KS ADVISOR BLOG

2022 Year-End Tax Planning Ideas for Individuals and Businesses

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As year-end approaches consider the following tax planning ideas and action items before ringing in the new year.

Individuals

Tax loss harvesting
Consider selling specified stocks, bonds, or other investments that are currently in a loss position prior to year-end. The sale of these investments creates capital loss deductions that may help lower taxable income for many taxpayers. Capital loses are allowed to offset capital gains on a dollar-for-dollar basis. However, if no capital gains exist to offset, the loss is limited the $3,000 in the year and the remainder carries forward to future years. Also note, “wash-sale” rules require you to be out of the position for 30 days to take the loss. For example, if you purchased AAPL for $175 and it now worth $150, you could sell it today and recognize a $25 loss for tax purposes. However, you can’t re-purchase AAPL shares for at least 30 days.

Charitable contributions
Charitable contributions fall into a basket of deductions known as itemized deductions and the charitable contribution rules can become complex. However, cash contributions are generally allowable up to 60% of Adjusted Gross Income (AGI) and non-cash contribution are generally allowable up to 30% of AGI (if the asset was held for more than one year). Consider donating appreciated securities (held for more than one year) to receive a full fair market value donation while avoiding capital gains. Donations of appreciated assets – other than publicly traded securities – will require an appraisal if the item is worth $5,000 or more. While some taxpayer may not receive the federal benefit of charitable donations because they do not itemize deductions, they will generally still receive the benefit as a deduction from their Oregon taxes. Moreover, some taxpayers, subject to Required Minimum Distributions, may be able to make charitable donations directly from their IRAs. For more information on deductions including charitable donations, watch this KS Advisor video about tax deductions.

Roth IRA conversions
While converting from a taxable IRA to Roth IRA is generally a taxable event, it may still be a good idea. For example, consider current market performance and year-to-date returns. If your IRA has decreased in value this year, consider converting some of your traditional IRA to Roth IRA, effectively at a discount. Furthermore, if your income from other sources is lower than “normal” this year (possibly due to retirement, change in job status, flow-through business losses, etc.), this may be an excellent time to convert some of your tradition IRA to take advantage of lower tax brackets. For more information on IRAs, check out this KS Advisor video.

Maximize 401k deferrals
The 401k deferral limit is $20,500 for the 2022 tax year. For those age 50 and older, there is an additional catch-up contribution allowed in the amount of $6,500. Thus, taxpayers age 50 and beyond can defer a maximum of $27,000 before the end of year. This is an excellent time to consider topping off 401k deferrals before the end of year. December salaries and bonuses can also be used to maximize 401k deferrals.

Maximize gift tax exemptions
The annual gift tax exemption is $16,000 for 2022. As such, taxpayers can gift up to $16,000 to any individual with no-strings, no reduction to lifetime exemptions, and no tax return filing requirements. Gifting has the benefit of reducing the gross estate (and possibly the taxable estate) of the taxpayer. For more information on gifting and estate planning, watch this KS Advisor video.

Businesses

Oregon PTE-E
The TCJA (2018 tax law) introduced a $10,000 limit for individuals with respect to federal itemized deductions of state and local taxes paid during the year. Beginning in 2022 Oregon created a workaround to this deduction limitation for owners of certain pass-through entities, by allowing a pass-through entity to make an election (PTE-E tax election) to be taxed at the entity level. Effectively this "elective tax" becomes a business deduction vs itemized deduction, and bypasses the $10,000 limit. In many cases it will make sense for eligible flow-through entities to make this election and pay tax before year end. However, before making an election talk to your tax professional as care needs to be exercised to determine eligibility and avoid traps for the unwary. For more information on Oregon PTE-E, read our KS Advisor blog article here.

Maximize bonus depreciation
Absent a congressional law change, 2022 will be the last year to receive 100% Bonus deprecation. Beginning next year in 2023, Bonus depreciation will be reduced to 80%, and will continue to be reduced by 20% per year until it fully sunsets in 2027. To receive the benefit of 100% Bonus depreciation and immediate write off of asset purchases, the asset must be placed in service and not simply purchased before year end.

