# 2023 YEAR-END INCOME TAX PLANNING FOR INDIVIDUALS

## INTRODUCTION

As we approach the end of another year, we believe it's important to take a moment to review 2023 for year-end tax planning opportunities. Examining your 2023 tax situation before year-end could lead to tax savings when you file your tax returns in 2024. With that in mind, we have included our 2023 year-end income tax planning letter to assist you with this process. We've included selected traditional as well as selected new planning ideas for your consideration. If you have questions or want to discuss planning ideas not included in our letter, please call our firm.

**Caution!** The IRS continues to release guidance on various important tax provisions. We closely monitor new tax legislation and IRS releases. Please call our firm if you want an update on the latest tax legislation, IRS notifications, announcements, and guidance or **if you need additional information concerning any item discussed in this letter.**

**Be Careful!** We suggest you call our firm before implementing any tax planning technique discussed in this letter. You cannot properly evaluate a particular planning strategy without calculating your overall tax liability with and without that strategy. This letter contains ideas for Federal income tax planning only. **State income tax issues are not addressed.**

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## POSSIBLE LEGISLATION BEFORE YEAR-END

Each year we work to provide you with our year-end planning letter in time to implement possible tax saving strategies before December 31st. As a result, it's possible Congress could pass new legislation between your receipt of this letter and year-end. As of the completion of this letter, it appears an omnibus spending package is the best chance for any provisions that may affect 2023 tax law. However, the Secure Act 2.0 segment of the Consolidated Appropriations Act, 2023 was passed on December 29, 2022, and has many provisions that are first effective in 2023. The following is a discussion of some of those provisions. Please contact our firm if you would like an update on possible legislation and how it could affect you.

## HIGHLIGHTS OF PROVISIONS INCLUDED IN SECURE ACT 2.0 FIRST EFFECTIVE AFTER 12/29/22 (DATE OF ENACTMENT) OR AFTER 12/31/22

On Thursday, December 29, 2022, the President signed H.R. 2617, the "Consolidated Appropriations Act, 2023," providing appropriations for the Federal government's fiscal year ending September 30, 2023. In the following summary, we've listed a few provisions of the Secure Act 2.0 segment of the Consolidated Appropriations Act, 2023 that could impact your 2023 year-end planning.

### Increase In Age For Required Minimum Distributions (RMDs)

- **Prior Provision.** Required minimum distributions from IRAs and qualified plan accounts were generally required to begin no later than April 1st following the calendar year in which an individual reached age 72. However, if the individual did not own more than 5% of the employer sponsoring the plan for the plan year ending in the calendar year in which the employee attained age 72, RMDs were not required until April 1st following the calendar year the individual retired. This delay until retirement does not apply to IRA owners.

- **RMDs Required After 73, Effective For Individuals Who Attain Age 72 After 2022.** The Act provides:

  - For an individual who attains age 72 after December 31, 2022, and age 73 before January 1, 2033, **age 72 is changed to age 73, and**

  - For an individual who **attains age 74 after December 31, 2032, the applicable age is 75.**

    **Planning Pointer! Individuals who reach age 72 in 2023 will not have an RMD for 2023.** An RMD will be required for 2024 and the required beginning date for that RMD is April 1, 2025. **Planning Alert!** The Act retains the provision allowing participants in an employer's retirement plan who do not own more than 5% of the employer sponsoring the plan for the plan year ending in the calendar year in which the employee attains age 73 to defer distributions until April 1st following the calendar year the employee retires (not applicable to an IRA).

### Reduction In 50% Excise Tax For Failures To Take RMDs

- **Excise Tax Generally Reduced To 25%.** Beginning with 2023, where the amount required to be distributed from an employer plan or IRA is less than the RMD, the 50% penalty tax under §4974(a) on the amount of the RMD that was not distributed is reduced from 50% to 25%.

  The penalty is reduced to 10% if the amount of the RMD not timely distributed is distributed and a return is filed to report the distribution and pay the 10% penalty tax during the **"correction window."** The **"correction window" begins** on the **date on which the penalty tax is imposed** with respect to a shortfall of distributions from a Plan. The **"correction window" ends** on the **Earliest of:**

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- The date the IRS mails a notice of deficiency with respect to the penalty,
- The date on which the penalty is assessed, **or**
- The last day of the second taxable year that begins after the end of the taxable year in which the penalty is imposed.

**New Exceptions From 10% Penalty Tax For Certain "Early Distributions" From Retirement Accounts**

- **No 10% Penalty Tax On Earnings On Excess IRA Contributions Withdrawn By Due Date Of Return.** A 6% excise tax is imposed on "excess contributions" to an IRA. To avoid the 6% excise tax on an excess contribution, the excess contribution, and any net earnings allocable to the excess contribution must be distributed from the IRA on or before the due date of a participant's tax return (including extensions). If the excess contribution plus any earnings is distributed by the due date of the return (including extensions) the contribution amount distributed is treated as an amount not contributed, and therefore is not subject to the 10% penalty tax. However, there was no specific exception from the 10% penalty for the earnings distributed. The Act provides that the earnings distributed along with the excess IRA contribution are not subject to the 10% penalty tax.

- **Exception For Distributions To Individuals With A Terminal Illness.** Distributions made to a plan participant on or after the date such participant has been certified by a physician as having a terminal illness (i.e., an illness or physical condition which can reasonably be expected to result in death in 84 months or less after the date of the certification) will not be subject to the additional 10% tax on early distributions.

- **Expansion Of Exceptions From 10% Penalty For Public Service Employees Age 50 Or Older.** Prior to the Act, distributions to qualified public safety employees from a governmental plan on or after reaching age 50 were not subject to the 10% penalty tax. The Act provides that public safety employees may take distributions from a governmental plan on or after reaching age 50 **or 25 years of service** under the plan, whichever is earlier, without a 10% penalty tax. This exception also applies to private sector firefighters who are participants in a qualified pension, profit-sharing or stock bonus plan under §401(a); a §403(a) plan; or a §403(b) plan (as well as to firefighters employed by a state or political subdivision of a state). In addition, the Act adds to the list of "public safety employees" employees of a State or a political subdivision of a State providing services as a corrections officer or as a forensic security employee providing for the care, custody, and control of forensic patients.

**Deductions For Charitable Conservation Easements Substantially Restricted**

The Act provides that a contribution of a conservation easement by a partnership, S corporation, or other pass-through entity is generally not deductible if the contribution exceeds 2.5 times the sum of each owner's basis in the partnership allocable to the portion of the real property with respect to which the contribution is made. The disallowance does not apply to a contribution made **at least 3 years after the later of** – **1)** the last date the partnership acquired any portion of the real property contributed, **2)** the last date any partner acquired any interest in the partnership, and **3)** if the interest in the partnership that made the contribution is held through one or more partnerships, **a)** the last date on which any such partnership acquired any interest in any other such partnership, and **b)** the last date on which any partner in any such partnership acquired any interest in such partnership. This disallowance provision **does not apply if substantially all the partnership interests are held,** directly or indirectly, **by an individual and members of the individual's family.** In addition, there is an **exception for** contributions to preserve buildings which are **certified historic structures.**

## HIGHLIGHTS OF PROVISIONS INCLUDED IN THE INFLATION REDUCTION ACT OF 2022

On August 16, 2022, President Biden signed the Inflation Reduction Act of 2022. The following is a summary of selected provisions included in the Inflation Reduction Act that could impact your 2023 tax planning.

