Will New Tax Legislation Lead to Major Changes?

Year-End Tax Planning Tips

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Benjamin Franklin wrote in 1789 that "in this world nothing can be said to be certain, except death and taxes," popularizing a phrase that is still with us over 230 years later. While taxes typically take center stage in our financial lives in the spring, it's important to take stock of your tax situation at year-end. There are a number of things you can do to reduce your tax burden that must be done before Dec. 31.

Complicating matters this year is the potential for new tax legislation from Congress. Tax changes are nothing new. In fact, like the change of seasons, we've come to expect regular changes to the tax code. In just the last four years the Tax Cuts and Jobs Act (2017), the SECURE Act (2019) and the CARES Act (2020) each have altered the tax landscape in the U.S.

We don't know yet what changes will be enacted, so the suggestions below are primarily evergreen strategies that work under any tax regime. In the closing section, we address some ideas to consider, based on the proposed legislation making its way through Congress.

Federal Income Tax Rates

Single	Pay	Plus	Of the Amount Over
Up to $9,950	$ 0	10%	$ 0
9,951 – 40,525	995.00	12	9,950
40,125 – 86,375	4,664.00	22	40,525
86,376 – 164,925	14,751.00	24	86,375
164,926 – 209,425	33,603.00	32	164,925
209,426 – 523,600	47,843.00	35	209,425
523,601 and up	157,804.25	37	523,600

Married, Filing Jointly	Pay	Plus	Of the Amount Over
Up to $19,900	$ 0	10%	$ 0
19,901 – 81,050	1,990	12	19,900
81,051 – 172,750	9,328	22	81,050
172,751 – 329,850	29,502	24	172,750
329,851 – 418,850	67,206	32	329,850
418,851 – 628,300	96,686	35	418,850
628,301 and up	168,993.50	37	628,300

Capital Gains Tax Rate

Single	Married, Filing Jointly	Capital Gains Tax Rate
Up to $40,400	Up to $80,800	0%
40,401 – 445,850	80,800 – 501,600	15
Over 445,850	Over 501,600	20

Understanding Marginal Tax Rates

Let's start with your tax rate. In the two charts at right, you can see the tax schedule for 2021. For example, if you're married filing a joint return, and you estimate your taxable income after all deductions is $75,000, your federal income tax will be $8,602 ($1,990 + 12 % of $55,100 = $6,612). If your income goes over $80,250 (but is less than $171,050), any of this additional income will be taxed at 22%. So your goal would be to figure out how to stay in the 12% bracket.

Long- and Short-Term Capital Gains Tax Rates

Long-term capital gains on securities (those held for more than one year) are currently taxed at a lower rate of between 0% and 20%. See the bottom chart at right.

Taxpayers who make less than $40,400 (single) or $80,800 (married filing joint) will not be taxed on their long-term gains. Filers with income above those thresholds, but below $445,850 (single) or $501,600 (married filing joint) will pay 15% on long-term capital gains.

In addition, there is a separate Medicare surtax of 3.8% on net investment income applied using a third set of income thresholds.

Single taxpayers who have modified adjusted gross income (AGI) over $200,000 and married couples who have modified AGI over than $250,000 will be subject to this 3.8% surtax on net investment income, in addition to the capital gains tax noted above. Gains from the sale of short-term holdings (those owned for one year or less) will be taxed as ordinary income — at a federal rate as high as 37% depending on your other sources of income.

If your overall capital losses exceed your capital gains, you can deduct up to $3,000 of that excess loss each year from ordinary income and unused capital losses above that amount can be carried forward indefinitely to be used in future years.

Taking Tax Losses

If you have an investment showing a loss, you may consider selling the shares to realize the loss and reduce your taxes. If you believe the holding is still a good long-term investment, there are two ways to do this.

First, you can sell the stock for a loss and repurchase it in 31 days (the Internal Revenue Service requires you to wait 30 days to do so to avoid erasing the tax loss, the so-called "wash rule").

Alternatively, if you're concerned about the stock moving up during the 30-day waiting period, you could double up on your position, wait 30 days and then sell the top-costing shares assuming they're still at a loss.

Obviously, you need to make the purchase before the end of November, in order to wait the 31 days and still take the loss in the 2021 tax year. Trades completed on the last business day of the year count for 2021, even if they don't settle until 2022.

Accelerating Deductions

Tax changes put in place in 2018 eliminated or limited many itemized deductions, in favor of an increased standard deduction that stands at $12,550 for single filers and $25,100 for married couples for 2021. If you are over 65 you get a slightly higher deduction — $13,850 for single filers, $27,700 for married filing joint.

As a result, you must have significant deductions (including state and local taxes, medical expenses, charitable contributions and mortgage interest) in order to itemize.

Charitable Contribution Deductions

Whether you contribute cash, stock or other assets, it's important to adhere to the year-end deadlines for 2021 charitable contributions. If you donate cash to a charitable organization, you can deduct your donation in 2021 as long as you mail your check by Dec. 31. This is true even if the organization doesn't cash your check until 2022. If you charge your donation to your credit card, your donation is treated as occurring on the date the charge occurs.

If you donate stock or other securities by mailing certificates, the date of mailing is the date of the donation. If you have the shares donated electronically, the date your brokerage statement shows it leaving the account is the date of the gift.

The value of your donation equals the average of the highest and lowest selling prices for that date. However you must have held the asset for a year to qualify for this deduction. If you have held it for a shorter period of time you can only deduct your cost.

Donations of clothing, household items and other goods can be deducted based on the fair market value of the goods. We recommend you make an itemized list and take pictures of your donated items in case your tax return is audited.

