KS ADVISOR BLOG

2023 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 losses are allowed to offset capital gains on a dollar-for-dollar basis. However, if no capital gains exist to offset, the loss is limited to $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 is now worth $150, you could sell it today and recognize a $25 loss for tax purposes. However, if you re-purchase AAPL shares within 30 days of the sale, the loss will be deferred until you sell the new shares.

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 contributions 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 taxpayers 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. 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. For example, assume a traditional IRA worth $500,000 was converted to Roth IRA at the beginning of the year. This would generally create $500,000 of taxable income upon conversion. However, now assume you waited to convert, and the market performance decreased the traditional IRA’s value to $400,000 at this time. If you now convert the IRA to Roth, you’ll only report $400,000 as taxable income. Moreover, 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 traditional IRA to take advantage of lower tax brackets. For more information on IRAs, check out this KS Advisor video.

New Rules Related to RMDs

Previously, required minimum distributions (RMDs) from IRAs were required upon reaching the age of 70 ½ through the year 2019. This age minimum was delayed to age 72 starting in 2020 and has been delayed once again in 2023 to age 73. In general, an IRA owner must now take their first RMD for the year in which they reach age 73. However, they can delay taking their first RMD until April 1 of the following year. Those who reached age 73 in 2023 must take their first RMD by April 1, 2024, and the second RMD by December 31, 2024.

Consider Qualified Charitable Distributions (QCDs)

If you are age 70½ or older by the end of 2023, and especially if you are unable to itemize your deductions, consider making 2023 charitable donations via qualified charitable distributions from your traditional IRA. These distributions are made directly to the charities of your choice from your IRAs. Moreover, the amount of the distribution is excluded from gross income, but is deemed to satisfy your RMD (if applicable). For example, suppose your RMD is $50,000 and you make a QCD to the charity of your choice in the amount of $10,000. The $10,000 will apply towards your RMD and you will now only be required to distribute $40,000 as a taxable RMD. Lastly, QCD’s do not reduce your standard tax deduction so you will still receive a full standard deduction if applicable.

Maximize 401k Deferrals

The 401k deferral limit is $22,500 for the 2023 tax year. For those age 50 and older, there is an additional catch-up contribution allowed in the amount of $7,500. Thus, taxpayers age 50 and beyond can defer a maximum of $30,000 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 $17,000 for 2023. As such, taxpayers can gift up to $17,000 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 married couples, each spouse is eligible to make gifts of $17,000 that are exempt from gift tax. As an example, if a married couple would like to gift money to their child, of whom is also married, then each parent would be able to gift $17,000 to both their child, as well as their child’s spouse. In this manner, a married couple is effectively gifting $68,000 of which all is under the annual gift tax exemption. Also note, the annual gift tax exemption increases to $18,000 for the 2024 tax year. For more information on gifting and estate planning, watch this KS Advisor video.

Oregon Kicker Credit

The Oregon surplus credit, known as the “kicker," is back for the 2021-23 biennium. The State of Oregon has confirmed a kicker of more than $5.61 billion. Taxpayers will claim the kicker as a refundable credit on their 2023 tax return filed in 2024. To calculate the amount of the credit, taxpayers can multiply their 2022 tax liability before any credits (line 22 on the 2022 Form OR-40) by 44.28 percent. The kicker may allow for modifications or reductions in estimated taxes but be sure to consult your tax professional before making any changes to your scheduled estimates or withholdings.

Electric Vehicle Credits

If you are looking to buy a new car this year, remember that the Inflation Reduction Act has extended and introduced various credits for buying both new and used electric vehicles. Credits range from up to $4,000 for used electric vehicles, to as high as $7,500 for new electric vehicles. Manufacturer's allowable credits may vary. Additional limitations apply, some of which include income limitations for taxpayers. For example, your Adjusted Gross Income (AGI) may not exceed $300,000 for married couples filing jointly or $150,000 for single taxpayers. Please consult your tax professional to discuss whether a vehicle purchase may qualify for E.V. credits.

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. Before making an election, talk to your tax professional as care needs to be exercised to determine eligibility and avoid traps for the unwary. Furthermore, if your business has experienced a significant change in income, please consult with your tax professional regarding modifying your fourth quarter PTE-E prior to year-end. It should also be noted that the PTE-E program was originally scheduled to expire at the end of this year, however, it has now been extended to December 31, 2025. For more information on Oregon PTE-E, read our KS Advisor blog article here.

Maximize Bonus Depreciation and 179 Expense

Bonus depreciation is currently at 80% for the 2023 tax year. Beginning next year in 2024, bonus depreciation will be reduced to 60%, and will continue to be reduced by 20% per year until it fully sunsets in 2027. To receive the benefit of bonus depreciation, the asset must be placed in service and not simply purchased before year-end.

For 2023, the maximum amount of Section 179 property that can be immediately expensed will be $1,160,000. That full amount is available until qualifying property placed in service during the year reaches $2,890,000, at which point deduction phase out begins. Additional limitations to Section 179 apply (such as income limitations and material participation limitations), consult with your tax professional to determine if Section 179 will be available to your business.

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 taxed 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 2023. Planning opportunities may be available before year-end such that pass-through business owners can maximize their 2023 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, 2024 – for the bonus to be deductible in 2023. However, the bonus compensation must be paid before the end of 2023 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
Research and experimental (R&E) expenditures incurred or paid for tax years beginning after December 31, 2021 are no longer immediately deductible for tax purposes. Instead, businesses are required to capitalize and amortize R&E expenditures over a period of five or fifteen years. 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. Note, this change does not impact the ability to claim the research and development tax credit allowed to business that incur R&E expenditures.

Fringe Benefit Reporting
Employers should ensure that applicable fringe benefits, such as health insurance premiums and HSA contributions, are properly included in 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.

1099 Reporting
The IRS now requires all businesses issuing 10 or more 1099s to file them electronically. Oregon also requires 1099s to be filed electronically through iWire.

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