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**Credit For Energy Efficient Residential Property Improvements**

- **Increased Credit Limitation Begins In 2023.** The Inflation Reduction Act provides an increased 30% credit generally with an **annual $1,200 limitation** for qualified energy efficient residential property improvements beginning in 2023 and before 2032. The credit for a tax year equals **30%** of the sum of: **1)** the amount paid or incurred by the taxpayer for qualified **Energy Efficiency Improvements installed during that year, 2)** the amount of the **Residential Energy Property Expenditures paid or incurred** by the taxpayer during that year, and **3)** amounts paid or incurred during the year for home energy audits of the taxpayer's principal residence. The maximum credit for home energy audits is **$150.**

- **Qualified Energy Efficiency Improvements.** Qualified Energy Efficiency Improvements are improvements to a dwelling unit located in the U.S. **owned and used as the taxpayer's principal residence,** the original use of which begins with the taxpayer, and reasonably expected to be in use for at least 5 years. Qualified Energy Efficiency Improvements include energy efficient building envelope components such as insulation, exterior windows (including skylights), and exterior doors. The maximum credit for any taxable year resulting from expenditures for all exterior windows and skylights **may not exceed $600.** In addition, the maximum credit for a taxable year **may not exceed $250 for any one exterior door and $500 for all exterior doors.** Exterior doors, windows and skylights must meet the applicable Energy Star requirements. Insulation materials or systems must meet the criteria established by the International Energy Conservation Code (IECC).

- **Residential Energy Property Expenditures.** Qualified Residential Energy Property Expenditures are expenditures made by the taxpayer for Qualified Energy Property, the original use of which begins with the taxpayer, installed on or in connection with a dwelling unit located in the U.S. and **used as a residence by the taxpayer.** Qualified Residential Energy Property Expenditures include any of the following which meet or exceed the highest efficiency tier (not including any advanced tier) established by the Consortium for Energy Efficiency in effect as of the beginning of the calendar year in which the property is placed in service: **an electric or natural gas heat pump or heat pump water heater; a central air conditioner; a natural gas, propane, or oil water heater; a natural gas, propane, or oil furnace or hot water boiler. For a full list of qualifying expenditures, please see the IRS website at** Frequently asked questions about energy efficient home improvements and residential clean energy property credits (irs.gov).

  Qualified Residential Energy Property Expenditures include expenditures for labor costs properly allocable to the **onsite preparation, assembly, or original installation** of the property. **Caution!** The maximum credit for any taxable year resulting from any item classified as an energy property expenditure **generally cannot exceed $600 except for the items discussed in the following paragraph.**

- **Higher Credit Limitation For Qualifying Heat Pumps, Heat Pump Water Heaters And Biomass Stoves And Boilers.** Notwithstanding the $1,200 and $600 limitations on the credit discussed previously, the **maximum aggregate credit is $2,000** for amounts paid or incurred in a taxable year for: **1)** qualified electric or natural gas heat pumps and heat pump water heaters which meet or exceed the highest efficiency tier (not including any advanced tier) established by the Consortium for Energy Efficiency which is in effect as of the beginning of the calendar year in which the property is placed in service and **2)** biomass stoves and boilers with a thermal efficiency rating of at least 75 percent (measured by the higher heating value of the fuel) used in a dwelling unit in the U.S. and used as a residence by the taxpayer.

- **Note!** Please see the IRS website at Frequently asked questions about energy efficient home improvements and residential clean energy property credits (irs.gov) for additional information concerning these 2023 energy credits.

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**Residential Clean Energy Credit**

After 2022, §25D provides a 30% credit for: **1)** solar electric property expenditures (solar panels); **2)** solar water heating property expenditures (solar water heaters); **3)** fuel cell property expenditures; **4)** small wind energy property expenditures (wind turbines); **5)** geothermal heat pump property expenditures; and **6)** battery storage technology expenditures. The credit applies to property installed in connection with a dwelling located in the United States and used as a residence by the taxpayer. The residence is not required to be taxpayer's "principal residence" except for fuel cell property. IRS says the credit applies to new homes or improvements to existing homes. Labor costs allocable to onsite preparation, assembly, or original installation of qualified property and for piping or wiring to interconnect the qualifying property to the home also qualifies for the credit.

**Credits For Buying Electric Vehicles Placed In Service During 2023**

- **"New Clean Vehicle Credit" For Vehicles Placed In Service After 2022 And Before 2033.** Taxpayers may qualify for a credit of up to $7,500 for taking possession of a qualified new electric vehicle during 2023. To qualify for the New Clean Vehicle Credit, the vehicle must be a qualified electric vehicle (EV) or a qualified fuel cell vehicle. The taxpayer must be the first user of the vehicle after the vehicle is sold, registered, or titled. **No credit is allowed for a new vehicle if the manufacturer's suggested retail price of the vehicle exceeds:** $80,000 for SUVs, pickups, and vans; and $55,000 for other vehicles. In addition, **no credit** will be allowed for a new vehicle **if the lesser of current or prior year modified adjusted gross income of the taxpayer is more than $300,000 for joint filers, $225,000 for head of households, and $150,000 for others.**

  **The requirements for a vehicle to qualify for the credit are different for vehicles placed in service before April 18, 2023, and those placed in service after April 17, 2023.** The IRS says a taxpayer places an EV in service when the taxpayer takes possession of the vehicle. Because of the complexity for determining whether a vehicle qualifies for the credit and determining the amount of the credit, we suggest using the IRS website to determine whether an EV acquired during 2023 qualifies for the new clean vehicle credit and the amount of the credit. The relevant web address is Federal Tax Credits for Plug-in Electric and Fuel Cell Electric Vehicles Purchased in 2023 or After (fueleconomy.gov). Once at the website you will need to enter: 1) whether the vehicle was placed in service after April 17, 2023 or before April 18, 2023; 2) the model year; 3) the make of the vehicle (e.g., Chevrolet, Ford, Toyota); 4) the model (e.g., Bolt, Mustang Mach-E); and 5) whether the vehicle is all electric or a plug-in hybrid vehicle.

- **Clean Vehicle Credit For Previously Owned Vehicles Placed In Service After 2022 And Before 2033.** Individuals are allowed a credit equal to the **lesser of $4,000 or 30% of the sales price** for used EVs placed in service during 2023. The used EV must be purchased in a **"qualified sale"** which is: **1)** a sale by a dealer licensed to sell vehicles in a state, D.C., Puerto Rico or other U.S. possession, an Indian tribal government, or any Alaska Native Corporation; **2)** for $25,000 or less (including delivery charges, but not taxes & fees); and **3)** the **first sale since August 16, 2022, to a "qualified buyer"** to claim the credit other than the original owner of the vehicle.

  **A "qualified buyer"** is **an individual** (**Note!** Only individuals qualify for this credit!): **1)** who purchases the vehicle for use and not for resale; **2)** who cannot be claimed as a dependent by another taxpayer; and **3)** who has not been allowed a credit for a previously owned clean vehicle during the three-year period ending on the date of sale.

  **No credit is allowed if lesser of current year or prior year AGI is more than** $150,000 for joint filers, $112,500 for head of households, and $75,000 for others.

  The model year of the EV must be at least two years earlier than the calendar year in which the individual acquires the vehicle, the original use of the vehicle must start with someone other than the taxpayer and the vehicle must be acquired in a qualified sale as outlined above.

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There are additional requirements for the used EV to qualify for the credit. However, if the above requirements are met, an individual can use the IRS website to determine if the vehicle qualifies for the credit – [Federal Tax Credits for Pre-owned Plug-in Electric and Fuel Cell Vehicles (fueleconomy.gov)].

