Accountants & Advisors

Dear PSK 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. This year's planning is more challenging than usual due to changes made by the Inflation Reduction Act of 2022 and the SECURE 2.0 Act.

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.

If proposed tax increases do pass, however, the highest income taxpayers may find that the opposite strategies produce better results: Pulling income into 2023 to be taxed at currently lower rates, and deferring deductible expenses until 2023, when they can be taken to offset what would be higher-taxed income. This will require careful evaluation of all relevant factors.

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. 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:

• New tax credits for EVs. If you are looking to buy a new car this year, remember that the Inflation Reduction Act has introduced various credits for buying both new and used electric vehicles.

• 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 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. Note, however, that in some cases, it may actually pay to accelerate income into 2023. For example, that may be the case for a person who will have a more favorable filing status this year than next (e.g., head of household versus individual filing status), or who expects to be in a higher tax bracket next year. That's especially a consideration for high-income taxpayers who may be subject to higher rates next year under proposed legislation.

• Many taxpayers won't want to itemize because of the high basic 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 (such as the $10,000 deduction limit on state and local taxes) or abolished (such as the miscellaneous itemized deduction and the deduction for non-disaster related personal casualty losses). You can still itemize medical expenses that exceed 7.5% of your AGI, state and local taxes up to $10,000, your charitable contributions, plus mortgage interest deductions on a restricted amount of debt, but these deductions won't save taxes unless they total more than your standard deduction.

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• 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.

• Consider using a credit card to pay deductible expenses before the end of the year. Doing so will increase your 2023 deductions even if you don't pay your credit card bill until after the end of the year.

• If you are age 70½ or older by the end of 2023, and especially if you are unable to itemize your deductions, consider making 2023 charitable donations via qualified charitable distributions from your traditional 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. (The qualified charitable distribution amount is reduced by any deductible contributions to an IRA made for any year in which you were age 70½ or older, unless it reduced a previous qualified charitable distribution exclusion.)

• 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 in December 2023 to make HSA contributions, you can make a full year's worth of deductible HSA contributions for 2023.

• 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 increasing your wage withholding 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 (60 days or less from the initial withdrawal) 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.

• 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 net long-term capital gain to the extent that, when added to regular taxable income, it is not more than the maximum zero rate amount (i.e., $89,250 for a married couple; estimated to be $94,050 in 2024).

• 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. This may be desirable, however, for those potentially subject to higher tax rates under pending legislation.

• New rules for required minimum distributions (RMDs) from an IRA or 401(k) plan (or other employer-sponsored retirement plan). In general, an IRA owner must take their first RMD for the year in which they reach age 72 (73 if they reach age 72 after December 31, 2022). However, they can delay taking their first RMD until April 1 of the following year. Those who reach age 72 in 2022 must take their first RMD by April 1, 2023, and the second RMD by December 31, 2023. If they reach age 72 in 2023, their first RMD for 2024 (the year they reach 73) is due by April 1, 2025.

• 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 to another year. These 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.

These are just some of the year-end steps that can be taken to save taxes. Again, by contacting us, we can tailor a particular plan that will work best for you.

Sincerely,

PSK LLP Tax Team