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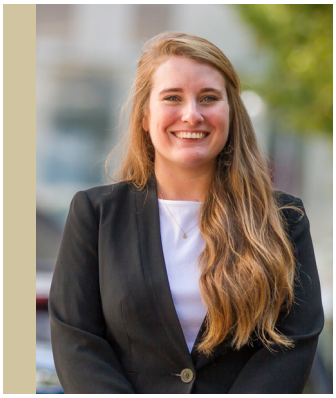
DECEMBER 11, 2020

Year End Tax Planning Tips

THERE'S STILL TIME! TOP 10 ITEMS TO DISCUSS WITH YOUR TAX ADVISOR BEFORE YEAR END



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With the end of 2020 in sight, don't miss out on last-minute tax planning items that could impact your financial situation for years to come.

Suspension of Required Minimum Distributions

- The CARES Act suspended Required Minimum Distributions (RMDs) from retirement accounts for 2020.
- RMDs will likely resume in 2021 for taxpayers who turned 70 ½ before January 1, 2020. Taxpayers under this age will not be required to take RMDs until age 72.
- If you typically have taxes withheld from your RMDs you may need to make this up by making quarterly tax payments. Both the IRS and state taxing authorities assess interest if minimum payment amounts are not met during the year. Interest continues to accrue until payments are received, so paying late is better than waiting until your return is filed.
- Qualified Charitable Distributions (QCDs) can still be made this year even though RMDs are suspended. Individuals can give up to $100,000 per year and donations must be made directly from your IRA to a qualified charity. The amount of the QCD is excluded from taxable income and is not deductible. QCDs must be made by December 31st.

Retirement Planning & Roth Conversion

- 401(k) contributions for employees and contributions into Solo 401(k)s for self-employed individuals are due by December 31st. For 2020, employees can contribute up to $19,500 into a 401(k), and Solo 401(k) plan owners can also contribute up to an additional 25% of their net self-employment income as a profit-sharing contribution. Total contributions into a Solo 401(k) are limited to $57,000 for the year.
- Taxpayers age 50 or above can also make catch-up contributions of up to $6,500 to a 401(k) plan or Solo 401(k) plan.
- SEP contributions for self-employed individuals can be made up to the filing date of the tax return, including extensions. SEP contributions are limited to the

lesser of 25% of net self-employment income or $57,000.

- Consider converting IRA funds to a Roth IRA and paying tax now if you expect to be in a higher tax bracket in the future. However, be cautious of other items that may be impacted by a conversion, such as capital gains tax rates and taxable Social Security income.

Working Remotely Due to COVID-19

- The Tax Cuts & Jobs Act eliminated the deduction for employee business expenses, including home office expenses for wage-earners. If you are a W-2 employee, the home office expense deduction will likely not be available to you even if you are working from home this year due to the pandemic.
- Self-employed taxpayers may be able to take a home office deduction against their business income. To qualify the space must be regularly and exclusively used as a home office, and it must be the principal place of your business. A desk in your guest room or your dining room table likely will not qualify.
- Taxpayers with a qualifying home office can use the Simplified Method, deducting $5 per square foot up to 300 square feet total, or prorate their actual expenses based on the square footage of the home used for business.
- Be aware of potential state tax implications of remote work. Employees who live and work in different states should look for state guidance regarding where this income will be taxable. Check with your employer to ensure that they are aware of your remote location and that tax is being withheld to the correct state.
- Employers should also check with their state taxing authority regarding withholding compliance. Employees working remotely could also impact state tax nexus and trigger a filing requirement for companies in states where they have employees located.

Tax Loss Harvesting

- If taxpayers have recognized capital gains in their portfolio this year, consider tax loss harvesting before year-end to reduce the net realized gains. If net capital losses exceed net capital gains, deductible losses are limited to $3,000 per year. Any remaining capital losses are carried forward indefinitely. Short-term capital gains are generally taxed at a higher federal income tax rate than long-term capital gains, so offsetting short-term capital gains with capital losses can be especially beneficial.

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- Any positions sold and repurchased within 30 days are considered a wash sale and the losses will not be deductible.

Charitable Giving

- The CARES Act increased limits on cash charitable gifting. Previously, taxpayers were limited to a deduction each year of up to 60% of Adjusted Gross Income (AGI) for cash gifts to qualified charities. In 2020, this limit is temporarily increased to 100% of AGI for any donations directly to charities.
- The CARES Act also created an above-the-line deduction up to $300 for cash gifts to qualified charities for taxpayers who do not itemize deductions. The $300 limit is applied per filing, so single and joint filers are both capped at this amount. Taxpayers should provide their tax preparers with information on cash charitable contributions for 2020 even if they typically take the standard deduction.
- For taxpayers who do not always itemize deductions or are facing a high-income year, consider bunching charitable donations while creating more flexibility in your charitable gifting through a Donor Advised Fund (DAF). Contributions to a DAF are deductible in the year the contribution is made, then the funds can be invested and grow tax-free as grants are made over time.
- Consider gifting appreciated securities instead of cash when possible. This results in a double tax benefit as taxpayers forgo taxes on the unrealized gains, while receiving an itemized deduction for the fair market value of the stock up to 30% of taxpayers' AGI.

