduction in the remaining years (2024 through 2027). The contributions within your donor-advised fund could still be disbursed to the charity on an annual basis, over the five-year period. However, it's important to understand that contributions to donor-advised funds are irrevocable.

3. Time your income and expenses

The timing of certain income and expenses can help reduce your tax liability. Deferring income, such as bonuses or self-employment income to 2024, and accelerating deductible expenses into 2023, can be an effective strategy if you expect to be in a lower tax bracket next year. However, the opposite approach may be beneficial if you expect to be in a higher tax bracket next year. Accelerating income will allow more income to be taxed at this year's lower rate, and deferring expenses will make the deductions more valuable next year when you're subject to a higher tax rate.

4. Maximize retirement plan contributions

Contributions to an employer retirement plan, such as a 401(k) or 403(b), is one of the most effective ways to help reduce taxable income. Traditional contributions are made on a pretax basis, reducing your modified adjusted gross income (MAGI). This can also help you reduce or avoid exposure to the 3.8% net investment income tax (NIIT). In 2023, you can contribute up to \$22,500 to your employer plan. If you're 50 or older, you can make an additional \$7,500 catch-up contribution, for a total maximum contribution of \$30,000. The deadline for employer plan contributions is December 31. If you're eligible to contribute to an individual retirement account (IRA), the deadline for 2023 contributions is the April 2024 tax deadline. IRA contributions limits for 2023 are \$6,500 and an additional \$1,000 catch-up contribution for those 50 or over, for a total annual contribution of \$7,500.² If you're self-employed, consider an individual 401(k), profit-sharing plan, or SEP IRA to defer a percentage of your compensation.

5. Consider a Roth IRA conversion

If you expect to be in a higher tax bracket in 2024, now may be the time to consider converting all or a portion of traditional IRA assets to a Roth IRA to help reduce taxable income in retirement while providing estate planning benefits. Since Roth IRAs are not subject to required minimum distributions (RMDs), the entire balance can grow tax-free over your lifetime for the benefit of your heirs. Keep in mind, the amount converted to a Roth is taxable in the year of the conversion.

6. Don't forget about annual gifts

The annual gift tax exclusion amount, which is \$17,000 per recipient in 2023 (\$34,000 for married couples filing jointly) allows you to gift to anyone you choose without cutting into your lifetime gift and estate tax exemption. These gifts are not deductible for income tax purposes.³

This information is not intended as tax advice. Before implementing any financial strategy, be sure to call the office and schedule a meeting to discuss the strategies that are right for you.

¹ "IRS provides tax inflation adjustments for tax year 2023." IRS.gov, 18 OCT 22, <https://www.irs.gov/newsroom/irs-provides-tax-inflation-adjustments-for-tax-year-2023>

² Taxpayers should review the 401(k) and IRA limit increases for 2023." IRS.gov, 21 NOV 22, <https://www.irs.gov/newsroom/taxpayers-should-review-the-401k-and-ira-limit-increases-for-2023>

³ "Frequently Asked Questions on Gift Taxes." IRS.gov, 9 AUG 2023, <https://www.irs.gov/businesses/small-businesses-self-employed/frequently-asked-questions-on-gift-taxes>

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Generally, a donor advised fund is a separately identified fund or account that is maintained and operated by a section 501(c)(3) organization, which is called a sponsoring organization. Each account is composed of contributions made by individual donors. Once the donor makes the contribution, the organization has legal control over it. However, the donor, or the donor's representative, retains advisory privileges with respect to the distribution of funds and the investment of assets in the account. Donors take a tax deduction for all contributions at the time they are made, even though the money may not be dispersed to a charity until much later.

Some IRAs have contribution limitations and tax consequences for early withdrawals. For complete details, consult your tax advisor or attorney.

Converting from a traditional IRA to a Roth IRA is a taxable event. A Roth IRA offers tax free withdrawals on taxable contributions. To qualify for the tax-free and penalty-free withdrawal of earnings, a Roth IRA must be in place for at least five tax years, and the distribution must take place after age 59 ½ or due to death, disability, or a first-time home purchase (up to a \$10,000 lifetime maximum). Depending on state law, Roth IRA distributions may be subject to state taxes.