2022 Year-end tax and financial planning

As we wrap up 2022, it's important to take a closer look at your tax and financial plans to identify opportunities for reducing, deferring, or accelerating tax obligations to help you pay the least amount of taxes over time. Though there has been a lot of political attention to tax law changes, inflation, raising interest rates and environmental sustainability, political compromise has led to small impacts on individual taxes this year. However, with the passage of the Inflation Reduction Act of 2022, there are new tax incentives for you to consider. There are also several tax provisions that have expired or will soon. We continue to closely monitor any potential extensions or changes in tax legislation and will update you accordingly.

In the meantime, here is a look at some issues impacting individuals to consider as we approach year-end. Please do not hesitate to contact us to discuss further.

Charitable contribution planning

If you are planning to donate to a charity, it is likely, but not always, better to make your contribution before the end of the year to potentially save on taxes. There are many tax planning strategies we can discuss with you about charitable giving. For example, opening and funding a donor advised fund (DAF) is appealing to many as it allows for a tax-deductible gift in the current year and the ability to dole out those funds to charities over multiple years. Qualified charitable distributions (QCDs) are another option for certain older taxpayers who don't typically itemize on their tax returns. It could make sense to use a "bunching strategy" whereby a taxpayer gives multiple years' worth of charitable gifts in a single tax year to itemize deductions in that year and then foregoes charitable gifts over the next several years while taking the standard deduction. Last year, individuals who did not itemize their deductions could take a deduction of up to $300 ($600 for joint filers). However, this opportunity is no longer available for tax year 2022. Also, note that it's important to have adequate documentation of all donations, including a letter from the charity for donations of $250 or more.

Investors with taxable accounts may hold highly appreciated equity positions. From a tax planning standpoint, gifting long-term appreciated securities is a very efficient charitable-giving strategy as the charity receives the same economic benefit as a cash donation, while the taxpayer receives a tax deduction for the full market value of the gift and avoids paying capital gains taxes on the gifted security.

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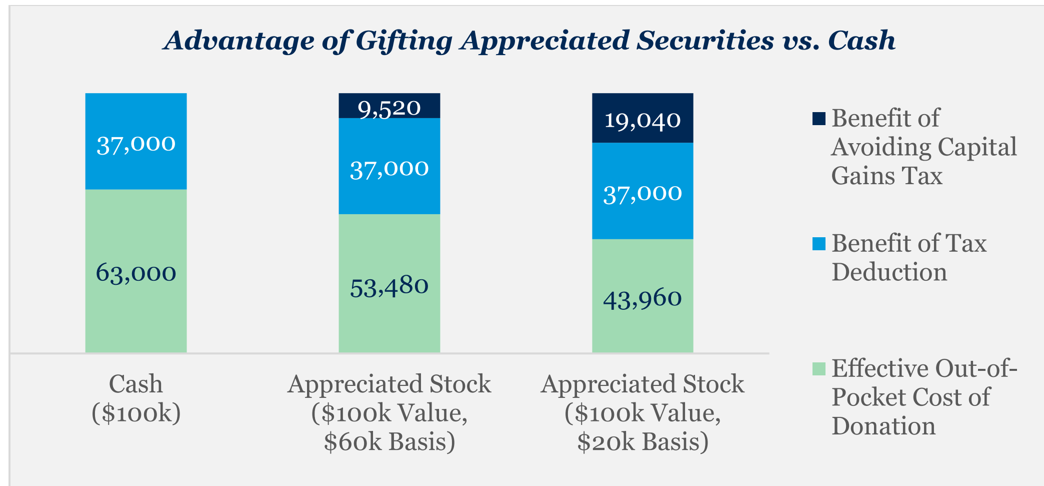


This is a hypothetical example for illustrative purposes only. Analysis assumes taxpayer subject to highest federal tax bracket (37 percent) and capital gains subject to 23.8 percent federal tax rate. Analysis assumes charitable gifts are made to qualified public charities.