## HIGHLIGHTS OF TRADITIONAL YEAR-END TAX PLANNING

Over the years, we've discussed several traditional year-end tax planning strategies to help reduce taxable income. One such strategy is reducing current year taxable income by deferring taxable income into later years and accelerating deductions into the current year. This strategy is particularly beneficial when your income tax rate in the following year is expected to be the same or lower than the current year. Consequently, in the following discussion we include traditional year-end tax planning strategies that would allow you to accelerate your deductions into 2023, while deferring your income into 2024. **Planning Alert!** For individuals who expect their 2023 taxable income to be much lower than their 2024 taxable income, the opposite strategy might be more advisable. In other words, individuals who have a significant drop in income during 2023, may decide a better year-end planning strategy is accelerating income into 2023 (to be taxed at lower rates), while deferring deductions into 2024 (to be taken against income that is expected to be taxed at higher rates).

**Tax Benefits Of Above-The-Line Deductions.** Traditional year-end planning includes accelerating deductible expenses into the current tax year. So-called **"above-the-line"** deductions reduce both your "adjusted gross income" and your "modified adjusted gross income", while **"itemized"** deductions (i.e., below-the-line deductions) do **not** reduce either adjusted gross income or modified adjusted gross income. Deductions that reduce your adjusted gross income (or modified adjusted gross income) can generate multiple tax benefits by: **1)** Reducing your taxable income and allowing you to be taxed in a lower tax bracket; **2)** Potentially freeing up other deductions (and tax credits) that phase out as your adjusted gross income (or modified adjusted gross income) increases (e.g., Certain IRA Contributions, Certain Education Credits, Adoption Credit, Child Credits, etc.); **3)** Potentially reducing your modified adjusted gross income below the income thresholds for the 3.8% Net Investment Income Tax (i.e., 3.8% NIIT only applies if MAGI exceeds $250,000 if married filing jointly; $200,000 if single); **4)** Possibly reducing your household income to a level that allows you to qualify for a "refundable" Premium Tax Credit for health insurance purchased on a government Exchange, **or 5)** As we will discuss later, potentially reducing your taxable income to a level that could maximize your 20% 199A Deduction (i.e., individuals reporting Qualified Business Income will generally find it much easier to qualify for the 20% 199A Deduction if their 2023 taxable income does not exceed **$364,200** if filing a joint return or **$182,100** if filing single).

As a cash method taxpayer, you can generally accelerate a 2024 deduction into 2023 by *"paying"* the deductible item in 2023. *"Payment"* typically occurs in 2023 if, **before the end of 2023: 1)** A check is delivered to the post office, **2)** Your electronic payment is debited to your account, or **3)** An item is charged on a *third-party credit card* (e.g., Visa, MasterCard, Discover, American Express). **Caution!** If you post-date the check to 2024 or if your check is rejected, no payment has been made in 2023 even if the check is delivered in 2023. **Planning Alert!** The IRS says that prepayments of expenses applicable to periods beyond 12 months after the payments are not deductible in 2023. If you think that you could benefit from accelerating ***above-the-line*** deductions into 2023, consider the following:

- **Possible Above-The-Line Deductions. Above-the-line** deductions include: Military Moving Expenses; Qualifying Alimony Payments (if the divorce or separation instrument was **executed before 2019);** Deductions for IRA or Health Savings Account (HSA) Contributions; Certain Business Expenses; and, Student Loan Interest. **Caution!** As discussed in more detail below, un-reimbursed employee business expenses are not deductible at all **for 2018 through 2025.** However, employee business expenses that are reimbursed under an employer's accountable plan are excluded altogether from the employee's taxable income. Moreover, there have been changes to the above-the-line deductions for **Moving Expenses,** and **Alimony Payments,** as follows:

  - **Moving Expenses.** Historically, the deduction for qualified **business-related moving expenses** was an above-the-line deduction. However, **for 2018 through 2025,** the deduction for **moving**

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**expenses** has been suspended for most individuals. **<u>Planning Alert!</u>** Generally, active members of the Armed Forces who move pursuant to a military order because of a permanent change of station may still deduct un-reimbursed qualified moving expenses as above-the-line deductions and may exclude the employer reimbursements of those moving expenses from income. For 2023, an **Armed Forces Member** may use the standard rate of **22 cents per mile** to determine the deduction for automobile expenses related to a qualified move.

- **<u>Alimony Payments.</u>** Historically, an individual making qualified alimony payments was allowed an above-the-line deduction for the payments and the recipient of the payments was required to include the payments in income. **However, effective for "Divorce or Separation Instruments" <u>executed after 2018,</u>** the **deduction for alimony payments has been repealed altogether.** The good news, however, is that these alimony payments **are no longer taxable to the recipient.** Alimony paid under a divorce instrument **<u>executed before 2019</u>** will generally be grandfathered under the previous rules. **<u>Planning Alert!</u>** If you are currently paying or receiving alimony pursuant to a divorce or separation instrument ***executed before 2019,*** the tax treatment of the alimony payments does not change. That is, if your alimony payments were deductible before 2019, they should continue to be deductible (and includible in the recipient's income). **<u>Caution!</u>** Form 1040, Schedule 1 requires individuals who ***receive*** taxable alimony to disclose the "*Date Of Original Divorce Or Separation Agreement,"* and the amount received. Individuals who ***deduct*** the alimony are required to list the social security number of the recipient and the "*Date Of Original Divorce Or Separation Agreement."*

- **<u>Contributions To A Health Savings Account (HSA).</u>** You may be eligible for an above-the-line deduction for contributions to an HSA if you are covered under a high-deductible health plan during 2023. The maximum deduction for a self-only coverage plan is **$3,850** and **$7,750** for a family coverage plan. In addition, if you are at least 55 by the close of 2023, you can add **$1,000 ($4,850 & $8,750). <u>Caution!</u>** Distributions from your HSA must be used for qualified medical expenses, or they will be taxed and, with a few exceptions, be hit with a 20% penalty.

- **<u>Deductions For Business Expenses Paid By Partners.</u>** Generally, the IRS allows a partner in a partnership (or owner of an LLC) to take an above-the-line deduction for business expenses the owner **pays on behalf** of the partnership (or an LLC taxed as a partnership) **only if** there is an agreement (preferably in writing) between the partner and the partnership providing that those expenses are to be paid by the partner, and that the expenses will not be reimbursed by the partnership. **<u>Tax Tip!</u>** If you are a partner or LLC owner paying unreimbursed business expenses on behalf of your partnership or LLC, to be safe, you should have a written agreement in place with the entity stipulating that those expenses are to be paid by you, and that the expenses will not be reimbursed by the partnership or LLC.

- **<u>Employee Business Expenses.</u> Starting in 2018 and through 2025, *un-reimbursed*** employee business expenses are not deductible at all. For example, you **will not be able to deduct** any of the following business expenses **you incur as an employee, even if the expenses are necessary for your work: Automobile expenses** (including auto mileage, vehicle depreciation); **Costs of travel, transportation, lodging and meals; Union dues** and expenses; **Work clothes and uniforms;** Otherwise qualifying **home office expenses; Dues** to a chamber of commerce; **Professional dues; Work-Related education expenses; Job search expenses; Licenses and regulatory fees; Malpractice insurance premiums; Subscriptions** to professional journals and trade magazines; and **Tools and supplies** used in your work.

