December 13, 2023

Dear Clients and Friends,

As the year-end approaches, it is time to start thinking about moves that may help lower your tax bill for this year and next.

Even though 2023 was a relatively quiet year regarding legislation, the Inflation Reduction Act of 2022 introduced two new corporate taxes that became effective beginning in 2023; and the retirement plan-related changes made by the SECURE 2.0 Act, which passed late in December 2022, also took effect beginning in 2023. In Oregon, the Oregon Office of Economic Analysis (OEA) announced a more than $5.61 billion revenue surplus in the 2021-2023 biennium, triggering a tax surplus credit, or “kicker,” for the 2023 tax year.

There are many tax provisions that will expire on December 31, 2025, and therefore we suggest looking to the future and potentially accelerating income into 2023, 2024, and 2025, to take advantage of these provisions now. They include the income tax rates and income brackets reverting to 2017 levels (adjusted for inflation), the lowering of the standard deduction, the reduction of the estate and gift tax exemption to around $6.5 million (cut in half from post 2017 Tax Cuts and Jobs Act), and the elimination of the 20% Qualified Business Income (QBI) deduction. Due to these and the expiration of other provisions, our advice this year and for the following two years is at odds with our usual advice of deferring income and accelerating deductions. You should think very hard about accelerating income to take advantage of these historically low, income tax rates.

Below is a checklist of items that may benefit you if you act before year-end. We can better identify the actions you can take if we meet with you to tailor a particular plan. Meanwhile, please review the following list. Contact us at your earliest convenience so that we can advise you on which tax-saving moves to make.

Year-End Tax Planning Moves for Individuals

- **2023 Oregon Kicker Credit**
  Consider adjusting your Oregon withholding amount for the remainder of the year if you are expecting a large refund as a result of the kicker credit. The 2023 kicker is calculated by multiplying your 2022 tax liability, before any credits, by 44.28 percent.

- **Surtax on Unearned Income for Higher Income Earners**
  Some taxpayers should consider ways to minimize (e.g. - through deferral) additional Net Investment Income (NII) for the balance of the year, others should try to see if they can reduce modified adjusted gross income (MAGI) other than NII, and other individuals will need to consider ways to minimize both NII and other types of MAGI.

The surtax is 3.8% of the lesser of: (1) Net Investment Income (e.g. – bonds, stocks, mutual funds, etc.) or (2) The excess of modified adjusted gross income over a threshold amount ($250,000 for joint filers or surviving spouses, $125,000 for a married individual filing a separate return, and $200,000 in any other case).

- **An additional Medicare Tax for Higher-Income Earners**
  The 0.9% additional Medicare tax also may require higher-income earners to take year-end action. It applies to individuals whose employment wages and self-employment income total more than an amount equal to the NIIT thresholds, above. Employers must withhold the additional Medicare tax from wages in excess of $200,000 regardless of filing status or other income. Self-employed persons must take it into account in figuring estimated tax.

  There could be situations where an employee may need to have more withheld toward the end of the year to cover the tax. This would be the case, for example, if an employee earns less than $200,000 from multiple employers but more than that amount in total. Such an employee would owe the additional Medicare tax, but nothing would have been withheld by any employer.

- **Long-term Capital Gain**
  Long-term capital gain from sales of assets held for over one year is taxed at 0%, 15% or 20%, depending on your taxable income. The 0% rate generally applies to net long-term capital gain to the extent that, when added to regular taxable income, it is not more than the maximum zero rate amount (e.g., $89,250 for a married couple; $41,675 for single individuals). If, say, $5,000 of long-term capital gains you took earlier this year qualifies for the zero rate then try not to sell assets yielding a capital loss before year-end, because the first $5,000 of those losses will offset $5,000 of capital gain that is already tax-free.

- **Postpone income until 2024 and accelerate deductions into 2023**
  Deferring income and accelerating deduction may enable you to claim larger deductions, credits, and other tax breaks for 2023 that are phased out over varying levels of adjusted gross income (AGI). These include deductible IRA contributions, child tax credits, higher education tax credits, and deductions for student loan interest. Postponing income is also desirable for those of you who anticipate being in a lower tax bracket next year due to changed financial circumstances. However, as noted above, it is important to look at the tax provisions expiring at the end of 2025, and to take advantage of those lower rates. This could mean accelerating income and deferring deductions, which is the opposite of what we normally advise. Please reach out to us for a personalized plan related to these provisions.

- **Roth IRA**

If you believe a Roth IRA is better for you than a traditional IRA, consider converting traditional-IRA money invested in any beaten-down stocks (or mutual funds) into a Roth IRA in 2023 if eligible to do so. Keep in mind that the conversion will increase your income for 2023, possibly reducing tax breaks subject to phaseout at higher AGI levels.

- **Payroll Bonuses**
  If you have a bonus coming your way at the end of 2023, it may be of benefit to have your employer defer it until 2024. This change could lower, as well as defer your tax.

