WHITINGER & COMPANY LLC
CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

YEAR-END TAX PLANNING

Dear Clients and Friends,

With the end of the year approaching, it is a good time to review your 2019 income tax situation and take steps to ensure that you are taking full advantage of the many tax planning strategies available.

Before we get to specific suggestions, here are two important considerations to keep in mind:

1. Effective tax planning requires considering both this year and next year, at a minimum. Without a multi-year outlook, you cannot be sure planning strategies intended to save taxes on your 2019 return will not backfire and cost additional money in the future.
2. Be on the alert for the Alternative Minimum Tax (AMT) in all of your planning. What may be a great planning strategy for regular tax purposes may create or increase an AMT problem.

Here are a few tax-saving ideas for you to consider. As always, you can call on us to help you sort through the options and implement strategies that make sense for you.

YEAR-END INVESTMENT MOVES

Depending on your taxable income, the 2019 federal income tax rates on long-term capital gains and qualified dividends are 0%, 15%, and 20%. High-income individuals can also be hit by the 3.8% NIIT which can result in a marginal long-term capital gains/qualified dividend tax rate as high as 23.8%. Still, that is substantially lower than the top regular tax rate of 37% (40.8% if the NIIT applies). To minimize your taxes, consider the following:

HOLDING ON FOR FAVORABLE RATES. Whenever possible, try to hold appreciated securities for a minimum of one year and one day to qualify for the more favorable long-term capital gains rates.

SELECT THE RIGHT SHARES TO BE SOLD. Use specific identification or standing orders, instead of the default first-in, first-out method, to identify the stock or mutual fund shares to be sold. Selecting the highest basis shares, even if held one year or less, can minimize your capital gains taxes in certain situations.

SELL DEPRECIATED SECURITIES TO HARVEST CAPITAL LOSSES. As long the same or similar investments are not acquired within 30 days of the sale, the loss can be used to offset capital gains. If capital losses exceed capital gains, up to $3,000 of capital losses can be used to offset other income.

TAKE ADVANTAGE OF 0% FEDERAL RATE ON LONG-TERM CAPITAL GAINS. If your taxable income is not greater than $78,750 married filing joint, $39,375 single, or $52,750 head of household, sell appreciated securities held for more than one year. Until taxable income exceeds the thresholds above, long-term capital gains are taxed at a 0% federal rate.

SECURE A DEDUCTION FOR NEARLY WORTHLESS SECURITIES. If you own any securities that are nearly worthless with little chance of recovery, sell them before year end so that you can deduct the loss in the current year. Do not sell the investments to a related party, which would result in a disallowance of the loss.

CONSIDER CONVERTING TRADITIONAL IRAS INTO ROTH IRAS. Conversions can be beneficial for many reasons, including when an individual would not pay federal income tax on the conversion or expects to be in the same or higher tax bracket in retirement. With tax rates at relatively low levels, now might be the time to convert part or all of your Traditional IRAs to Roth IRAs.

CHECK YOUR BENEFICIARY DESIGNATIONS. Retirement plans, pensions, IRAs, life insurance policies, annuities, payable on death accounts, and certain other accounts transfer to the beneficiaries designated on the respective account forms. These designations have priority over designations in wills, trusts, etc. Be sure your beneficiary designations are up to date, especially if you have experienced a significant life event such as marriage, divorce, birth of a child, etc.

MAXIMIZING NONBUSINESS DEDUCTIONS AND CREDITS

GIFT APPRECIATED STOCK. If you have appreciated stock that you have held for more than a year and you plan to make significant charitable contributions, keep your cash and donate the stock instead. You will avoid paying tax on the appreciation and will be able to deduct the donated property's full value. If you want to maintain a position in the donated securities, you can immediately buy back a like number of shares. On the other hand, if the stock is now worth less than when you acquired it, sell the stock, take the loss, and then give the cash to the charity. Also, if you sell the stock at a loss, you cannot immediately buy it back as this will trigger the wash sale rules. This means your loss will not be deductible, but instead will be added to the basis in the new shares.

