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INDIVIDUAL TAX PLANNING

We hope that you are looking forward to the Holiday Season. As the end of the year is fast approaching, we should consider any last-minute strategies that might help reduce your 2019 tax bill. Last year was the first year to be impacted by the Tax Cuts and Jobs Act of 2017 ("TCJA"). While there was no significant new legislation in 2019 affecting individual taxes, situations do change from year to year, thus requiring a fresh look at how to approach year-end tax planning. The following are strategies that may benefit you and that we can discuss before December 31st.

Much of tax planning for the current year depends on what you expect to happen next year and beyond. Will there be any major life changes next year, such as a marriage, additional dependents, a change in jobs, or retirement? The year-end tax strategies will also depend on whether you expect your income to go up or down next year or, correspondingly, whether you expect significant changes in your deductions. The following are some of the items we should review when discussing year-end tax planning options that may be of relevance to your situation.

Marginal Tax Rates for 2019

For 2019, the top tax rate of 37 percent will apply to incomes over $510,300 (single), $612,350 (married filing jointly and surviving spouse), $306,176 (married filing separately), and $510,301 (heads of households). However, high-income taxpayers are also subject to the 3.8 percent net investment income tax and/or the .9 percent Medicare surtax. Finally, as discussed below, there are several tax breaks which expire this year. If you think you may qualify for any one of them, we should nail down what actions need to be taken to get a jump on them before they disappear.

Bunching Deductions into 2019

As you probably are already aware, TCJA significantly increased the standard deduction for all taxpayers. The result is that many individuals who previously received a tax benefit by itemizing deductions no longer do, because taking the standard deduction is more advantageous. For 2019, the standard deduction is $12,200 for single taxpayers, $24,400 for married taxpayers filing a joint return, $18,350 for taxpayers filing as head of household, and $12,200 for married taxpayers filing separately.

In addition, there is a $10,000 limitation ($5,000 in the case of married taxpayers filing separately) on the combined amount of state income taxes and property taxes that may be deducted when itemizing. Unfortunately, this $10,000 limitation applies to single as well as married taxpayers and is not indexed for inflation.

If the total of your itemized deductions in 2019 will be close to your standard deduction amount, alternating between bunching itemized deductions into 2019 and taking the standard deduction in 2020 (or vice versa) could provide a net-tax benefit over a two-year period. For example, if you give a certain amount to charities each year, and if it's financially feasible, you might consider doubling up this year on your contributions rather than spreading the contributions over a two-year period. If these amounts, along with your mortgage interest and medical expenses exceed your standard deduction, then you should double up on the expenses this year and take the standard deduction next year.

Similar opportunities may be available for bunching property tax payments and state income tax payments, subject to TCJA's $10,000 limitation on deductions for such payments. This strategy can be especially attractive for single taxpayers because the standard deduction is so much lower for single individuals. It's important to remember, however, that the deduction for property taxes applies only to property taxes that have been assessed. Thus, if the assessment for 2019 property taxes occurred in 2018 and the taxes are due in 2019, you can deduct in 2019 the taxes assessed for 2019 that you have paid as well as the property taxes assessed for 2020, assuming you also pay the 2020 taxes in 2019.

Finally, if any of your real estate or income taxes can be allocated to a trade or business, they are not subject to the $10,000 limitation.

Mortgage Interest Deduction

If you sold your principal residence during the year and acquired a new principal residence, the deduction for any interest on your acquisition indebtedness (i.e., mortgage) could be limited. The TCJA limits the interest deduction on mortgages of more than $750,000 obtained after December 14, 2017. The deduction is limited to the portion of the interest allocable to $750,000 ($375,000 in the case of married taxpayers filing separately). For mortgages acquired before December 15, 2017, the limitation is the same as it was under prior law: $1,000,000 ($500,000 in the case of married taxpayers filing separately). However, as discussed below, if you operate a business from your home, an allocable portion of your mortgage interest is not subject to these limitations.

You can potentially deduct interest paid on home equity indebtedness, but only if you used the debt to buy, build, or substantially improve your home. Thus, for example, interest on a home equity loan used to build an addition to your existing home is typically deductible, while interest on the same loan used to pay personal living expenses, such as credit card debts, is not.

Home Office Expenses

When the TCJA eliminated the miscellaneous itemized expense deduction, it also eliminated the ability of employees to deduct home office expenses. However, taxpayers with their own business can still file a Schedule C and take a home office expense deduction if part of the home is used for that business. State income taxes, property taxes, and home mortgage interest allocable to your business can also be deducted and such deductions are not subject to the limitations that apply to individual taxpayers who do not operate a Schedule C business from their home.

