

2020 YEAR-END TAX PLANNING CHECKLIST



With the countless challenges we have faced this year, it is understandable that tax planning may not have been top of mind for many of us. The good news is there is still time to consider tax-saving opportunities and develop a plan to reduce your tax and financial burden for 2020.

The Coronavirus Aid, Relief and Economic Security (CARES) Act that was passed in late March 2020 as a means to provide immediate economic relief provides a number of tax-saving possibilities. In addition, the SECURE Act, officially enacted on January 1, 2020, provides changes for retirement savings. And we can't forget the massive Tax Cuts and Jobs Act (TCJA), which went into effect two years ago, but still remains important for year-end tax planning.

Executive Summary

In this guide, we will discuss the following year-end tax planning strategies:

- Benefits of accelerating deductions into 2020 and deferring income into 2021 and when it makes sense to do the opposite
- Planning to maximize your itemized deductions
- Retirement planning for contributions, distributions, and conversions
- Simple estate planning moves to make before year end and next year as well
- Maximizing the qualified business income (QBI) deduction
- Generous asset-expensing opportunities

2020 Tax Planning Opportunities — Individuals

The following section highlights some tax planning opportunities for individual taxpayers. The time-honored tactic of accelerating deductions and deferring income may not always be the best strategy for every taxpayer. It's important to consider target income thresholds to maximize the benefit of deductions (itemized, tuition and fees, student loan interest) and/or the utilization of credits (child credit, education credits) that are based upon a percentage of adjusted gross income or income levels and then plan to shift income or deductions in order to maximize these tax benefits.

For individuals who expect to be in the same or a higher tax bracket - or have higher income - in 2020 than in 2021, it may be advantageous to defer income into the next year. Options to do so this close to year end include:

- **Installment Sales** – If you expect to sell property before the end of 2020, and it makes economic sense, consider selling the property and reporting the gain under the installment method.
- **Delay Billing** – An option for taxpayers utilizing the cash method of accounting.
- **Interest and Dividend** – Since interest earned on CD's or treasury securities with maturities of one year or less are not includible in income until received at maturity, consider buying short term bonds or certificates that will not mature until next year.
- **Year-end Bonuses** – Consider arranging with your employer to defer, until early 2021, a 2020 year-end bonus.

2020 Tax Planning Opportunities — Individuals (Continued)

- On the other hand, if you expect to be in a higher tax bracket in 2021 than you were in 2020, accelerating income into this year may be the advantageous move. Some ways to accelerate income this close to year end include:
 - **Issue Bills and Pursue Collection** – An option for taxpayers utilizing the cash method of accounting.
 - **Interest and Dividends** – If you are not in the highest capital gains bracket for 2020, but you expect to be in 2021 and you have control over when dividends are paid on an investment or from your closely held corporation that pays qualified dividends, consider authorizing such dividends prior to year end.
 - **Year-end Bonuses** – If you receive a year-end bonus that is paid out in the following year, request that the bonus be paid out before year-end.
- Review your investment portfolio: determine if there are losses you can harvest to offset capital gains realized earlier in the year. If you have a capital loss, consider selling investments with gains before year end. These gains will be sheltered from tax by the loss. Control taxable income to less than \$80,000 (married filing joint) to take advantage of the zero capital gains tax rate. Be sure to consult your portfolio advisor, as these steps should only be taken if the results also align with your overall investment plan.
- Even though planning for itemized deductions is made complex by factors such as AGI levels, AMT, filing status, and the increased standard deduction (\$12,400 for single filers, \$24,800 for married filers filing jointly and \$18,650 for heads of household), being familiar with the following concepts will help you navigate some of this complexity and maximize your itemized deduction.
 - **Deduction in Year Paid** – An expense is deductible in the year in which it was paid. Medical expenses and charitable contributions paid with a credit card before year-end will generate a tax deduction in the current year even if the credit card bill is not paid until next year.
 - **Donor-Advised Fund** – Interested in making a significant charitable contribution prior to year-end, but aren't sure what charity you want to donate to? Consider establishing a donor-advised fund. Money contributed to the fund can be deducted in the current year and you can decide later which charity or charities will receive the funds.
 - **Bunching Itemized Deductions** – If your itemized deductions are consistently near the standard deduction, perhaps slightly below or above, consider postponing current year deductible expenses (i.e., charitable contributions) until next year to “bunch” your itemized deductions. Analyze your position from year to year to itemize your bunched itemized deductions in years of high income.
- For 2020, two special rules apply to charitable contributions. First, for taxpayers that do not itemize, a \$300 above-the-line deduction, in addition to the standard deduction, will be allowed for cash contributions to public charities. Second, for taxpayers that itemize, the general 60% of AGI deduction limit for cash gifts has been increased to 100% of AGI.
- Consider donating appreciated stock. You will receive a charitable contribution for the full fair market value and will avoid capital gain on the sale. Different deduction rules may apply to donations of cars, boats, and airplanes.
- If you are age 70½ or older by the end of 2020 and have traditional IRAs, consider making 2020 charitable donations via a qualified charitable distribution directly from your IRA. Such distributions, up to \$100,000 per year, are made directly to charities (excluding donor-advised funds) from your IRA. Although RMD's have been waived for 2020, this is an attractive option for smaller contributions if you are not itemizing deductions, as the amount of the contribution is neither included in your gross income nor deductible as an itemized deduction. (See next item if you contribute to an IRA after age 70½. As discussed below, you'll need to reduce the qualified distribution by the amount of aggregate post 70½ IRA contributions.)