Oregon Family Leave Act
Beginning January 1, 2023, all Oregon employers must allow employees to take up to 12 weeks of paid leave off in a year. If your business has 25 or more employees, you are required to contribute to Paid Leave Oregon. If you have fewer than 25 employees, you are not required to make payments, but your employees still pay their portion, and you still need to collect and submit their payments via withholdings. Employers may also be eligible to provide an equivalent plan at a lower cost. For more information, please click here.

Maximize Qualified Business Income (QBI) deductions
The TCJA (2018 tax law) brought about the Qualified Business Income (QBI) deduction for flow through entities such as S-Corporation and Partnerships (or LCCs tax as partnerships). The deduction is up to 20% on flow through profits, however the deduction may be limited based on industry, W2 wages, and assets used in the business. It's important to note that the deduction is not available for W2 wages (S-Corporation) or Guaranteed Payments (partnership). Planning opportunities may exist prior to year-end to optimize flow through profits accordingly.

Plan for pass-through business loss utilization
Certain tax basis and active participation requirements must be met for losses of pass-through entities to be deductible by a partner or S corporation shareholder. In addition, an individual's excess business losses from their pass-through entities are subject to overall limitations in 2022. Planning opportunities may be available before year-end such that pass-through business owners can maximize their 2022 loss deductions.

Analyze year-end bonuses and timing of payments
Generally, for calendar year accrual basis taxpayers, accrued bonuses must be fixed and determinable by year end and paid within 2 ½ months of year end – by March 15, 2023 – for the bonus to be deductible in 2022. However, the bonus compensation must be paid before the end of 2022 if it is paid by a Personal Service Corporation to an employee-owner, by an S corporation to any employee-shareholder, or by a C corporation to a direct or indirect majority owner.

Understand new rules for R&E Expenditures
Under the 2018 TCJA, research and experimental (R&E) expenditures incurred or paid for tax years beginning after December 31, 2021 will no longer be immediately deductible for tax purposes. Instead, businesses are required to capitalize and amortize R&E expenditures over a period of five or 15 years beginning in 2022. The mandatory capitalization rules also apply to software development costs, including software developed for internal use. The new rules present additional considerations for businesses that invest in R&E.

A recent article from *Thomson Reuters* says: "The Senate's senior democratic tax writer said tax break discussions will be part of the Congressional agenda for the upcoming lame duck session and suggested that Democrats may be willing to do some horse trading to move the process along. 'There's going to be a clear debate about tax choices, and this whole debate about child tax credit is front and center on that discussion,' Senate Finance Committee Chairman Ron Wyden told reporters on November 15, adding that Democrats might support some business tax breaks coveted by Republicans.

For their part, Republicans have pushed for bonus depreciation deductions that allow businesses to write off their equipment purchases in a single year, a deduction for interest expenses and extension of the research and development credit."

Consider Employee Retention Tax Credit (ERTC) opportunities still available

The Employee Retention Credit (ERC) is a refundable payroll tax credit for qualifying employers that were significantly impacted by COVID-19 in 2020 or 2021. For most employers, the compensation eligible for the credit had to be paid prior to October 1, 2021. However, the deadline for claiming the credit does not expire until the statute of limitations closes on Form 941. Therefore, employers generally have three years to claim the ERC for eligible quarters during 2020 and 2021 by filing an amended Form 941-X for the relevant quarter. Employers that received a Paycheck Protection Program (PPP) loan can claim the ERC but the same wages cannot be used for both programs.

Fringe benefit reporting

Employers should ensure that applicable fringe benefits, such as health insurance premiums and HSA contributions, are properly included 2% S corporation shareholders’ taxable wages and reported on their W-2s. Partners and LLC members, including owners of capital interests and profits interests, should not be issued W-2s, but their applicable fringe benefits should generally be included in Guaranteed Payments.

Please contact your tax professional at Kernutt Stokes to discuss how year-end tax planning opportunities may benefit you.