  - **<u>Note! An Employer's Qualified Reimbursement Of An Employee's Business Expenses Is Deductible By The Employer And Tax Free To The Employee.</u>** Generally, employee business expenses that are reimbursed under an employer's qualified **"Accountable Reimbursement Arrangement" are deductible by the employer** (subject to the limit on business meals), and the reimbursements are **not taxable to the employee.** However, reimbursements under an arrangement that is ***not*** a qualified accountable reimbursement arrangement generally must be treated as compensation and included in the employee's W-2.

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In addition, the employee would get no offsetting deduction for the business expense. **<u>Planning Alert!</u>** Generally, for an employer to have a qualified **Accountable Reimbursement Arrangement: 1)** The employer must maintain a reimbursement arrangement that requires the employee to substantiate covered expenses, **2)** The reimbursement arrangement must require the return of amounts paid to the employee that are more than the amounts substantiated, and **3)** There must be a business connection between the reimbursement (or advance) and the business expenses.

- **<u>Deducting Food And Beverage Expenses.</u>** The Tax Cuts And Jobs Act generally repealed business deductions with respect to entertainment, amusement, or recreation activities after 2017. **<u>Planning Alert!</u>** Fortunately, the IRS says that taxpayers can generally deduct 50% of the cost of meals (i.e., food and beverages) with a business associate (e.g., a current or potential business customer, client, supplier, employee, agent, partner, professional advisor). The IRS also says that a taxpayer can deduct 50% of the cost of food and beverages provided during a nondeductible entertainment activity with a business associate provided the food and beverages are purchased separately from the entertainment, or the cost of the food and beverages is stated separately from the cost of the entertainment on one or more bills, invoices, or receipts. **<u>Caution!</u>** If an employer reimburses an employee's deductible business food and beverage expense under an Accountable Reimbursement Arrangement, the employer could deduct 50% of the reimbursement. This same rule applies if you are employed by your own S corporation. However, as discussed previously, an employee who is not reimbursed by the employer for the business meal would get no deduction because un-reimbursed employee business expenses are not currently deductible. **<u>Remember!</u>** The 100% deduction for otherwise deductible business food and beverages provided by a restaurant expired for restaurant meals paid or incurred after 2022.

- **<u>Be Careful If You Are Working For Your Own S Corporation.</u>** If you operate your business as an S corporation and you also work for your S corporation as its employee, then it is particularly important that you have your S corporation (i.e., your employer) reimburse all your employee business expenses under an accountable plan. Under this arrangement, the reimbursement will be deductible by your S corporation, the deduction from the reimbursement will pass through to you as the S corporation shareholder, and your S corporation/employer will be able to exclude the reimbursement from your W-2 wages. **Please call our firm if you need assistance. We can help you establish a qualifying Accountable Reimbursement Arrangement with your employer.**

- **<u>Student Loan Interest Deduction.</u>** You may be able to deduct up to $2,500 of interest paid on a qualified student loan during 2023. The deduction is allowed to taxpayers who, per the loan agreement, have a legal obligation to make the interest payments. The $2,500 maximum deduction is phased out between **$155,000 and $185,000** of modified adjusted gross income if filing a joint return **($75,000 and $90,000 if filing single). <u>Caution!</u>** The deduction is not allowed to: **1)** A taxpayer filing as married filing separately, or **2)** A taxpayer who may be claimed as a dependent on someone else's tax return.

**<u>Itemized Deductions.</u>** Although **itemized** deductions (i.e., below-the-line deductions) do **not** reduce your adjusted gross income or modified adjusted gross income, they still may provide valuable tax savings. **Starting in 2018 and through 2025,** recent legislation substantially increased the Standard Deduction. For 2023, the Standard Deduction is: **Joint Return - $27,700; Single - $13,850;** and **Head-of-Household - $20,800.** Recent legislation also made changes to the following itemized deductions:

- **<u>Charitable Contributions.</u> Starting in 2018** (with no sunset date), a charitable contribution deduction is not allowed for contributions made to colleges and universities in exchange for the contributor's right to purchase tickets or seating at an athletic event (prior law allowed the taxpayer to deduct 80% as a charitable contribution). **<u>Planning Alert!</u>** If you think your itemized deductions this year could likely exceed your Standard Deduction of $27,700 if filing jointly ($13,850 if single) and you want to accelerate your charitable deduction into 2023, please note that a charitable contribution deduction is allowed for

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2023 if the check is **"mailed" on or before December 31, 2023,** or the contribution is made by a credit card charge in 2023. However, if you merely give a note or a pledge to a charity, no deduction is allowed until you pay the note or pledge. In addition, if you are considering a significant 2023 contribution to a qualified charity (e.g., church, synagogue, or college), it will generally save you taxes if you contribute *appreciated* long-term capital gain property, rather than selling the property and contributing the cash proceeds to the charity. By contributing capital gain property held more than one year (e.g., appreciated stock, real estate, Bitcoin, etc.), a deduction is generally allowed for the full value of the property, but no tax is due on the appreciation. If instead you intend to use "*loss*" stocks to fund a charitable contribution, you should sell the stock first and then contribute the cash proceeds. This will allow you to deduct the capital loss from the sale, while preserving your charitable contribution deduction.

- **Casualty Losses.** **From 2018 through 2025,** the itemized deduction for personal casualty losses and theft losses has been suspended. However, personal casualty losses attributable to a Federally declared disaster continue to be deductible. **Planning Alert!** Personal casualty losses generally continue to be deductible to the extent the taxpayer has personal casualty "gains" for the same year. In addition, casualty losses with respect to property held in a trade or business or for investment are still allowed.

  - **Planning Alert! Extension For Filing Returns And Making Certain Payments Until February 15, 2024.** The IRS has announced that individuals living in and businesses located in the counties designated as "covered disaster areas" in Florida, South Carolina, and Georgia because of Hurricane Idalia now have until February 15, 2024, to file returns and to make certain payments **due during the period beginning August 27, 2023, for Florida, August 29, 2023, for South Carolina, and August 30, 2023, for Georgia, and ending February 15, 2024.** If you live or have a businesses located in FL, SC or GA, please go to the following website https://www.irs.gov/newsroom/tax-relief-in-disaster-situations for more information. This website also provides a listing of all federal disaster areas for 2023 and the due date for returns of taxpayers located in those disaster areas. Please consult this website if there has been a major disaster in your area to find the extended return due dates.

- **Medical Expense Deductions.** If you think your itemized deductions this year could likely exceed your standard deduction of $27,700 if filing jointly ($13,850 if single), but you do not expect your itemized deductions to exceed your Standard Deduction next year, you could save taxes in the long run by accelerating elective medical expenses (e.g., braces, new eyeglasses, etc.) into 2023. **Planning Alert!** For 2023, you are allowed to take a medical expense itemized deduction only to the extent your aggregate medical expenses exceed 7.5% of your AGI.

- **$10,000 Cap On State And Local Taxes.** **From 2018 through 2025,** your aggregate itemized deduction for state and local real property taxes, state and local personal property taxes, and state and local income taxes (or sales taxes if elected) is **limited to $10,000** ($5,000 for married individuals filing separately). Foreign real property taxes are not deductible at all unless the taxes are paid in connection with a business or in an activity for the production of income. You are still allowed a full deduction (i.e., an above-the-line deduction) for state, local, and foreign **property** or **sales** taxes paid or incurred in carrying on your **trade or business** (e.g., your Schedule C, Schedule E, or Schedule F operations).