Retirement Plans Considerations

Fully funding your company 401(k) retirement plan with pre-tax dollars will reduce current year taxes, as well as increase your retirement nest egg. For 2019, the maximum 401(k) contribution you can make with pre-tax earnings is $19,000. For taxpayers 50 or older, that amount increases to $25,000.

If you have a "SIMPLE" retirement plan, the maximum pre-tax contribution for 2019 is $13,000. That amount increases to $16,000 for taxpayers age 50 or older.

If certain requirements are met, contributions to an individual retirement account (IRA) may be deductible. For taxpayers under 50, the maximum contribution amount for 2019 is $6,000. For taxpayers 50 or older but less than age 70 1/2, the maximum contribution amount is $7,000. Contributions exceeding the maximum amount are subject to a 6 percent excise tax. Even if you are not eligible to deduct contributions, contributing after-tax money to an IRA may be advantageous because it will allow you to later convert that traditional IRA to a Roth IRA. Qualified withdrawals from a Roth IRA, including earnings, are free of tax, while earnings on a traditional IRA are taxable when withdrawn.

If you already have a traditional IRA, we should evaluate whether it is appropriate to convert it to a Roth IRA this year. You'll have to pay tax on the amount converted as ordinary income, but subsequent earnings will be free of tax. And if you have a traditional 401(k), 403(b), or 457 plan that includes after-tax contributions, a new rule allows you to generally rollover these after-tax amounts to a Roth IRA with no tax consequences. A rollover of a SIMPLE retirement into a Roth IRA may also be available. As with all tax rules, there are qualifications that apply to these rollovers that we should discuss before you take any actions.

Finally, if you make qualified retirement savings contributions during 2019 you may claim a retirement savings credit of up to $1,000 (single or head of household) or $2,000 (joint filers) if your adjusted gross income does not exceed $64,000 (married filing jointly), $48,000 (head of household), or $32,000 (all other taxpayers).

Reevaluating Your Stock Portfolio

Year-end is a good time to review your stock portfolio to see if you might want to divest yourself of stocks that have lost value since you originally bought them. We should evaluate whether you might benefit from selling off appreciated stocks, particularly those that would generate a short-term capital gain, and using the resulting gain to limit your exposure to a long-term capital loss on stocks you may want to liquidate, since the deduction of long-term capital gains is limited. Any net capital gain you may reap will be taxed at the substantially reduced capital gain tax rate.

The tax rate for net capital gain is generally no higher than 15 percent for most taxpayers. Some or all of your net capital gain may be taxed at 0 percent if your income is not above $39,375 (single), $78,750 (joint), or $52,750 (head of household). However, a 20 percent tax rate on net capital gain does apply to the extent that your ordinary taxable income is over $434,550 (single), $488,850 (joint), $244,425 (married filing separately), or $461,700 (head of household). Additionally, the following types of capital gains have different tax rate structures:

(1) The taxable part of a gain from selling certain qualified small business stock is taxed at a maximum 28 percent rate
(2) The net capital gain from selling collectibles (such as precious metals, coins or art) is taxed at a maximum 28 percent rate
(3) The portion of certain unrecaptured gain from selling real property is taxed at a maximum 25 percent rate.

If you have been involved in any such transactions during the year, we should review your options for reducing the tax on those transactions

Substantial Increases in Deductions or Nontaxable Income Could Result in AMT Exposure

Fewer taxpayers are subject to the alternative minimum tax ("AMT") as a result of the TCJA increasing exemption amounts and raising the exemption phase-out levels, the AMT is not completely eliminated. Certain adjustments to your taxable income, or certain exclusions from gross income, for regular tax purposes are not allowed for AMT purposes and will increase your AMT income ("AMTI"), thus potentially subjecting you to the AMT. Typical items which may reduce regular income but are not allowed for AMTI purposes include the standard deduction, the state and local income tax deduction, and the deduction for property taxes. In addition, the exercise of incentive stock options can result in AMT income, whereas such income is not recognized for regular tax purposes. Thus, if you have exercised any incentive stock options or have had a substantial increase in certain deductions in 2019, but have not previously been subject to the AMT, there is the possibility that you could be subject to the AMT for 2019.