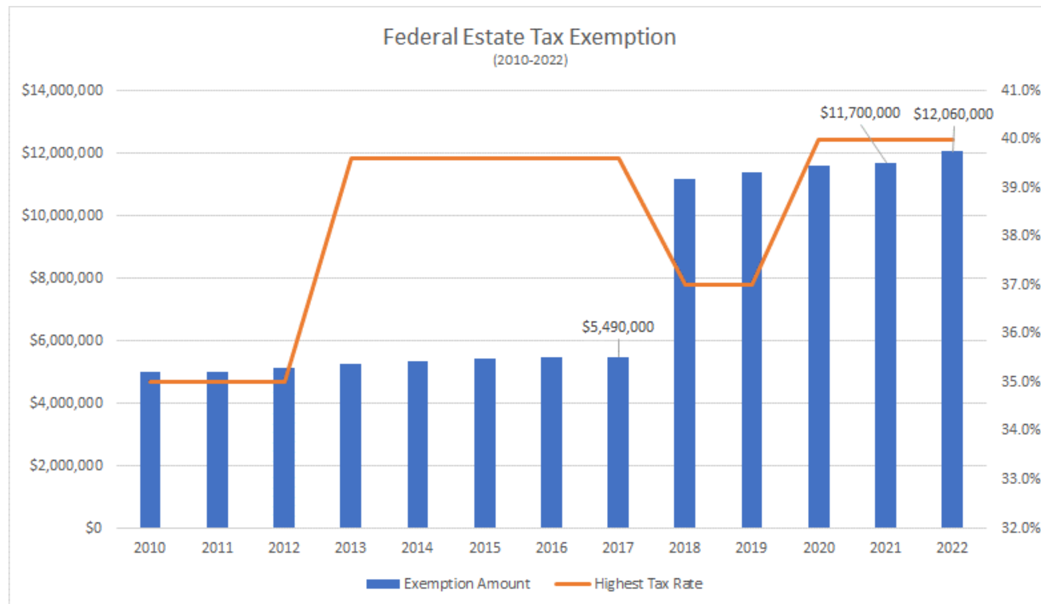
Investors who have a portfolio overweight to equities may use charitable gifting to rebalance back to target weights. In doing so, an investor can achieve philanthropic goals while avoiding having to sell appreciated equities to return to a desired target allocation.

Keep in mind that gifts of long-term appreciated securities to qualified public charities (including donor-advised funds) are limited to 30 percent of adjusted gross income (AGI) while similar gifts to a private foundation are limited to 20 percent of AGI. Charitable gifts in excess of the AGI limits result in a charitable carryforward which can be used over the next 5 years.

Utilize the Lifetime Gift Tax Exemption

The Tax Cuts and Jobs Act (TCJA), which passed in December 2017, approximately doubled the estate exemption – from $5.49 million per person in 2017 to $11.18 million per person in 2018. For 2022, the lifetime gifting exemption currently stands at $12.06 million per person, with a top federal estate tax rate of 40 percent. The increased exemption amounts, under TCJA, are scheduled to run through 2025, after which the basic exclusion amount is set to revert to the 2017 level of $5 million per person, plus inflation adjustments.

While the elevated exemption might remain in place through 2025, high net worth individuals should not lose perspective of the unique planning opportunity to get additional assets out of one's taxable estate.



Source: TheBalance, May 23, 2022

The lifetime gifting exemption is $12.06 million per person in 2022 and increases to $12.92 million per person (with a top federal estate tax rate of 40 percent), the increased exemption in 2023 would allow a married couple to an additional $1,720,000 if they had already reached the 2022 maximum. The Treasury Department and IRS issued final regulations in November 2019 clarifying that taxpayers taking advantage of the increased exemption amounts would not be subject to a claw back, should the exemption amount decrease from current levels.

High net worth individuals should evaluate current assets and assess how much might be needed for their remaining lifetime, with consideration to gift 'excess assets' to loved ones. Depending on the size of an outright gift, estate planning which incorporates making gifts to trusts may be advisable to provide parameters or safeguards for the intended beneficiaries.

Individuals who are likely to one day have a taxable estate should also consider direct payments (to the educational/medical provider) for tuition and medical expenses, which

do not constitute gifts, as well as annual exclusion gifts ($16,000 for 2022 increasing to $17,000 for 2023 to each donee). Such gifts can be an effective strategy for further reducing the size of a taxable estate.

Keep in mind that any gifts in excess of the annual gift tax exclusion per donee should be properly recorded on a gift tax return.

Review Estate Plans & Retirement Account Beneficiaries

The Setting Every Community Up for Retirement Enhancement (SECURE) Act, enacted on January 1, 2020, effectively eliminated what was known as "the stretch IRA." Under the SECURE Act, most non-spouse beneficiaries will be required to fully withdraw all inherited IRA assets by the end of the 10th year after the IRA holder died. Estate plans which previously incorporated this "stretch" strategy are now outdated and in need of updating.

Periodically reviewing and updating estate plans is a recommended best practice in light of potentially changing estate planning rules and limits. Individuals who have recently experienced a significant life event (marriage, divorce, birth/adoption) may also need to make updates to existing estate plans and beneficiary designations.

