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COMMENTARY

2023 Year-End Tax Planning Guidance and Tips

As we reach the end of the year, it is a good time to focus on addressing year-end tax planning. At this late juncture, many of our clients (and, hopefully, readers too) have already started to implement or, at least, think about year-end planning.

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Trusts and Estates

By Amy Neifeld Shkedy and Rebecca Rosenberger Smolen | December 18, 2023 at 09:34 AM

As we reach the end of the year, it is a good time to focus on addressing year-end tax planning. At this late juncture, many of our clients (and, hopefully, readers too) have already started to implement or, at least, think about year-end planning. In this article we have listed some key issues to consider before the end of 2023:

- **Annual Exclusion Gifts.**

Each individual can make cumulative annual gift tax exclusion gifts of $17,000 per donee during 2023 ($34,000 for a married couple electing to split gifts). The IRS has announced that this amount will increase to $18,000 for 2024 ($36,000 for a married couple electing to split gifts in 2024). Annual exclusion gifts do not use any portion of an individual's federal estate and gift tax exemption (discussed below). Annual exclusion gifts can be made outright, through 529 Plan benefits (education savings accounts), or in special qualifying trust structures. For those still considering such gifts, it may be worthwhile to plan for 2023 and 2024 at the same time, keeping in mind that gifts for 2024 can be made effective as of Jan. 1.

- **Use of Exemption.**

For 2023, the federal and gift tax exemption amount is $12.92 million per individual (allowing a married couple to shield up to $25.84 million from federal estate and gift taxes), and is projected to increase for inflation in 2024 to $13.61 million per individual (or $27.22 million for a married couple). There is no guarantee that these exemption amounts will remain at such high level. Under current law, the exemptions are set to be cut in 2026 to 50% of the current levels.

High net worth individuals may consider whether to make large gifts in order to use their exemptions before the amounts are reduced. Many have already implemented such gift tax planning and may choose to make additional gifts beyond the annual gift tax exclusion gifts to take advantage of the inflation adjusted increases. This isn't necessarily a year-end deadline, however, we can never know with certainly when the tax laws may change and the exemptions may be reduced, so we should be mindful of the potential decrease in the exemptions and consider whether exemptions should be used sooner rather than later (particularly before 2026).

- **Accelerate Deductions.**

Taxpayers can prepay deductible expenses due in January (including state and local income tax estimated payments which may not be due until January). However, because of the $5,000 per person cap (i.e., $10,000 for a married couple) for deductions for all state and local taxes, it's important to ascertain whether the limit has been reached before accelerating a payment of such taxes which may be deferred until 2024.

- **Loss Harvesting.**

Taxpayers can harvest tax deductible losses to offset taxable gains for 2023. However, be mindful of the 30 day wash sale rule of Internal Revenue Code Section 1091, which could disqualify a deduction of the capital loss if the same, or substantially identical, security is purchased within 30 days after selling at a loss.

- **Required Minimum Distributions.**

For those of you who have reached your required beginning date or who hold inherited IRA accounts, you should take your required minimum distribution for 2023 from your traditional IRA or qualified plan account by Dec. 31. Taxpayers who are 72 or older are able to transfer up to $100,000 from an IRA (other than an inherited IRA) directly to a qualifying charity (a charitable rollover) in partial or full satisfaction of their required minimum distribution for 2023.

For the participant, the required minimum distribution amount can be calculated based on the participant's life expectancy. After the participant's death, determining the required minimum distributions of inherited IRAs is different, and falls under the updated distribution rules of the Secure Act. As we have previously noted in our past articles, the required minimum distribution period for most beneficiaries is limited to 10 years after the death of the IRA owner or retirement plan participant. However, it has remained uncertain whether or not beneficiaries are required to take distributions each year during the 10-year period or if they can wait until the expiration of the 10-year period. Due to the uncertainty, the IRS had previously issued Notice 2022-53 which related to 2021 and 2022 distributions and this year the IRS has issued another notice (Notice 2023-54), under which the IRS has waived the annual requirement for distributions for 2023 for beneficiaries who would be subject to the 10-year distribution period. In the event that it is ultimately concluded that annual distributions are required during the 10-year period, the deadline for the first annual distribution under the new Secure Act rules wouldn't be until Dec. 31, 20224. Without the waiver of this requirement for 2023, taxpayers faced the risk of a 50% tax penalty on required annual distributions that were not timely made.