- **Itemized Deductions**

  Similar to last year, if you routinely claimed itemized deductions, you may not have been able to do so on your Federal return. That is because the basic standard deduction was increased. For the 2023 tax year, it is as follows:
    - $27,700 for joint filers,
    - $13,850 for singles,
    - $20,800 for heads of household
    - $13,850 for married filing separately

  Many itemized deductions remain either cut back or abolished.

For example:

(1) No more than $10,000 of state and local taxes may be deducted.

(2) Miscellaneous itemized deductions (e.g. – investment advisory fees) and unreimbursed employee expenses are no longer deductible.

(3) Personal casualty and theft losses are deductible only if they're attributable to a federally declared disaster and only to the extent the $100-per-casualty and 10%-of-AGI limits are met.

You can still itemize medical expenses to the extent they exceed 7.5% of your adjusted gross income, state and local taxes up to $10,000, your charitable contributions, and interest deductions on a restricted amount of qualifying personal residence debt. But, payments of those items will not save on Federal taxes if they do not cumulatively exceed the new, higher standard deduction.

For those filing Oregon returns, itemizing is still beneficial to many. Be sure to still hang on to required documentation to support your itemized deductions.

Here are some possible strategies to help with these limitations that remain in effect.

- Some of you may be able to work around these deduction restrictions by applying a bunching strategy to pull or push discretionary medical expenses and charitable contributions into the year where they will do some tax good. For example, if you will be able to itemize deductions this year but not next will benefit by making two years' worth of charitable contributions this year. The COVID-related increase in the income-based charitable deduction limit for cash contributions from 60% to 100% of MAGI no longer assists in this bunching strategy as it has expired for 2023.

- Consider using a credit card to pay deductible expenses before the end of the year. Doing so will increase your 2023 deductions even if you don't pay your credit card bill until after the end of the year.

- If you expect to owe state and local income taxes when you file your return next year and you will be itemizing in 2023, consider asking your employer to increase withholding of state and local taxes (or make estimated tax payments of state and local taxes) before year-end to pull the deduction of those taxes into 2023. But this strategy is not good to the extent it causes your 2023 state and local tax payments to exceed $10,000.

- The SECURE 2.0 Act increased the age for required beginning date for mandatory distributions. If you were 73 or older in 2023 you must take a required minimum distribution (RMD) during 2023. Those who turn 73 this year have until April 1 of 2024 to take their first RMD but may want to take it by the end of 2023 to avoid having to double up on RMDs next year.

- If you have an inherited IRA, please be aware that IRS has clarified the 10-year rule regarding distributions. In 2019, the Secure Act was passed, which made several changes to retirement accounts. One change was the requirement that certain beneficiaries empty the inherited IRA account within ten years of the original owner's death. This rule made many believe that RMDs did not have to be paid. However, IRS recently clarified that RMDs still must be paid each year, and the account has to be emptied within ten years. If you have an inherited IRA, it is important that you reach out to your investment adviser. We can also assist with planning in regards to how the RMDs will affect your taxes.

- 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 IRAs. These distributions are made directly to charities from your IRAs, and the amount of the contribution is neither included in your gross income nor deductible on Schedule A, Form 1040. However,

you are still entitled to claim the entire standard deduction. (The qualified charitable distribution amount is reduced by any deductible contributions to an IRA made for any year in which you were age 70½ or older, unless it reduced a previous qualified charitable distribution exclusion.)

- If you are facing a penalty for underpayment of estimated tax, taking an eligible rollover distribution from a qualified retirement plan before the end of 2023 and increasing your wage withholding will not sufficiently address the problem. Income tax will be withheld from the distribution and will be applied toward the taxes owed for 2023. You can then timely roll over the gross amount of the distribution, i.e., the net amount you received plus the amount of withheld tax, to a traditional IRA. No part of the distribution will be includible in income for 2023, but the withheld tax will be applied pro rata over the full 2023 tax year to reduce previous underpayments of estimated tax.

- Consider increasing the amount you set aside for next year in your employer's FSA if you set aside too little for this year and anticipate similar medical costs next year. If you become eligible in December of 2023 to make HSA contributions, you can make a full year's worth of deductible HSA contributions for 2023.

- Make gifts sheltered by the annual gift tax exclusion before the end of the year if doing so may save gift and estate taxes. The exclusion applies to gifts of up to $17,000 made in 2023 to each of an unlimited number of individuals. You can't carry over unused exclusions to another year. These transfers may save family income taxes where income-earning property is given to family members in lower income tax brackets who are not subject to the kiddie tax.

- If you were in a federally declared disaster area, you may want to settle an insurance or damage claim in 2023 to maximize your casualty loss deduction this year.

Year-End Tax-Planning Moves for Businesses & Business Owners

- **Oregon Pass-Through Entity Election**
  Oregon established an elective Pass-Through Entity Tax (PTE-E), a business alternative income tax in response to the $10,000 cap on the federal State and Local Tax (SALT) deduction added in the 2017 federal Tax Cuts and Jobs Act. Entities taxed as S corporations and partnerships may elect annually to be subject to the PTE-E tax at a rate of 9 percent tax on the first $250,000 of distributive proceeds and 9.9 percent tax on any amount exceeding $250,000. The law will expire if the federal SALT deduction limitation expires or is repealed.