While all taxpayers are eligible for an exemption from the AMT, the amount of the exemption depends on your filing status. For 2019, the exemption amounts for individuals, other than those subject to the kiddie tax, are:

(1) $111,700 in the case of a joint return or a surviving spouse
(2) $71,700 in the case of an individual who is unmarried and not a surviving spouse
(3) $55,850 in the case of a married individual filing a separate return

However, these exemptions are phased out by an amount equal to 25 percent of the amount by which your alternative minimum taxable income (AMTI) exceeds:

(1) $1,020,600 in the case of married individuals filing a joint return and surviving spouses
(2) $510,300 in the case of all other individuals

Child-Related Expenses and Credits

While the TCJA eliminated the personal and dependent exemption deductions that applied to tax years before 2018, it increased the child tax credit available for years after 2017 and increased the income level at which taxpayers are eligible for the credit. For 2019, if you file a joint return and your modified adjusted gross income (MAGI) is $400,000 or less, you are eligible for a $2,000 child tax credit for each qualifying child, with a refundable amount up to $1,400 per child. If you are filing as single, head of household or married filing separately, the MAGI limitation for claiming a child tax credit is $200,000 or less. For income above those levels, a pro rata credit may be available depending on total MAGI. Taxpayers with income below certain thresholds may be eligible for a refundable child tax credit.

A new non-refundable credit up to $500 is available for each dependent who does not qualify for the child tax credit (child over 17 or qualifying relative).

Additionally, if you paid someone to take care of your child or a dependent so you can work or look for work, you may be entitled to a tax credit for up to 35 percent of the expenses paid. The amount of employment-related expenses used to calculate the credit is generally limited to $3,000 for one qualifying individual or $6,000 for two or more qualifying individuals. Various qualifications must be met in order to be eligible for the credit, but if you incurred such expenses, you may qualify. Additionally, if you paid someone to come to your home and care for a child or dependent, you may be a household employer subject to employment taxes.

If you incurred expenses to adopt a child, you may be eligible for a tax credit of up to $14,080 for some or all of those expenses. The determination of the tax year in which qualified adoption expenses are allowable as a credit depends on whether the expenses were paid before the year in which the adoption became final or whether they were paid during or after the year in which the adoption became final.

Avoiding the Net Investment Income Tax

A 3.8 percent tax applies to certain net investment income of individuals with income above a threshold amount. The threshold amounts are $250,000 (married filing jointly and qualifying widow(er) with dependent child), $200,000 (single and head of household), and $125,000 (married filing separately). In general, investment income includes, but is not limited to: interest, dividends, capital gains, rental and royalty income, non-qualified annuities, and income from businesses involved in trading of financial instruments or commodities. Thus, while the top tax rate for qualified dividend income is generally 20%, the top rate on such income increases to 23.8% for a taxpayer subject to the net investment income tax.

If it appears you may be subject to the net investment income tax ("NIIT"), the following actions may help avoid the tax. We should discuss whether any of these options make sense in light of your financial situation.

(1) Donate or gift appreciated property. By donating appreciated property to a charity, you can avoid recognizing the appreciation for income tax purposes and for net investment income tax purposes. Or you may gift the property so that the donee can sell it and report the income. In this case, you'll want to gift the property to individuals that have income below the $200,000 (single) or $250,000 (couples) thresholds.
(2) Replace stocks with state and local bonds. Interest on tax-exempt state and local bonds are exempt from the NIIT. In addition, because such interest income is not included in adjusted gross income, it can help keep you below the threshold for which the NIIT applies.
(3) If you are in the real estate business, we should review the criteria for being classified as a real estate professional. If you meet these requirements, your rental income is considered nonpassive and thus escapes the NIIT.
(4) If you intend to sell any appreciated assets, consider whether the sale can be structured as an installment sale so the gain recognition is spread over several years.
(5) Since capital losses can offset capital gains for NIIT purposes, consider whether it makes sense to sell any losing stocks, but keeping in mind the transaction costs associated with selling stocks.
(6) If you have appreciated real property to dispose of and are not considered a real estate professional, a like-kind exchange may be more advantageous. By deferring the gain recognition, you can avoid recognizing income subject to the NIIT.

Because the NIIT does not apply to a trade or business unless

(1) The trade or business is a passive activity with respect to the taxpayer

(2) The trade or business consists of trading financial instruments or commodities; we may want to look at ways in which a venture you are involved with could qualify as a trade or business. However, such classification could have Form 1099 reporting implications whereas personal payments are not reportable.

