Year-End Tax Planning Strategies

Waiting until just before April 15 to start thinking about your taxes may prove to be a costly mistake. Preparing a draft of your tax return before the end of the year will provide you with a more complete picture of what you are likely to owe, and it may leave you with enough time to reduce your tax liability by contributing to tax-advantaged savings accounts or qualifying for deductions. Advance tax planning is especially important if your circumstances have changed over the past year due to events such as marriage, divorce, the birth of a child, or the death of a family member.

Deferring income into the next tax year and accelerating deductions into the current year can reduce your adjusted gross income (AGI). Lowering your AGI could make you eligible for certain tax breaks that phase out at higher income levels, such as personal exemptions and education credits. Here are some strategies that may help you trim your tax bill:

Defer income

Discuss with your employer the possibility of deferring some of your income by postponing payment of all or part of your annual bonus or salary until January.

Buy on credit

Accelerate deductions by making tax-deductible purchases before the end of the year using a credit card. This will allow you to take the deduction in the current year, but pay for the purchases later.

Prepay state and local taxes

If you pay state and local taxes before the end of the calendar year, you may deduct these payments on your Federal tax return.

Donate to charity

By donating appreciated assets held for more than a year to charity, you avoid paying taxes on the gains, and you can still deduct the full value of the assets. Charitable contributions of cash, personal property, or miles driven are also tax deductible, provided the charity receives the gifts by the end of the year.

Qualify for a medical expenses deduction

After adding up your medical expenses, you may discover that they are close to the AGI threshold that would allow you to claim a deduction. To qualify, look for ways to accelerate your health care purchases, such as buying an

Copyright © 2016 Liberty Publishing, Inc. All rights reserved.
Distributed by Financial Media Exchange.

advance supply of prescription drugs, investing in medical equipment, or scheduling an elective surgery before the end of the year.

Offset gains with losses

If you have been thinking about selling assets that have declined in value, now may be the time to act. Sale of capital losses can be used to offset realized capital gains. In addition, up to $3,000 in losses can be offset against ordinary income. If losses exceed this amount, they can be carried forward to future tax years. Keep in mind, however, that short-term capital gains taxes apply to the sale of assets held for less than a year, which could make selling these investments less attractive.

Transfer capital gains and income to children

If you are a higher income taxpayer and wish to sell assets held for more than a year, it may make sense to gift these assets for subsequent sale to a child or another family member in a lower tax bracket. When gifting to children under the age of 19 (or 24 for full-time students), be aware that these gifts may be subject to the kiddie tax. You can also reduce your gift and estate tax liabilities by making tax-exempt gifts of up to $14,000 per beneficiary.

Save for retirement

Contribute the maximum dollar amount, or at least enough to receive the full employer match, to your 401(k) account. If your employer has added the Roth feature to your company 401(k) plan, consider whether moving to this after-tax option would save you money in the long run.

Review your flexible spending account (FSA)

If you have an FSA through your employer, check to see if all the funds have been spent. If there is cash left over in the account, consider using the money for qualified purchases, such as prescription drugs, eyeglasses, or contact lenses. If you do not currently have an FSA, consider whether you would benefit from joining your employer's flexible spending plan for the coming year. The money in this account may be withdrawn tax free for qualified medical and childcare expenses, but all funds must be used before a certain date or the money will be forfeited.

Prepay your mortgage bill

If you make your January 2017 mortgage payment by December 31, 2016, you are permitted to deduct the interest charge on your 2016 tax return.

Before acting on these tax-savings strategies, it is important to consider your potential alternative minimum tax (AMT) liability. It may not be possible to avoid the AMT, a parallel tax system which has its own set of rates and does not allow most exemptions and deductions. Knowing, however, whether you are likely to owe taxes under the AMT can help you plan your deductions to prevent increasing the amount you owe in taxes. It is especially important to plan carefully when exercising incentive stock options, as doing so can trigger the AMT.

Decisions about whether to delay income and accelerate expenses will, of course, depend on your particular situation. If, for example, your tax bracket is likely to be higher in the coming year due to a change in circumstances, it may not be worthwhile to delay income. For specific guidance on year-end tax planning, contact one of our qualified tax professionals.

Copyright © 2016 Liberty Publishing, Inc. All rights reserved.
Distributed by Financial Media Exchange.