Qualifying members of an electing PTE are eligible for a credit equal to 100 percent of the member's distributive share of the PTE-E tax paid. This allows for the State tax on the pass-through earnings to be paid at the entity level, thereby lowering the Federal taxable income for the shareholder or partner's income tax return.

- **Qualified Business Income (QBI)**
  Taxpayers other than corporations may be entitled to a deduction of up to 20% of their qualified business income (QBI). This deduction expires at the end of 2025.

  For 2023, if taxable income for joint filers exceeds $464,200 (about half of that for others), the deduction may be limited based on whether you are engaged in a service-type trade or business (such as law, accounting, health, or consulting), the amount of W-2 wages paid by the trade or business, and/or the unadjusted basis of qualified property (such as machinery and equipment) held by the trade or business. The limitations are phased in; for example, the phase-in applies to joint filers with taxable income up to $100,000 above the threshold, and to other filers with taxable income up to $50,000 above their threshold.

- **Cash Method of Accounting**
  More small businesses are able to use the cash (as opposed to accrual) method of accounting in than were allowed to do so in earlier years. To qualify as a small business a taxpayer must, among other things, satisfy a gross receipts test. For 2023, the gross-receipts test is satisfied if, during a three-year testing period, average annual gross receipts don't exceed $29 million (next year the dollar amount is estimated to increase to $30 million). Cash method taxpayers may find it a lot easier to shift income, for example by holding off billings till next year or by accelerating expenses, for example, paying bills early or by making certain prepayments.

- **Business Property Expensing**
  Businesses should consider making expenditures that qualify for the liberalized business property expensing option. For tax years beginning in 2023, the expensing limit is $1,160,000, and the investment ceiling limit is $2,890,000. Expensing is generally available for most depreciable property (other than buildings) and off-the-shelf computer software. It is also available for qualified improvement property (generally, any interior improvement to a building's interior, but not for enlargement of a building, elevators or escalators, or the internal structural framework), for roofs, and for HVAC, fire protection, alarm, and security systems.

  The generous dollar ceilings mean that many small and medium sized businesses that make timely purchases will be able to currently deduct most of their outlays for machinery and equipment. What's more, the expensing deduction is not prorated for the time that the asset is in service during the year. The fact that the expensing deduction may be claimed in full (if you are otherwise eligible to take it) regardless of

how long the property is in service during the year can be a potent tool for year-end tax planning. Thus, property acquired and placed in service in the last days of 2023, rather than at the beginning of 2024, can result in a full expensing deduction for 2023.

However, key business tax provisions for the 2024 fiscal year budget include a proposal to increase the U.S. corporate income tax rate from 21% to 28%. Deferring big purchases into future years might result in a better strategy if a future corporate tax rate increase does pass. At this time, we don't feel a corporate tax increase is likely to occur until after the next general election but keep this issue in mind as this issue could very likely raise its head a year from now.

- **Bonus Depreciation**
  For 2023, a first-year bonus depreciation deduction falls to 80% from the previous 100% for machinery and equipment bought used (with some exceptions) or new if purchased and placed in service this year, and for qualified improvement property, described above as related to the expensing deduction.

  The deduction is permitted without any proration based on the length of time that an asset is in service during the tax year and is available even if qualifying assets are in service for only a few days in 2023.

  The bonus depreciation deduction will continue to decrease 20% every year until it reaches 0% for property placed into service in 2027.

- **De Minimis Safe Harbor Election**
  Businesses may be able to take advantage of the de minimis safe harbor election (also known as the book-tax conformity election) to expense the costs of lower-cost assets and materials and supplies, assuming the costs don't have to be capitalized under the Code Sec. 263A uniform capitalization (UNICAP) rules. To qualify for the election, the cost of a unit of property can't exceed $5,000 if the taxpayer has an applicable financial statement (AFS; e.g., a certified audited financial statement along with an independent CPA's report). If there's no AFS, the cost of a unit of property can't exceed $2,500. Where the UNICAP rules aren't an issue, consider purchasing such qualifying items before the end of 2023.

- **Net Operating Loss (NOL)**
  A corporation (other than a large corporation) that anticipates a small net operating loss (NOL) for 2023 (and substantial net income in 2024) may find it worthwhile to accelerate just enough of its 2024 income (or to defer just enough of its 2023 deductions) to create a small amount of net income for 2023. This will permit the corporation to base its 2024 estimated tax installments on the relatively small amount of income shown on its 2023 return, rather than having to pay estimated taxes based on 100% of its much larger 2024 taxable income.

- **Other Ideas to reduce 2023 taxable income**
    - To reduce 2023 taxable income, consider deferring a debt-cancellation event until 2024.
    - To reduce 2023 taxable income, consider disposing of a passive activity in 2023 if doing so will allow you to deduct suspended passive activity losses.

These are just some of the year-end steps that can be taken to save taxes. Again, by contacting us, we can tailor a particular plan that will work best for you.

Cheers to a safe and peaceful rest of 2023.

Sincerely,

HMW CPAs & Associates, LLC