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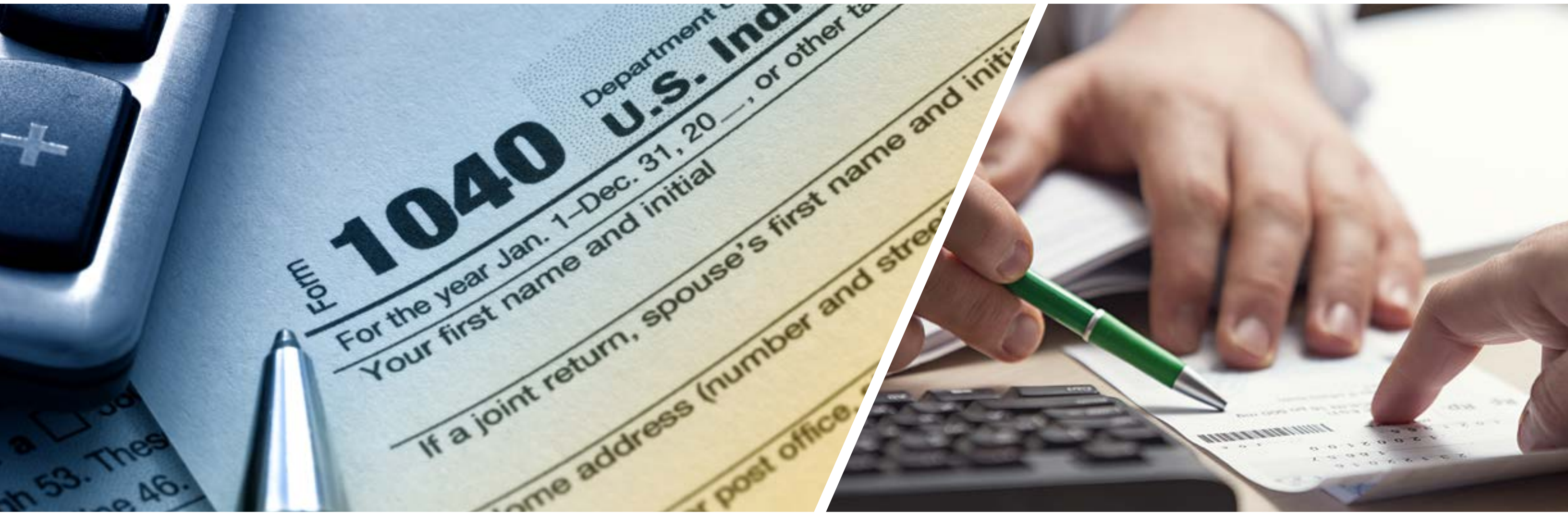
End-of-Year Moves to Trim Your 2019 Tax Tab



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It's time to look for last-minute moves that can shrink your 2019 tax bill. But the end of the year is coming fast, so don't procrastinate.

Before the New Year arrives, it's time to look for last-minute moves that can trim your 2019 tax bill. The good news is that the tax law is pretty similar to last year, which should make estimating your tax bill easier. "Things haven't changed a lot," says Mark Luscombe, principal analyst for Wolters Kluwer Tax and Accounting. "Changes from the 2017 tax act were in effect last year and this year." The bad news is the end of the year is coming fast, so don't procrastinate.

First, estimate your 2019 tax tab by adding up your taxable income streams, then subtracting the tax breaks you know you will use. This exercise should help you determine whether you'll take the standard deduction this year or itemize. The standard deduction for 2019 is $12,200 for single taxpayers and $24,400 for those married filing jointly. Each spouse who is 65 or older can add an extra $1,300 to the standard deduction, while singles 65-plus can add $1,650.

To avoid underpayment penalties, your estimated tax tab should be $1,000 or less, or you should pay tax, through withholding or estimated tax payments, throughout the year that equals at least 100% (110% for high-income taxpayers) of your 2018 tax bill or at least 90% of your 2019 tax tab. The IRS lowered the 90% threshold to 80% for 2018, but Luscombe notes that there's "no indication the IRS will do it again for 2019." Be prepared to stick to the regular rules.