- **Qualified Retirement Plan Establishment.**

Business owners who are considering funding a new retirement plan have the opportunity to establish a qualified retirement plan by the end of the year but defer the decision about the funding amount (and the actual contribution) until later during 2024 (contributions can generally be delayed until at least Sept. 15). The limitation for tax deductible contributions for 2023 is $66,000 per participant for defined contribution plans (or up to $73,500 when including the $7,500 catch-up contribution for a participant who has reached the age of 50). Next year this cap is projected to be increased to $69,000 (or $76,500 when including the unchanged $7,500 catch-up for 2024).

- **Roth IRA Conversion.**

Taxpayers can consider converting a traditional IRA to a Roth IRA in order to take advantage of lower brackets or absorb excess deductions. By converting a traditional IRA to a Roth IRA, any untaxed amounts that are rolled over to the Roth IRA are subject to income taxation. The conversion must take place by Dec. 31. Under current law, Roth IRA conversions can no longer be reversed. It's important to be mindful that the tax proposals being considered in Congress include higher tax rates for higher income individuals, as well as the imposition of AGI limitations on the ability of a taxpayer to qualify for a conversion, so, special attention should be paid to this powerful tax planning option in 2023, before it may be eliminated for many in the future.

- **Basis Step-Up Planning.**

For individuals who have funded "grantor" trusts for their families, year-end is a good time to consider swapping back low basis assets (e.g., appreciated stock) for high basis assets (e.g., cash) to help make tax reporting after the swap cleaner (rather than switch tax identification numbers in the middle of a tax year). It is better to own the lower basis assets at death because of the opportunity for a basis step-up to fair market value under Internal Revenue Code Section 1014. There is always a chance that this planning could change in the future if the step-up basis at death is ever

eliminated or if grantor trusts will be treated differently for tax purposes. Less favorable tax treatment of grantor trusts has been proposed by the current administration in the past, but, it remains uncertain when or if any of the proposed less favorable changes will be implemented.

- **Charitable Giving.**

Taxpayers in a high-income year can consider "prepaying" future charitable contributions to generate current income tax deductions. This is also something to consider given the new higher standard deduction (for 2023, $13,850 for individuals and $27,700 for married couples), which might make bunching of charitable deductions worthwhile so you can benefit from the standard deduction in a year where your charitable deductions are reduced due to the prior year bunching/prepayment. This can be accomplished by increasing the contributions to your favorite charities, in general, or by deferring the receipt by the charitable organizations (or even defer the decision as to which ones to benefit) by contributing to a donor advised fund, a private foundation, charitable lead trust or charitable remainder trust or purchasing a charitable gift annuity. Both the charitable gift annuity and charitable remainder trust options allow you to retain an income stream for life and defer the transfer of the remaining funds to the charity until after your death.

- **IRAs and HSAs.**

Taxpayers have until April 15, 2024, to fund their individual retirement accounts and health savings accounts for 2023, however, it is always a good idea to start planning for such funding at year end. For those with children who have earned income, consider helping your children fund tax favored Roth IRAs if possible. The maximum contributions for IRAs for 2023 is $6,500 and will increase to $7,000 in 2024 (plus an extra $1,000 catch up for those who have reached the age of 50). The maximum family contribution for an HSA in 2023 is $7,750 (or $3,850 for individuals), with an extra $1,000 available for those who have reached the age of 55. For 2024, the maximum family contribution for an HSA will increase to $8,300 (or $4,150 for individuals).

- **Trust Income Tax Planning.**

While a trustee will generally have until 65 days after the end of the tax year to shift trust taxable income to a beneficiary, it is worthwhile to monitor the issue at year end to get a jump start on evaluating the issue. This has become a more consequential issue with the Medicare tax imposed at 3.8% and the extra 5% tax imposed on dividends and capital gains at the higher brackets (which are reached pretty quickly for a trust).

- **Estate Plan Review.**

Finally, although not year-end sensitive, the end of the year is a great time to review your overall estate plan to see if changes might be in order (whether due to tax law changes, wealth changes or family circumstances). Even if you don't intend to make any changes to your estate plan before year end, many times it is helpful to set an artificial deadline to review everything and make sure everything is in order before it's too late. Perhaps, a New Year's resolution for 2024!

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