Liability for the .9 Percent Medicare Tax

An additional Medicare tax of 0.9 percent is imposed on wages, compensation, and self-employment income in excess of a threshold amount. The threshold amounts are $250,000 (joint return or surviving spouse), $125,000 (married individual filing a separate return), and $200,000 (all others). However, the threshold amount is reduced (but not below zero) by the amount of the taxpayer's wages. Thus, a single individual who has $145,000 in self-employment income and $130,000 of wages is subject to the .9 percent additional tax on $75,000 of self-employment income ($145,000 - $70,000). No tax deduction is allowed for the additional Medicare tax.

For married couples, employers do not take a spouse's self-employment income or wages into account when calculating Medicare tax withholding for an employee. If you and your spouse will exceed the $250,000 threshold in 2019 and have not made enough tax payments to cover the additional .9 percent tax, you can file Form W-4 with the IRS before year end to have an additional amount deducted from you paycheck to cover the additional .9 percent tax. Otherwise, underpayment of tax penalties may apply.

Charitable Contribution Deductions

As a result of the increase in the standard deduction, some taxpayers are no longer getting a benefit from itemizing their deductions, such as charitable contributions, as they once were. However, as noted above, you can still help charities and get a tax benefit if you contribute enough to get over the standard deduction amount or bunch itemized deductions that would otherwise be spread over multiple years into one year.

Additionally, you can reap a larger tax benefit by donating appreciated assets, such as stock, to a charity. Generally, the higher the appreciated value of an asset, the bigger the potential value of the tax benefits. Donating appreciated assets not only entitles you to a charitable contribution deduction but you also avoid the capital gains tax that would otherwise be due if you sold the stock. For example, if you own stock with a fair market value of $1,000 that was purchased for $250 and your capital gains tax rate is 15 percent, the capital gains tax would be $113 ($750 gain x 15%). If you donate that stock instead of selling it, and are in the 24 percent tax bracket, you get an ordinary income deduction worth $240 ($1,000 FMV x 24%). You also save $150 in capital gains tax that you would otherwise pay if you sold the stock. Thus, the after-tax cost of the gift of appreciated stock is $647 ($1,000 - $240 - $113) compared to the after tax cost of a donation of $1,000 cash which would be $760 ($1,000 - $240). However, it's important to also keep in mind that tax deductions for appreciated property are limited to 30 percent of your adjusted gross income.

If you have an unusually high-income year, you may want to consider the use of a donor advised fund (“DAF”) for current and future charitable gifting. This approach can be even more advantageous if you have appreciated investments to fund the DAF. DAF's allow you to place multiple years of charitable contributions in a mutual fund platform to be distributed at your discretion while allowing the tax deduction to be claimed in the first year. Let us know if you would like to consider this strategy.

Direct tax-free distributions from IRA's to 501(c) (3) charities continue to be available and should be considered for certain situations.

Finally, taxpayers 70 1/2 years old and older who own an individual retirement account (IRA) are required to take minimum distributions from that account each year and include those amounts in taxable income. If you are in this category, a special rule allows you to make a charitable contribution directly from your IRA to a charity. This has several benefits. First, since charitable contributions deductions are usually only available to individuals who itemize individuals who take the standard deduction instead can benefit from this rule. Second, making the contribution directly to a charity counts towards your required minimum distribution but that amount is not included in income and thus reduces your taxable income and adjusted gross income (AGI). A lower AGI is advantageous because it increases your ability to take medical expense deductions that you might not otherwise be able to take. For example, medical expenses are only deductible to the extent those expenses exceed 10 percent of your AGI and a lower AGI means you can deduct more medical expenses. In addition, as AGI increases, more of your social security income is subject to tax. Finally, the 3.8 percent net investment income tax applies to the extent your AGI exceeds a certain level.

The TCJA no longer allows taxpayers to deduct payments made in exchange for college athletic event seating rights.