Satisfy Required Minimum Distributions (RMDs)

You cannot keep retirement funds in your account indefinitely. RMDs are the minimum amount you must annually withdraw from your retirement accounts once you reach a certain age (generally age 72). Failure to do so can result in penalties. And withdrawals usually have tax impacts. There are also opportunities to roll retirement funds to a qualified charity to satisfy the RMD without incurring taxes.

Under this provision, a taxpayer may gift up to $100,000 each year from an IRA to qualified 501(c)(3) charitable organizations (donor-advised funds, private foundations and supporting organizations are excluded). A qualified charitable distribution neither counts as an itemized deduction nor as taxable income, though it does count towards satisfying the RMD for that year.

Also, note that the IRS has issued new life expectancy tables effective for the 2022 tax year, resulting in lower RMD amounts. We can help you calculate any RMDs to take this year and plan for any tax exposure.

Consider a Roth Conversion

With markets down sharply for the year and with income tax rates at historically favorable levels, the timing may be opportune for ***some*** individuals to execute a Roth conversion.

Individuals who believe their future tax rate might be higher than their current tax rate might consider concerting a portion - or all – of existing Traditional IRA assets to a Roth IRA. Assuming the Traditional IRAs have no basis, the amount of the conversion is treated as ordinary income; in exchange, the Roth IRA grows tax-free with qualified distributions also treated as tax-free. ***It is important to make sure you have liquidity to pay the tax due on the ordinary income.***

This strategy can be particularly beneficial for individuals with a taxable estate, as the tax cost of the conversion effectively reduces the size of the estate, while the named beneficiaries one day receive a very tax-favorable asset, compared to inheriting a Traditional IRA. In some cases, high net worth individuals might pair a Roth conversion with accelerated charitable giving, as the charitable deduction will help to offset the effective tax cost of the conversion.

Harvest Losses

Review unrealized gains and losses in taxable investment accounts and harvest losses where available. Realized losses can offset other realized gains. To the extent that realized losses exceed realized gains, net realized losses can offset up to $3,000 of ordinary income with any remainder resulting in a loss carryforward to be used in future years.

Beware of the "wash sale rule" which states that a loss cannot be realized for tax purposes if a *substantially identical* position was bought within 30 days before or after the sale. As a practical example, an investor could sell an actively managed equity fund and could redeploy the sales proceeds to an equity index fund. In doing so, the investor recognizes a tax loss while also keeping similar, but not identical, portfolio exposure to capture a subsequent market recovery.

Despite the 2022 market decline, cumulative market gains over the past several years may limit unrealized losses, but your team at NEIRG will maximize losses where appropriate in your managed accounts.

Analyze Mutual Fund Year-End Capital Gain Distributions

Mutual funds are required to pass along capital gains to fund shareholders. Regardless of whether the fund shareholder benefited from the fund's sale of underlying securities, the shareholder will receive the capital gain distribution if the mutual fund is held as of the dividend record date.

Mutual fund families typically provide estimates for year-end dividend distributions over the course of October and November, with such distributions most commonly paid in December.

Capital gain distributions can be either short-term or long-term. Short-term capital gain dividends are treated as *ordinary income* and thus *cannot* be offset by realized losses; in contrast, long-term capital gain dividends are treated as capital gains and can be offset by realized losses.

It is important to review unrealized gains and losses across mutual fund holdings in taxable accounts and to compare those figures against capital gain distribution estimates to determine if selling a mutual fund position before the year-end distribution would produce a tax savings.

NEIRG conducts regular review of mutual funds in client portfolios to ensure we are not buying ahead of large gain distributions and selling when appropriate ahead of distributions to avoid potential taxable gains.

Digital assets and virtual currency

Digital assets are defined under the U.S. income tax rules as any digital representation of value that may function as a medium of exchange, a unit of account and/or a store of value. Digital assets may include virtual currencies such as Bitcoin and Ether, Stablecoins such as Tether and USD Coin (USDC) and non-fungible tokens (NFTs).

The sale or exchange of virtual currencies, the use of such currencies to pay for goods or services or holding such currencies as an investment, generally have tax impacts – and the IRS continues to increase its scrutiny in this area. We can help you understand any tax and investment consequences.

Energy tax credits

From electric vehicles to solar panels, "going green" continues to provide tax incentives. The Inflation Reduction Act of 2022 included new and newly expanded tax credits for solar panels, electric vehicles and energy-efficient home improvements. The rules are complex, and some elements of the law are not in effect until 2023, so careful research and planning now can be beneficial.

Additional tax and financial planning considerations

We recommend you review your retirement plans at least annually. That includes making the most of tax-advantaged retirement saving options, such as traditional individual retirement accounts (IRAs), Roth IRAs and company retirement plans. It is also advisable to take advantage of health savings accounts (HSAs) that can help you reduce your taxes and save for medical-related expenses.