  **Planning Alert!** Most states have enacted legislation allowing partnerships and S corporations to elect to pay state and local income taxes on the partnership's or S corporation's income. If this election is made, the state and local taxes paid by the partnership or S corporation are deductible by the entity and reduce the income flowing through to the partners or shareholders. This treatment may be beneficial to owners who have state and local taxes above the $10,000 cap discussed above. If the entity pays the state and local income taxes on its income, the owner does not pay tax on the same income. States either give the partners or S corporation shareholders a state credit or deduction on their personal returns for the state and local tax paid or income reported by the entity. Interestingly, the IRS has approved this avoidance of the $10,000 limitation for state and local taxes on partnership and

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S corporation income. Please give us a call if you would like to know more about your state's law allowing state and local taxes to be paid by the partnership or S corporation.

- **Limitations On The Deduction For Interest Paid On Home Mortgage "Acquisition Indebtedness."** Before the Tax Cuts And Jobs Act (TCJA), individuals were generally allowed an *itemized* deduction for home mortgage interest paid on up to $1,000,000 ($500,000 for married individuals filing separately) of **"Acquisition Indebtedness"** (i.e., funds borrowed to purchase, construct, or substantially improve your principal or second residence and secured by that residence). Subject to certain transition rules, TCJA reduced the dollar cap for **Acquisition Indebtedness incurred after December 15, 2017, from $1,000,000 to $750,000** ($375,000 for married filing separately) for **2018 through 2025.** Generally, any Acquisition Indebtedness incurred on or before December 15, 2017, is "grandfathered" and will still carry the $1,000,000 cap. Moreover, subject to limited exceptions, if you incurred *Acquisition Indebtedness* on or before December 15, 2017 (i.e., grandfathered Acquisition Indebtedness), the refinancing of that indebtedness after December 15, 2017, will still be entitled to the $1,000,000 cap (to the extent of the outstanding balance of the original *Acquisition Indebtedness* on the date of the refinancing). **Caution!** The $750,000 cap that generally applies to Acquisition Indebtedness incurred after December 15, 2017, is reduced by the outstanding balance of any grandfathered Acquisition Indebtedness. **Planning Alert!** If you think your itemized deductions this year could likely exceed your *Standard Deduction*, paying your January 2024 qualifying home mortgage payment **before 2024** should shift the deduction on the interest portion of that payment **into 2023.**

- **"Home Equity Indebtedness" Suspended For 2018 Through 2025.** TCJA suspended the deduction for **interest** with respect to **"Home Equity Indebtedness"** (i.e., up to $100,000 of funds borrowed that do not qualify as Acquisition Indebtedness but are secured by your principal or second residence). **Caution!** Unlike the interest deduction for Acquisition Indebtedness, TCJA **did not grandfather** any interest deduction for **Home Equity Indebtedness** that was **outstanding before 2018. Planning Alert!** A loan that has been labeled by your lender as a home equity loan, home equity line of credit (HELOC), or second mortgage on a Qualified Residence may, in certain situations, be classified as **Acquisition Indebtedness.** This would be the case where the borrowed funds were used to **substantially improve** your Qualified Residence that secures the loan. For example, assuming you have not exceeded the dollar caps on Acquisition Indebtedness, you will still be able to deduct the interest on a second mortgage taken out as a home improvement loan so long as the improvement: **1) Adds to the value** of your home that secures the second mortgage, **2) Prolongs** your **home's useful life,** or **3) Adapts** your home to **new uses. Caution!** These new rules can be tricky. We suggest that you talk with us before you sign off on a new mortgage: to buy your main house, to buy a second home, to place a second mortgage on your existing home, or to refinance your existing home mortgage. We will gladly review your situation and determine if there are ways to structure the loan that maximizes your interest deduction.

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**Postponing Taxable Income May Save Taxes.** Generally, deferring taxable income from 2023 to 2024 may also reduce your income taxes, particularly if your effective income tax rate for 2024 will be lower than your effective income tax rate for 2023. Moreover, deferring income from 2023 to 2024 may provide you with the same tax benefits listed previously when you accelerate deductions into 2023 (i.e., Freeing up other deductions and tax credits that phase out as your adjusted gross income or modified adjusted gross income increases; Reducing your modified adjusted gross income below the income thresholds for the 3.8% Net Investment Income Tax; Reducing your household income to a level that allows a "refundable" Premium Tax Credit; or, Reducing your taxable income to a level that maximizes the 20% 199A Deduction). **Planning Alert!** If, after considering all factors, you believe deferring taxable income into 2024 will save you taxes, consider the following:

- **Planning For Tax Rates.** The deferral of income could cause your 2023 taxable income to fall below the thresholds for the highest 37% tax bracket (i.e., $693,750 for joint returns; $578,125 if single). If you have income subject to the 3.8% Net Investment Income Tax (3.8% NIIT) and the income deferral reduces your 2023 modified adjusted gross income below the thresholds for the 3.8% NIIT (i.e., **$250,000 for married filing joint, $125,000 for married filing separate, and $200,000 for all others**), you may avoid this additional 3.8% tax on your investment income. In addition, if you reduce your

modified adjusted gross income below the NIIT thresholds above, you may not be subject to the **additional Medicare tax of 0.9%.** **Caution!** If your employment wages and/or self-employment income for 2023 are greater than $250,000 for married filing joint, $125,000 for married filing separate, and $200,000 for all others, it may be necessary, especially if you have multiple employers during 2023, to adjust your withholding for the additional Medicare tax before year-end. If you are self-employed, you may need to adjust your final federal estimate, in January 2024, for the additional Medicare tax.

- **Deferring Self-Employment Income.** If you are a self-employed individual using the cash method of accounting, consider delaying year-end billings to defer income until 2024. **Planning Alert!** If you have already received the check in 2023, deferring the deposit of the check does not defer the income. Also, you *may not* want to defer billing if you believe this will increase your risk of not getting paid.

## TAX PLANNING FOR INVESTMENT INCOME (INCLUDING CAPITAL GAINS AND NIIT)

**Planning With The 3.8% Net Investment Income Tax (3.8% NIIT).** The **3.8% Net Investment Income Tax (3.8% NIIT)** applies to the Net Investment Income of higher-income individuals. This tax applies to individuals with modified adjusted gross income exceeding the following **thresholds: $250,000 for married filing jointly; $200,000 if single; and $125,000 if married filing separately.** The 3.8% NIIT is imposed upon **the lesser of** an individual's: **1)** Modified adjusted gross income in excess of the **threshold,** or **2)** Net investment income. **Note! Trusts and estates** are also subject to the **3.8% NIIT** on the **lesser of: 1)** The adjusted gross income of the trust or estate in excess of $14,450 (for 2023), or **2)** The undistributed net investment income of the trust or estate. The 3.8% NIIT not only applies to traditional types of investment income (i.e., interest, dividends, annuities, royalties, and capital gains), it also applies to "business" income that is taxed to a "passive" owner (as discussed in more detail below) unless the passive income is subject to S/E taxes. If you believe that the 3.8% NIIT may apply to you, consider the following planning techniques:

- **Shifting To Investments That Generate Income Exempt From The 3.8% NIIT.** Fortunately, the following types of income are **not subject** to the 3.8% NIIT: **tax-exempt bond interest; gain on the sale of a principal residence** otherwise excluded from income under the **home-sale exclusion** rules (i.e., up to $250,000 on a single return, up to $500,000 on a joint return); and **distributions from qualified retirement plans** (e.g., 401(k) plans, IRAs, §403(b) annuities, etc.). **Tax Tip!** Investments that generate tax-exempt income (e.g., tax exempt municipal bonds) potentially provide higher-income individuals with a double benefit: **1)** The interest will not be included in the individual's modified adjusted gross income, thus reducing the chance that the individual will exceed the income thresholds for the 3.8% NIIT, and **2)** The tax-exempt interest itself is exempt from the 3.8% NIIT as well as from Federal income taxes. **Planning Alert!** Although taxable distributions from qualified retirement plans (e.g., IRAs, 401(k) plans, etc.) are exempt from the 3.8% NIIT, the taxable distributions will increase your modified adjusted gross income. Therefore, to the extent the taxable distributions cause your modified adjusted gross income to exceed the thresholds for the 3.8% NIIT (e.g., $250,000 for joint returns; $200,000 for singles), the distributions could cause your other net investment income (e.g., dividends, interest, capital gains, rents, passive income) to be hit with the 3.8% NIIT.