Use the **IRS' withholding estimator** to see if you're on track to meet one of those safe harbor tests. If you are off track, you still have time to fork over some more cash to Uncle Sam to pass one of those tests and skirt underpayment penalties. Lowering your taxable income will also reduce your tax tab, which could help you avoid those penalties, too. "The traditional approach of deferring income and accelerating deductions still holds true," says Paul Gaudio, wealth planning strategist at Bryn Mawr Trust.

With year-end so close, your 2019 tax estimate should be fairly accurate, which means your tax-trimming moves can be more precise. Consider the following moves to trim your 2019 tax bill before the calendar flips to next year.

Max out. If you are still working, you can stash up to $19,000 in a 401(k) or other employer retirement account by year-end. "Those 50 and older by the end of the year are allowed an extra catch-up contribution," notes Kevin Martin, lead tax research analyst for H&R Block's Tax Institute. That extra $6,000 for 2019 means a boomer could put away up to $25,000 for the year. "That will reduce adjusted gross income and taxable income," says Martin.

You can put up to $6,000 in an IRA for 2019, plus an extra $1,000 if you are 50 or older. Check whether your contributions will be deductible if you put them in a traditional IRA (search "IRA deduction limits" at **IRS.gov**); if not, consider contributing to a Roth IRA instead if you fall below the income thresholds. The sooner the money goes into the IRA, the longer it can grow in the tax shelter, but the IRS lets you make 2019 IRA contributions up until the April 2020 tax-filing deadline.

If one spouse is retired, the working spouse can stash up to the maximum limit into a spousal IRA for the retired spouse. "You can double up," says Judith Ward, senior financial planner for T. Rowe Price. The working spouse must have enough earned income to cover all the IRA contributions for the couple.

If you have a health savings account, April 15 is also the deadline for making 2019 contributions of up to $3,500 for single coverage and up to $7,000 for family coverage. Once you are on Medicare, though, you can no longer contribute to an HSA. In that case, "the contribution limit is prorated by month," says Martin. If you turned 65 in July and enrolled in Medicare, you can only stash up to half a year's worth of contributions in an HSA.

- **Withdraw your RMD.** If you haven't already done so, withdraw required minimum distributions from your retirement accounts. While your first RMD can be delayed until April 1 of the year after you turn 70½, subsequent RMDs must be taken by December 31. Most experts advise not waiting past the first week or two of December.

Miss taking your RMD on time and you could get socked with a 50% penalty on the shortfall. You can request a waiver of that penalty by filing Form 5329, but avoid the issue altogether by taking the RMD before the deadline. You can use **Kiplinger's RMD calculator** to ensure you take out the correct amount.

For traditional IRAs, you can figure the RMD for each account you own but then take the total RMD from one or any combination of those IRAs. Roth IRAs have no RMDs, but Roth 401(k)s do; avoid those RMDs by rolling the Roth 401(k) money into a Roth IRA.

If you own multiple 401(k)s, you'll need to figure and take an RMD from each 401(k) separately. If you still work and don't own more than 5% of the company, you don't need to take an RMD from your current employer's 401(k) until April 1 of the year after you retire.

With a first RMD, you'll need to decide whether to make use of that delayed deadline. "It's a tax calculation as to whether to double up RMDs or not," says Gaudio. Delaying the first RMD means you will have to take your second one in the same year. So compare the tax consequences of spreading those two distributions over two years, versus taking both in one year.

- **Use the RMD solution.** Are you at risk of getting hit by the underpayment penalty? If so, before you take your RMD, ask your custodian to increase the withholding on the distribution. That withholding can help cover the tax bill on any of your taxable income sources. (Keep in mind that you can also adjust withholding on Social Security benefits, pensions and annuities.)

Even if you take the RMD in December, the withholding is considered to have been paid evenly throughout the year. "That would be more advantageous than paying a big fourth quarter payment," says Luscombe.

Making a large estimated tax payment for the fourth quarter will help you avoid some underpayment penalties, but if you had a large windfall in the first quarter, for instance, you may still get socked for not having paid the estimated tax in the same quarter as your income. Increase withholding and the timing isn't a problem.