Rental Real Estate

If you own rental real estate, you may be eligible for a special tax break - TCJA's IRC Section 199A deduction - which is based on a percentage of income earned by the rental real estate activity. In order to be eligible for the deduction, the activity must be considerable, regular, and continuous in scope. In determining whether your rental real estate activity meets those criteria, relevant factors include, but are not limited to, the following:

(1) The type of rented property (commercial real property versus residential property)
(2) The number of properties rented
(3) You or your property management agent's day-to-day involvement

(4) The types and significance of any ancillary services provided under the lease
(5) The terms of the lease (for example, a net lease versus a traditional lease and a short-term lease versus a long-term lease)

Under a safe harbor issued by the IRS, a rental real estate activity will be treated as a business eligible for the special deduction if certain requirements are satisfied, such as:

(1) Separate books and records are maintained to reflect the income and expenses for each rental real estate enterprise
(2) For rental real estate enterprises that have been in existence less than four years, 250 or more hours of rental services are performed per year with respect to the rental real estate enterprise (with slightly less stringent requirements for rental real estate enterprises that have been in existence for at least four years)
(3) Contemporaneous records have been maintained, including time reports, logs, or similar documents, regarding the following:
   a. hours of all services performed;
   b. description of all services performed;
   c. dates on which such services were performed
   d. who performed the services
(4) Certain compliance requirements are met

If you think you may be eligible for this deduction, we should get together to nail down any last steps you may need to take to fall within the safe harbor. Alternatively, even if you don't meet the safe harbor requirements, you may still be eligible for this deduction.

In addition, if you rent out a vacation home that you also use for personal purposes, we should review the number of days it was used for business versus pleasure to see if there are ways to maximize tax savings with respect to that property.

American Opportunity Credit

If you, your spouse, or any dependent incurred "qualified" education expenses to attend an accredited post-secondary institution (e.g., a college or university); you may be eligible for the American Opportunity Credit. The maximum annual credit is $2,500 per eligible student. Expenses which qualify for the tax credit include tuition and required fees for the enrollment or attendance at an eligible educational institution.

In order to claim an American Opportunity or lifetime learning credit or a deduction for education-related tuition and fees, you must have received a Form 1098-T. The form reports qualified tuition and related expenses received by the educational institution. The information reported on this form will be matched against the information reported to the Internal Revenue Service ("IRS"). If you have educational expenses eligible for the credit or deduction, you should receive Form 1098-T from the educational institution to which you made payments by January 31, 2019. While the form is supposed to report the aggregate amount of payments received by the educational institution, there is a one-year transition period where institutions may report the amount billed for 2018 rather than the amount paid.

Because the form only reports qualified tuition and related expenses, you may see a discrepancy between the amounts you paid and the amounts reported. This is due to the fact that certain expenses, such as fees for room, board, insurance, medical expenses, transportation, etc. are not considered qualified tuition and related expenses and thus are not reported on Form 1098-T.

Foreign Bank Account Reporting

The IRS has become increasingly aggressive at tracking down individuals who have not reported foreign bank accounts. If you have an interest in a foreign bank account, it must be disclosed; failure to do so carries stiff penalties. You must file a Report of Foreign Bank and Financial Accounts (FBAR) if:

(1) You are a U.S. resident or a person doing business in the United States
(2) You had one or more financial accounts that exceeded $10,000 during the calendar year
(3) The financial account was in a foreign country
(4) You had a financial interest in the account or signatory or other authority over the foreign financial account. If you are unclear about the requirements or think they could possibly apply to you, please let me know at your earliest convenience.

The deadline for filing the form was moved up and it is now due April 15. However, a six-month extension is available. If an individual is abroad, the due date is automatically extended until October 15.

Health Savings Account ("HSA")

For 2019, your medical expenses are only deductible as an itemized deduction to the extent they exceed 10 percent of your adjusted gross income. Depending on what your taxable income is expected to be in 2019 and 2020, and whether itemizing deductions would be advantageous for you in either year, you may want to accelerate any optional medical expenses into 2019 or defer them until 2020. The right approach depends on your income for each year, expected medical expenses, as well as your other itemized deductions.

However, health saving accounts ("HSA's") presents an attractive alternative. If you are eligible to set up such an account, you can deduct the amount you contribute to the account in computing Adjusted Gross Income ("AGI"). Thus, the contributions are deductible whether you itemize deductions or not. Distributions from an HSA are tax-free to the extent they are used to pay for "qualified" medical expenses (i.e., medical, dental, Rx, and vision expenses). The deductible amounts are $1,350 for individuals and $2,700 for family plans; while out of pocket expenses are limited to $6,750 for individuals and $13,500 for family plans Contributions can only be made while the account holder remains covered by an HDHP; and can funded by payroll deductions, employer contributions, or individuals. Contributions are limited to $3,500 for individual and $7,000 for families in 2019. (Individuals who are age 55 or older at the end of 2019 can contribute an additional $1,000). Any amounts in excess of these limits are subject to a 6% excise tax. You are allowed to remove the excess amounts prior to filing your current income tax return without any penalties (will be subject to income tax on the excess plus any gains on the amount).