Education Planning

- 529 College Savings Plans enable taxpayers to make cash contributions to a tax-advantaged education savings plan on behalf of a beneficiary. Investments inside the 529 plan grow tax free and distributions are tax free to the extent used to cover qualified education expenses. The Tax Cuts and Jobs Act of 2017 expanded the definition of qualified education expenses to include up to $10,000 per student per year for private elementary and secondary education. The SECURE Act, which was passed in December 2019, further expanded qualified use of 529 funds to include paying off up to $10,000 of student loan debt. This limit applies per lifetime, but it can apply to more than one student. Many states offer tax deductions for contributions into a 529 plan; these opportunities vary by state.
- A Coverdell Education Savings account is similar to a 529 plan and can be used to pay either

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qualified higher education expenses or qualified elementary or secondary education expenses. These accounts provide a wider range of control in investments compared to 529 plans. However, there are income limits for those who make the contribution to the account, and contributions are limited to $2,000 per beneficiary per year.

- Taxpayers may be eligible to take a deduction or credit for qualified tuition and related expenses. The American Opportunity Tax Credit, Lifetime Learning Credit, Tuition and Fees Deduction, or Student Loan Interest Deduction are all available for the 2020 tax year. Each incentive has its own requirements and income limitations for qualification. The IRS provides an interactive tool on their website which can be used to determine whether you may be eligible to claim any of these credits.

Health Savings Accounts

- A Health Savings Account (HSA) is a great savings vehicle that allows taxpayers to set aside pre-tax funds to pay for medical expenses. The funds do not expire but rather "roll over" each year if they are not spent, and the account may earn interest or other tax-free earnings. If the funds are used to pay for qualified medical expenses, the distributions are generally not taxable. Taxpayers are only eligible to contribute to an HSA if they have a High Deductible Health Plan. For 2020, the minimum deductible for a high deductible health plan to qualify for use with an HSA is $1,400 for self-only coverage or $2,800 for family coverage, however plan policies may vary so confirm with your plan administrator that your specific plan qualifies before setting up an account. The maximum annual deductible contribution to an HSA is $3,550 for self-only or $7,100 for family coverage. If taxpayers are over age 55, they can make catch-up contributions of $1,000 per year. Contributions may be made until April 15, 2021 to be applied for the 2020 tax year.

Timing of Business Income & Deductions

- Cash basis taxpayers should consider timing of invoicing and payment for year-end income and expenses for purposes of accelerating or delaying income and deductions in the 2020 tax year.
- Consider purchasing and placing into service necessary equipment purchases before year-end to take advantage of 100% bonus depreciation or Section 179 expensing. Bonus depreciation is now available on both new and used property.
- The CARES Act retroactively fixed language in the Tax Cuts and Jobs Act of 2017, providing a 15-

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year depreciable life on qualified improvement property making this property eligible for 100% bonus depreciation. Generally, qualified improvement property is any internal improvement to a nonresidential building that is not related to enlargement of the building, does not involve elevators or escalators, and is not related to the internal structural framework of a building. Taxpayers may file an accounting method change in 2020 to adjust the deduction retroactively for tax years 2018 and 2019.

Paycheck Protection Program (PPP)

- As part of the CARES Act, many small businesses received forgivable loans in 2020 through the Small Business Administration's Paycheck Protection Program (PPP). The IRS and the Treasury provided additional guidance in November to PPP Loan recipients. For recipients that qualify for forgiveness, the income associated with the forgiveness is tax-free, however any expenses paid with PPP funds are not deductible for tax purposes. This applies even if the PPP loan recipient has not applied for forgiveness before year-end but intends to do so in the next taxable year. Legislation has been introduced challenging this treatment.

Estate & Gift Tax Considerations

- The current estate and gift tax exemption is $11.58 million. If the value of a decedent's estate plus the total of lifetime taxable gifts is over this amount, the excess is subject to federal estate tax at 40%.
- Biden's tax proposals include reducing the gift and estate tax exemption from $11.58 million to $3.5 million and eliminating the step-up in basis for inherited assets.
- Outright gifts of up to $15,000 per person per year are exempt from gift tax. This amount applies to each donor and each recipient. If gifts are made from joint funds donors should write separate checks, otherwise a gift tax return may be required.

2020 has brought many changes in all our lives, including new implications with tax planning. Every taxpayer's situation is different, so make sure to work closely with your advisors to ensure alignment with your overall financial goals.

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