



To Our Clients and Friends:

As we approach year-end, it's time to think about steps you can take to help reduce your 2021 tax bill. In what appears to be the new normal, 2021 is shaping up to be a year with plenty of tax law changes. COVID-related disaster relief signed into law last December made several favorable (mostly temporary) changes to the 2021 rules. Then, in March, the American Rescue Plan Act, with another set of tax law changes, was enacted. We'll highlight some of the planning opportunities these provide.

In addition to all the known changes impacting 2021, it looks like we may end the year with some other big (and probably not so favorable) tax law changes. As you undoubtedly know, President Biden has proposed raising the ordinary income and capital gains tax rates on individuals. The ordinary income tax rate increase is proposed to take effect in 2022. Some members of the House are trying to make any increase in the capital gains rate retroactive to sales after 9/13/21, but there's no guarantee that will happen. A corporate tax rate hike has also been proposed for tax years beginning after 2021. Currently, the House is negotiating to come up with a bill based on the President's proposals.

Even though we don't know yet what, if anything, will become of President Biden's proposals, there are still many things you might consider doing before year-end to minimize your 2021 tax bill. We'll point out some strategies and things to consider in light of potentially higher tax rates in 2022. Clearly, uncertainty makes tax planning challenging, but putting it off until we know the fate of these proposals may leave you with too little time to make any moves before year end. It's best to have a plan in case of a tax increase, so that you can pull the trigger if need be.

Year-end Planning Moves for Individuals

- *Make Your Plan for Possible Higher Income Tax Rates.* If you think that you will be in a higher tax bracket in 2022 than in 2021, the conventional wisdom of deferring income and accelerating deductions is flipped upside down. Instead, you generally should try to accelerate income into 2021 (where it will be taxed at the lower rate) and defer deductions until 2022, when they will generate a bigger tax benefit. Of course, whenever you accelerate income, you have to keep the time value of money in mind and realize that you are giving up some deferral to have the income taxed at a lower rate. We can help you determine whether the tax savings associated with accelerating income into 2021 to have it taxed at a lower rate exceeds the cost of giving up the tax deferral.
- *Bunch Itemized Deductions to Maximize Their Worth.* For 2021, the standard deduction amounts are \$12,550 for singles and those who use Married Filing Separate (MFS) status, \$25,100 for Married Filing Joint (MFJ) couples, and \$18,800 for Heads of Household (HOH). If your total annual itemizable deductions for 2021 will be close to your standard deduction amount, consider bunching your expenditures for itemized deductions so that they exceed the standard deduction in one year, and then use the standard deduction in the following year. Note that if you decide to take the standard deduction in 2021 (and bunch itemized deductions in 2022), you can still take an "above the line" deduction for charitable contributions in 2021, up to \$300 (\$600 if MFJ).
- *Decide Whether Selling Investment Assets before Year-end Makes Sense.* Regardless of whether you think you will be in a higher tax bracket in 2022, you should look at your investment portfolio held in a taxable account and see if selling before year end could make tax sense. To the extent you have capital losses that were recognized earlier this year or capital loss carryovers from before 2021 (or you have some capital losses you can trigger), selling winners before year-end will not result in any tax hit. Triggering short-term capital gains that can be sheltered with capital losses is a sweet deal because net short-term gains would otherwise be taxed at higher ordinary income rates. If you have investments that have declined in value, you might want

to take the resulting capital losses this year. Those losses would shelter capital gains, including high-taxed short-term gains, from other 2021 sales.

- *Take Advantage of Tax Credits Extended through 2021.* Credits are still available for: (1) energy-efficient home improvements, (2) residential energy efficient property (including solar energy equipment), (3) fuel-cell vehicles, (4) electric motorcycles, and (5) alternate fuel vehicle refueling equipment. If you're thinking about purchasing any of these, let us know. We can help you determine whether your expenditure qualifies for a credit.
- *Consider a Roth IRA Conversion.* This may be the perfect time to make that Roth conversion you've been thinking about, especially if you think you will be in a higher tax bracket in 2022. Although you will pay tax as if the assets had been distributed from the traditional IRA, your future Roth IRA distributions can potentially be tax-free. And, unlike traditional IRAs, Roth IRAs don't have minimum distribution requirements during the account owner's lifetime.
- *Claim the 100% Gain Exclusion for Qualified Small Business Stock.* 100% of the gain on eligible sales of Qualified Small Business Stock (QSBS) that was acquired after 9/27/10 can be excluded from income. QSBS must be held for more than five years to be eligible for the gain exclusion. Either 50% or 75% of the gain (depending on when the QSBS was acquired) can be excluded for stock acquired before 9/28/10. Contact us if you think you own stock that could qualify.
- *Consider Intrafamily Loans.* Interest rates are at a historic low. This scenario creates an attractive opportunity for those interested in assisting family members financially and transferring assets in a tax-efficient manner. Intrafamily loans, along with proper gift tax planning, may be a smart move.
- *Contribute to a Traditional IRA.* Individuals over the age of 70½ who are still working in 2021 can contribute to a traditional IRA. However, if you're over age 70½ and considering making a charitable donation directly from your IRA (known as a Qualified Charitable Distribution or QCD) in the future, making a deductible IRA contribution for years you are age 70½ or older will affect your ability to exclude future QCDs from your taxable income.

Year-end Planning Moves for Small Businesses

If you own a business, consider the following strategies, in addition to planning for possibly higher tax rates in 2022 as discussed above. Note that proposed tax rate increases would potentially affect income earned by sole proprietors, pass-through entities, and corporations.

- *Establish a Tax-favored Retirement Plan.* If your business doesn't already have a retirement plan, now might be the time to take the plunge. Current retirement plan rules allow for significant deductible contributions. Contact us for more information on small business retirement plan options, and be aware that if your business has employees, you may have to cover them too.
- *Plan Asset Purchases.* 100% first-year bonus depreciation is available for qualified new and used property that is acquired and placed in service in calendar-year 2021 (and unless something changes, 2022). That means your business might be able to write off the entire cost of some or all of your 2021 asset additions on this year's return. Some assets that don't qualify for bonus depreciation are eligible for Section 179 expensing. For qualifying property placed in service in tax years beginning in 2021, the maximum Section 179 deduction is \$1.05 million. The Section 179 deduction begins to phase-out when the cost of Section 179-eligible property placed in service during the year exceeds \$2.62 million.

This letter only covers some of the year-end tax planning moves that could potentially benefit you, your family, and your business. Please contact us if you have questions, want more information, or would like us to help in designing a year-end planning package that delivers the best tax results for you.

-Karla Havemeier, Ltd CPAs