Key advantages of a HSA are that the money can be rolled over to the following year (without reducing your contribution limit) and the HSA goes with the employee regardless of whether contributions were made by the employee or employer.

The funds in a HSA can be used for qualified medical expenses without any penalties or taxes owed. If an individual withdraws funds for reasons unrelated to medical expenses, there is a 20% penalty as well as taxes to be owed (think of it as a traditional IRA distribution). Individuals over 65 are allowed to withdraw funds without incurring the penalty but taxes will be owed.

You are able to bequeath your HSA account as long as the beneficiary is designated at time of death.

Flexible Spends Account ("FSA")

A FSA is similar to a HSA regarding the use pre-tax contributions to pay for qualified medical expenses tax-free. FSAs are established by the employer and can be funded by the employee and employer. Contributions are limited to $2,700 per individual, so you and your spouse can have a FSA account each for a total limit of $5,400.

Unlike the HSA, the FSA allows you to have any type of health insurance coverage. A downside to this flexibility is that any money not used by the end of the year will be forfeited. Employers are allowed to grant a two and half month grace period that runs into the following year (to March 15th) for you to use the excess money. Employers can allow enrollees to carry over up to $500 to the next year instead of allowing for the grace period.

The full annual contribution amount is available for use immediately (or after the first contribution is made). If the employee uses the full amount and then quits or is terminated prior to the end of the year, FSA funds do not have to be paid back to the employer. The FSA is linked to your job, so a change of employers will terminate the account.

Education-Related Deductions and Credits

While the tuition and fees deduction that had previously been available expired at the end of 2017 along with the miscellaneous itemized deduction for work-related education expenses, other education-related tax deductions, credits, and exclusions from income may apply for amounts paid in 2019. Tax-free distributions from a qualified 529 tuition program of up to $10,000 are now allowed for elementary or secondary school tuition. In addition, if your modified adjusted gross income level is below certain thresholds, the following are available for 2019:

(1) An exclusion from income for education savings bond interest
(2) A deduction for student loan interest
(3) A lifetime learning credit of up to $2,000 for tuition and fees paid for the enrollment or attendance of yourself, your spouse, or your dependents for courses of instruction at an eligible educational institution

Revised Kiddie Tax Rules

One of the changes made by TCJA involves what is known as the "kiddie tax." The kiddie tax applies to a child's net unearned income (e.g., dividends, interest, and capital gain distributions) over $2,200. While such income used to be taxed at the parent's marginal income tax rate and took into consideration the unearned income of any siblings, TCJA simplified the calculation so that the child's unearned income is taxed at trust and estate tax rates. Although the trust and estate tax rates are similar to the individual tax rates, the tax brackets are much lower, meaning higher rates of tax apply to lower levels of income.

For 2019, the top marginal tax rate for a couple filing a joint return is 37% for taxable income over $612,350. For income subject to the estate and trust tax rates, the 37% tax rate begins at taxable income over $12,750. There is a way to save some taxes here, however, if your child is under the age of 18 at the end of 2019 and didn't have earned income that was more than half of the child's support, or a full-time student at least age 19 and under age 24 and the end of 2019 and didn't have earned income that was more than half of the child's support. For such children, you can elect to include the child's income on your tax return. However, we would need to evaluate whether adding such income to your tax return would subject you to the net investment income tax of 3.8 percent.

Capital Loss Deductions and Worthless Securities

Annually you are permitted to deduct up to $3,000 in net capital losses against ordinary income. You are also able to net any capital gains against capital losses prior to applying the $3,000 limitation. The strategy is to review your investment portfolio and recognize up to $3,000 in capital losses in excess of capital gains prior to December 31st. Also, do not overlook any securities that may have become worthless. These investments should also be reported to recognize the capital loss. If you have any near-worthless securities, you may want to consider selling or surrendering the position so that the capital loss can be recognized in 2019. Finally, do not overlook any capital loss carryovers from prior years that can benefit you in 2019.

Virginia Education Savings Plan ("529 Accounts")

The 2019 Virginia deduction for contributions to a Virginia 529 plan is $4,000 per account. If you are 70 years old or older, there is no limit on the deduction for contributions. We suggest you review your 2019 contributions to any Virginia 529 plan to be sure you are maximizing your benefits.