- **Do a QCD.** Another smart way to make use of your RMD: Give all or part of it to charity through the qualified charitable distribution move. Traditional IRA owners who are age 70½ or older can give up to $100,000 from their IRA directly to charity every year. The QCD amount can count toward the owner's RMD and won't be included in his adjusted gross income.

"The greatest benefit is the income never comes into the tax return," says Suzanne Shier, chief tax strategist for Northern Trust. "You can manage AGI and benefit charity." She notes that married taxpayers can each make a QCD.

This move is a boon to the charitably inclined who take the standard deduction and can no longer get a tax break from charitable gifts by itemizing. But it can also work for itemizers. Because the QCD lowers AGI, "it might help you qualify for other deductions that phase out with AGI," says Luscombe.

- **Bunch deductions.** With the standard deduction doubling under tax reform and the additional standard deduction amount for seniors, you may be hard-pressed to find itemizing worthwhile. But, "if you are on the cusp of itemizing, it might make sense to bunch deductions," says Lisa Featherngill, a certified public accountant and member of the American Institute of CPAs Personal Financial Planning Executive Committee. Consider your tax situation for the next two or three years, and weigh whether it would be beneficial to bunch deductions this year or a future year.

Unreimbursed medical expenses that exceed 10% of AGI are deductible in 2019; that is a higher threshold than last year. Consult **IRS Publication 502** for a list of qualifying expenses, which include a portion of long-term-care insurance premiums and certain home improvements made to accommodate a medical condition or disability.

Let's say this year you had a lot of deductible medical expenses, which you don't anticipate having next year. You may want to make a sizable charitable gift this year to increase your itemized tax deductions for 2019 over the standard deduction threshold. If you make that gift next year but end up using the standard deduction, you'd forgo the itemized charitable tax deduction.

See **IRS Publication 526** for the rules on documenting charitable gifts. Remember that you can deduct 14 cents a mile for any miles driven in service of a charity.

If you want to donate a large amount in 2019 to trim your tax bill but don't yet know which charities you want to support, consider donating money or appreciated stock to a donor-advised fund at a brokerage firm or local community foundation. You can take the itemized charitable deduction for the gift in 2019, and direct grants to various charities from your donor-advised fund in future years. "You can bunch up gifts, but smooth out your actual giving to charities," says Shier.

- **0% rate.** The stock market has been soaring, so it could be prime time to consider taking some profits off the table if you qualify for the 0% long-term capital-gains tax rate. For 2019, the 0% rate applies for single filers with taxable income up to $39,375, joint filers with taxable income up to $78,750, and head-of-household filers with taxable income up to $52,750. So, for example, if a married couple filing jointly has only $60,000 of income for 2019, they could sell investments for a profit of $18,750—and pay no tax on that gain.

While you have to be careful about buying back investments sold at a loss, there is no concern about immediately buying back investments sold at a profit and locking in a new, higher basis.

Harvest losses. While the market's done well in 2019, it wasn't a straight shot up nor will every investment be a winner. Consider harvesting losses to offset capital gains and up to $3,000 in ordinary income.

If you like the investment, wait at least 30 days before buying back identical shares. Otherwise, you could run afoul of the wash-sale rule and disallow your capital loss.

- **Convert to a Roth.** Converting money from a traditional IRA to a Roth IRA won't save you money on taxes today but could deliver tax savings in the future. The tax-free distributions are "not included in income, are not in your tax bill and can be used for any purpose," says Martin. Tapping a Roth in retirement may help rein in taxes on Social Security benefits and mitigate Medicare premium surcharges that hit high-income taxpayers. And with pending legislation threatening the stretch IRA, heirs could benefit from inheriting a Roth instead of a traditional IRA with taxable distributions.

A Roth conversion will add to your taxable income, but the silver lining is that tax rates are relatively low until 2026. You can mitigate the pain of the extra taxable income by making smaller conversions over a number of years. A smart strategy is to convert just enough to keep your income in the same tax bracket. With year's end nearly here, it should be easier to pinpoint exactly how much room you have left in your current bracket to convert money to a Roth account. If you instead do a hefty Roth conversion, you could spike your income into a higher bracket unnecessarily.

For more information, please email us: **info@lhfcpa.com**

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