- **Roth IRAs (Including Roth IRA Conversions).** Tax-free distributions from a Roth IRA are exempt from the 3.8% NIIT, and do not increase your modified adjusted gross income (and thus will not increase your exposure to the 3.8% tax). Therefore, these tax-favored features should be factored into any analysis of whether you should contribute to a Roth IRA. However, if you are considering converting a traditional IRA into a Roth, the income triggered in the year of conversion would increase your modified adjusted gross income and, therefore, may increase your exposure to the 3.8% NIIT on your net investment income (e.g., dividends, interest, capital gains). **Planning Alert!** If you want a Roth conversion to be **effective for 2023,** you must transfer the amount from the regular IRA to the Roth IRA **no later than December 31, 2023** (you do not have until the due date of your 2023 tax return). **Caution!** Whether you should convert your traditional IRA to a Roth IRA can be an exceedingly complicated issue, and the 3.8% NIIT is just one of many factors you should consider. **Please call us** if you need help in deciding whether to convert to a Roth IRA.

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- **Tax-Deferred Investments.** The 3.8% NIIT does not apply to earnings generated by a **tax-deferred annuity** (TDA) contract **until the income is distributed.** Thus, after first considering the economics, investing in a TDA in your higher-income years may allow you to defer the annuity income until later years when your modified adjusted gross income is below the 3.8% NIIT thresholds.

- **Passive Income.** "Net Investment Income" for purposes of the 3.8% NIIT generally includes net income from a business activity if you are a passive owner (unless the income constitutes self-employment income that is subject to the 2.9% Medicare tax). You will generally be deemed a "passive" owner if you do not "materially participate" in the business as determined under the traditional "passive activity loss" rules. For example, under the passive activity loss rules, you may be a passive owner unless you spend more than 500 hours working in the business during the year or meet one of the other "material participation" tests. Furthermore, rental income is generally deemed to be passive income under the passive activity loss rules, regardless of how many hours you work in the rental activity. **Tax Tip!** In certain situations, real estate rentals may not be treated as passive income and could also be exempt from the 3.8% NIIT. For example, if you are a "qualified real estate professional," or you lease property to a business in which you materially participate, the rental income may be exempt from the 3.8% NIIT. If you believe you may qualify for one of these rental real estate exemptions, or you otherwise believe you may have passive income from non-rental business activities, **please contact our firm.** We will gladly evaluate your situation to determine whether there are steps you could take before the end of 2023 to avoid passive income classification, and thus, reduce your exposure to the 3.8% NIIT.

**Traditional Year-End Planning With Capital Gains And Losses.** Generally, net capital gains (both short-term and long-term) are potentially subject to the 3.8% NIIT. This could result in an individual filing a joint return with taxable income for 2023 of **$553,850 or more ($492,300 or more if single)** paying Federal income tax on **net long-term capital gains** at a **23.8%** rate (i.e., the maximum capital gains tax rate of 20% plus the 3.8% NIIT). In addition, an individual's **net short-term capital gains** could be taxed as high as **40.8%** (i.e., 37% plus 3.8%), for Federal income tax purposes. Consequently, traditional planning strategies involving the timing of your year-end sales of stocks, bonds, or other securities continue to be as important as ever. The following are time-tested, year-end tax planning ideas for sales of capital assets. **Planning Alert!** Always consider the **economics of a sale or exchange first!**

- **Zero Percent Tax Rate For Capital Gains And Dividends.** For individuals filing a **joint return** with 2023 taxable income of **less than $89,250 (less than $44,625 if single),** their long-term capital gains and qualified dividends are taxed at a **zero percent rate. Tax Tip!** Individuals who have historically been in higher tax brackets but are now expecting a significant drop in their 2023 taxable income, may find themselves in the zero percent tax bracket for long-term capital gains and qualified dividends for the first time. For example, a significant drop in 2023 taxable income could have occurred because you are between jobs; or you recently retired; or you are expecting to report higher-than-normal business deductions in 2023. **Planning Alert!** If you are experiencing any of these situations, **please call us** and we will help you determine whether you can take advantage of this zero percent tax rate for long-term capital gains and qualified dividends. If you wait too late to contact us, you may run out of time before the end of this year to take the recommended steps to maximize your tax savings.

- **Lower-Income Retirees.** The zero percent rate for long-term capital gains and qualified dividends is particularly important to lower-income retirees who rely largely on investment portfolios that generate dividends and long-term capital gains. Furthermore, gifts of appreciated securities to lower-income individuals who then sell the securities could reduce the tax on all or part of the gain from as high as 23.8% to as low as zero percent. **Caution!** If the lower-income individual is subject to the so-called kiddie tax, this planning technique will generally not work.

- **Timing Your Capital Gains And Losses.** If the value of some of your investments is less than your cost, it may be a good time to harvest some capital losses. For example, if you have already recognized capital gains in 2023, you should consider selling securities **prior to January 1, 2024,** that would trigger a capital loss. These losses will be deductible on your 2023 return to the extent of your recognized capital gains, plus $3,000. **Tax Tip!** These losses may have the added benefit of reducing your income and allowing you to qualify for other tax breaks, such as: **1)** The $2,500 American Opportunity Tax

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Credit, **2)** The $2,000 Child Tax Credit, **3)** The Adoption Credit of $15,950, or **4)** The 20% 199A Deduction (discussed in more detail later).

**Planning Alert!** If, within 30 days before or after the sale of loss securities, you acquire the same securities, the loss will not be allowed currently because of the "wash sale" rules (although the disallowed loss will increase the basis of the acquired stock). **Tax Tip!** If you are afraid of missing an upswing in the market during this 61-day period, consider buying shares of a different company in the same sector. Also, there is no wash sale rule for gains. Thus, if you decide to sell stock at a gain to take advantage of a zero capital gains rate, or to absorb capital losses, you may acquire the same securities within 30 days without impacting the recognition of the gain.

- **Planning With Capital Loss Carryforwards.** If you have substantial capital loss carryforwards coming into 2023, consider selling enough appreciated securities **before the end of 2023** to decrease your net capital loss to $3,000. Stocks that you think have reached their peak would be good candidates. All else being equal, you should sell the short-term gain (held 12 months or less) securities first. This will allow your net capital loss (in excess of $3,000) to offset your short-term capital gain, while preserving favorable long-term capital gain treatment for later years. **Planning Alert!** Your net short-term capital gains can be used to free up a deduction for any investment interest you have incurred (e.g., interest you have paid on your margin account). If you eliminate your short-term capital gains by recognizing your short-term capital losses, you may be restricting your ability to deduct your investment interest.