MAXIMIZE THE BENEFIT OF THE STANDARD DEDUCTION. The tax reform bill almost doubled the standard deduction amounts. For 2019, the standard deduction is $24,400 for married filing joint, $12,200 for single, and $18,350 for head of household. If your total itemized deductions are normally close to these amounts, you may be able to maximize the benefit of your deductions by bunching deductions in every other year. This allows you to time your itemized deductions so that they are high in one year and low in the next. You claim actual expenses in the year they are bunched and take the standard deduction in the intervening years. For instance, you might consider moving charitable donations or state tax payments you normally would make in 2020 to 2019. However, be careful with the timing of state and local tax payments as the maximum amount you can deduct for state and local taxes is now $10,000 per year ($5,000 if married filing separate).

CONTRIBUTE TO A 529 PLAN. For Indiana taxpayers, contributions to an Indiana 529 Plan can provide a 20% state tax credit (maximum credit of $1,000). Contributions to an Indiana 529 Plan must be designated as either for K-12 tuition or higher education expenses. Specific to K-12 tuition paid with 529 Plan funds, distributions are limited to $10,000 per beneficiary and the tuition must be for attendance at an in-state school. Many other states offer deductions or credits for contributions to that state's 529 Plan. Contributions must be postmarked or received by the 529 Plan on or before December 31.

YEAR-END MOVES FOR SENIORS AGE 70 ½ PLUS

MAKE CHARITABLE DONATIONS DIRECTLY FROM YOUR IRA. You can make cash donations totaling up to $100,000 per individual IRA owner per year to IRS-approved charities directly from your IRA ($200,000 per year maximum on a joint return if both spouses make Qualified Charitable Distributions [QCDs] of $100,000). QCDs are not treated as taxable distributions, and you receive no itemized deduction for the contribution. QCDs have many potential tax benefits such as reducing your Adjusted Gross Income (which may decrease the phase-out of other tax benefits and reduce the amount of your Social Security benefits that are taxable), receiving a state tax benefit where you otherwise would not, and effectively allowing you to deduct charitable contributions and claim the standard deduction on the same return. If you decide to make a QCD, be sure to transfer the funds directly from your IRA to the charity.

TAKE YOUR REQUIRED MINIMUM DISTRIBUTIONS. Individuals with retirement accounts must generally take withdrawals based on the size of their account and their age every year after they reach age 70½. Failure to take a required withdrawal can result in a penalty of 50% of the amount not withdrawn. QCDs discussed above count as payouts for purposes of the required distribution rules. This means you can donate all or part of your 2019 required distribution (up to the $100,000 per

individual IRA owner limit on QCDs) and convert taxable required distributions into tax-free QCDs.
If you turned age 70½ in 2019, you can delay your 2019 required distribution until April 1, 2020. However, waiting until 2020 will result in two distributions in 2020 (the amount required for 2019 plus the amount required for 2020). While deferring income is normally a sound tax strategy, here it results in bunching income into 2020, which might throw you into a higher tax bracket or have a detrimental impact on your tax deductions.

YEAR-END MOVES FOR YOUR BUSINESS

MAXIMIZE THE DEDUCTION FOR PASS-THROUGH BUSINESS INCOME. For tax years beginning in 2019, the deduction could be up to 20% of a pass-through entity owner's qualified business income, subject to restrictions that could apply when taxable income from all sources exceeds $321,400 if married filing joint and $160,700 for all others. For pass-through entity owners subject to the restrictions, it is extremely important to manage taxable income to maximize the deduction.

The deduction can also be claimed for up to 20% of income from qualified REIT dividends and publicly traded partnerships. For purposes of this deduction, pass-through entities are defined as sole proprietorships, partnerships, S corporations, and LLCs that are treated as one of the former for tax purposes. The deduction is only available to individuals, trusts, and estates. Because of the various limitations and restrictions on the deduction, other tax planning moves can have a positive or negative affect on your allowable deduction.

TAKE ADVANTAGE OF TAX BREAKS FOR PURCHASING EQUIPMENT, SOFTWARE, AND CERTAIN REAL PROPERTY ACQUIRED AND PLACED IN SERVICE DURING 2019.