The TCJA modified the Section 529 to allow such plans to distribute no more than $10,000 for expenses incurred for the tuition and attendance of a public, private or religious elementary or secondary school. The limitation is on a per-student basis and not by account. Any amount over $10,000 will be treated as a distribution subject to tax.

Gifting Appreciating Investments

If you have children, particularly of college age, consider if there is any income that can be shifted to them so that the tax on the income is paid at the child's tax rate. One strategy is gifting appreciated stock to the child. Where a child has earned income and is taxed at the bottom two income brackets, capital gains generated on the stock sale are taxed at 0%, instead of the 15% or more that the parent would pay. However, if the child has little or no earned income, the kiddie tax could be a factor. In this case, you will want to limit the child's unearned income to $2,200 or less for 2019 in order to avoid having your top tax rate apply to the child's income.

Timing Income and Deductions

If there is going to be a dramatic swing in your taxable income or your life circumstances between 2019 and 2020, it may make sense to do one or more of the following:

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Accelerating Income into 2019

(1) Harvesting gains from your investment portfolio, keeping in mind the 3.8 percent NIIT
(2) Converting a retirement account into a Roth IRA and recognizing the conversion income this year
(3) Taking IRA distributions this year rather than next year
(4) If you are self-employed and have clients that owe you money, try to get them to pay before year-end
(5) Settling any outstanding lawsuits or insurance claims that will generate income this year

Deferring Deductions into 2020

If you anticipate a substantial increase in taxable income next year, it may be advantageous to push deductions into 2020 by:

(1) Postponing year-end charitable contributions, property tax payments, and medical and dental expense payments, to the extent deductions are available for such payments, until next year
(2) Postponing the sale of any loss-generating property

Deferring Income into 2020

If it looks like you may have a significant decrease in income next year, either from a reduction in income or an increase in deductions, it may make sense to defer income into 2020 or later years. Some options for deferring income include:

(1) If you are due a year-end bonus, having your employer pay the bonus in January 2020
(2) If you are considering selling assets that will generate a gain, postponing the sale until 2020
(3) If you are considering exercising stock options, delaying the exercise of those options
(4) If you are planning on selling appreciated property, consider an installment sale with larger payments being received in 2020
(5) Consider parking investments in deferred annuities

Accelerating Deductions into 2019

If you expect a decrease in income next year, accelerating deductions into the current year can offset the higher income this year. Some options include:

(1) Prepaying property taxes in December, keeping in mind the $10,000 limitation on deducting state income and property taxes and the fact that the property taxes must have been assessed in order to be deductible
(2) If you owe state income taxes, making up any shortfall in December rather than waiting until your state income tax return is due (and similarly keeping in mind the $10,000 limitation)

(3) Making your January mortgage payment in December
(4) Making any large charitable contributions in 2019, rather than 2020
(5) Selling some or all loss stocks
(6) If you qualify for a health savings account, setting one up and making the maximum contribution allowable

Other Considerations

Here are some additional items to consider:

Flexible Spending Accounts: Generally, you will lose any amounts remaining in a health flexible spending account at the end of the year unless your employer allows you to use the account until March 16, 2020, in which case you'll have until then. You should check with your employer to see if the employer gives employees the optional grace period to March 16, 2020.

Life Events: Life events can significantly impact your taxes. For example, if you are using head of household or surviving spouse filing status for 2019, but will change to a filing tax status of single for 2020, your tax rate will go up. Thus, accelerating income into 2019 and pushing deductions into 2020 may also yield tax savings.

Individual Healthcare Penalty: For 2019, the tax penalty on individuals who fail to carry health insurance, which was enacted as part of the Affordable Care Act, has been eliminated.

Moving Expense Reimbursement: If you received a reimbursement from your employer for moving expenses incurred in 2019, the reimbursement is taxable income. While taxpayers could previously deduct employment-relating moving expenses, this deduction is no longer available for moves taking place in years 2018-2025, unless you are a member of the U.S. Armed Forces on active duty and move pursuant to a military order to a permanent change of station.

Casualty and Theft Losses: If you incurred a casualty loss in a presidentially declared disaster area in 2019, it may be deductible. Any other casualty losses, along with all theft losses, are not deductible.

IRC Section 199A Pass-through Tax Break: Enacted as part of TCJA, the Section 199A tax break allows a 20 percent deduction for qualified business income from sole proprietorships, S corporations, partnerships, and LLCs taxed as partnerships. If you qualify for the deduction, which is available to both itemizers and nonitemizers, it is taken on your individual tax returns as a reduction to taxable income. The new tax break is subject to some complicated restrictions and limitations, but the rules that apply to individuals with taxable income at or below $160,700 ($321,400 for joint filers; $160,725 for married individuals filing separately) are simpler and more permissive than the ones that apply above those thresholds.