## CONSIDER RECENT CHANGES TO IRAS AND QUALIFIED RETIREMENT PLANS

**Secure Act Imposes A New 10-Year Pay-Out Requirement.** Effective for **individuals dying after 2019,** the Secure Act generally requires a decedent's entire remaining IRA or qualified account balance to be distributed to a named beneficiary, other than an "eligible designated beneficiary", **by December 31 of the 10th year following** the year of the decedent's death. This required 10-year payout does not apply if the named beneficiary is an "eligible designated beneficiary" which includes the decedent's spouse, or an individual with a qualified disability, who is chronically ill, or is no more than 10 years younger than the decedent. If the named beneficiary is a child under age 21, the 10-year pay-out requirement does not kick in until the child reaches age 21. **Planning Alert!** If you currently have an estate plan based on the assumption that the non-spouse beneficiaries of your IRAs or qualified retirement plan accounts will be able to take Required Minimum Distributions (RMDs) over their life expectancies, it might be a good time to review and possibly update your estate plan. We will gladly assist you in determining how this new 10-year payout requirement affects your family's tax planning.

**Planning Alert!** On February 23, 2022, the IRS issued proposed regulations interpreting this new 10-year rule for beneficiaries that are not "eligible designated beneficiaries." The proposed regulations proposed to require beneficiaries of a decedent dying **on or after the decedent's required beginning date** (April 1st following age 72 or following age 73 for those turning 72 after 2022) to begin required minimum distributions (RMDs) in the calendar year following the year of the decedent's death and also required any remaining account balance of that beneficiary to be distributed to the beneficiary by the end of the 10th calendar year following the year of the decedent's death. However, the proposed regulations allowed beneficiaries who were not "eligible beneficiaries" of a decedent dying **before the decedent's required beginning date** to take distributions in any manner as long as the entire account balance of the beneficiary was distributed by the end of the 10th calendar year following the year of the decedent's death. Most believed a beneficiary that was not an "eligible designated beneficiary" was not required to take a distribution prior to the 10th calendar year following the decedent's death whether the decedent died before or after the decedent's required beginning date. Even the IRS's own publication seemed to say that was the case. The interpretation in the proposed regulations meant that non-eligible beneficiaries of a decedent who died in 2020 or 2021 after the decedent's required beginning date would have a 50% penalty if RMDs were not made in 2021 for beneficiaries of decedents dying in 2020 and in 2022 for decedents dying in 2021. **In October 2022, the IRS issued Notice 2022-53** providing that this provision in the proposed regulations will not be effective prior to 2023. In addition, the IRS said that beneficiaries who are not "eligible designated beneficiaries" of individuals dying in 2020 or 2021 on or after the decedent's required beginning date will not be penalized for failing to take an RMD in 2021 or 2022.

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**Update!** In July of this year, the IRS released **Notice 2023-54** which **says the proposed RMD regs will not be effective any earlier than 2024**. The Notice also extends the relief provided by Notice 2022-53 to RMDs required in 2023. In other words, where an employee or IRA account owner died in 2022 on or after the required beginning date, a beneficiary who is subject to the 10-year rule will not be penalized for failing to take a distribution in 2023.

**Planning For Rollovers By Surviving Spouses.** The 10-year payout requirement does not apply to a surviving spouse who is the named beneficiary of the decedent's IRA or qualified retirement plan. In that event, the surviving spouse would generally treat the IRA as an inherited IRA and would be required to take RMDs over the surviving spouse's *single life expectancy* (with no 10-year payout requirement). However, it is generally advisable for the surviving spouse to roll the decedent's qualified plan or IRA account into the name of the surviving spouse (i.e., convert it into a spousal IRA). This is generally advisable because, once the decedent's qualified plan or IRA account is converted to a spousal IRA: **1)** The surviving spouse will not be required to begin taking RMDs until the April 1st following the year the surviving spouse reaches age 72 (age 73 if surviving spouse turned **72 after December 31, 2022,** and **age 73 before January 1, 2033),** and **2)** When the RMDs begin, the surviving spouse's RMDs will be determined using the *Uniform Lifetime Distributions Table* (with no 10-year payout requirement), which will result in a smaller annual required payout than under the single life expectancy computation that would otherwise be required had the surviving spouse not converted the decedent's qualified plan or IRA account into a spousal IRA. **Caution!** If you (as surviving spouse) are not yet 59 ½, leaving the IRA or qualified plan account in the name of your deceased spouse (and not converting it to a spousal IRA) may actually be the better option if you think you will need to withdraw amounts from the retirement account before you reach age 59 ½. Otherwise, if your deceased spouse's account is transferred into your name as a spousal IRA and you take a distribution before reaching age 59 ½, the distribution could be subject to a 10% early distribution penalty.

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## SELECTED MISCELLANEOUS YEAR-END PLANNING CONSIDERATIONS

**Contributing The Maximum Amount To Your Traditional IRA.** As your income rises and your marginal tax rate increases, deductible IRA contributions generally become more valuable. Also, making your deductible contribution to the plan as early as possible generally increases your retirement benefits. As you evaluate how much you should contribute to your IRA, consider the following limitations. If you are married, even if your spouse has no earnings, you can generally deduct in the aggregate up to **$13,000 ($15,000 if you are both at least age 50 by the end of the year)** for contributions to you and your spouse's traditional IRAs. You and your spouse must have *combined earned income* at least equal to the total contributions. However, no more than **$6,500 ($7,500 if at least age 50)** may be contributed to either your IRA account or your spouse's IRA account for 2023. If you are an active participant in your employer's retirement plan during 2023, your IRA deduction is reduced ratably as your adjusted gross income increases from **$116,000 to $136,000** on a joint return **($73,000 to $83,000** on a single return). However, if you file a joint return with your spouse and your spouse is an active participant in his or her employer's plan and you are not an active participant in a plan, your IRA deduction is reduced as the adjusted gross income on your joint return goes from **$218,000 to $228,000. Caution!** Every dollar you contribute to a deductible IRA reduces your allowable contribution to a nondeductible Roth IRA. The sum of your contributions for the year to your Roth IRA and to your traditional IRA may not exceed the $6,500/$7,500 limits discussed above. For 2023, your ability to contribute to a Roth IRA is phased out ratably as your adjusted gross income increases from **$218,000 to $228,000** on a joint return or from **$138,000 to $153,000** if you are single. **Planning Alert!** Unlike the rule for traditional IRA contributions, the amount you may contribute to a Roth IRA is reduced if your adjusted gross income falls within these phase-out ranges regardless of whether you or your spouse is a participant in another retirement plan. In addition, contributions to a Roth IRA are not deductible. **Planning Alert!** You have until **April 15, 2024,** to make a 2023 traditional IRA contribution.

**Contributing The Maximum Amount To Your 401(k).** Participants have until December 31st to contribute to their 401(k). For 2023, the maximum contribution amount is **$22,500 ($30,000 if at least 50 years old).** Contributions to your 401(k) will decrease your current year taxable income and add to your retirement savings.

**If You Are 70½ Or Older By December 31st, Consider A Qualified Charitable Distribution (QCD).** A Qualified Charitable Distribution (QCD) allows a donation to a charitable organization of up to $100,000 from a traditional IRA. These contributions are excluded from income and count toward your RMD for 2023.

**<u>Caution!</u>** These contributions are not deductible as itemized deductions. However, if you normally take the standard deduction, a QCD could be even more beneficial since the distribution will be excluded from your income.