2020 Tax Planning Opportunities — Individuals (Continued)

- Maximize your retirement plan contributions to 401(k)s and IRAs. Maximizing pre-tax retirement contributions is generally a good tax-saving move. Under the SECURE Act, beginning in 2020 individuals can continue to contribute to their IRA's regardless of their age as long as they have earned income. The Act eliminated the ban on contributions after age 70½.
- For 2020 only, the CARES Act waived required minimum distributions (RMD's) for IRAs and retirement plans, including beneficiaries with inherited accounts. If you have not already taken your RMD for 2020, consider forgoing this year's distribution if possible.
- Born after June 30, 1949? Thanks to the SECURE Act, you can wait until the year in which you turn 72 (or until April 1st of the following year) to begin taking your RMD's.
- Consider converting your traditional IRA to a Roth IRA if you anticipate lower income in the current year. The advantage to a Roth IRA is that the future income distributions will not be taxed. The drawback to the conversion is that the amount transferred is subject to tax now. Conversions to a Roth IRA make sense if you anticipate paying higher taxes in the future, if you have a number of years before you might tap into the Roth IRA which gives you a chance to recoup the tax you paid at conversion, and if you will not need the income during retirement and would like to pass it on to your beneficiaries.
- Take advantage of estate planning opportunities still available - make gifts sheltered by the annual gift tax exclusion before year end and save gift and estate taxes. The exclusion applies to gifts of up to \$15,000 made in 2020 to each of an unlimited number of individuals. Married couples can make joint gifts up to \$30,000 per donee. You cannot carry over unused exclusions from one year to the next so don't pass up this year's opportunity. Consider transferring income-earning property to family members in lower income tax brackets. Also, maximize contributions to a Section 529 Plan, which allows the equivalent of five years of gifts (\$75,000) to each beneficiary. Make direct payments to providers for medical expenses and to schools for qualified tuition expenditures. Such payments have no amount cap and can be made in addition to the annual exclusion gifts.

2020 Tax Planning Opportunities — Business Owners

- Manage taxable income to take advantage of the 20% qualified business income (QBI) deduction. For 2020, if taxable income does not exceed \$326,600 (joint filers) or \$163,300 (all other taxpayers), the deduction is generally the lesser of 20% of QBI or 20% of taxable income. Limitations may apply if taxable income exceeds these thresholds. The deduction may be reduced or eliminated if you are engaged in a specified service trade or business (such as law, accounting, or health). If your business is not considered a specified service business and you exceed the income thresholds, your QBI deduction may be limited by the amount of W-2 wages and/or the unadjusted basis of qualified property (such as machinery and equipment) held by the trade or business.
- Consider changing to the cash method of accounting. To qualify, a business must, among other things, satisfy a gross receipts test. This test is satisfied if, during a three-year testing period, average annual gross receipts do not exceed \$26 million. Cash method taxpayers may find it a lot easier to shift income as a tax planning strategy.
- Accelerate Deductions – Consider charging expenses on a credit card, as the deduction will be allowed in 2020 even if the credit card bill is not paid until 2021.
- Consider making expenditures that qualify for the liberalized business property expensing option. For 2020, the expensing limit is \$1,040,000, and the investment ceiling limit (at which point a phase-out begins) is \$2,590,000. Expensing is generally available for most depreciable property (other than buildings) and off-the-shelf computer software. This expensing opportunity is available

2020 Tax Planning Opportunities — Business Owners (Continued)

for qualified improvement property (generally, any interior improvement to a building, but not for enlargement of a building, elevators or escalators, or the internal structural framework) roofs, and nonresidential HVAC, fire protection, alarm, and security systems. The expensing deduction is not prorated for the time that the asset is in service during the year. Thus, property acquired and placed in service in the last days of 2020 will result in a full expensing deduction for the year.

- Businesses may also claim a 100% bonus first-year depreciation deduction for machinery and equipment bought used (with some exceptions) or new if purchased and placed in service this year. The 100% write-off is permitted without any proration based on the length of time that an asset is in service during the tax year. As a result, the 100% bonus first-year write-off is available even if qualifying assets are in service for only a few days in 2020. Note that limits on eligibility may exist for certain auto dealerships with floor plan financing as well as for some real estate ventures.
- As in previous years, businesses, including self-employed individuals and owners of certain real estate, may be able to take advantage of the de minimis safe harbor election to expense the costs of lower-cost assets and materials and supplies.
- For tax years beginning in 2020, businesses can establish and fund a profit-sharing plan up through the extended due date of the 2020 corporate tax return. This allows a tax deduction to the company and jump starts individual retirement savings.
- Excess Loss Limitations – The TCJA limited individuals from using more than \$250,000 (\$500,000 for married filers filing jointly) of business losses to offset nonbusiness income. The CARES Act repealed this limitation for years beginning before January 1, 2021. It may be advantageous to amend your 2018 or 2019 returns if business losses were limited in these years.

These are just some year-end tax planning strategies that you may benefit from, but it is important to keep in mind that tax planning is very much an individualized tool. While this article has focused on tips for 2020, it is not too early to begin thinking about steps to take for 2021. The month of December is usually when employers distribute 2021 paperwork, so:

- Estimate your 2021 out-of-pocket medical expenses and childcare expenses in order to contribute pre-tax income to your FSA (flexible spending accounts);
- Plan your 401(k) contribution, aiming to contribute, at a minimum, the amount required to receive your employer's match; and
- If you have a qualified HDHP (high deductible health plan) to maximize contributions to your HSA (health savings account).

If you have any questions about year-end tax planning, or if you need further assistance, please contact us.

Susan Waterloo, CPA, Partner, has over 25 years of complex experience and focuses on a consultative approach to understanding her clients' needs and providing compliance services, tax strategies, and planning. Well versed in individual, partnership, corporate, and trust taxation, Susan focuses on family groups, including their active businesses, real estate holdings, investment partnerships, and trusts. Susan is recognized as the firm's technical resource in flow-through entity taxation.

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