- Your business can claim first-year bonus depreciation equal to 100% of the cost of most new and used equipment and software placed in service by December 31 of this year. Heavy SUVs, pickups, and vans with a Gross Vehicle Weight Rating above 6,000 pounds also qualify for 100% bonus depreciation. For cars, light trucks, and light vans subject to the luxury auto depreciation limits, the annual limits, including bonus depreciation, were increased to $18,100 in year 1, $16,100 in year 2, $9,700 in year 3, and $5,760 for year 4 and beyond.

- For assets used for both business and personal purposes, an effective planning strategy is to maximize the business use during the year of acquisition. For example, a $60,000 heavy SUV placed in service in December 2019 and used 95% for business could generate a $57,000 deduction for 2019, even if the business use is less than 95% in future years. However, the business use must remain above 50% in all future years to avoid having to recapture the accelerated depreciation as income.

- Under Section 179, an eligible business can claim significant first-year depreciation for the cost of new and used equipment, software additions, and qualifying real property. Qualifying real property is any improvement to an interior portion of a nonresidential building that is placed in service after the date the building is first placed in service, except for expenditures attributable to the enlargement of the building, any elevator or escalator, or the building's internal structural framework. Qualifying real property also includes roofs, HVAC equipment, fire protection and alarm systems, and security systems for nonresidential real property if placed in service after the nonresidential building was placed in service. For tax years beginning in 2019, the maximum Section 179 deduction is $1,020,000, but this amount is reduced to the extent qualified purchases exceed $2,550,000. If your business has a tax loss for the year before considering any Section 179 deduction, you cannot claim a Section 179 deduction that would create or increase the overall business tax loss.

REVISIT BUSINESS NEXUS FOR MULTI-STATE BUSINESSES. In 2018, the U.S. Supreme Court decision in Wayfair overturned the physical presence standard that had been in place for decades. This decision has opened the door for states to require an out-of-state business to collect and remit sales tax on sales into those states, even if the business does not have any physical presence in the state. Many states have now adopted economic nexus standards that require out-of-state businesses to collect sales tax if there are more than a certain number of transactions or sales into the state. Those thresholds are generally 200 transactions and/or $100,000 - $500,000 of sales but can be more or less depending on the state. The Wayfair decision could also have an impact on income tax nexus.

REVIEW AND UPDATE ACCOUNTING POLICY FOR EXPENSING SMALL-DOLLAR EQUIPMENT AND FIXED ASSET PURCHASES. The IRS generally allows taxpayers to expense equipment and fixed assets up to $2,500 per item using the de minimis safe harbor. The de minimis safe harbor requires that an accounting policy be established at the beginning of the tax year that requires items costing less than a certain dollar amount or lasting less than 12 months be expensed for both book and tax purposes. The accounting policy does not have to be written. For taxpayers that have Applicable Financial Statements (generally, certified audited or provided to any federal or state agency other than IRS), the de minimis threshold increases to $5,000 per item. Additionally, the accounting policy for taxpayers with applicable financial statements must be written.

CHECK YOUR PARTNERSHIP AND S CORPORATION STOCK BASIS. If you own an interest in a partnership or S corporation, your ability to deduct any losses it passes through is limited to your basis. Although any unused loss can be carried forward indefinitely, the time value of money diminishes the usefulness of these suspended deductions. If you expect the partnership or S-corporation to generate a loss this year, and you lack sufficient basis to claim a full deduction, you should consider making a capital contribution or loan additional funds to the business before year end.

EMPLOY YOUR CHILD. Employing your child provides tax benefits by shifting income from you to your child, who normally is in a lower tax bracket or may avoid tax entirely due to the standard deduction, which could be as high as $12,200 for 2019. There can also be payroll tax savings since wages paid by sole proprietors to their children age 17 and younger are exempt from both social security and unemployment taxes. Employing your children has the added benefit of providing them with earned income, which enables them to contribute to a traditional or Roth IRA. Remember a couple of things when employing your child. First, the wages paid must be reasonable given the child's age and work skills. Second, if the child is in college, or is entering soon, having too much earned income can have a detrimental impact on the student's need-based financial aid eligibility.