**<u>IRS Increases Standard Mileage Rates Effective January 1, 2023.</u>** The standard mileage deduction rate for your deductible **business miles** was increased from 62.5 cents per mile to **65.5 cents per mile** effective January 1, 2023. The **charitable mileage rate is still 14.0 cents per mile** and the rate for **medical and moving mileage remained at 22.0** cents per mile for 2023. **<u>Planning Alert!</u>** Be sure to keep proper records for business, medical/moving, and charitable mileage for use as a possible deduction for 2023.

**<u>The 20% 199A Deduction For Qualified Business Income.</u>** Don't overlook the **20% Deduction** under **Section 199A (20% 199A Deduction)** with respect to **"Qualified Business Income," "Qualified REIT Dividends,"** and **"Publicly-Traded Partnership Income."** The 20% 199A deduction does not reduce your adjusted gross income or impact your calculation of self-employment tax. Instead, the deduction simply reduces your taxable income (regardless of whether you itemized deductions or claim the standard deduction). In other words, the 20% 199A Deduction is allowed ***in addition to*** your itemized deductions or your standard deduction. **<u>Note!</u>** The 20% 199A Deduction **expires after 2025!**

- **<u>What Type Of Income Qualifies For The 20% 199A Deduction?</u>** Generally, the following types of income are eligible for the 20% 199A Deduction: *Qualified REIT Dividends*, *Qualified Publicly-Traded Partnership Income*, and *Qualified Business Income*. The rules for determining the 20% 199A Deduction for Qualified REIT Dividends and Publicly-Traded Partnership Income are relatively straightforward. However, the 20% 199A Deduction for **Qualified Business Income** (QBI) is by far having the biggest impact on the greatest number of individual taxpayers and can be complicated and tricky.

- **<u>Who Can Qualify For The 20% 199A Deduction For Qualified Business Income (QBI)?</u>** Taxpayers who may qualify for the 20% 199A Deduction generally include taxpayers who report Qualified Business Income from a trade or business such as: Individual owners of S corporations and partnerships; Sole Proprietors; Trusts and Estates; and Certain beneficiaries of trusts and estates. It is not feasible to provide a thorough discussion of the 20% 199A Deduction with respect to **Qualified Business Income (QBI)** in this letter. However, if you own an interest in a business as a sole proprietor, an S corporation shareholder, or a partner in a partnership, you are a very good candidate for the 20% 199A Deduction. If you want more information on the 20% 199A Deduction, **please call our firm** and we will be glad to provide you with more details.

**<u>No Deduction For Expenses Of A "Hobby".</u>** Before the 2017 Tax Cuts and Jobs Act, otherwise deductible trade or business expenses attributable to an activity that was *"not engaged in for profit"* (i.e., a hobby loss activity) were deductible: **1)** only as *miscellaneous itemized deductions,* and **2)** only to the extent of the activity's gross income. Since these hobby loss expenses are classified as miscellaneous itemized deductions, no deduction is allowed for these expenses ***from 2018 through 2025.*** **<u>Planning Alert!</u>** This makes it even more important for owners engaged in activities commonly subject to IRS scrutiny, to take steps to demonstrate the business is operated with the intent to make a profit.

- **<u>Three Out Of Five Year Rule Or Two Out Of Seven Year Rule.</u>** To reduce the potential controversy over the question of profit motive, Congress provided that if an activity generates gross income more than expenses in three years out of five (two years out of seven in the case of raising, showing or racing horses) the activity is presumed to be engaged in for profit. **<u>Planning Alert!</u>** If the IRS challenges your business losses for the first few years of activity, let us know. We may be able to make an election to extend the statute and prevent a "hobby loss" disallowance until the business has been operating for five years (seven years for a horse activity).

- **<u>Protecting Against Hobby Classification.</u>** To avoid a loss of all deductions related to a business activity that is not profitable, you should: **1)** investigate the potential profitability of a new business activity and document the investigation before entering into the business; **2)** prepare a business plan before entering into a new business activity; **3)** maintain a separate business bank account and good books and records; and **4)** document any changes made and persons consulted to help produce a profit. **Please call us if you need help with this process.**

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**Lower Form 1099-K Threshold For 2023 Transactions.** For each calendar year between 2010 and 2022, Payment Settlement Entities have been required to file Form 1099-K annually with the IRS with respect to payees and furnish information to the payees, reporting the gross amount of reportable payment transactions. **However, prior to 2023,** third-party settlement organizations were not required to file Form 1099-K where: **1)** the payee had **200 or fewer otherwise reportable transactions** during the calendar year and **2)** the **gross amount of such transactions during the calendar year was $20,000 or less.**

- **American Rescue Plan Act Changed The 1099-K Reporting Threshold To $600.** The American Rescue Plan Act lowered the exception from filing Form 1099-K by Payment Settlement Entities to gross payments of **$600 or less, with no minimum number of transactions. The new $600 reporting threshold applies beginning with 2023 transactions.**

- **Caution!** The American Rescue Plan Act provided that only payments for goods and services are reportable third-party network transactions. Payment services such as PayPal and Venmo generally allow users to designate a payment as personal. The Taxpayer Advocate Service advises taxpayers to *"Be sure to ask those friends or family members to correctly designate the payment as a non–business-related transaction and then make a note yourself of what the payment was for and from whom it was received."*

**Gift And Estate Tax Planning.** For 2023, a donor can **gift $17,000** to each donee. It is not a taxable gift to the donor and gifts are not included in the recipient's income. That exclusion amount will **go to $18,000 in 2024. Each taxpayer's** amount of unified credit if **used against gift tax or estate tax is $12,920,000 for 2023 and is scheduled to go to $13,610,000 in 2024. Planning Alert!** Using the annual gift tax exclusion (i.e., $17,000 for 2023) is an effective tool to move assets out of your estate without creating any gift tax or using any of an individual's unified credit amount.

**Social Security Tax Wage Base.** It may be worth noting that **for 2023,** wages and self-employment income subject to the 15.3% Social Security Tax is **$160,200,** which is an increase from $147,000 in 2022.

**Use The IRS Tax Withholding Estimator To Avoid Surprises.** As you get to the end of 2023, it's a good idea to revisit your withholding and estimated tax payments to avoid an unexpected tax bill which could include penalties and interest. The IRS encourages taxpayers to use its Tax Withholding Estimator at https://www.irs.gov/individuals/tax-withholding-estimator to ensure they have the correct amount of taxes paid-in before December 31st. **Planning Alert!** It is especially important to review your withholding if you have had a significant event occur during 2023 such as a job change or loss, additional income stream, marriage, divorce, etc. If you believe your tax liability has been affected because of a significant event, and you have questions, **please call our firm** so we can discuss.

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## FINAL COMMENTS

Please contact us if you are interested in a tax topic that we did not discuss. Tax law is constantly changing due to new legislation, cases, regulations, and IRS rulings. Our Firm closely monitors these changes. In addition, please call us before implementing any planning ideas discussed in this letter, or if you need additional information. **Note!** The information contained in this material should not be relied upon without an independent, professional analysis of how any of the items discussed may apply to a specific situation.

**Disclaimer:** Any tax advice contained in the body of this material was not intended or written to be used, and cannot be used, by the recipient for the purpose of promoting, marketing, or recommending to another party any transaction or matter addressed herein. The preceding information is intended as a general discussion of the subject addressed and is not intended as a formal tax opinion. The recipient should not rely on any information contained herein without performing his or her own research verifying the conclusions reached. The conclusions reached should not be relied upon without an independent, professional analysis of the facts and law applicable to the situation.