Mortgage Interest Deduction: Was lowered to $750,000 of indebtedness. Mortgages incurred at the old limitation ($1,000,000) prior to December 14, 2017 will be grandfathered in. The TCJA has also eliminated the deduction for interest on home equity loans. Unless the proceeds from the loan go to improvement/renovation of the home they are secured by, then $100,000 is deductible.

Alimony: For any divorce agreement executed or modified after December 2018, alimony payments will no longer be deductible and alimony received will no longer be included in taxable income. Divorce agreements that are finalized prior to December 31, 2018 will be grandfathered in under the prior rules.

Qualified Teacher Expense: Deduction by elementary and secondary school teachers of up to $250 of qualified expenses they paid during the year ($500 on a joint return if both spouses were eligible educators) and expand the deduction to include expenses in connection with the professional development activities of an educator.

Virginia Livable Home Credit

Virginia has increased the credit to 50% of the cost limited to $5,000 in tax credits for certain qualified home improvements designed to improve the accessibility of your home.

Virginia Conservation Easement Credit

Virginia taxpayers have an opportunity to purchase tax credits at a discount of .87 - .92 cents to the dollar. These credits can be applied to your total Virginia income tax liability up to $20,000 for each taxpayer. We are available to assist you to determine the amount of credits that should be considered.

Virginia Neighborhood Assistance ("NAP") Credits

The purpose of the Virginia Neighborhood Assistance Act is to encourage individuals, trusts and businesses to make donations to pre-approved 501(c) (3) non-profit organizations, known as Virginia Neighborhood Assistance Programs ("NAPs"). Tax credits are available to individuals and married couples donating cash or securities directly to NAPs. The minimum amount to be donated is $500 by an individual or married couple. Any eligible charitable organization must have applied to participate in the Virginia Neighborhood Assistance Program to be allocated credits. If you contribute to a participating charitable organization, you must fill out the Contribution Notification Form and submit it to the charitable organization. The charitable organization will then notify the Virginia Department of Taxation that you have been transferred credits and you will be issued a tax credit certificate, which will need to be attached to your Virginia tax return.

Only a limited amount of credits are available for each qualifying charity each year. You might not receive a credit if the organization has already distributed its share of credits. If you receive more credits than you can use this year, the credits may be carried-forward for up to five years.

For more information about the Virginia Neighborhood Assistance Act and for a full list of qualifying charitable organizations, go to the Department of Social Services website at http://www.dss.virginia.gov/community/nap.cgi. Please contact our office if you have questions on the Virginia NAP.

Virginia Education Improvement Scholarship Tax Credits

Individuals or businesses can make monetary or marketable securities donations to approved foundations. The donations will be used to provide scholarships to low-income new students of non-public schools. Donors will then receive a Virginia tax credit for 65% of the donation, in addition to the normal charitable donation deductions on federal and state taxes for taxpayers that itemized their deductions. This credit requires a preauthorization process to qualify for tax credits.

Estate Tax Exemption and Rate

The maximum estate tax rate is 40%. An $11,400,000 exemption amount is available for estates of individuals dying in 2019. The exemption amount is indexed for inflation each year.

Gift Tax

The Act unified the estate exemption amount with the gift tax. In other words, the $11,400,000 exemption amount is available to reduce the gift tax during life and any unused amount of the $11,400,000 exemption is available to be used for estate tax purposes at death. The annual exclusion for 2019 is $15,000 and it if an election is made to split the gifts among spouses, the annual exclusion per recipient increases to $30,000.

Life Events

Certain life events can also affect your tax situation. If you got married or divorced, had a birth or death in the family, lost or changed jobs, or retired during the year, we need to discuss the tax implications of these events.

Miscellaneous Items

Finally, these are some additional miscellaneous items to consider:

(1) Spend any remaining health flexible spending account balances before year end (unless your employer allows you to go until March 16, 2020, in which case you'll have until then). You should check with your employer to see if they give employees the optional grace period to March 16.
(2) If you rent out a vacation home, we should review at the number of days it was used for business versus pleasure to see if there are ways to maximize tax savings with respect to that property.

Let us know if you have any questions, or if you require any clarification of any of these subjects. We wish you a successful conclusion to the year and a Happy Holiday Season.

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