

4 Smart Year-End Tax Planning Strategies to Consider Now

One of the greatest myths about tax planning is that it's only for the wealthy. Yet, nothing could be further from the truth. If you earn income, the goal is to keep as much of your money working for you, no matter your income level. That requires having a plan in place for how you will manage taxes on your various sources of income, such as workplace earnings and investments. That's among many reasons why tax planning is an integral part of a comprehensive financial plan designed to help you meet multiple goals and priorities, while keeping more of what you earn.

Below are four strategies to consider to help with your tax planning before year end. Be sure to meet with your professional tax advisor before putting these or other strategies in place.

1. Maximize your retirement plan contributions

Maximizing contributions to the qualified retirement plans you are eligible to participate in—such as a 401(k), 403(b), individual retirement account (IRA), or SEP IRA—is one of the smartest ways to help reduce taxable income while building wealth. Retirement plan contributions can be made on a pre-tax (traditional) or after-tax (Roth) basis. Pre-tax contributions can reduce the amount of your taxable income by the amount of your contribution, up to the plan's annual limit. Those age 50 and older are also eligible to make catch-up contributions.

Roth contributions are made on an after-tax basis, which means you can't deduct contributions. However, earnings compound on a tax-deferred basis. Qualified withdrawals from a Roth are generally income tax-free, whereas withdrawals from a traditional IRA are taxed as ordinary income in retirement.

For most employer plans, December 31 is the last day you can make contributions for the current tax year. For IRAs and certain plans for self-employed business owners, you have until April 15, 2022, to make 2021 contributions.

Retirement Plan Contribution Limits	2021
401(k), 403(b), most 457 plans	\$19,500
Catch up contribution, over age 50	\$6,500
Total:	\$26,000
IRA	\$6,000
Catch up contribution, over age 50	\$1,000
Total:	\$7,000

Source: IRS.gov

2. Consider a Roth conversion

If you expect to be in a lower tax bracket this year than in the future, you may want to think about initiating a Roth conversion. A Roth conversion takes place when you roll over assets from an existing traditional IRA or qualified employer plan into a Roth plan. Partial conversions are also permitted. The amount converted is included in your gross income and taxes are owed on the assets in the year they are converted. While there is no limit on the amount of assets you can convert in 2021, Congress is considering proposals that may seek to impose future income limits on Roth conversions, so be sure to discuss your plans with your tax advisor before taking action.

3. Don't miss this opportunity to maximize cash contributions to charity

For taxpayers planning to itemize their deductions, the Coronavirus Aid, Relief, and Economic Security (CARES) Act of 2020 increased the deductible limit for cash gifts to qualified charitable organizations from 60% of adjusted gross income (AGI) to 100% of AGI. This was extended for 2021.

The CARES Act also allowed taxpayers claiming the standard deduction to deduct up to \$300 of cash donations to qualified charities in 2020. This was not only extended for 2021, but the maximum deduction was increased to \$600 for married couples filing jointly. Before you donate, make sure the charity you're considering is a qualified charity that is eligible to receive tax-deductible contributions. Cash donations must be made by December 31, 2021, to qualify under these special provisions.¹

4. Harvest investment losses

Last year, many investors took the opportunity to harvest investment losses, following the significant stock market drop in March 2020. However, with markets surging throughout most of 2021, fewer investors may have an opportunity to harvest losses this year. Tax-loss harvesting occurs when you sell portfolio holdings that are trading below your purchase price to lock in the tax loss. Applying losses against gains can help to lower your investment tax burden. However, you also have to apply the right types of losses against gains. Short-term losses are associated with assets held for a period of less than 12 months, while long-term losses pertain to assets sold after being owned for 12 months or more. This is important because short-term capital gains are generally taxed at a higher federal income tax rate than long-term capital gains.²

Investors also need to be cognizant of the wash-sale rule, which states that if you sell a security at a loss and then purchase a "substantially identical" security within 30 days prior to or after the sale, the loss is disallowed for income tax purposes.³ Tax-loss harvesting can be complex for investors to do on their own, which is another good reason to consider professional portfolio management.

To learn more about tax-smart investment strategies, contact the office to schedule time to talk.

¹ <https://www.irs.gov/newsroom/expanded-tax-benefits-help-individuals-and-businesses-give-to-charity-during-2021-deductions-up-to-600-available-for-cash-donations-by-non-itemizers>

² <https://www.investopedia.com/terms/t/taxgainlossharvesting.asp>

³ <https://www.investor.gov/introduction-investing/investing-basics/glossary/wash-sales>

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