In the past, charitable cash contributions were limited to 60% of your adjusted gross income. But this limit was temporarily removed for 2020 and 2021. This year you can make deductible contributions of up to 100% of your adjusted gross income, wiping out your 2021 tax liability entirely. In order to qualify the gifts must be made in cash to a public charity during 2021. While that may not be feasible for many, this also means you have increased ability to lower your tax bracket through charitable deductions.

In order to get tax benefits for charitable contributions you generally must itemize deductions, as noted above. There is one exception that hascarried over from the CARES Act passed last year, however. This provision allows taxpayers to deduct up to $300 in cash charitable contributions ($600 for married couples) if the taxpayer does not itemize deductions. This provision expires after this year.

Contribute the Maximum You Can to a Qualified Retirement Plan

In 2021, you can contribute the lower of $19,500 or whatever you earned to your 401(k) or 403(b) plan. If you're age 50 or older, you can add another $6,500 to that number. Contributing the maximum lowers your taxable income and the money in the 401(k) compounds tax-deferred. These contributions must be made in the form of payroll deductions before the end of the year.

If your AGI is below $105,000 as a married person filing jointly or $66,000 as a single/head of household, you can also make a tax-deductible contribution of $6,000 (or $7,000 if you are age 50 or older) to an individual retirement account, even if you are covered by a 401(k) plan at work. Contributions to an IRA for 2021 can be made any time before the normal filing deadline of April 15, 2022, or when you file your 2021 tax return on extension, whichever date comes first. Thus this is an action you can take after year-end.

Planning for Potential Changes to Tax Law

While it remains to be seen what form the final tax legislation will take, it appears that the primary focus will be on corporations and high net worth taxpayers, with less impact being felt by those not in the highest tax bracket.

The proposed changes include a new top income tax bracket of 39.6% and a new top capital gains tax bracket of 25%, for those with incomes over $400,000 (single) or $450,000 (married couples). In the case of ordinary income, if you have control over the timing you may want to accelerate that income into 2021, to pay at a lower rate. In the case of capital gains, the changes may be retroactive to Sept. 14, 2021, leaving no room to strategize.

There are also additional taxes and limits on IRAs proposed for the ultra-wealthy, which apply to only a select few taxpayers. But there are three other changes that would apply more broadly if passed.

First, it is likely that the "backdoor Roth" strategy may be eliminated going forward. In short, this is the strategy where a taxpayer who earns too much to contribute to a Roth makes an

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facial recognition. Enabling MFA will provide added protection if your account password is stolen.

■ **4. Maintain Computer Security**. Security software packages with anti-virus, anti-spam, and spyware detection features are a must if you engage in online financial transactions. For computers, be sure to use up-to-date security software and configure the software for automatic updates. For all devices, install security updates as soon you receive a security update notification. Check your computer hardware and software provider's websites for tips to improve the security of your system.

■ **5. Use Your Own Device — and Secure It.** If possible, avoid using public computers or devices that are not yours to access your financial accounts. Public computers may contain software that captures passwords and PINs, which others can access. If you use another computer, be sure to delete your "Temporary Internet Files," or "Cache" and clear your "History" after you log out of your account. And be sure to use strong passwords, pass-phrases, or biometrics to protect not only your mobile devices but also your financial apps.

■ **6. Be Cyber Safe When Using Wi-Fi.** Many public hot spots, such as wireless networks in airports, hotels, and restaurants, reduce their security settings so it is easier for individuals to access and use these wireless networks. This also increases the possibility that someone could intercept your information. Some hackers will even create their own public networks with familiar-sounding names to lure in unsuspecting internet-seekers. Red flags to watch for include slow connections or networks that don't ask for you to agree to their terms of service. If accessing your financial accounts through a wired connection is not an option, do your best to balance the security risks of Wi-Fi. Wait until you can access a trusted, encrypted network. And when using Wi-Fi at home, secure your network with the strongest available encryption and a strong password.

■ **7. Review All Correspondence from Your Financial Institutions.** This bears repeating. Review your account activity and monthly account statements as soon as they are available. Be sure your financial institution has your current contact information and that you are regularly receiving statements. If you see a mistake or unauthorized activity in your account, contact your financial institution immediately.

*If you suspect your identity has been stolen or want resources on identity theft, visit the Federal Trade Commission's **IdentityTheft.gov**. Report concerns about your investment accounts to FINRA, the SEC and your state regulator.*

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after-tax contribution to a traditional IRA and then turns around shortly thereafter and converts that account to a Roth IRA. This loophole has been debated for years and may finally be closing. If you're phased out of the Roth IRA contribution, you might want to do one last "backdoor Roth" conversion before year-end.

Second, the estate tax appears to be in line for a change. Under current law the $11.7 million estate tax exemption was set to "sunset" and return to the old $5 million level in 2025. We may see this "sunset" moved up to 2022, with the exemption adjusted for inflation to something in the neighborhood of $6 million. Older taxpayers with larger estates may consider making gifts to heirs before year-end, to reduce the size of their estate at death.

Lastly, the child tax credit may be expanded permanently, increasing from $2,000 to $3,000, or $3,600 for children under age 6. This credit does begin to phase out for households with income above $400,000, but would be a boon for families in lower tax brackets.

Consulting Your Tax Adviser

This time of year is an excellent time for you to check in with your accountant about your situation (the earlier the better!). Your accountant can advise you as to whether you should be making estimated federal or state tax payments by year-end or in January based on the information you provide.

By taking some steps now, you should be able to reduce your tax bill somewhat. In addition, it will be easier for you to put together your tax information in January. Good luck!

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