REVIEW YOUR HEALTH CARE COSTS AND COVERAGE

TAKE ADVANTAGE OF FLEXIBLE SPENDING ACCOUNTS (FSAs). If your company has a healthcare and/or dependent care FSA, you must specify how much of your salary to convert into tax-free contributions to the plan. You can then take tax-free withdrawals next year to reimburse yourself for out-of-pocket medical and dental expenses and qualifying dependent care costs. Keep in mind, however, that FSAs are "use-it-or-lose-it" accounts. You do not want to set aside more than what you will likely have in qualifying expenses for the year. If you currently have a healthcare FSA, make sure you spend it by incurring eligible expenses before the deadline for your plan.

CONSIDER A HEALTH SAVINGS ACCOUNT (HSA). If you are enrolled in a high-deductible health plan and do not have any other coverage, you may be eligible to make pre-tax or tax-deductible contributions to an HSA of up to $7,000 for family coverage or $3,500 for individual coverage, plus an extra $1,000 if you will be 55 or older by the end of 2019. Distributions from the HSA will be tax-free as long as the funds are used to pay unreimbursed qualified medical expenses. Furthermore, there is no time limit on when you can use your contributions to cover expenses. Unlike a healthcare FSA, amounts remaining in the HSA at the end of the year can be carried over indefinitely.

MANAGE YOUR ADJUSTED GROSS INCOME (AGI)

Many tax deductions and credits are only available to taxpayers with AGI below certain levels. Some common AGI-based tax breaks include the child tax credit (phase-out begins at $400,000 for married filing joint and $200,000 for single and head of household), the $25,000 rental real estate passive loss allowance (phase-out range of $100,000–$150,000 for most taxpayers), and the exclusion of social security benefits ($32,000 threshold for married filing joint; $25,000 for most other filers).

Accordingly, strategies that lower your income or increase certain deductions might not only reduce your taxable income, but also help increase some of your other tax deductions and credits. Managing your AGI can also help you avoid (or reduce the impact of) the 3.8% Net Investment Income Tax that potentially applies if your AGI exceeds $250,000 for joint returns, $200,000 for unmarried taxpayers, and $125,000 for married filing separately.

Managing your AGI can be somewhat difficult, since it is not affected by many deductions you can control, such as deductions for charitable contributions and real estate and state income taxes. However, you can effectively reduce your AGI by increasing "above-the-line" deductions, such as those for retirement plan contributions. For sales of property, consider an installment sale that shifts part of the gain to later years when the installment payments are received or use a like-kind exchange that defers the gain until the exchanged property is sold. If you're age 70½ or older, consider making charitable contributions from your IRA, as discussed previously. If you own a cash-basis business, delay billings so payments are not received until 2020 or accelerate payment of certain expenses, such as office supplies and repairs and maintenance, to 2019. Of course, before deferring income, you must assess the risk of doing so.

CHECK YOUR WITHHOLDINGS

Due to the lower tax rates beginning in 2018, some individuals' federal tax withholding from wages and other sources decreased. As a result, these individuals may receive a smaller refund or owe more tax because the decrease in federal tax withholding was greater than the decrease in income tax. Some may need to adjust their withholding or make estimated tax payments to make up for this shortfall.

ESTATE AND GIFT PLANNING

For 2019, the unified federal gift and estate tax exemption is $11.4 million, and the federal estate tax rate is 40%. As long as a decedent's taxable estate and lifetime taxable gifts are below the exemption amount, no estate tax will be due. If a married taxpayer dies, it may be beneficial to file an estate tax return to preserve any unused exemption for the surviving spouse even though no estate tax will be due.

TAKE ADVANTAGE OF THE ANNUAL GIFT TAX EXCLUSION. For 2019, the annual gift tax exclusion is $15,000. Therefore, a taxpayer can give $15,000 per year to any number of recipients without owing any federal gift tax. Direct payments to providers for medical expenses and tuition do not count towards the annual exclusion.

CONCLUSION

The ideas discussed in this letter are a good way to get you started with year-end planning, but they are no substitute for personalized professional assistance. Please do not hesitate to call us with questions or for additional strategies on reducing your tax liability. We would be glad to set up a planning meeting or assist you in any other way that we can.

Very truly yours,

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