You may be able to reduce your taxes by contributing as much as you can to IRAs and employee retirement plans. These contributions are subject to the following limits:

- IRA Contributions: The maximum you can contribute to all your traditional and Roth IRAs for 2022 is $6,000 ($7,000 if you are 50 or older). Remember, you can make contributions to your IRA until April 15, 2023, for the 2022 tax year. For 2023, these limits increased to $6,500 ($7,500 if you are 50 or older).
- 401(k) or 403(b) Contributions: The 2022 employee deferral limit on 401(k) or 403(b) contributions is $20,500 (plus an additional $6,500 if you are 50 or older). For 2023 these limits are $22,500 and $7,500 respectively.

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Federal Income tax rate brackets for 2022 and 2023 are as follows:

2022:

Rate	For Unmarried Individuals, Taxable Income	For Married Individuals Filing Joint Returns, Taxable Income	For Heads of Households, Taxable Income	For Married Individuals Filing Separate Returns, Taxable Income	For Estate and Trusts
10%	$0 - $10,275	$0 - $20,550	$0 - $14,650	$0 - $10,275	$0 - $2,750
12%	$10,276 - $41,775	$20,551 - $83,550	$14,651 - $55,900	$10,276 - $41,775	
22%	$41,776 - $89,075	$83,551 - $178,150	$55,901 - $89,050	$41,776 - $89,075	
24%	$89,076 - $170,050	$178,151 - $340,100	$89,051 - $170,050	$89,076 - $170,050	$2751 - $9,850
32%	$170,051 - $215,950	$340,101 - $431,900	$170,051 - $215,950	$170,051 - $215,950	
35%	$215,951 - $539,900	$431,901 - $647,850	$215,951 - $539,900	$215,951 - $323.925	$9,851 - $13,450
37%	Over $539,900	Over $647,850	Over $539,500	Over $323,925	Over $13,450

2023:

Rate	For Unmarried Individuals, Taxable Income	For Married Individuals Filing Joint Returns, Taxable Income	For Heads of Households, Taxable Income	For Married Individuals Filing Separate Returns, Taxable Income	For Estate and Trusts
10%	$0 - $11,000	$0 - $22,000	$0 - $15,700	$0 - $11,000	$0 - $2,900
12%	$11,001 - $44,725	$22,001 - $89,450	$15,701 - $59,850	$11,001 - $44,725	
22%	$44,726 - $95,375	$89,451 - $190,750	$59,851 - $95,350	$44,726 - $95,375	
24%	$95,376 - $182,100	$190,751 - $364,200	$95,351 - $182,100	$95,376 - $182,100	$2,901 - $10,550
32%	$182,101 - $231,250	$364,201 - $462,500	$182,101 - $231,250	$182,101 - $231,250	
35%	$231,251 - $578,125	$462,501 - $693,750	$231,251 - $578,100	$231,251 - $346,875	$10,551 - $14,450
37%	Over $578,125	Over $693,750	Over $578,100	Over $346,875	Over $14,450

Long-Term Capital Gains Rate Brackets for 2022 and 2023:

2022:

Rate	Single Filers (taxable income)	Married Filing Jointly	Heads of Household	Married Filing Separately	Estates and Trusts
0%	$0 - $41,675	$0 - $83,350	$0 - $55,800	$0 - $41,675	Below $2,800
15%	$41,676 - $459,750	$83,351 - $517,200	$55,801 - $488,500	$41,676 - $258,600	$2,801 - $13,700
20%	Over $459,750	Over $517,200	Over $488,500	Over $258,600	Over $13,700

2023:

Rate	Single Filers (taxable income)	Married Filing Jointly	Heads of Household	Married Filing Separately	Estates and Trusts
0%	$0 - $44,625	$0 - $89,250	$0 - $59,750	$0 - $44,625	Below $3,000
15%	$44,626 - $492,300	$89,251 - $553,850	$59,751 - $523,050	$44,626 - $276,900	$3,001 - $14,650
20%	Over $492,300	Over $553,850	Over $523,050	Over $276,900	Over $14,650

Net Investment Income Tax

The Net Investment Income Tax (NIIT) is a 3.8% surtax on a portion of modified adjusted gross income over certain filing status-based thresholds:

- $250,000 for married filing jointly or qualifying widow(er)
- $125,000 for married filing separately and
- $200,000 in all other cases

Net investment income includes interest, dividends, capital gains, non-qualified annuity distributions, income from passive investment activities, etc.