Year-End Tax Planning

Keeping up with the complex credit landscape can be difficult for organizations with limited resources. The Tax Cuts and Jobs Act (TCJA) adds another level of complexity to tax planning. In this article, we have outlined how the TCJA will impact key tax provisions and tax minimizing strategies.

Alternative Minimum Tax

Alternative minimum tax (AMT) should be considered before you and/or your accountant begin to time income and deductions. AMT is a separate tax system that limits some deductions and disallows others, such as state and local income tax deductions, property tax deductions, and other miscellaneous itemized deductions that are subject to the 2% of AGI. Deductions include investment advisory fees and non-reimbursable employee business expenses.

The purpose of the AMT is to ensure those who receive a lot of tax breaks are still paying some level of federal income taxes. The AMT, originally intended to target high-income households, became problematic once it began affecting more and more taxpayers. Failing to account for inflation, the AMT began to impact middle-income households as wages increased.

To ensure that the AMT functions properly, the Tax Cuts and Jobs Act:

- Increases the AMT exemption amounts
- Raises the phaseout thresholds for these exemptions
- Permanently indexes the exemptions for inflation going forward

Under the Tax Cuts and Jobs Act, fewer taxpayers will be affected by the alternative minimum tax. Speak with your tax professional regarding the changes made to the AMT exemption amounts.

Timing Income and Expenses

Timing is everything when it comes to income and expenses. Smart timing will reduce your tax liability, while poor timing can unnecessarily increase it.

If you don't expect to be subject to AMT in the current or following year, consider income deferment. Deferring income and increasing deductible expenses for the current year is typically a good idea because it will postpone tax. If you expect to be in a higher tax bracket, or if tax rates are expected to increase, the opposite approach rings true.

Whatever the reason for timing your income and deductions, here are some income items you may be able to control:

- Bonuses
- Consulting or other self-employment income
- U.S. Treasury bill income

- Retirement plan distributions (to the extent they won't be subject to early withdrawal penalties)

Followed by potentially controllable expenses:

- State and local income taxes
- Property taxes
- Mortgage interest
- Margin interest
- Charitable contributions

Charitable Donations

Good deeds in the form of cash or in-kind items can reap great tax benefits. While the new tax reform does not eliminate charitable deductions, it does limit the tax incentive for charitable contributions. The new plan increases the standard deduction and reduces the tax bracket, meaning fewer people will itemize their deductions.

There are several giving strategies to consider, including:

1. **Bunching.** Taxpayers whose itemized deductions fall short of the standard deduction should consider bunching their charitable contributions every other year. This idea works out very well for donors, allowing those who fall below the deduction threshold to exceed it every other or every third year.
2. **Donor-Advised Funds (DAF).** The itemized donor gives an initial, larger gift to a donor-advised fund and receives the allowed tax deduction. The contribution grows tax-free and serves as a charitable fund from which the taxpayer can recommend gifts to charity in subsequent years.
3. **Charitable Gifts.** Under the new tax law, donors can still take an income tax deduction on the full fair market value of appreciated assets that have been gifted to charity.
4. **IRAs.** Taxpayers 70.5 years of age and older can request a distribution of up to $100,000 per year directly from their IRAs to charity. This gift would help satisfy the annual required distributions from the IRA and be removed from the donor's taxable income.

Before making a large donation to the charity of your choosing, discuss options with your tax professional.

Healthcare Breaks

The Tax Reform and Jobs Act changed the AGI threshold for medical expenses from 10% to 7.5% for 2017 and 2018 for all taxpayers.

If medical expenses were not paid through tax-advantaged accounts or were reimbursable by insurance and exceed 7.5% of your AGI, you can deduct the excess amount. Eligible expenses may include:

- Health insurance premiums
- Long-term care insurance premiums (limits apply)
- Medical and dental services
- Prescription drugs

You may be able to save tax by contributing to one of these accounts:

- **HSA** - You can contribute pretax income to an employer-sponsored Health Savings Account — or make deductible contributions to a personal HSA. For 2018, contributions are $3,450 for self-only coverage and $6,850 for family coverage. As a bonus, if you're age 55 or older, you may contribute an additional $1,000. Like an IRA, HSAs can bear interest or be invested, growing tax-deferred. Balances can be carried over from year to year, and withdrawals for qualified medical expenses are tax-free.
- **FSA** – An employer-sponsored Flexible Spending Account can be used to redirect pretax income. The plan pays or reimburses you for qualified medical expenses, not to exceed $2,650 in 2018. The balance that remains at the end of the year you lose, unless your plan allows you to roll the balance over (up to $500).

Sales Tax Deduction

The state and local tax deduction, or SALT, now has a cap. While it remains in place for those who itemize their taxes, it now has a $10,000 limit. This is a significant change as filers could previously deduct an unlimited amount for state and local property taxes, plus income or sales taxes.

Self-Employment Taxes

As a self-employed taxpayer, you may benefit from other above-the-line deductions. You can deduct 100% of health insurance costs for yourself, your spouse, and your dependents, up to your net self-employment income. You can also deduct retirement plan contributions and, if you're eligible, an HSA. The Self-Employment Health Insurance deduction remained untouched in the Tax Cuts and Jobs Act, however employed taxpayers must itemize on their returns to claim it.

Estimated Payments and Withholdings

You can become subject to penalties if you don't pay enough tax through estimated tax payments and withholding. Here are some strategies to help avoid underpayment penalties:

- Know the minimum payment rules
- Use the annualized income installment method
- Estimate your tax liability and increase withholdings

Tax Credits

Now is also a great time for organizations to re-evaluate their annual budgets to improve profit margins and consolidate spending. One strategy worth exploring is new or revised tax credits to help offset the amount owed to federal and state governments and take advantage of any county or city localized tax credits. Capturing 2018 credits, as well as retroactive 2017 tax credit opportunities, can help your organization reduce its liability, lower its tax rate, and improve the bottom line.

For example, the employer tax credit, which was created by the TCJA, is available to employers who offer paid family and medical leave to their employees who earned $72,000 or less in 2017 or 2018. To qualify, employers must have a written policy that

- covers all workers employed for a year or more,
- provides at least two weeks of annual paid family and medical leave for each full-time qualified employee and offers a proportionate amount of leave for part-time qualified employees, and
- pays at least 50 percent of the employee's wages during the leave.

Whether you are an individual taxpayer or a small business owner, understanding your tax credit eligibility is important.

If you have questions about these or other tax saving tips, please contact one of our professionals to schedule your year-end planning meeting.